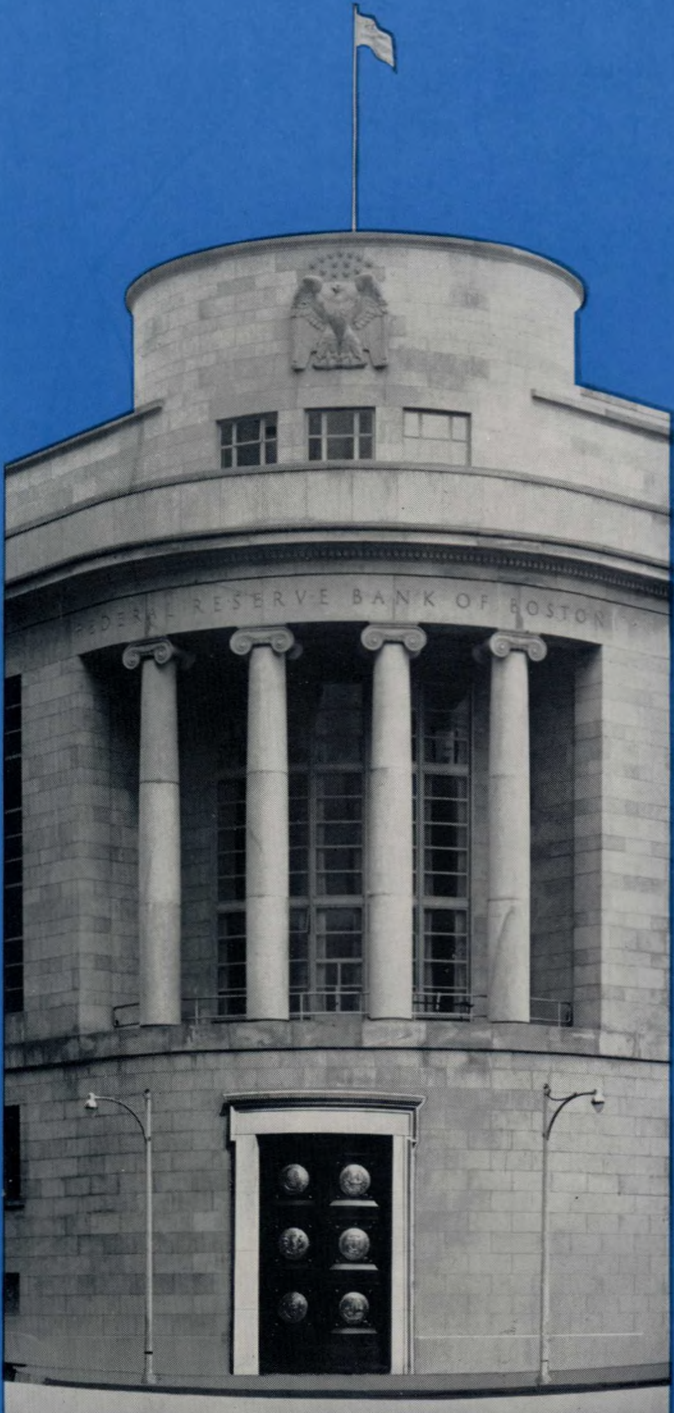


1953

FEDERAL RESERVE BANK
of BOSTON

Welcome to the new building of the Federal Reserve Bank. In this booklet we introduce you by words and pictures to our enlarged and renovated quarters. We wish to show to you of New England how with these improved facilities and modernized equipment we shall be able better to serve you.

These words and pictures indicate only the physical side of the bank. More important are the intangible factors of loyalty, will to work, and cooperation of the men and women who make up its staff. It is these unseen factors which in the final analysis determine the quality of the bank's services.

President

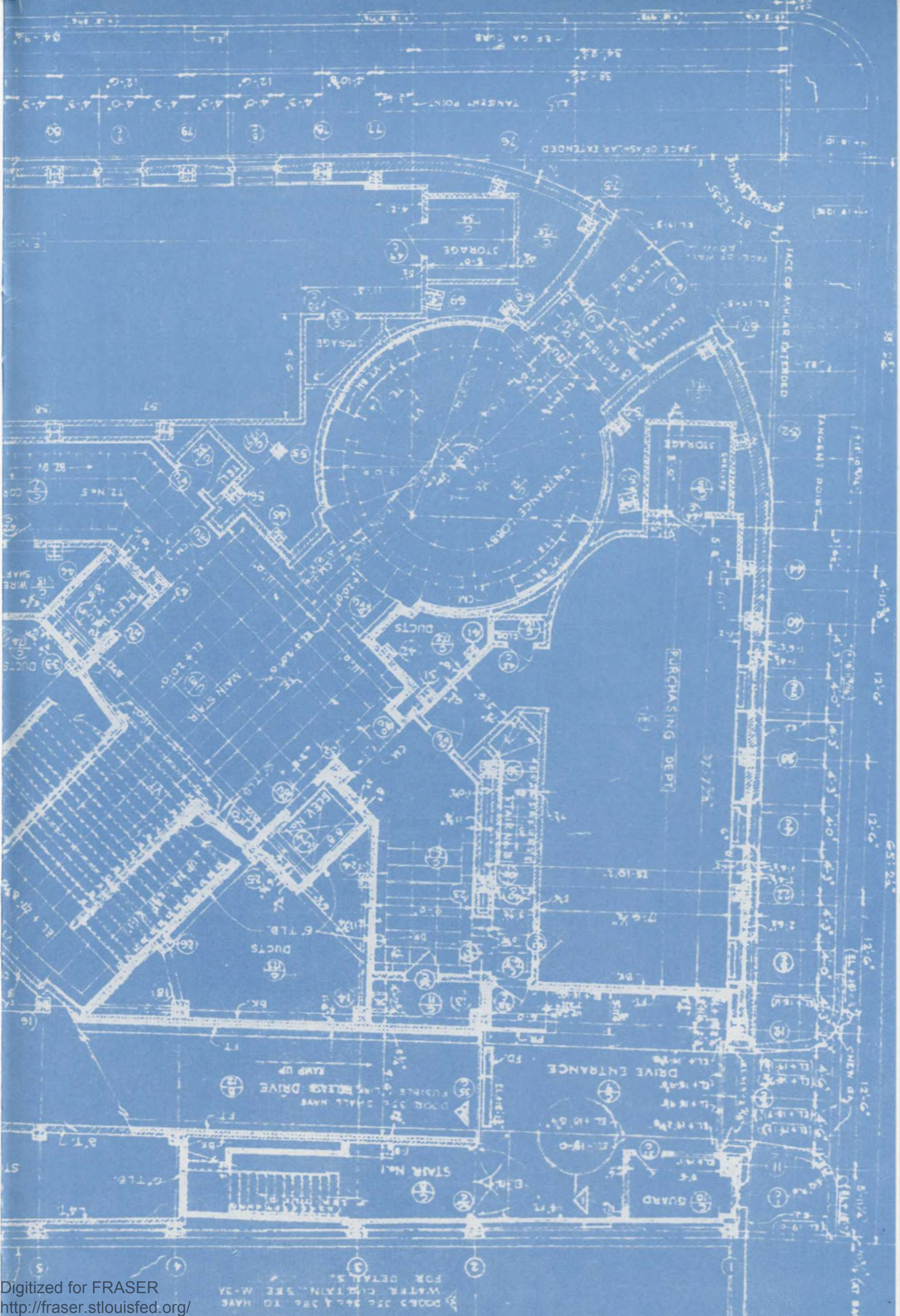
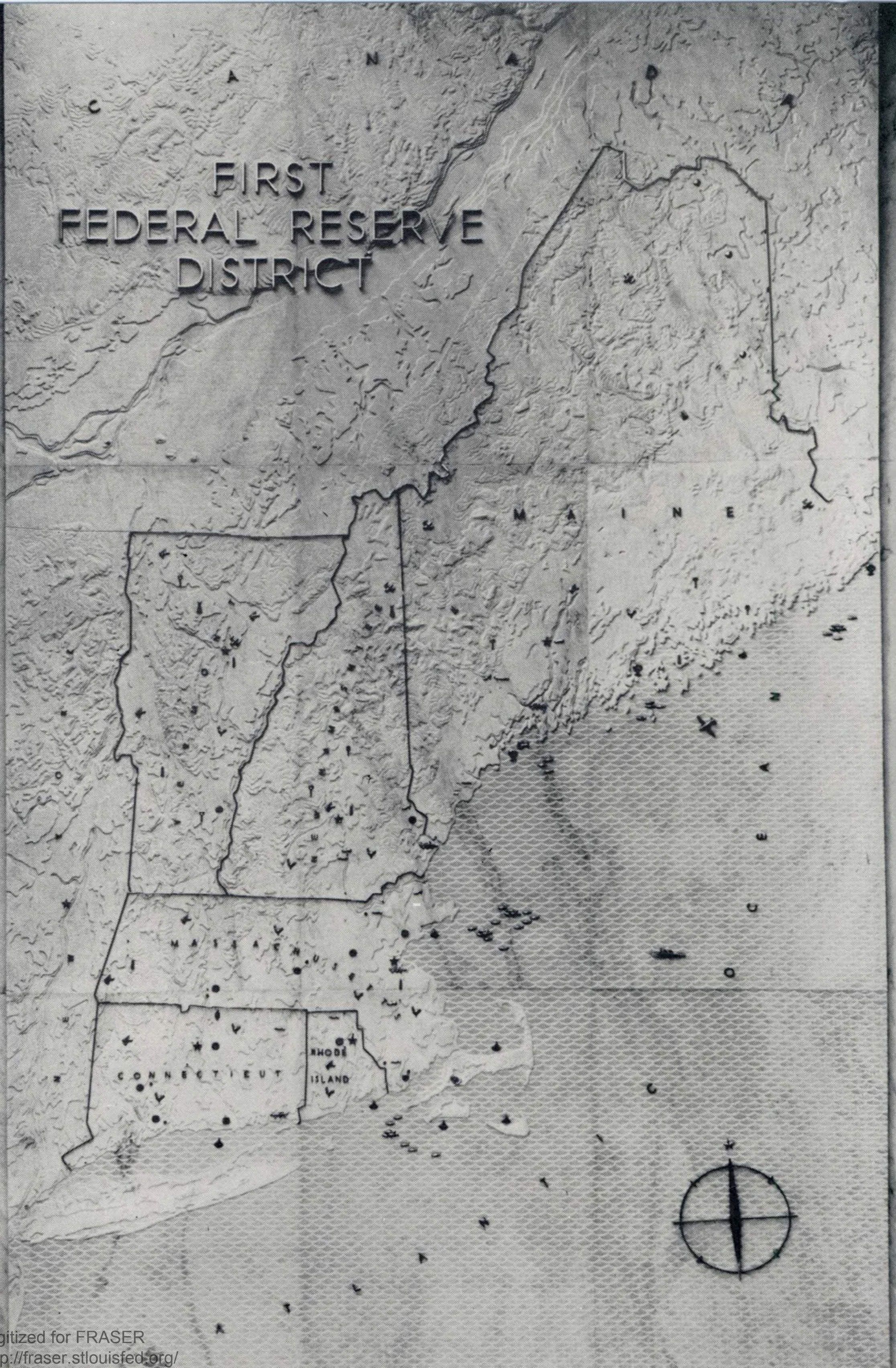

STORAGE
ENTRANCE LOBBY
MAIN STAIR
PURCHASING DEPT
DUCTS
DRIVE ENTRANCE
STAIR No. 1
GUARD

TABLE OF CONTENTS


FIRST
FEDERAL RESERVE
DISTRICT
MAINE
CONNECTICUT
RHODE ISLAND

New Look

Out of the changing, noisy maze of brick and rubble, steel and concrete, cranes and beams, scaffolding and stone, has emerged the new building of the Federal Reserve Bank of Boston. It is of classic design, inspired by New England Federal architecture of the early nineteenth century. The exterior is built of limestone, to match the original building, with pink granite trim from New Hampshire.

Large mahogany paneled doors two stories high form the entrance. Rugged New England philosophy speaks from the six state seals executed by Sculptor Donald De Lue which adorn the door panels. Above the entrance is a three-bay loggia with four Ionic columns of solid stone. Perched atop this composition on the setback fifth floor wall of the oval Directors' Room is an American eagle carved from an eighteen-ton block of stone.

