

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM

June 16, 1945

To: Chairman Eccles

From: Woodlief Thomas

Attached is a report of the System Research Advisory Committee dealing with the development of the System research program. The emphasis in this report, in view of the nature of the Committee, is on the System program, meaning by that those activities that have involved cooperative action on the part of the Reserve Banks and the Board's staff.

This report has also been submitted to the Presidents' Conference Committee on Research and Statistics for transmission to the Presidents' Conference.

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DEVELOPMENT OF SYSTEM RESEARCH PROGRAM

Report of the System Research Advisory Committee
June 13, 1945

Research activities of the Federal Reserve System have been considerably expanded in recent years, both at the Federal Reserve Banks and at the Board. At the same time they have been more closely coordinated and unified through cooperative action. The System Research Advisory Committee was established early in 1944 to provide closer cooperation between all the units of the System in planning and coordinating research activities. Through this Committee and other System committees and subcommittees, much has been accomplished along these lines during the past year or more. This report describes some of these accomplishments and sets forth plans that are being developed for future activities.

It should be pointed out that the greater part of the activity of each Bank research department consists of work in connection with the regular affairs of the Bank and research on problems important to the region in which the Bank is located. This report deals primarily with activities involving System-wide cooperation through which knowledge and experience gained throughout the System are brought together and focused upon national problems; it deals with the regular internal work of the Bank and Board research staffs only so far as phases of that work have been matters of System cooperation.

Principal Activities

Papers on postwar problems

Two sets of papers on postwar problems have been prepared, with the participation of a large number of the System's research people as authors and a much larger number as critics. The first of these dealt with banking and credit problems and policies for the war and postwar periods and the second set covered a variety of fields of economic activity. Some of the results of these studies were formally presented at joint sessions of the Board of Governors and the Conference of Reserve Bank Presidents. The papers are now in the process of revision and completion with the view to their publication, and this process has entailed further participation by a great many of the research people as well as by others in the System and by a number of outside advisers.

Work in process or contemplated

Other studies have been made, are in process, or are being planned, covering subjects which have a direct or indirect bearing upon the System's responsibilities. These include studies on the following subjects:

- (1) Continued study of banking and credit developments and policies.
- (2) The role of interest rates in the economy -- a subject which is basic to many of the System's activities and policies.
- (3) Business financial needs and ways of meeting them.
 - (a) Short and medium term credit needs.
 - (b) Longer term capital needs.
- (4) Capital markets and speculation.
- (5) Financial needs of agriculture.
 - (a) Study of needs and facilities for meeting them.
 - (b) Federal Reserve discount policies and practices with relation to agricultural paper.
- (6) Supplies and prices in the postwar period.
- (7) The effect of state and local fiscal operations upon the economy.

Public relations and education

The Federal Reserve System is organized and equipped to assemble and interpret information not only for its own use but also for bankers, businessmen, farmers, and the general public. The various publications of the System contribute to this end, and much along this line is likewise done through participation in local meetings and forums at which economic problems are discussed. Efforts are being made to improve the content and form of System publications in order to make them more informative and attractive. Interchange of views and experiences and discussion of new plans and methods among the System research people have contributed further to improvements in methods of presenting economic information to the public. While public relations are the responsibility of Reserve System officials generally, the research staffs are in a position to contribute much to that work by providing information and interpretation of economic developments.

Current statistical reports

The Federal Reserve System regularly collects a considerable amount of current statistical information on banking, consumer credit, stock market credit, and retail trade. These activities, which account for a large amount of the working time of each department, contribute essential information that is used in the regional and national analyses of business developments and also constitute an important item of public service rendered by the System. In the performance of this task a great many problems arise which are common to all Reserve Banks. Arrangements have been set up for frequent consideration of these mutual problems by a System committee with a broad representation.

