Thirty-fifth Annual Report

Federal Reserve Bank of New York

For the Year Ended December 31, 1949

Second Federal Reserve District

FEDERAL RESERVE BANK OF NEW YORK

March 9, 1950

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

I am pleased to transmit herewith the thirty-fifth annual report of the Federal Reserve Bank of New York reviewing the year 1949.

ALLAN SPROUL,
President.

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Federal Reserve Bank of New York

Thirty-fifth Annual Report

THE recession which had been recurrently expected since the end of the war finally arrived in 1949, having been foreshadowed by some slackening of business in the final quarter of 1948. The buoyant strength of the American economy overcame any tendency toward cumulative depression, however, and by late summer recovery was under way. At the close of 1949 the aggregate output of goods and services (in value) was within about five per cent of the peacetime peak achieved late in 1948. The distortions introduced by the war and the postwar reconversion, although not entirely eliminated, were no longer acute. By comparison with previous periods of readjustment or depression, the recession of 1949 was extremely mild, comparing favorably in duration and intensity with the minor downturn of 1923-24.

The price reductions and the unloading of inventory which dominated the downward movement of business from October 1948 to July 1949 were essentially healthful corrections. Both followed more or less inevitably from a tapering off in the great (but necessarily transitory) rise in consumer spending and capital expansion that had been fed by wartime accumulations of liquid assets and motivated by backlogs of war-deferred demand. Total consumer spending in 1949 remained remarkably constant from quarter to quarter, and as productive capacity was finally released from most shortages and bottlenecks, there was a general return of buyers' markets and vigorous competition. The stocks that had been appropriate to a continued rapid expansion of sales became top-heavy. Seasonally adjusted inventories of wholesalers and retailers began to drop below their postwar peak in December 1948. By March of 1949 the impact of this reduction had reached most manufacturers' inventories of materials and goods in process. And by the fourth quarter of the year, when inventories were beginning to level out, five sixths of the drop in gross national product from the record fourth quarter of 1948 was traceable to the curtailment that had occurred in acquisition of business inventories.

Price corrections began somewhat earlier than the general turnaround in inventories. Farm and food prices, which had risen further above prewar levels than all others, fell back through much of 1948 and edged downward more slowly through 1949. Most other prices in producers' and wholesalers' markets turned decisively at the beginning of 1949, and reached bottom in midsummer at levels generally 5 to 15 per cent below the 1948 peak. However, the index of consumers' prices —statistically insensitive to bargain sales and reflecting the contradictory effects of rising rents, declines in apparel and housefurnishings, cross currents in food prices, and relatively stable price quotations for utilities and the miscellaneous group—declined only slightly further after the moderate reduction in the last quarter of 1948.

The return of buyers' markets and the lessening of disparities among prices appeared to exert a sustaining influence on consumer outlays and on expenditures for cost-saving capital equipment, and to have a stimulating effect on residential construction. Consumers' spending for nondurable goods, which had risen uninterruptedly for a decade, finally reached a peak late in 1948 and sales fell off moderately in 1949. But spending for durable goods, after slackening during the early part of 1949, rose steadily under the influence of price adjustments, of remaining demand backlogs (chiefly for automobiles), and of the attractions of new designs and new products. Spending on services continued to rise gradually. Thus shifts in demand, matched by adaptations in the flow of consumer goods and services, combined to produce the phenomenon of constant aggregate consumer expenditures during a period of underlying readjustment and moderately declining disposable income.

The same tapering off that occasioned the shift in inventories was also associated, of course, with a shrinkage in outlays on capital equipment identified with a quantitative expansion of capacity. Some of the fears concerning the economic outlook since the end of the war had been rooted in the expectation that private investment must eventually slow down. But these fears often did not take account of the capital outlays necessary for modernization, for extending technical innovations throughout existing plants, or for additional cost-saving equipment—in general, for the qualitative improvement of productive capacity that is characteristic of rising productivity in a vigorous economy. And it was this latter type of capital expenditure that was nourished by the disappearance of sellers' markets and the return of aggressive price competition in 1949. Although outlays of a purely expansionary character dropped off substantially, the increased amount of cost-reducing investment held the total decline from 1948 to 1949 for nonfarm producers' plant and equipment to less than 7 per cent—without adjustment for any changes in machinery and building costs.