Within the doors a circular entrance lobby leads from the entrance to the main stairway. At the head of the first flight of Vermont marble steps is a decorative relief map of the First Federal Reserve District. This map, designed by Artist Austin Purvis, Jr., is carved on Vermont marble and on it are names and symbols in different metals significant of the economic and natural characteristics of the various sections of New England.

In the basement is a loading and receiving room with limited space for automobile parking and a pistol range for the protection staff. Ground floor corridors connect the entrance lobby with the public banking room and the Personnel and Purchasing Departments. On the first floor, offices for the Chairman of the Board, the

THAT FREQUENT RECURRENCE
TO FUNDAMENTAL PRINCIPLES
AND A FIRM ADHERENCE
TO JUSTICE, MODERATION, TEMPERANCE,
INDUSTRY AND FRUGALITY
ARE ABSOLUTELY NECESSARY
TO PRESERVE THE BLESSINGS OF LIBERTY
AND KEEP GOVERNMENT FREE

☆ ☆ ☆

FROM ARTICLE XVIII
OF THE VERMONT BILL OF RIGHTS
ADOPTED 1777

IN THE FEDERAL RESERVE ACT
WE INSTITUTED A GREAT AND VITAL BANKING SYSTEM
NOT MERELY TO CORRECT AND CURE
PERIODICAL FINANCIAL DEBAUCHES
NOT SIMPLY INDEED TO AID THE BANKING COMMUNITY ALONE
BUT TO GIVE VISION AND SCOPE AND SECURITY TO COMMERCE
AND AMPLIFY THE OPPORTUNITIES
AS WELL AS TO INCREASE THE CAPABILITIES
OF OUR INDUSTRIAL LIFE AT HOME
AND AMONG FOREIGN NATIONS

☆ ☆ ☆

AN ADVENTURE IN CONSTRUCTIVE FINANCE
CARTER GLASS

Inscriptions in Raised Bronze Lettering on Marble Walls of Opposite Sides of Circular Entrance Lobby

President and other officers are done in early New England Federal style. The second floor provides space principally for the Department of Research and Statistics and the third floor extends the area of the main building used for check collections. The fourth floor is devoted mainly to services for the staff. A first-aid medical suite has examination, treatment and rest rooms, all equipped for modern medical needs. The main area of this floor has folding partitions permitting the space to be used as one large meeting room or divided into smaller areas for staff recreation and social activities. Should the occasion arise, part of this area can be used for working space. The fifth floor contains the Board room, committee rooms, conference room and dining rooms with kitchen pantry. The sixth floor and penthouses contain the ventilation, air-conditioning equipment and elevator machinery.

All areas are being air-conditioned for the comfort of the staff in both the new and the original building. New, modern locker and washrooms are provided on each floor. The entire building is provided with modern, electric equipment including underfloor ducts for flexibility of space, protective devices, emergency call stations, and other uses, to insure maximum protection.

Comparative Statement of Condition

	1952	1922
ASSETS	*December 31, 1952*	*December 31, 1922*
Gold Certificate Reserves	$ 753,319,645	$208,146,603
Other Cash	22,031,579	15,351,719
Loans and Advances	2,214,000	61,583,891
Bankers' Acceptances Purchased	0	25,406,781
U. S. Government Securities	1,693,012,000	29,593,330
Federal Reserve Notes of Other Federal Reserve Banks	5,996,000	1,613,130
Uncollected Cash Items	387,995,133	54,907,157
Bank Premises	4,071,254	4,434,271
Other Assets	11,396,916	719,241
Total Assets	$2,880,036,527	$401,756,123
LIABILITIES		
Federal Reserve Notes	$1,603,208,415	$201,313,755
Deposits:		
Member Bank Reserve Accounts	835,721,105	126,342,136
U. S. Treasurer—Collected Funds	44,086,174	534,002
Foreign	32,457,000	73,000
Other	10,012,896	1,015,600
Total Deposits	$ 922,277,175	$127,964,738
Deferred Availability Cash Items	293,075,152	47,789,689
Other Liabilities	713,468	211,939
Total Liabilities	$2,819,274,210	$377,280,121
CAPITAL ACCOUNTS		
Capital Paid In	$ 13,611,750	$ 8,126,250
Surplus (Section 7)	36,461,592	16,312,376
Surplus (Section 13b)	3,010,527	0
Reserves for Contingencies	7,678,448	37,376
Total Capital Accounts	$ 60,762,317	$ 24,476,002
Total Liabilities and Capital Accounts	$2,880,036,527	$401,756,123

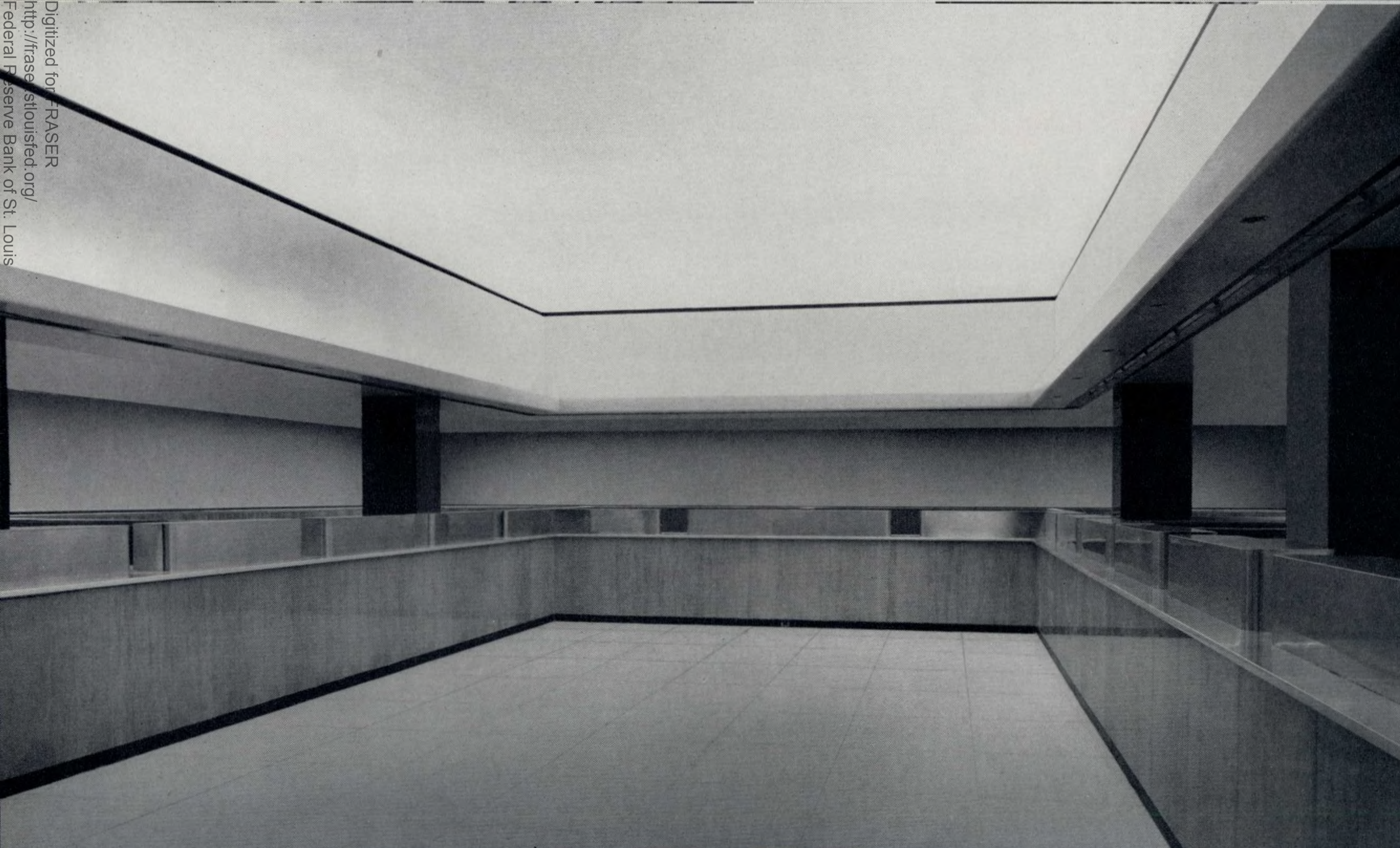
The Enlarged Quarters Now Extending from Franklin Street
to Milk Street on Pearl Street

Atlantic National Bank
of Boston Built in 1924

Converse Building
Where Federal Reserve Bank Opened
in October 1914
and Site of New Addition

New England Mutual Life
Building

The Main Entrance Lobby



The Public Banking Lobby

A Tour of the Bank

To appreciate the volume of business accomplished at the Federal Reserve Bank of Boston, you need only to make a trip through our various departments. Here you will see where and how we make thousands of transactions, large and small, which go into an average day's work. Here you will get an understanding of the close tie-in which exists between the bank's operations and the daily business needs throughout the First Federal Reserve District.

As business expands in New England, so do the operations of the Federal Reserve Bank. There are more checks to be handled, more currency and coin to be put into circulation, more bonds to be issued or redeemed. The new building, where our tour starts, is a symbol of the expansion in our activities over the past three decades, an expansion which has seen our staff more than doubled.

Let's take a tour of the bank right now, so that you can observe for yourself the operations which are so essential to the needs of New England banks and their customers. We start at the main entrance of the new building. As we pass down the corridor to the right, you will see our Personnel Department where job applicants are interviewed and vital statistics on the more than 1,400 members of our staff are kept up to date. To your left is the public banking room where various transactions with banks and the public are conducted.

We proceed into the service corridor and take the elevator to the fifth floor. Here you will see our cafeteria where lunches are served to our staff members at less than cost. You next see some of

Fourth Floor Lounge Area, Convertible to Operating Space if Necessary

the kitchen facilities and the dining rooms in the new building. After viewing our Directors' Room and Committee Rooms, we take you down to the fourth floor where you visit our modern Medical Department. From here we go to the staff's recreation rooms and to the auditorium where concerts by the glee club, organ recitals, and other activities are held during lunch-hour periods.

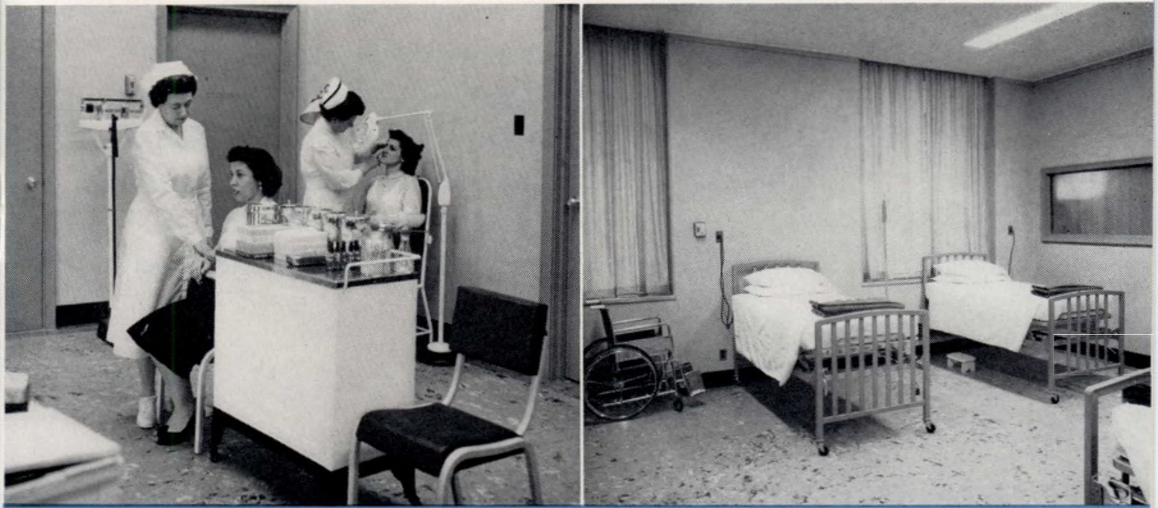
Crossing the service corridor, we visit the Fiscal Agency Department where the Federal Reserve Bank performs services as agent of the U. S. Treasury Department. This department issues and redeems millions of dollars in savings bonds and other Government securities every business day.