Special problems

From time to time special questions arise which are especially suited for consideration by the System economists. These may be handled by reference to some standing committee, by special ad hoc committees, or by informal conference. For example, a committee was set up, at the request of the Investment Committee of the Retirement System, to prepare a report on the trend of interest rates. Another example is assistance given by individual research people to the House of Representatives Committee on Postwar Economic Policies and Planning. Arrangements for cooperation with the National Bureau of Economic Research, the Committee for Economic Development, and similar organizations -- public and private -- frequently involve cooperative System arrangements.

Work of Various Committees

Generally speaking, the procedure followed in carrying out System-wide projects has been that of having the initial work done by a small group of persons who specialize in the subject under consideration. This may explain the existence of what seems to be a large number of separate research committees whose activities are briefly described in the following pages of this report. The membership of each special committee is determined by the System Research Advisory Committee or, in the case of joint committees, by the System Research Advisory Committee and the Subcommittee of the Presidents' Conference Committee on Research and Statistics. One of the senior research persons in the System is designated as chairman of the group. This working group drafts plans, which are approved by the parent committee, and then goes ahead to conduct the basic research work and draft a preliminary report. The preliminary report is submitted to the parent committee for consideration and, whenever time permits, it is then presented to the heads of research at all Banks and to other Bank officials in order to obtain their comments and suggestions prior to drafting a final report. The final report is then presented to the Board of Governors and the Presidents' Conference.

This procedure, by which it has been possible to bring forth concerted System action in meeting problems falling within the System's responsibilities, has several other advantages as well. It enables the initial work to be done by a small working group but at the same time provides for review by System officials prior to the issuance of a final report. It also has the marked advantage of providing for the division of labor throughout the System, thereby relieving the heads of research of much spade work which would otherwise have to be done by them. Furthermore, it brings together people in the System having similar interests in particular fields of economic activity, thereby making for better day-to-day working arrangements and for a better common understanding of the problems encountered in various regions and the relationship of these regional problems to one another and to the national problems of which they are a part.

More detailed reports of the activities of the various committees concerned with separate phases of the System research program follow. A list of these committees, together with their membership, is given at the end of this report.

Committee on Banking and Credit Policy

At the suggestion of the Conference of Reserve Bank Presidents, a committee, with Mr. Sienkiewicz as chairman, was organized in 1943 to make a special study of postwar banking and credit problems that might face the System. This study was in process for over a year and the results, given in a number of papers, were presented to the Board and the Presidents last December. It is contemplated that some of these papers, partly revised, and a new paper, representing a synthesis of the others, will be published as a part of the series of postwar studies.

The Committee is being continued as a subcommittee of both the System Research Advisory Committee and the Subcommittee of the Presidents' Conference Committee on Research and Statistics to promote and coordinate research studies in the field of banking and credit.

At its last meeting, the Committee undertook to outline a program which would enable it to keep in close touch with developing situations in order to be prepared to make recommendations helpful in the formulation of System policy. In carrying out this objective, the Committee recommends that research staffs watch and anticipate significant developments in the following broad fields directly related to System responsibility:

- (1) Production, trade, employment, and commodity prices.
- (2) Banking developments and attitudes.
- (3) Capital markets.
- (4) Government security market.
- (5) Fiscal policy and its implications.

Means of keeping abreast of developments in these areas include the following:

- (1) Special studies.
- (2) Current statistics.
- (3) Interviews.
- (4) Surveys.
- (5) Coordination and analysis of results.

With more particular reference to the immediate situation, the following specific problems are recommended for study by the System research organization:

- (1) Implications of low interest rate structure for monetary, fiscal, and price policies.
- (2) Developments in the capital markets and speculation in those markets.
- (3) Local developments particularly with respect to cut-backs, war savings bond redemptions, demand and time deposits, and bank loan and investment policies.
- (4) Prices, controlled and uncontrolled, the effectiveness of controls, and the spread of black markets.
- (5) The supply situation--this should include production as well as inventories.
- (6) Local investment and expenditure plans.

While some of these topics fall within the scope of other existing committees, some may be handled by the Committee on Banking and Credit Policy. Among the studies of this latter type are those concerned with treasury finance, the significance of changing character of bank assets, bank earnings and their distribution, and the adequacy of bank facilities and services in the period ahead.