Passing by the Non-Cash Collection Department where items such as notes, maturing bonds, non-Government coupons, and drafts are collected for member banks, we go down to the third floor where you will see our largest operation — check collection. This department occupies the third floor of both buildings. A total of 530 people are employed here. The output of the Check Collection Department seems almost unbelievable. Last year it handled a *daily* average of 966,274 items, more than double the volume handled in 1943.

The machines you see are called "proof machines," which are used to sort the bundles of checks which come in to us from member banks and to add the amounts for which they are drawn. A battery of 169 proof machines, each with 32 pockets, insures great speed and accuracy in getting these checks to their ultimate destinations. Most of the incoming checks are microfilmed so that they can be easily traced if lost or misplaced after they leave us.

We now proceed to the second floor of the new building to the Research and Statistics Department where the Federal Reserve Bank collects, analyzes and interprets economic information needed by its member banks, the New England business community and the Federal Reserve System.

Our tour takes us back across the service corridor where we visit the Accounting Department which keeps a daily record of all the financial transactions of the bank. Member banks are required by



This Modern Medical Suite Provides for First Aid and Health Service for the Staff

Executive Section of Fiscal Agency

Connecticut Unit of Check Collections

Section of Research Department

law to keep a certain percentage of their deposits in reserve with us, and the Accounting Department maintains this record and sends out daily statements to the member banks. Next to Accounting is the Auditing Department which keeps a constant check on all other departments.

Down on the first floor we visit another one of the bank's major operations — the Currency Department. Here we maintain New England's supply of paper money, putting out new money as it is ordered by the member banks and sorting out worn, mutilated and dirty notes received from member banks. This department received or shipped over one-half billion pieces of currency last year. In the currency division you will see the money-sorting machines, and the machine which slices unfit currency for shipment to the Treasury in Washington where it is destroyed.

We next visit the Discount and Credit Department. This department extends credit to member banks by lending on their investments and discounting their customers' notes. The adjacent Safekeeping Department receives billions of dollars in securities from member banks, holds them in safekeeping, and clips the coupons as they mature.

We view the Officers' quarters in the new building and return through the Junior Officers' quarters, past the Legal Department, then down to the ground floor to the Wire Transfer and Planning Departments, with the Fiscal Agency vault on the left. Around the corner past the Registered Mail Post Office, between the Security Court on the right and the Currency Vault on the left, we enter the Coin Department where the new automatic coin-wrapping machines are in action. This department handles daily in receipts and shipments more than 36 tons of coin. Our tour ends under the flags in the Members' Court.

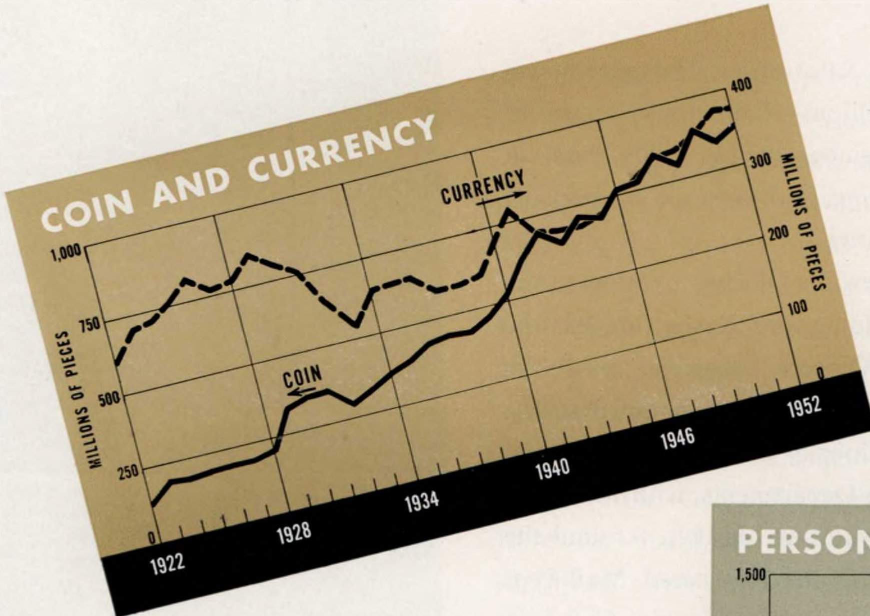
Time has not permitted visits to other departments, including Bank and Public Relations, Bank Examinations, Building Maintenance, Expense, Filing, Mail and Messenger, Machine Repair, Note Teller, Printing, Protection, Purchasing, Supply and Telephone.

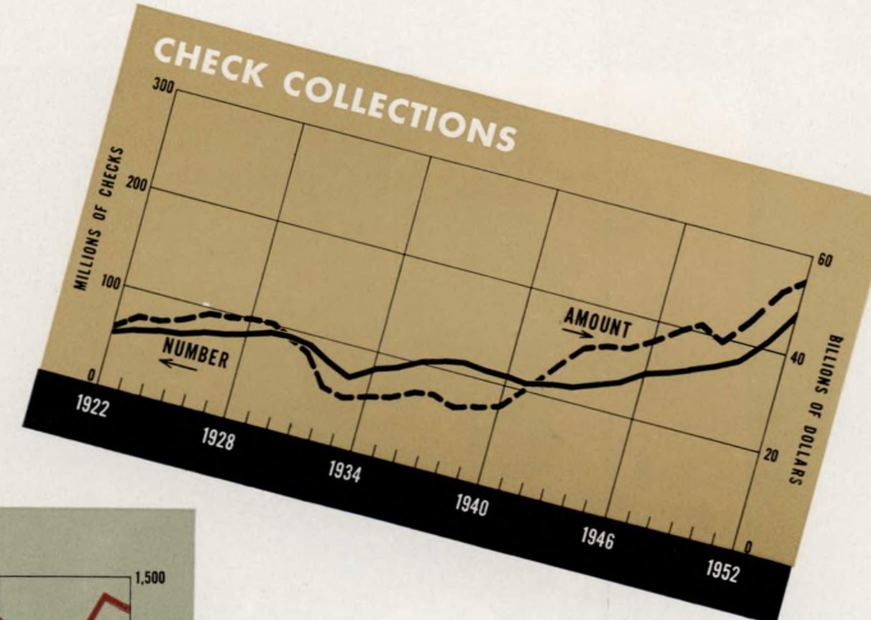
Accounting Department

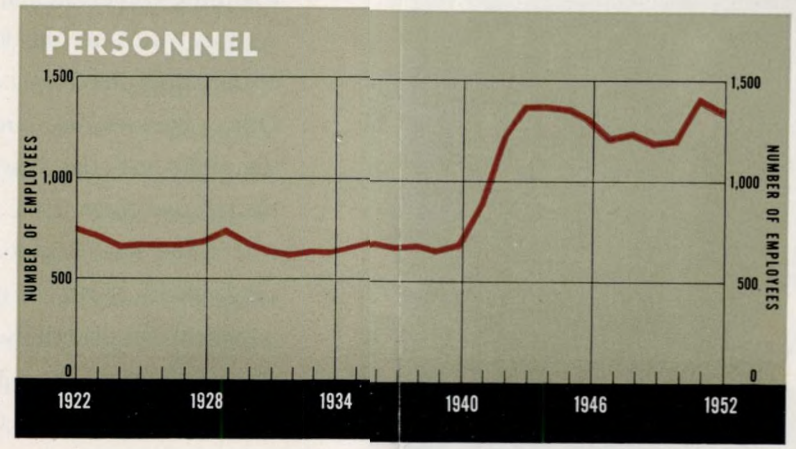
Sorting Currency

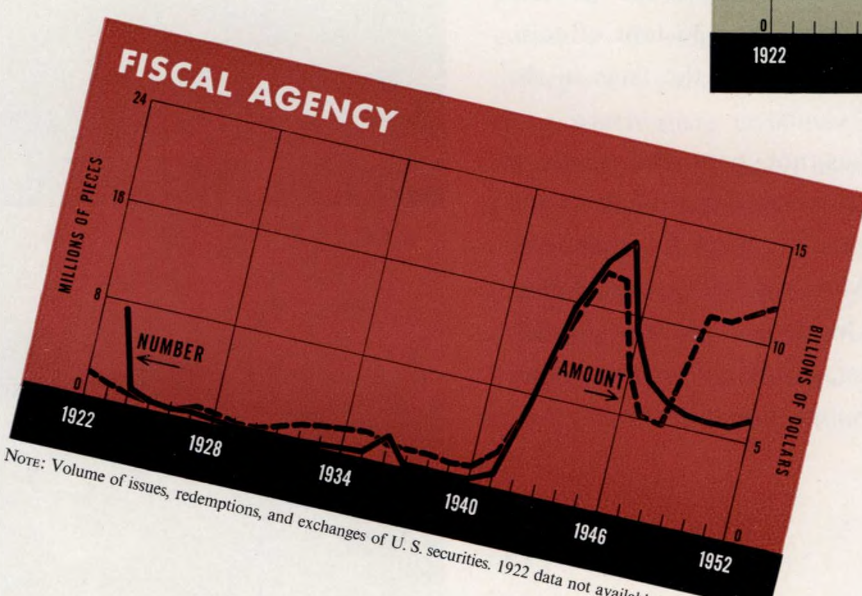
New Automatic Coin Wrappers

1922 *through* 1952









NOTE: Volume of issues, redemptions, and exchanges of U. S. securities. 1922 data not available.

NOTE: Subsequent to 1933, discounts and advances for member banks consisted principally of member banks' collateral notes secured by U. S. securities, while prior to 1934 member banks rediscounted their customers' notes in large volume. This accounts for the relatively small number of pieces of units handled since 1933.

THIRTEEN MEMBERS OF THE ORIGINAL STAFF OF SEVENTEEN

Standing — Russell B. Spear, Lewis E. Stoyle, Frank W. Chase, Earle P. Perkins, William Willett, George A. Stearns, Carl B. Pitman, Harry A. Saunders, Chester C. Bullen.

Seated — Ernest M. Leavitt, Frederic H. Curtiss, Alfred L. Aiken, F. M. Howe.

Those Were the Days!

By an author whose high ideals and winning personality have endeared him to thousands.[1]

STOP! HOLD EVERYTHING! DON'T TURN THIS PAGE! Give us a chance and let us explain. We want to tell you, very briefly, about this bank, why and when it was started, some of the things it has done through the years, and how it has served and helped New England through two wars and a depression.

Let us confess at once that this is not "a tale which holdeth children from play and old men from the chimney corner." We believe, nevertheless, that in the next few pages it can be shown that banking, as a profession, is not as cold and austere as is commonly supposed. Even statistics can be made interesting, believe it or not. Give heed.

Following the financial panic of 1907, Congress established the National Monetary Commission to study the banking system abroad with a view toward improving the banking structure then in existence in the United States.

Based upon the findings of this committee Congress, after a long-winded debate, established the Federal Reserve System comprised of twelve regional Federal Reserve Banks with the Federal Reserve Board in Washington as the guiding head.

The Federal Reserve Act was signed by President Wilson on December 23, 1913, but it was not until the fall of 1914 that things really began to happen. Directors were appointed, officers were chosen, banking quarters were obtained and clerks were hired.

[1] That's what he thinks. Let him dream. (Editor's note.)

In Boston, the Federal Reserve Board appointed Frederic H. Curtiss, Chairman and Federal Reserve Agent. The directors elected Alfred L. Aiken, President of the Worcester National Bank, as Governor, and Florrimon M. Howe, Assistant Cashier of the Old Colony Trust Company, as Cashier. Quarters were obtained at 101 Milk Street, which, oddly enough after 38 years, is the site of our new building.

As these rooms did not have adequate vault facilities, the first instalment of capital stock payments amounting to $1,620,000 was received at the Subtreasury in the old Post Office Building on November 2, 1914.

The Federal Reserve Bank of Boston was opened for business on November 16, 1914, with three officers and fourteen clerks who reported for duty at the unearthly hour, for bankers, of 7:30 A.M. Having no precedent by which to judge, the officers had no idea as to the amount of business which might confront them and it was thought best to have every one on hand early. A lot of good it did them.

HARDLY A RIPPLE

In a couple of rooms containing a few desks, one telephone with an extension, and two typewriters as total equipment,[1] the entire staff stood by in apprehension to see what would happen when the doors were thrown open.

There was no need to be worried. A few newspaper men came in, admired the flowers on the officers' desks, asked some questions and departed. Curiosity seekers straggled in spasmodically, took off their hats respectfully and went out with bowed heads. One might have thought that here was a modest wake where the corpse had only a few friends who were faithful to the end.

[1] There was also a hat rack and some coat hangers.

The only real activity was at the Subtreasury where the first payment of member bank reserves was received. A number of clerks loaned by the Subtreasury and some of the Boston banks started in at 8.00 A.M. to count these receipts. The task was completed at 1.30 A.M. on November 17 with total receipts of about $14,500,000.

While most of the member banks were inclined to give the new Reserve System a trial, a few of them were antagonistic and quite outspoken in their criticism.

One bank made payment of its instalment of reserves by filling an old shoe box with torn and dirty one- and two-dollar bills, inscribing on the accompanying tag, "Three cheers for the Union but to hell with the way it's run." The same bank designated its next reserve payment as "Another steal."

Some months later, Senator Borah rose in all his majesty in the Senate and gave it as his opinion[1] that the Federal Reserve System was "a sort of antediluvian mastodon, too dead for a menagerie and too much alive for the operating table, designed for the Treasury but seemingly on its way to the Smithsonian Institution." Come to think of it, the Federal Reserve System seems to have been born in argument, nurtured in controversy and matured on criticism.

BUSINESS BRISK

Although business was quiet on the opening day, things picked up a bit shortly. The next day a Vermont bank rediscounted two notes for $5,000 each at 6 per cent. One of these notes was immediately pledged with the Federal Reserve Agent as collateral and $5,000 in Federal Reserve notes were issued, $3,000 in fives and $2,000 in tens. Note number one of each denomination was sent

[1] He didn't like it.

to the Federal Reserve Board in Washington for preservation. This first issue of Federal Reserve currency was quite an event and was solemnized by the attendance of the entire official staff — all three of them. Today several million are issued at one time and nobody gives the matter a second thought.

By the end of 1914 only ten banks had rediscounted, earnings were low, operating expenses were rising steadily, vault facilities were practically nonexistent, and the officers and directors were in a distinctly unhappy frame of mind.

Nothing much could be done about earnings at this time, but steps were taken to alleviate the vault situation. New quarters were leased in the Exchange Building at 53 State Street, where the bank was able to rent vaults adequate for its needs from the State Street Safe Deposit Company.

From this time until April 1917, when the United States became an active participant in World War I, this bank went through a period of gradual development. It was designated as a Depository and Fiscal Agent of the United States Treasury on November 24, 1915, and a transfer of government funds from the Subtreasury was made on January 1, 1916.

TROUBLE STARTED HERE

As Fiscal Agent, the bank coasted along without much difficulty until war was declared by Congress on April 6, 1917. What happened after that can best be described by the definition of the word "bedlam" in the dictionary, to wit, "an excited crowd; a scene of wild uproar and confusion; a madhouse."[1] It was all of that, doubled and redoubled.

[1] Sales of aspirin increased tremendously.

The bank started 1917 with 78 clerks and wound up the year with 256, most of them wondering if there wasn't some other way to make a living.

It is a regrettable thing to expand and grow strong on the adversities of war, but it must be confessed that the first World War did much to establish the Reserve banks as instruments of real service in their districts. The only other agencies available to the U. S. Treasury to float the huge Liberty loans necessary to conduct the war were a few subtreasuries and the post offices. It was a gargantuan task as it was; it would have been impossible otherwise.

Patriotic fervor ran high. The Liberty loan committees formed to sell the bonds lacked no dearth of volunteers. Neither did they want for ingenuity in dreaming up ways and means to get every last dollar from the populace.

NO HOME LIFE

The Reserve Bank, faced with the assignment of receiving the subscriptions and delivering the bonds, found itself in an unenviable position. Never before in the history of the country had the government attempted to finance a war of such gigantic proportions.

Additional quarters were obtained at 60 and 131 State Street, help was borrowed from banks and brokerage houses, and a strong and determined effort was made to stem the tide. This effort was not too successful, and many of the clerks got their first (but by no means last) taste of night work which lasted for weeks at a time.[1]

During the period before each loan was announced until the final allotment of bonds had been delivered, the situation was

[1] There were unhappy wives in the suburbs.

chaotic. Many men saw their families at breakfast-time only, a few others not at all, as rooms were reserved for them in Boston hotels so they would be nearer the bank. Why waste time commuting? Saturdays were full days, but Sundays and holidays were unusually well regarded; there were no telephones that had to be answered on those days.

Two Liberty loans were floated in 1917, two in 1918, and a Victory loan early in 1919, along with sales of numerous issues of certificates of indebtedness and War Savings Stamps.

DON'T STOP NOW

Many of the borrowed clerks remained with the bank as permanent employees after the last bond hah been delivered and the volume of work had receded. This was a real nice thing for them to do. They came in right handy when the War Savings Stamps were redeemed in 1922, and the veterans' Adjusted Service Certificates were issued in 1936.

Those who were still on the staff during World War II found out that history never changes; there was plenty of night work when the U. S. Treasury once again had to finance a war.

Through the years the personnel of the Fiscal Agency Department has fluctuated, naturally enough, with the volume of work handled. In 1933, smack in the middle of the depression, there were 18 clerks assigned to this department as compared with nearly 280 in 1919. In 1944, at the height of the war financing, there were 435.

The period of Liberty loan activity witnessed the start of the Collateral Department. All types of government securities, flagged with the names of the owning banks, were kept in small steel boxes of assorted sizes. Each night the boxes were stored away in the vaults, only to be hauled out again in the morning. As soon as the management could get around to it, certain of the vaults were turned over to the Collateral Department and the securities were delivered there, to be held at the pleasure of the owning bank.

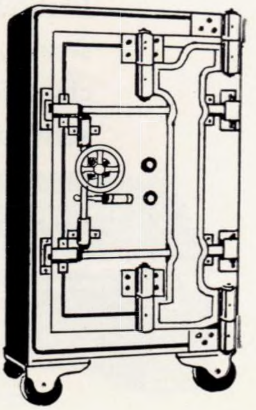
It was also during 1917 that the Discount Department came into its own. Rediscounts by member banks, brought about by industries in this district manufacturing arms, munitions and other war requisites, increased this bank's earnings considerably.[1]

According to some of the recipients, the most popular circular letter ever to be sent out by this bank was mailed to the member banks in December 1917. It stated in simple and direct language that a dividend at the rate of 6 per cent, covering all accumulated dividends from November 16, 1914, to December 31, 1917, was being credited to the member bank's account in the Federal Reserve. While this welcome notice hardly caused dancing in the streets, it did serve to allay the suspicions of many bankers that their investment in the capital stock of this bank should be written off as a poor risk.

AND NOW COME CHECKS

Now let's trace the gradual development of a department that has the dubious distinction of probably causing more criticism and more headaches than anything else the bank has undertaken.

The bank joined the Boston Clearing House on November 13, 1914, and five days later began to clear its Boston checks through that institution. Little further progress was made until June 15, 1915, when the collection of checks outside of Boston was started. Forty-three banks put forth the tender leaves of hope and joined the new undertaking. The first day's total number of checks handled was 226, but as time



[1] Out of the red at last.

went on the situation slowly improved until on October 15, 1915, the department racked up the outstanding number of 1,803 checks handled in one day.

The real beginning of the Check Collection Department, however, took place on July 15, 1916, when this bank took over the so-called Foreign Department of the Boston Clearing House, a department that handled checks drawn on New England banks.

As most of the member banks outside of Boston preferred to send their checks to their Boston correspondents for collection, progress was far from rapid in the new department for some time. However, with the elimination, on June 15, 1918, of the service charge which had been imposed on member banks for clearing their checks when the system was first inaugurated, volume picked up considerably.

START OF NIGHT FORCE

The average number of New England checks handled daily increased from 9,000 to 35,000, requiring a force of 116 clerks, to say naught of three men who had been inveigled into forming a Night Force (probably frustrated with their daily existence and wanted to try something different.[1] They got it.).

Several different procedures and systems have been adopted by the bank in an endeavor to speed up the work and get the clerks out at a reasonable hour with enough energy left to enjoy the evening.

The system used in the beginning was thorough, to say the least. Each check was handled eight times: first, at the sorting table; second, listed on block sheet; third, run through endorsing machine; fourth, examined to be sure check had been endorsed; fifth, sorted into rack; sixth, rechecked for missorts; seventh, listed on outgoing cash letter; and eighth, listed again for verification.

[1] They had no reason for going home. They were bachelors.

The clerks got attached to the checks after so long an association and hated to see them leave the bank at the end of the day. Incidentally, it is said that one girl, when she encountered a check for a million dollars, took it home to show her mother. When she brought it back the next day she couldn't understand why the manager seemed so upset and distraught.

The personnel of this department has increased through the years. In 1917 there were 25 clerks handling checks and there are now 346 on the day force. With three as a start in 1917, the Night Force now has a staff of 184, mostly women.

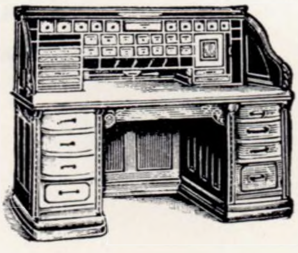
As the Fiscal Agency and Check Collection departments grew and expanded through the early years, so did other departments which were no less important, especially from the viewpoint of providing service to the member banks. Prominent among them were the Accounting, Non-Cash Collection and Currency and Coin departments, all of which required the service of a sizable number of clerks.

NOT EFFICIENT

In 1918 the various departments of this bank were spread all over the financial district. The main office was at 53 State Street, check collections were handled at 84 State Street and the Fiscal Agency could be found at 131 State Street. The Accounting, Auditing and Supply departments were located at 20 Kilby Street. Messengers wore out a lot of shoe leather unnecessarily.

In four years the number of personnel had increased from the original 17 to nearly 300 and was continually climbing. Space was at a premium and, what was worse, the vault situation had become acute once more.

The directors got busy and appointed a Building Committee which canvassed the city for available sites on which to erect a building sufficiently large to house



all the departments of the bank and all the vaults they needed.

After several months a plot of land bounded by Pearl, Franklin and Oliver streets was acquired, an architect was chosen, and on March 1, 1920, work was started on tearing down the old buildings.

Many problems were encountered as the building took shape. There was a period of uneasiness throughout the country, unemployment was severe and robberies and holdups were frequent. This situation made the Building Committee nervous and one meeting of the committee clearly showed their apprehension.

The matter of protection came up for discussion. One member thought it would be a good idea to have two revolving turrets above the main door containing two men, armed with sawed-off shotguns, peeping out through slits in the walls. Another favored water as the best means of dispersing a mob without bloodshed, and suggested water curtains for the doors and high-pressure hose placed at strategic spots.[1]

A third member, who had taken no part in the discussion suddenly remarked, "Mr. Chairman, I move that this matter be referred to the Secretary of War." It sounds amusing now but the situation was serious then.

ROSY FUTURE

On March 20, 1922, the building was officially opened with a total personnel of 775. Vault accommodations were excellent. Instead of one main vault it had been decided to build the vaults three stories high and group the departments which handled cash or securities around them.

A Security Court that opened on Oliver Street provided guarded entrances and exits for armored cars carrying cash or securities.

[1] A few soldiers could have been installed in the basement.

A Members' Court, easily reached from the main entrance, was available to officers and guests of member banks who desired a meeting place.

As originally designed, this Court was supposed to have two rows of potted trees leading to a bubbling fountain in the rear. A member of the Building Committee took the view that trees would attract bugs which, in turn, would necessitate spraying. This, to complete the vicious circle, would require extra labor which would run into money. And there was also the dread possibility, he pointed out, that stray dogs might get by the guards occasionally. So trees never grew in the Members' Court.

FEDERAL RESERVE SOCIETY

The fountain bubbled nicely for many years but it also leaked. After one of the girls fell into it, in a careless moment, it was torn out and the present memorial to members of the staff who served in World War II was installed.

The Members' Court has served as a meeting place for Stockholders' meetings, Federal Reserve Society affairs, panel discussions and the like for many years. It will, of course, be superseded by the auditorium in the new building.