Steps are being taken to define the various aspects of these problems. Howard Ellis has been asked to review the possibility of conducting a study on the role of interest rates in the economy, and others have been designated to explore other phases of banking and credit problems.

The Committee also recommends that the Reserve Banks continue their analysis of assets and liabilities of individual banks and important groups of banks. It also proposes that periodical analysis be made of banking attitudes gained from interviews and other discussions with representative officials of banks and financial institutions generally.

In making the foregoing proposals, the Committee is mindful of their importance in the formulation of Federal Reserve Policy.

Committee on Business Finance

Early in the war Federal Reserve officials began to give attention to the question of business financial needs in the reconversion and postwar period. A committee of operating officials was appointed by the Presidents' Conference in 1943 to study the problem. The Conference decided that the problem was primarily one for further research and a research committee was appointed. The Committee on Business Finance, which was established with Mr. Upgren as chairman, is a subcommittee both of the System Research Advisory Committee and of the Subcommittee of the Presidents' Conference Committee on Research and Statistics.

Studies undertaken. - The Committee has promoted research projects along three lines of inquiry:

- (1) Measurement of overall changes in the financial structure of business during the war with particular reference to their bearing on probable reconversion and postwar needs. Two sources of information have been utilized in making these studies:
 - (a) Published financial statements of large corporations, and
 - (b) Financial statements of small and medium-sized businesses supplied by members of the Robert Morris Associates.
- (2) Studies of the needs of individual businesses, especially of problem cases. Such studies have been made by some of the Federal Reserve Banks for businesses in their regions and also by the Board's Research Division through analysis of borrowers under Regulation V and Section 13b.
- (3) Proposals of methods and standards for taking care of businesses that might have difficulty in arranging financing. Work along this line is focused upon the development of supporting evidence for the Wagner-Spence bill, with some studies of other proposals.

Presentation of results. - Some of the results of the Committee's work have been made available in Bulletin articles prepared by Mr. Dirks. These have given the results of overall surveys of wartime business finance with some indications of future needs. Several of the Reserve Banks have also published results of their surveys and studies in their Monthly Reviews. These include reports on manufacturers' postwar plans and financial problems, published in the Monthly Reviews of the Federal Reserve Banks of Philadelphia, Dallas, and San Francisco. Analyses of Regulation V and Section 13b loans by the Board's staff and by some of the Reserve Banks have been made available through internal memoranda.

Mr. Hopkins, who was added to the Board's Research staff to study proposals for providing adequate financing for small business, has written a number of memoranda for internal use and has also visited a number of Reserve Banks in the study of special cases. He and Miss Burr have been working with Governor Draper and the Division of Bank Operations on these problems. Mr. Hopkins assisted in preparing statements presented by Governor Draper before the House Special Committee on Post-War Economic Policy and Planning and by Chairman Eccles before the House Committee on Small Business. These statements include comprehensive reviews of the problem with suggestions for action.

Conclusions from studies and plans for further work. - The various studies show that business in general has accumulated a large amount of liquid assets during the war through retained profits, unused depreciation allowances, and deferrals of tax and other liabilities. In trade, considerable funds have also been provided by liquidation of inventories and of customer credit.

This information on wartime developments casts some light on prospective financing requirements for the transition and postwar period. Some of the accumulated funds will be used in reduction of the large outstanding tax liabilities, and in trade some will be needed to build up inventories and customer credit. Considerable capital expenditures for plant and equipment also will be needed.

Accumulated funds will be adequate to meet a large part of these financial needs -- in fact, many concerns may have enough to meet all their needs. The amount of outside financing needed will depend to a considerable extent upon the rapidity with which sales expand. If they should expand very rapidly, much outside credit will be required to finance the expansion.