A cafeteria was opened on the fifth floor for the benefit of the clerks, and rest and smoking rooms were provided for both sexes.

A reference library was started with a handful of books, later to expand and to assist in the work of the Research Department which has done so much for the New England economy.

Shortly after the end of the first World War the bank club, called the Federal Reserve Society, was formed and later a monthly publication for the benefit of the employees was started.

Plays, mock trials and minstrel shows have been produced, parties held in the cafeteria and summer outings enjoyed. An annual dinner at some Boston caravansary has been paid for by the bank since 1919.

We have come a long way since November, 1914. There are clouds on the horizon once more and no one can tell what lies ahead. But come what may, there is one thing certain: This bank has served New England in the past to the best of its ability; it will continue to do so in the future.

LEWIS E. STOYLE
First employee of the Federal Reserve Bank of Boston

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HARBESON, HOUGH, LIVINGSTON & LARSON, Philadelphia
KILHAM, HOPKINS, GREELEY & BRODIE, Boston, Associated Architects

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OTIS ELEVATOR COMPANY, Boston, Massachusetts

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"I See Great Days Ahead"

In this brochure we have dealt with yesterday and today. What of tomorrow? No one knows what lies ahead, but read what Carl Sandburg says in an interview with Frederick Van Ryn quoted from *This Week:*

"I have spent as strenuous a life as any man surviving three wars and two major depressions, but never, not for a moment, did I lose faith in America's future. Time and time again, I saw the faces of her men and women torn and shaken in turmoil, chaos, and storm. In each major crisis, I have seen despair on the faces of some of the foremost strugglers, but their ideas always won.

"I see America, not in the setting sun of a black night of despair ahead of us. I see America in the crimson light of a rising sun fresh from the burning, creative hand of God. I see great days ahead, great days possible to men and women of will and vision. . . .

"May I offer my favorite toast? 'To the storms to come and the stars coming after the storm. . . .' "


SIGILLUM REIPUBLICÆ CONNECTICUTENSIS
SEAL OF THE STATE OF NEW HAMPSHIRE
1776
STATE OF RHODE ISLAND AND PROVIDENCE PLANTATIONS
1636
VERMONT
FREEDOM AND UNITY

Report on

STEPS TO MAINTAIN ECONOMIC STABILITY

REPORT

ON

STEPS TO MAINTAIN ECONOMIC STABILITY

BY THE

Committee on Economic Stabilization

of the BOARD OF DIRECTORS *of the*
FEDERAL RESERVE BANK
OF BOSTON

PREFACE

On June 9, 1952, the Board of Directors of the Federal Reserve Bank of Boston appointed a committee of its members to study and formulate a program of economic stabilization for submission to the Board. The committee members were Harvey P. Hood, Class B Director (Chairman), Karl T. Compton, Class C Director, and Earle W. Stamm, Class A Director.

The committee's report was adopted and approved by the Board of Directors on December 22 and released for distribution to member banks in the First Federal Reserve District and others having an interest in the subject. The views expressed in the report are not necessarily those of the Federal Reserve System or of those persons listed below.

The committee was assisted in preparing the report by Dr. Alfred C. Neal, First Vice-President, and members of the research staff at the bank. Acknowledgment is made of helpful suggestions from the following persons who replied to the committee's request for comment upon an early draft: O. Kelley Anderson, President, New England Mutual Life Insurance Company; Robert B. Bangs, Special Assistant, Office of the Secretary, United States Department of Commerce; Bernard M. Baruch; Albert Bradley, Executive Vice-President, General Motors Corporation; Paul F. Clark, President, John Hancock Mutual Life Insurance Company; Grover W. Ensley, Staff Director, Joint Committee on the Economic Report; Ralph E. Flanders, Senator from Vermont; William A. Irwin, Economist, The American Bankers Association; O. B. Jesness, Chief of Division of Agricultural Economics, University of Minnesota; Arthur Kemp, Assistant to Herbert Hoover; Henry C. Murphy, International Monetary Fund; Howard B. Myers, Committee for Economic Development; Edwin G. Nourse; Ralph Robey, Vice-President and Chief Economist, National Association of Manufacturers; Harold V. Roelse, Vice-President, Federal Reserve Bank of New York; Beardsley Ruml; Emerson

P. Schmidt, Director of Economic Research Department, Chamber of Commerce of the United States; Sumner H. Slichter, Lamont University Professor, Harvard University; Walter E. Spahr, Executive Vice-President, Economists' National Committee on Monetary Policy; George Terborgh, Research Director, Machinery and Allied Products Institute; Donald B. Woodward, Vice-President for Research, The Mutual Life Insurance Company of New York; and Ralph A. Young, Director of the Division of Research and Statistics, Board of Governors of the Federal Reserve System.

In releasing this report, the committee and the Board of Directors of the Federal Reserve Bank of Boston do not represent that it contains anything particularly original or revolutionary. The report is intended as a consistent composite of many points of view which is intended to secure a maximum of agreement from those who have studied the problem.

It is this Board's belief that to make a program of economic stabilization effective requires concerted effort by practically everyone, including governmental agencies. It is its belief that although self-interest is a dominant motive in human behavior, economic stability is sufficiently in the long-range interest of all that a program to maintain economic stability should secure wide support. It is its further belief that at least a part of the recent inflation could have been prevented by more prompt and vigorous action along the lines suggested in this report without materially affecting production or employment. Such action might have been taken earlier had there been a clearer understanding of the problems involved and of the action appropriate for dealing with them.

It should be noted finally that the report is written in the light of existing monetary policy. Policy in this field is in an evolutionary state and is subject to new developments which may modify some of the statements made here.

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JOSEPH A. ERICKSON
President, FEDERAL RESERVE BANK OF BOSTON,
Boston, Massachusetts

Boston, Massachusetts
January, 1953

INTRODUCTION

THE AMERICAN ECONOMY has been subject to recurring periods of unhealthy boom accompanied often by inflationary price increases and followed by periods of depression and widespread unemployment. These conditions — whether of feverish boom or paralyzing depression — because of their demoralizing effect on many individuals give rise to attacks upon our system of private competitive enterprise, attacks which often lead to the development of programs of expediency rather than programs which produce long-term solutions. We believe that the overwhelming majority of Americans abhor the devaluation of their dollars as they do the loss of work or wages and would therefore welcome any effort directed toward maintaining greater economic stability.

Economic stability at progressively rising levels of employment and production has become a matter of more than domestic concern. Greater stability will strengthen our own capacity for defense and that of our allies. Friendly nations abroad, united with us in resisting Russian Communism, depend heavily for their own economic strength and stability upon the American economy.

We are now and will be in the future seriously affected by the results of two major world wars and the limited fighting war within a world-wide "cold war" in which we are engaged. Principles drawn from previous peacetime conditions cannot be applied easily to the conditions which may prevail in the next few years. If, however, the next few years are to be characterized by international tension and high defense expenditures, it is all the more important that stabilizing measures consistent with a free economy be better understood and more effectively applied. Should war become more widespread, stronger measures might well be required, and some principles now appropriate could not then be used.

The only possibility of all groups joining unanimously in support of a program for greater stability is a statesmanlike approach to the problem with recognition that the long-time gain for all is more to be desired than the immediate short-time profit for any particular group. To insure precedence of long-time over short-time interest, it is important that the objective should be agreed upon in advance, and that the causes and effects should be understood as clearly as economic variables will allow, so that the Federal Reserve System and others will be encouraged at all times, courageously and without delay, to take those steps which they believe will be most helpful toward maintaining that stability which is in the best interest of the nation as a whole. Agreement on a common objective should permit minor differences to be submerged in a joint endeavor.

In considering measures for maintaining stability, we have been guided first of all by the principle that we wish to preserve the maximum degree of freedom in the economy. We have therefore concentrated upon general measures which affect the whole economy, or at least a major part of it, rather than measures which involve displacing private decisions and bargains by decisions of public officials. By this test, we do not favor imposing direct controls, such as price and wage controls, except in war emergencies which are not considered in this discussion.

Similarly, we have emphasized those measures which are likely to be most effective and which at the same time are not subject to such diverse views that they would not be generally accepted. By this test, the immediate return to free convertibility of all money into gold coin is not discussed, even though eventually such a standard might well be appropriate to a period of lasting economic stability.

Because we believe that a free economy is the most efficient for raising production and the standard of living, we have made no attempt to specify a "fair" level of profits, salaries, or other compensation. The rewards of enterprise, work, or investment should, in a free economy, be determined by economic forces as free as possible from government control.

Report on

STEPS TO MAINTAIN ECONOMIC STABILITY

What is Economic Stability?

WHEN ECONOMIC STABILITY is set up as a desirable goal, economists and the public usually have in mind a state of affairs characterized by a high and rising level of production and a minimum amount of unemployment, coexisting with a reasonably stable average level of prices. These conditions are explained below.

A *high and rising level of production* provides the basis for a high and rising standard of living. The stability which we desire, therefore, does not involve a fixed level of production. Our objective requires a growing national output and increased production per person. Increasing total output must accompany a growing population, and increasing production per person will permit rising consumption per person — a higher standard of living.

A *minimum amount of unemployment* admits that some unemployment must exist even when the economy is stable because people are between jobs or laid off because production is unevenly distributed through the year or interrupted by temporary shutdowns for various causes. A person is considered to be unemployed when he is ready, able, and willing to work but cannot find a job. Because unemployment is not easily measured and its severity depends upon how long it has persisted, upon adequacy of unemployment compensation and relief, and upon other considerations as well, it is not possible to specify in advance precisely at what point unemployment exceeds a practicable minimum. Any substantial increase in unemployment would be cause for concern.

A *reasonably stable level of prices* means that the purchasing power of the dollar is maintained. Stable purchasing power preserves both the letter and spirit of long-term contracts, maintains normal incentives to save and invest and so to improve productive capacity, removes much of the pressure exerted by special interest groups, and avoids distortions of business planning which accentuate booms and depressions.

The level of prices which we seek to stabilize must be a realistic one. It would not serve the interests of stability to try to return to a prewar price level, because a major deflation of a price level is accompanied almost invariably by declining production, rising unemployment, and inequities comparable to those caused by inflation. Therefore it is probably desirable to try to maintain a level of prices close to that which has prevailed in the recent past.

Stability as defined does not mean that individual prices would not be free to move. For example, increased and more efficient production of a specific commodity may make possible a reduction in its price. Higher cost or temporary scarcity may result in higher prices of other commodities. Because many prices have been distorted by the Korean war, some readjustment of present price relationships is likely and desirable. Only a pronounced and persistent general drift of prices upward or downward over a period of six months to a year would indicate a departure from price stability.

Stability does not mean a fixed level of either money incomes or what they will buy, but is consistent with a rising level of both. For example, so long as money wages do not rise faster than increases in output per man-hour of work, higher money wages do not raise costs or prices. Historically, we have had great gains in productivity and in wages, often with lower prices.

It is possible for the worker, farmer, owner, and consumer all to profit as a result of increased production per man-hour of work, whether made possible by more efficient machinery, a better use of time, or some other means. And of course this has been the historical evolution. It is not our purpose to get into the question of how gains from increased productivity should be divided, nor do we believe that ordinarily the government should resolve the debate by the use of its power or influence.

However, to the extent that any group gains more than it has produced, the extra gains must come from somewhere else. As other groups resist an inroad into what they have considered their share of gain, or perhaps simultaneously seek a greater share for themselves, the result is likely to be pressure toward higher prices as a line of least resistance. A rising level of prices results in a levy being made upon those who have invested in government or other bonds, pensions, life insurance, and similar savings programs, and upon those whose salaries are relatively inflexible.

If either workers, farmers, or owners endeavor to gain more than advances in productivity warrant, and provided they have the power to gain their demands, the end result is likely to be inflation unless the majority of public opinion insists otherwise. In other words, little can be done about inflation unless public opinion wants something done about it.

Some economists take the position that the best way for *all* to share in the fruits of increased productivity is to lower the costs of enough commodities and services so as to bring about a slightly lower average price level from year to year. With the inflationary forces that exist at present and may be in prospect, we believe, however, that we will do well to maintain a reasonably stable price level over the years ahead.

Stability of the average level of prices is fundamentally the result of the over-all relationship between the total supply of money and the available supply of goods, together with the average rate at which the supply of money is spent. Simply stated, too much money chasing too few goods means inflation, usually resulting in higher prices. Too many goods chasing too little money means deflation, usually resulting in lower prices.

The price level is affected by many things which disturb the money-goods relationship. For example, a government deficit financed by additions to the money supply adds to the money side of the relationship; if nothing else happens, it has an inflationary effect. An increase in wages not accompanied by a corresponding increase in output also adds to the money side of the relationship but not proportionately to the goods side; its effect is inflationary. Dumping goods from inventory adds to the goods side of the relationship; taken alone, the effect is deflationary. Reducing the pay for the same amount of work reduces the money side of the relationship without affecting the goods side; the effect is deflationary.

Can we have rising production and minimum unemployment with a stable price level and increased consumption per person? Such stability has prevailed in this country for limited periods in the past, and to us there are no convincing reasons why a goal encompassing these conditions should not be a sound goal that we should hope to attain. The nation has never followed consistent policies directed toward these objectives, and until it has tried such policies it would be premature to conclude that greater stability than we have had in the past is impossible.

What is Economic Instability?

INSTABILITY has characterized our economy for a much longer period than stability. Instability occurs in one form when prices, production, profits, and employment all move down persistently for a period of time. Such movements are called deflations or depressions. By our standards, anti-deflationary action may be required when production lags to such an extent that unemployment exceeds a reasonable minimum for a significant period *and* prices generally move downward or remain at reduced levels.

The task of preventing or offsetting a recession or deflation will be easier to the extent that the previous boom has avoided excesses. Timely and courageous use of the steps called for in an inflationary period will weaken the causes of recession and render less difficult the task of offsetting it. The best remedy for recession or deflation is to avoid the inflationary conditions which precede it.

Our objective, if deflation sets in, should be to work toward the previously stable level of prices and to raise production and employment to and beyond the level prevailing under previously stable conditions.

Instability also occurs when prices move up at a time when production and employment are at very high levels. Our objective, then, should be to work toward the price level that prevailed under previous conditions of stability without materially affecting the level of production and employment. At such times, we should be as quick to fear inflation as at other times we are quick to fear deflation. It is far less harsh on the community to prevent inflation than it is to endure a subsequent depression.

Steps which Might Be Taken to Preserve or Restore Stability

SYSTEMATIC ACTION to preserve economic stability must come primarily from the monetary and financial activities of government, but the citizens and private organizations of the nation can help provide economic leadership, and they can contribute to the goal through their own financial and other economic decisions.

Because economic forces do not move in fixed patterns or combinations, it is impossible to prescribe in advance precise rules as to when or how much action should be taken to correct what might be an inflationary or deflationary situation. A general method which has been followed in the past and which appears still to be appropriate involves a continuous review of economic developments with special study of those forces which are most influential at the time. On the basis of these studies, forecasts are made at frequent intervals. If the forecast is definite and subsequent events immediately begin to confirm it, action is taken. If the forecast is somewhat uncertain and subsequent events do not give a clear indication of what may happen to the level of the economy, action should be withheld until events clarify the situation. The strength of any action that should be taken depends upon its timing, the definiteness of the forecast, the size of the job to be done, and the reaction to any steps taken previously.

So far as Federal Reserve action is concerned, an attempt to obtain agreement with other agencies of government on proposed Federal Reserve actions may delay and inhibit action. Consultation and exchange of information should be continuous, but the Federal Reserve must take sole responsibility for those actions which are within its jurisdiction. Therefore, the Federal Reserve must be so well equipped, both in terms of its economic intelligence work and in terms of men of judgment and courage in policy-making positions, that it is competent to act independently in those matters which are under its control. Only in this way can it assert the leadership expected of it in its inception and required by contemporary conditions. A record of courageous and correct leadership should be persuasive to other agencies of the government and should progressively command wide public support and approval, despite temporary objection from those who may feel injured by any particular action.

The following sections indicate steps which would be appropriate if unstabilizing forces are imminent or are apparent. The steps are grouped into those appropriate to inflation and those appropriate to deflation or recession.

Some or all of these steps would be appropriate to particular inflationary or deflationary situations. The number used and the vigor with which they are used must depend upon the degree of certainty as to the outlook and the strength of the forces to be combatted. For convenience, those steps which are subject to the authority of the Federal Reserve and those which are not are indicated. Order does not indicate relative importance or desirable sequence of use.

Monetary and Credit Control Policies
— *Inflation*

Inflation cannot occur unless there is an increase in money or money turnover in relationship to goods. The principal part of the money supply is bank deposits. Member banks of the Federal Reserve System, which together have about 85 per cent of all bank deposits in the country, must keep about one dollar of reserves with the Federal Reserve Bank for every five dollars of their deposits. Control over increases in the supply of money, therefore, depends largely upon controlling member bank reserves, which in turn influences the expansion or contraction of bank credit.

When the Federal Reserve System buys government securities on the open market it allows an increase in total bank deposits equivalent approximately to five dollars for every dollar it spends. This is because banks can create deposits, through loans and investments, of about five dollars for every new dollar they add to their reserves with the Federal Reserve System, and the purchase of securities by the System introduces new dollars which the banks can use for this purpose. The Federal Reserve System, other things being equal, can affect the money supply in a similar way by lowering the reserve requirements which member banks must keep on deposit with the System.

Effective control of credit (and the money supply) in an inflationary situation depends upon a coordinated policy with respect to required reserves, discount rates, and open market operations which affects the supply, availability, and cost of credit, and which also can impose restraint upon the banks because of uncertainty as to what Federal Reserve policy will be.

In addition to reserve requirement, discount and open market policy, the Federal Reserve at times may impose selective controls which prescribe terms and conditions on which credit of certain types may be extended, e.g., real estate and consumer credit and credit for purchasing or carrying securities. (Consumer credit control is not presently authorized by Congress.) These selective controls influence the use of credit and supplement the general control exercised by discount and open market policy.

The following are the steps available to the Federal Reserve System for combatting inflation.

(Within Federal Reserve Authority)

a. *Increase the discount rate.*

The discount rate is the rate of interest a bank must pay when it obtains reserves by borrowing from its Federal Reserve Bank. An increase in the discount rate would indicate that monetary and credit policy is being directed toward restraint.

An increase in the discount rate usually exerts a significant influence on credit psychology, inducing the banking system to reexamine its lending policies and other lenders to reappraise credit conditions. This result occurs whether or not the volume of member bank borrowing from the Reserve Banks is substantial and whether or not the increase in the rate indirectly raises the costs of customer borrowing, as it is likely to do for the more sensitive part of the market.

b. *Adopt a restrictive open market policy.*

The availability of credit to borrowers is likely to be reduced when customer borrowing demand exceeds the volume of lending permitted by the existing volume of reserves. Under these conditions, unless the banking system can obtain additional reserves by making net sales of government securities through the open market to the Federal Reserve or by borrowing from the Federal Reserve, it cannot maintain or increase the volume of its loans and investments or deposits. If the ratio of required reserves to deposits is one to five, the banks must reduce deposits (and therefore loans or investments) five dollars in order to get one dollar of reserves.

The extent to which the Federal Reserve is prepared to make purchases or sales of government securities in the open market or to lend will thus determine the extent to which the banking system will need to borrow to obtain reserves. The Federal Reserve can follow a range of open market action running from restraint to outright restriction.

Net sales of government securities by the Federal Reserve reduce member bank reserves because the Federal Reserve must be paid in reserve funds. Reduction in their reserves causes banks to restrict their lending and investing. Such restriction causes interest rates on various types of securities and on loans to go up, and moves up rates in the market in relation to the discount rate, and may prepare the way for an increase in the discount rate. Small fluctuations in the market rates create uncertainty which, by inducing caution, further serves to restrain credit.

Open market operations are undertaken at the initiative of the Federal Reserve and are broad and impersonal in their effects. On the other hand, member banks take the initiative in borrowing from the Federal Reserve and the amount of credit released is determined by the need of the particular bank; the effect thus tends to be regional. Borrowing is subject to repayment and since banks are disinclined to go into debt and since the Federal Reserve discourages them from staying in debt, these funds tend to be repaid as soon as other funds become available.

Open market operations enable the Reserve Banks to maintain continuous contact with the money market and the existing credit situation. By coupling open market operations with the rediscount mechanism, the System is able to graduate the degree of intensity of its restrictive policy.

A coordinated discount and open market policy operating in the interests of stability would be directed toward providing the banking system with a volume of reserves adequate to permit it to finance a high and rising volume of production and employment without putting upward pressure on the price level.

c. *Impose or tighten selective controls on stock market credit, consumer credit, and real estate credit to the extent permitted by law.*

Selective controls do not have a direct effect on the amount of bank reserves. These controls provide specific terms under which credit may be used for certain purposes and thus they influence the demand for credit. They reinforce the action specified in a and b.

d. *Increase required reserves, thereby reducing the reserve base for credit expansion.*

An increase in required reserves raises the amount of reserves which member banks must keep per dollar of deposits. Raising required reserves causes banks either to acquire more reserves or to reduce deposits by curtailing lending and investing activities.

Changes in required reserve ratios are not generally suited to the continuous need of credit policy and increases should be limited to those circumstances where it is necessary to adjust the total reserve requirements of the banking system in order to prevent a significant credit expansion, control of which for one reason or another is beyond the influence of other instruments.

An increase in reserves is a broad and blunt device because it affects banks with and without excess reserves. An increase in required reserves is particularly appropriate when it is necessary to absorb excess reserves which are well distributed among the banks throughout the country.

The existence of authority on the part of the Reserve System to increase reserves may, even if that power is used infrequently, induce banks to be more cautious and thus reinforce a restrictive credit policy. Required reserves are presently at the maximum limits permitted under present law, except in New York and Chicago (central reserve city) banks.

e. *Discourage banks from making speculative loans or other loans which do not contribute to the maintenance of sound credit conditions.*

In an inflationary period, the Federal Reserve Banks should take special steps to discourage the extension by member banks of an undue amount of credit for speculative purposes in securities, real estate, or commodities, or the extension by member banks of other credit which would be inconsistent with the maintenance of sound credit conditions. If these steps fail, access to the credit facilities of the Federal Reserve Banks in specific instances, or generally, may be denied to the member banks concerned.

(Outside Federal Reserve Authority)

f. *Suspend or tighten government loan and loan-guarantee programs.*

Government loan and loan-guarantee programs have been appropriate and effective as anti-depression, relief, or veterans' benefit measures. There is danger that they will be continued unchanged through inflationary periods.

Government encouragement to lending and borrowing, as in the case of the FHA and GI housing loans, GI business loans, Farm Credit and RFC loans, even though it may not involve direct use of bank credit, nevertheless stimulates economic activity which results in credit expansion by banks and establishes credit terms which encourage banks to expand their own loans. Therefore, government loan and loan-guarantee activities stimulate bank credit expansion in inflationary periods and should be reviewed in terms of general credit policies.

Monetary and Credit Control Policies — *Deflation or Recession*

It is generally accepted that monetary and credit policies can be more effective in checking a boom than in checking a recession.

However, if the excesses of the boom have been avoided, the task of checking a recession will be easier.

The essential task of monetary and credit policies in a recession is to provide abundant monetary and credit resources for expansion. There is not much that the Federal Reserve System itself can do to utilize the resources that it makes available. Recovery from a recession depends, therefore, more importantly upon other measures than upon actions by the Federal Reserve System, but the Federal Reserve System and the banking system should do everything they can to foster the forces of revival.

(Within Federal Reserve Authority)

a. *Adopt an expansive open market policy.*

The Federal Reserve should add to its holdings by purchasing securities in the open market, thereby providing reserves to the banking system. It should exchange or replace maturing securities so as to avoid the deflationary effect resulting from the retirement of government debt held by the Federal Reserve System.

b. *Reduce discount rate.*

Although banks are not likely to borrow heavily from the Federal Reserve in a recession, a lower discount rate signalizes credit ease and encourages any borrowing that may be necessary.

c. *Reduce required reserves.*

Lowering required reserves provides the banking system with unemployed funds, which banks usually seek to put to work.

d. *Relax or eliminate selective controls on consumer credit, real estate credit, and stock market credit.*

e. *Encourage banks to give more consideration to loans which might be made with the assistance of Section 13b of the Federal Reserve Act.*

Section 13b loans to private business for working capital purposes can be made by the Reserve Banks, participated in by the Reserve Banks, or guaranteed by them. They are loans which would not otherwise be made by existing financial institutions.