As to facilities available for providing credit, it seems clear that banks generally are in a position to make as large a volume of loans as may be demanded. It appears also that the credit standing of most businesses will be such as to enable them to obtain any needed short-term credits from banks. There will undoubtedly be, however, a large number of marginal cases needing credit of types which banks will be reluctant to supply. It is cases of this sort which support the position for special measures such as the Wagner-Spence bill.

The studies so far have not been such as to bring out adequate information about individual cases. More detailed studies along this line will be needed if we are to be informed as to actual credit needs. A step in this direction is represented by a recent letter sent by the Board to the Reserve Banks requesting that they obtain information regarding businesses needing credit. The first replies to this letter are now being analyzed, and they are expected to indicate lines for further inquiry.

The Committee believes that inquiries of this nature to ferret out and analyze individual marginal cases should be carried on by the Reserve Banks over a period of time. Attempt should be made to find out what changes in procedures and standards may be needed to meet the requirements of such cases. This will involve a combination of efforts by the research and the operating (discount, examinations, and bank relations) departments of the Board and the Reserve Banks.

Committee on Current Business Developments

A new committee, the Committee on Current Business Developments, with Orin Burley as chairman, was appointed by the System Research Advisory Committee at its June 1945 meeting. This Committee has the responsibility for working out arrangements by which the System can keep in close touch with current and prospective changes in employment, production, inventories, retail trade, and commodity prices. Emphasis will be placed on both regional and national developments. The Federal Reserve System, because of its regional organization and its contacts with business and finance, is especially well equipped to do this sort of work. Many useful surveys of this nature were made on a cooperative System-wide basis before the war and a resumption of these will be needed when economic developments are determined less by large-scale governmental activities and become more dependent on the views and decisions of individual businessmen.

Committee on Agriculture

The Committee on Agriculture, of which Arthur Bunce is chairman, is a subcommittee of the System Research Advisory Committee. It was appointed in the spring of 1944 as a standing committee to consider and make recommendations on agricultural problems of interest to the System and has been active during the past year along several different lines.

- (1) Through frequent meetings (eight have been held since the Committee's formation) the agricultural economists of the System have been brought together and have gained a knowledge of one another's problems and an understanding of how the problems of each district fit into the overall agricultural problems of the country. Along with this, good working arrangements have been developed for the dissemination of agricultural information between the research staffs of the Board and the Banks.

- (2) The Committee is now drafting a paper on the history of Federal Reserve policy with regard to the rediscount of agricultural paper and advances to country banks. This study was prompted by reports from people visiting country banks in certain districts which seem to indicate that there has been some misunderstanding either by Federal Reserve officials about country bankers' attitudes toward discount facilities or by the bankers concerning the facilities available.

It is recognized that large-scale rediscounting of agricultural paper is unlikely in the postwar period because of the large and widespread holdings of Government securities and the strong cash position of country banks. Also, the discount facilities of the System have been greatly broadened as a result of the provisions of Section 10b. It is felt, however, that the study now under way is desirable in view of the likelihood of large shifts in deposits after the war and the possibility that the Federal Reserve Banks may receive an increasing number of inquiries from country banks with respect to discount policy on agricultural paper, particularly in the event of deflationary pressures on agricultural prices. Although the position of country banks is strikingly different from what it was at the close of World War I, the System should make every effort to forestall uninformed criticism from agricultural communities that its policies are contributing to a possible decline in agricultural values.

The study will review the powers which the System now has in these matters and may suggest changes that might be made in these powers. It may also recommend a statement that might be issued to inform the public of these powers. It is contemplated that before completion of the study the views of persons in the Federal Reserve Banks who have dealt with the rediscounting of agricultural paper will be obtained.

- (3) The Committee meets on occasion with representatives of various governmental agencies concerned with agriculture and with representatives of the American Bankers Association and similar organizations to discuss matters of mutual interest.

In addition, the Committee has spent considerable time during the past year in the preparation of papers covering various aspects of postwar agricultural problems and policies. This work has been done as a part of the System project on postwar problems and policies.

Committee on Current Reporting Series

The Committee on Current Reporting Series, of which Morgan Rice is chairman, is a subcommittee of the System Research Advisory Committee. It was appointed as a standing committee to consider and make recommendations regarding all problems which arise in connection with established series, excluding those falling within the scope of the Board's Division of Bank Operations.

During the past year the Committee has had to consider numerous problems arising in connection with statistics collected on the ownership of bank deposits; customer loan rates; department store and furniture store sales and stocks, and various consumer credit information obtained from commercial and industrial banks, small loan companies, credit unions, sales finance companies, furniture stores, jewelry stores, household appliance stores, and mail order companies. It has also been called upon to consider questions arising in connection with trading day adjustments and adjustments for seasonal variations. Some of the particular projects sponsored by this Committee have been the Retail Credit Survey, the revision of the System's indexes of department store sales and stocks, and the revision of several of the consumer credit series. The Committee has been instrumental in developing uniform methods for handling data throughout the System and in contributing to a more thorough understanding of the difficulties of collecting information and the development of methods to overcome these difficulties.

Committee on Retirement System Investment Policy

The Committee on Retirement System Investment Policy, of which Charles O. Hardy is chairman, is a subcommittee of the System Research Advisory Committee. It was appointed as a special committee to prepare a report on the prospect for interest rates as it might be related to the investment problems of the Retirement System, which was requested by Mr. C. S. Young, chairman of the Investment Committee of the Retirement System of the Federal Reserve Banks. A copy of this report which has been presented to Mr. Young is attached.

Committee on State and Local Finance

The Committee on State and Local Finance, of which George Mitchell is chairman, is a subcommittee of the System Research Advisory Committee. It was appointed as a standing committee to consider problems which might arise on state and local finance. Its principal activity during the past year has been that of preparing papers on state and local finance in the postwar period. This work has been done as a part of the System project on postwar economic problems and policies.

Committee on Publications

The Committee on Publications, of which Lloyd Raisty is chairman, is a subcommittee of the System Research Advisory Committee and the Subcommittee of the Presidents' Conference Committee on Research and Statistics. It was appointed as a special committee to make a study of Federal Reserve Bank publications and to present recommendations as to matters of general content of the publications and forms of presentation which might be followed in order to stimulate the public's interest in and use of Federal Reserve Bank publications, particularly the Monthly Reviews. This Committee has made a survey and has submitted a preliminary report of its findings but the work is still in a tentative stage and no final conclusions or recommendations of a major character have been formulated.

Committee on Bank and Public Relations

The Committee on Bank and Public Relations, of which Karl Bopp is chairman, is a subcommittee of the System Research Advisory Committee. It was appointed to make a preliminary survey of this subject and make recommendations as to the membership of a permanent committee and as to the topics that seemed to require the most immediate attention. This Committee has not yet held a meeting but will do so in the near future.

SYSTEM RESEARCH COMMITTEES

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Lloyd B. Raisty	(Atlanta)
Henry H. Edmiston	(St. Louis)
Charles O. Hardy	(Kansas City)
Oliver P. Wheeler	(San Francisco)
John O. Bergelin	(Board), Secretary

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Lloyd B. Raisty	(Atlanta), Secretary

SPECIAL COMMITTEES

The Chairman of the System Research Advisory Committee (Mr. Thomas) and the Chairman of the Subcommittee of the Presidents' Conference Committee on Research and Statistics (Mr. Roelse) are ex-officio members of all of these special committees.

Committee on Banking and Credit Policy

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Committee on Retirement System Investment Policy

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Committee on Publications

Lloyd B. Raisty	(Atlanta), Chairman
Oliver P. Wheeler	(San Francisco)
John O. Bergelin	(Board)

Committee on Bank and Public Relations

Karl R. Bopp	(Philadelphia), Chairman
E. A. Kincaid	(Richmond)
John K. Langum	(Chicago)
John O. Bergelin	(Board)

* The Chairman of this Committee is authorized to invite representatives from Banks not regularly on the Committee to attend any meeting of the Committee and persons so attending the meeting shall be considered as members of the Committee for that meeting.