Fiscal Policy, Government Expenditures, and Debt Management — *Inflation*

It should be recognized that monetary and credit control actions within the control of the Federal Reserve System may or may not be fully effective in checking a boom or inflation. The power of the Federal Reserve over the supply of money is not absolute. For example, although the Federal Reserve does not guarantee the rates on new issues of government securities, it nevertheless as a matter of policy cannot permit disorderly markets to develop during the issuance or refunding of marketable securities, and it may have to add to its holdings at such times unless some other means can be devised to eliminate the need for such action. Similarly, very rapid and explosive increases in the turnover of money through rapidly increased business, consumer, or government spending cannot be offset adequately by Federal Reserve action alone. For these and other reasons, not the least of which is the fact that the Federal Reserve is responsible to the Congress which determines whether the federal budget is to be balanced or to run a cash surplus or deficit, *the maintenance of stability depends upon the coordination of many actions and policies devoted to that end. The most important of these are the fiscal and debt management actions of the government itself.*

(Outside Federal Reserve Authority)

a. *Reduce government expenditures and/or increase taxes so as to produce a cash surplus in the budget.*

Possibilities of increasing tax rates further without damaging effects to the economy have been virtually exhausted in the present situation. Federal, state, and local taxes are now taking more than a third of the national income. In our judgment this is well above the proportion which is compatible with the most efficient operation of the American economy in the absence of a full-scale war. In all-out war, of course, the peacetime limits to taxation can be stretched. Because the over-all burden of taxes cannot safely be increased, the major change required to produce a cash surplus must be a reduction in expenditures.

b. *Reduce government debt, particularly in the forms held by the commercial banking system and the Federal Reserve Open Market Account.*

In a boom or inflationary period the government should achieve a substantial net cash surplus from taxes. The net cash surplus provides one of the most effective instruments for reducing inflationary pressures.

> The effect on the supply of money of using a net cash surplus from taxes to retire federal debt is a combination of the following three possibilities, which depend upon whether the public, commercial banks, or the Federal Reserve Banks hold the debt which is retired. (Usually, all three types of holders are involved.) In all three cases, the collection of the cash surplus in the form of an excess of cash receipts over expenditures reduces (a) private deposit accounts, reduces (b) member bank reserve accounts as the checks are collected by the Treasury, and eventually* increases (c) the Treasury's account at the Federal Reserve Banks.

* The funds may remain for a time in Tax and Loan Accounts of the banks, but are eventually called in to the Treasury's accounts at the Reserve Banks.

(1) When the Treasury uses a current cash surplus to pay off debt held by the public, its checks will be deposited to (a) private accounts and will increase (b) reserve accounts of the banks when the checks are collected by a charge to (c) the Treasury's account at the Reserve Banks. Therefore, *the use of a current Treasury cash surplus to retire debt held by the public restores private deposits and reserve accounts.*

(2) When the Treasury uses a current cash surplus to pay off debt held by commercial banks, the banks will collect the Treasury's checks and obtain increased reserves (b) as the Treasury's account (c) is charged. Private deposits (a), reduced by the tax collection, are not restored. Therefore, *use of a cash surplus to retire debt held by the commercial banks will reduce the money supply (bank deposits) dollar for dollar.*

(3) When the Treasury uses a current cash surplus to pay off debt held by the Reserve Banks, the Treasury's checks when collected reduce the Treasury's account (c) at the Reserve Bank. Reserves (b) and private deposits (a) which were reduced by the collection of the surplus are not restored. Therefore, reserves are reduced, and because one dollar of reserves supports about five dollars of deposits, the banking system is put under pressure to reduce its deposits by five dollars for every one dollar of debt retirement. *Retirement of Federal Reserve held debt is therefore the most anti-inflationary use of a Treasury cash surplus.*

c. *The Treasury should offer savings bonds more attractive to the public and both new and refunding issues which are more attractive to noncommercial bank investors.*

Increased saving, both personal and business, provides one of the most effective means of promoting stability in inflationary periods. If additions to savings are invested in government securities, the government obtains funds without resort to the use of additions to the money supply which are likely to result from government borrowing from the banks. When the government borrows additional saving made by the public, private spending is reduced by the amount the government borrows and spends. When the government borrows from the banks in an inflationary period, the government's spending of the funds borrowed is not likely to be accompanied by a reduction in private spending.

In a boom or inflationary period the competition of private demand for credit is likely to require higher rates on government securities. If the Treasury does not offer higher rates, its issues will not be well received in the market, and the Federal Reserve System may be asked to support them to prevent their failure. Furthermore, in an effort to attract the funds of noncommercial bank investors from uses that will add to inflation, the Treasury should offer intermediate and long-term issues at rates which are attractive to such investors. In particular, the Treasury should offer savings bonds on such terms that the public will buy and hold increasing amounts.

If in an inflationary period the Treasury persists in offering only short-term issues or issues not attractive in rate, noncommercial bank investors may not buy the securities in a volume which would permit the Federal Reserve to stay out of the market. It is therefore essential in a boom or inflationary period that the Treasury's issues be attractive to the noncommercial bank market. This will mean offering competitive rates and making a vigorous effort to place intermediate and long-term securities with investors for whom such securities are suitable.

d. *Tax policy should be directed toward restricting demand without restricting production.*

Excise taxes (e.g., taxes on tobacco, automobiles, jewelry, etc.) remove buying power from the consumer goods' markets without discouraging the expansion of productive capacity generally as do taxes on business or personal income. During an inflationary period, productive capacity is likely to be inadequate to meet consumer demand. Therefore taxes which reduce consumer demand without generally discouraging expansion of productive capacity provide a means of restricting demand to the available supply.

The replacement of obsolete or high cost plant and equipment constitutes a major source of economic progress and can be a means of promoting stability. Such replacement can be stimulated by making it easier to recover capital invested in plant and equipment through depreciation allowed for federal tax purposes. Liberalization of these allowances can be made an instrument for influencing both the volume and timing of capital expenditures on plant and equipment, and is a subject which should be studied by the Congress.

e. *Government expenditures which can be postponed — particularly public works — should be laid on the shelf.*

Government expenditures for public works compete for men and materials with expenditures for expanding productive capacity. Deferment of government public works expenditures would permit the expansion of productive capacity without undue strain and if undertaken in a later period of slack business activity would serve to support the level of economic activity.

f. *Scheduled increases in tax rates to support the existing social security and unemployment compensation programs should be made at this time.*

Taxes for old age and unemployment insurance serve to reduce current consumption in the interest of paying adequate retirement and unemployment benefits. Adequate tax payments during inflationary periods help to preserve stable employment by withholding purchasing power from the market at such times.

FISCAL POLICY, GOVERNMENT EXPENDITURES, AND DEBT MANAGEMENT — *Deflation or Recession*

(Outside Federal Reserve Authority)

a. *Reduce taxes which most discourage investment and consumption.*

It would be appropriate to reduce the corporate income tax, to allow accelerated depreciation on new investment in plant and equipment, and to reduce excise taxes which discourage consumption.

If the Federal budget runs a deficit by pursuing the policies outlined in this report, it would be theoretically logical to finance a fairly substantial proportion by temporary borrowing from the banking system. However, the proportion so financed should depend in part upon the intensity and probable duration of the recession or deflation and in part upon the success which had been obtained in selling government securities outside the banking system in a previous period of inflationary tendencies (i.e., on how inflated the money supply was at the time).

b. *Encourage the Treasury to issue securities for refunding or for new money, if necessary, which are attractive to commercial bank buyers.*

To make new securities attractive to commercial banks may mean increasing the proportion of short or intermediate term securities. Commercial bank purchases of government securities in a period of recession put otherwise idle credit facilities to work and serve to maintain the volume of bank investments and so to maintain the supply of money.

c. *Inaugurate federal, state, and local public works programs which have been planned in the preceding boom and increase public works expenditures.*

d. *Make unemployment compensation payments under existing law and provide relief, if needed, when unemployment compensation is exhausted.*

Other Measures to Maintain Stability — *Inflation*

While monetary and fiscal policies provide the main tools to be used in an attempt to preserve stability, other policies of government, of business, and of consumers are also important in this connection. The appropriate direction of some of these policies is indicated below.

(Outside Federal Reserve Authority)

a. *Existing programs of support for farm prices and of lending or guaranteeing loans by federal agencies should be re-examined to determine whether they are flexibly administered in the interest of economic stability, and those elements which contribute toward inflation should be modified.*

b. *Wage increases geared to genuine improvements in output per man-hour of work are non-inflationary and might be made in a boom or inflationary period, but other types of general wage increases not compensated for by increases in output should be discouraged.*

c. *New business investment of all types should be geared to long-range growth.*

Avoidable investments such as those relating to a change in design or model should be discouraged unless they result in significant economies in labor and materials. Design and model changes and deferrable maintenance should be avoided so far as possible.

d. *Business expenditures for research and development should be maintained at a high level.*

Because research and development expenditures lower costs, bring about increased productivity, and lead to new products which can expand markets in depressed periods, they should be held at the highest sustainable rate at all times. Such expenditures should not be increased in booms and curtailed in depressions.

e. *Savings should be encouraged by all possible methods.*

One of the most important means of saving is repayment of debt. Expansion of debt should be discouraged, consumer credit and mortgage terms should be kept at restrictive levels, and outstanding debt should be paid off so far as possible. Savings bond sales and other means of saving should be pushed vigorously.

f. *Imports should be encouraged so as to increase the domestic supply of goods in relation to domestic income.*

g. *Government financed foreign investment programs should, like public works programs, be planned but not encouraged or expanded during this period except to the minimum extent required by our obligations abroad.*

h. *All citizens should make the utmost effort to encourage economy and efficiency in government at all times.*

Local and regional demands for public works, river and harbor improvements, reclamation projects, and the like should be resisted during a boom period; desirable economic projects of these types might be undertaken in a recession.

Other Measures to Maintain Stability
— *Deflation or Recession*

(Outside Federal Reserve Authority)

a. *Let competition determine prices subject to continuing programs designed to insure against disorderly markets.*

b. *Maintain social security and farm price support programs at reasonable levels.*

Both of these programs will in a recession help to maintain the purchasing power of a large number of people.

c. *Maintain established programs to guarantee mortgages, other credits, and bank deposits.*

d. *Stimulate foreign investment and exports.*

e. *Encourage private capital investment by both business and consumers.*

In addition to fixed capital expenditures justified by the long-term outlook, expenditures for research, development, and promotion of new products and for housing should be maintained and expanded if possible.

The New England Banker's Contribution to Stability

ECONOMIC STABILITY or instability of a region, state, or community depends generally upon stability or instability in the nation. Financial and other leaders in each community recognize the interdependence of local and national stability, and their actions can contribute importantly to preserving stability. They can help to lessen the impact of inflation on the local economy as well as help to preserve local employment and income when downturns in business threaten.

An informed public opinion is a first requirement for maintaining stability. Bankers who are well informed of national trends and of the kinds of action appropriate to each type of situation can in their daily contacts make a substantial contribution toward better public understanding of steps needed to preserve stability. Their understanding of fundamental economic relationships enables them to initiate or support the right actions at the right times. It is both a privilege and an obligation of member bankers to exercise intellectual leadership along these lines.

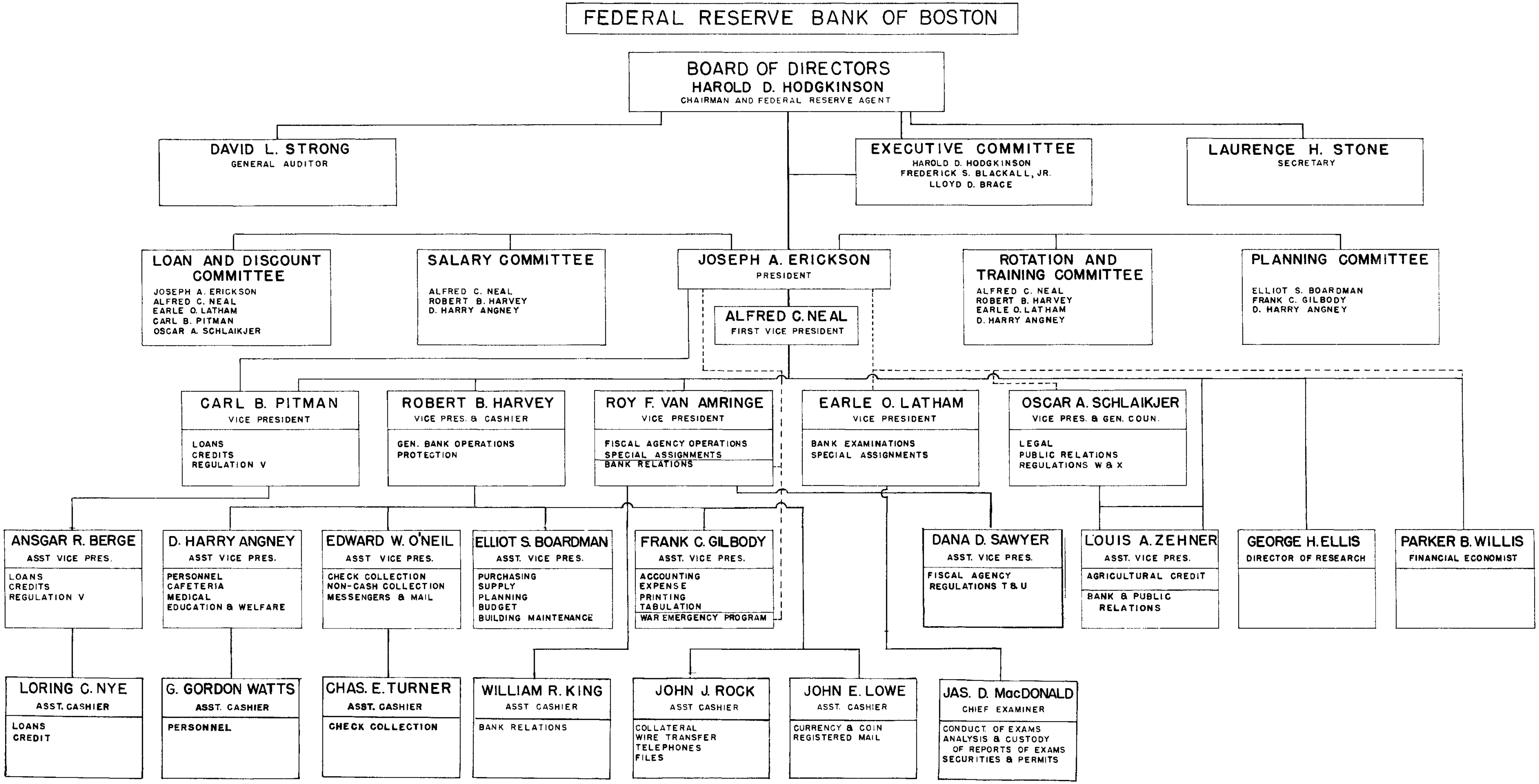
Bankers are also participants, through the operations of their own institutions, in actions which can help or hurt stability. If the national trend is inflationary and the local economy reflects this condition, bankers can help by making efforts to hold down the use of credit by their own customers to minimum needs, to discourage avoidable borrowing by local or state governments, to encourage economy in government, and to stimulate repayment of debt and the accumulation of savings, including the sale of savings bonds. The ability of bankers to follow these desirable policies depends upon their competitors following similar policies. All banks are more likely to be able to follow similar helpful policies if federal and state governments and their agencies and the Federal Reserve take those actions which are appropriate for preserving stability that have been outlined in this report.

If the national trend is deflationary, bankers in operating their own institutions can help by encouraging borrowing for sound purposes, supplementing their own facilities, if necessary, with loans from the Reserve Banks or participations in 13b loans. Their own problems, like those of the nation, will be less if they have avoided excesses in the preceding boom.

The leadership of bankers should extend to state and local government finances. Perhaps the greatest opportunity for contributions to economic stability by state and local governments is through stabilizing necessary capital expenditures by means of advance planning. Government capital outlays should be scaled down if possible when inflation threatens and increased when deflationary tendencies become strong. Similarly, state and local governments should balance their budgets and repay debt in good times so as to be able to finance capital outlay and relief programs if depression occurs.

Because economic stability requires growth to provide for an increasing population and a rising standard of living, bankers have a leading role at all times in the financing of new and growing businesses. The importance of this function is critical in communities which are likely to suffer more than others because they are tied to unstable or declining industries. It would not be in the interest of stability in a community with a large amount of unemployment to try to restrict sound loans for business expansion, even though restriction of such loans might be desirable in most other areas of the country.

Leaders in the banking community can and do influence growth and balance in the economy which they serve. They help local businesses to raise needed capital from sources outside the regular banking structure, where such action is appropriate, and they assist local firms with management advice to the full extent of their ability. They cooperate with local development groups seeking to diversify or strengthen the industrial structure of the community. And they encourage research by local firms to use more effectively the community's human and natural resources through the development of new products or processes. In performing these and other functions, bankers and other local leaders contribute to both local and national economic stability.



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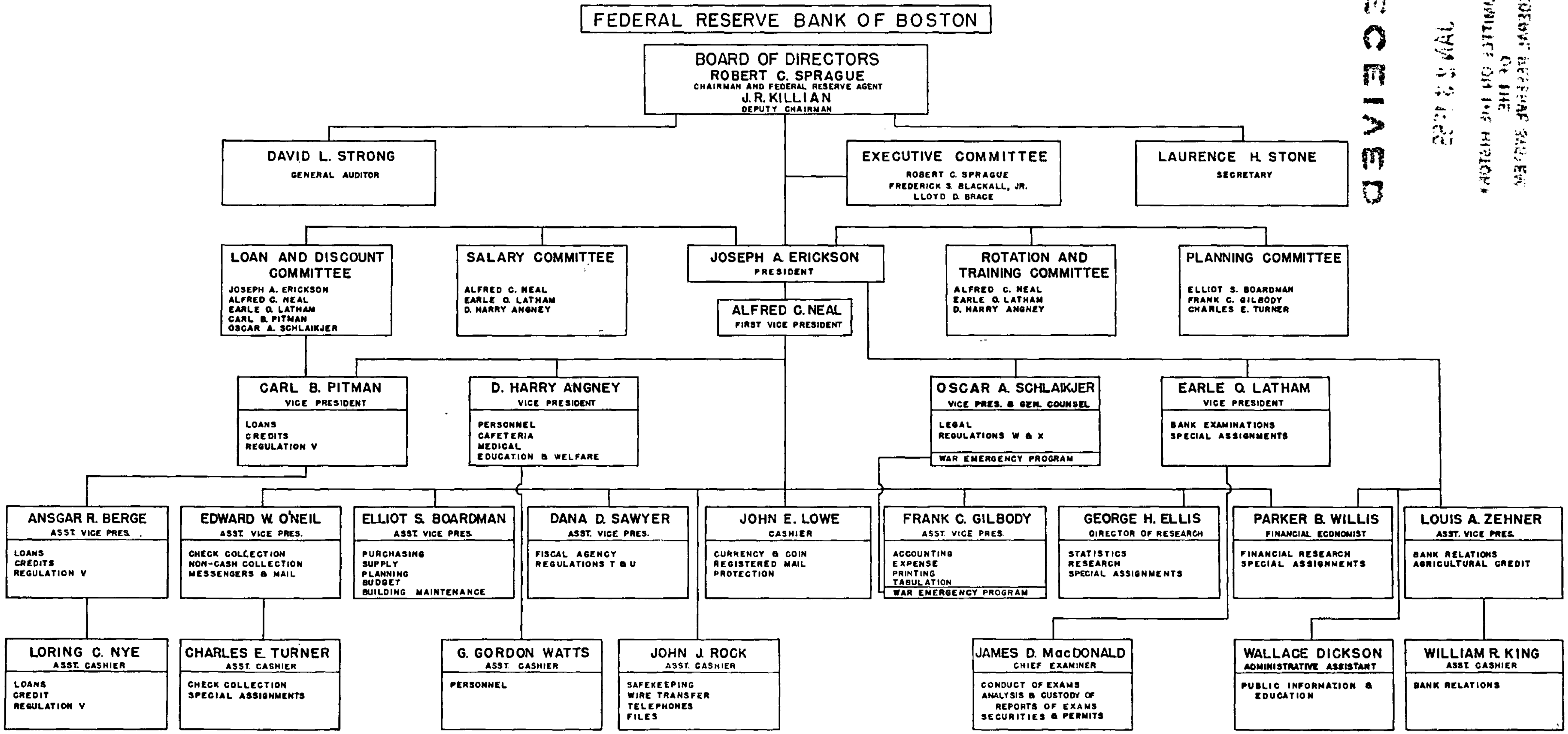

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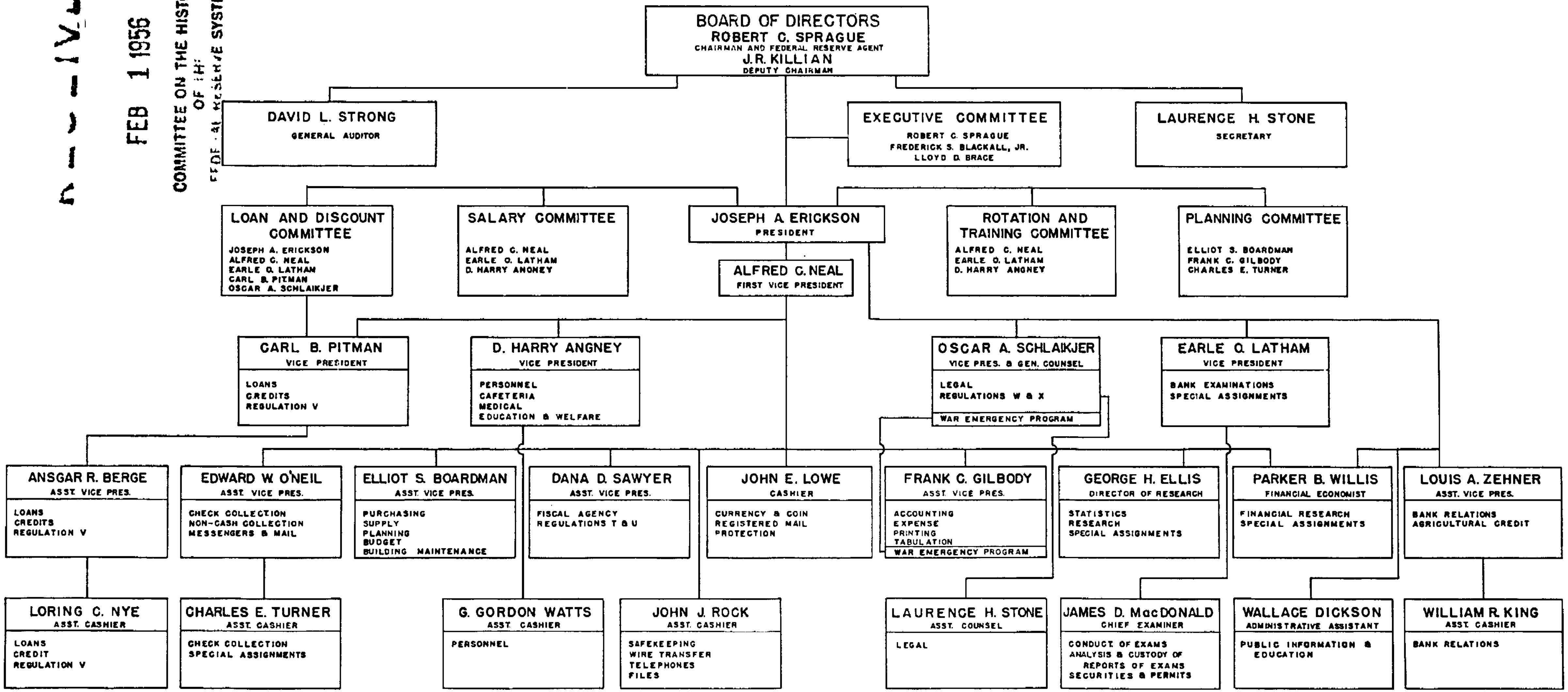

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