The direct stimulating effect of price declines (and increased availabilities of materials and financing) was most marked in residential construction. By August, the wholesale prices of building materials, and over-all costs of residential construction, had fallen 8 per cent from their high point in 1948, and a large volume of new demand came into the housing market. For the last four months of 1949, contract awards indicated a rise of nearly nine tenths in the number of new units planned over the corresponding period of 1948; dollar volume rose by about three quarters. Moreover, the fourth-quarter increase in 1949 was mainly in one and two-family dwellings, privately financed, without an appreciable change in the proportion of Government mortgage guarantees. Under the pressure of autumn demand, building costs leveled out, but did not rise appreciably, and at the end of the year a volume of winter building of unprecedented proportions was under way.

These economic developments of 1949 reflected the price-responsive potential of an adaptable economy. But shifts in the composition of consumer and business spending and the resulting diversion of productive capacity away from some uses and into others did come at the expense of a slight increase in unemployment, and in business failures. Average monthly unemployment in 1948 had been about 2.1 million; at its peak for the year in July 1949, it was 4.1 million. Yet even at the latter date, the typical (median) duration of unemployment was less than six weeks. Less than one third of a million workers had been unemployed more than 26 weeks (the maximum period for which unemployment insurance applies in most industrial States). The over-all rise in unemployment was, in considerable measure, a reflection of the fact that more people were again on the move from one job to another, and that the typical period from severance to reemployment was two weeks longer than in 1948.

A somewhat similar phenomenon occurred in the business population. There were seven business failures in the first half of 1949 for every four in the comparable period of 1948; the volume of liabilities involved grew correspondingly. Discontinuances (mergers, voluntary liquidations, etc., as well as failures) rose for all business groups during the first two quarters of 1949, with the incidence particularly heavy in manufacturing. Yet new concerns continued to be formed at a high rate, throughout all business groups. The net result was a decline of less than 2 per cent in the total number of operating businesses from September 1948 to June 1949, although the absorption or merger of many small and marginal manufacturers (who had been lingering on after the war) caused a net reduction in that group of nearly 10 per cent over the same period.

Looking backward, it seems reasonably clear that the mobility of labor and enterprise during 1949 was a necessary part of the continuous change that produces economic progress. To have taken direct action, Governmental or otherwise, based on some single fixed indicator of economic conditions, might only have slowed down (or perhaps have prevented) the wholesome shifts that were taking place under the guidance of the price system. Appropriate recourse was taken, however, to the broad and impersonal influence of general ease in the availability of credit, through a series of measures that began in March and continued through the summer. The Federal Government also initiated a modest effort to shift its contracts, wherever feasible, to concerns located in regions of relatively high unemployment; but there was no hasty attempt to adapt aggregate Government purchases of goods and services to the spring downturn in business. Although all levels of government incurred net cash deficits, these were incidental to the general downturn, not planned to counteract it.

The internal resiliency demonstrated by the economy in 1949 was not uniformly interpreted, however, as reassuring evidence that a high level of activity would continue into the future. There was a widespread disposition, not limited to the proponents of large-scale economic planning, to think of the nation's gross product as necessarily divided into fixed compartments of investment and consumption, and to doubt whether the needed amount of investment could be found for sustained over-all activity at a high level. That doubt raises challenging questions for which there can be no categorical answers, but the experience of 1949 does, at least, suggest the possibility of shifts between investment and consumption, and among the components of each—shifts which cannot always be tagged and earmarked in advance, but which are set in motion by free market forces when a competitive environment is maintained.

The mild economic readjustment in the United States had amplified effects abroad. The decline of one quarter of a billion dollars in our imports of goods and services during the first half of the year, small though it appeared, meant a reduction of roughly 10 per cent in the current dollar earnings of the rest of the world; for the sterling area alone, there was a drop of nearly 20 per cent from the first to the second quarter of 1949. Our import cuts, however, resulted not only from the domestic inventory correction, but also to an indeterminate extent from growing uncertainty over the values of some foreign currencies. The effects abroad of the import cuts were magnified because the general scarcity of hard-currency reserves left no cushion against a short-run decline in dollar sales. As an offset, however, the scheduled volume of net U. S. Government aid, combining all programs, had risen about one billion dollars over 1948. And at some time before or during 1949, most of the countries embraced in the European Recovery Program passed their inflation peaks, completed the rapid growth that is possible when recovering lost (but familiar) ground, and came squarely against the more stubborn problems of expanding their output and trade in new and unexplored directions. As one step toward fundamental adjustment, beginning with the British action of September 18, more than thirty countries devalued their currencies, hoping to help bring their comparative prices and productivity into better relationship with those of the United States.

The consequences of devaluation can be only sketchily suggested by the record of the final quarter of 1949. A substantial short-run improvement in foreign exchange reserves was experienced by some countries, largely because decisive exchange rate action removed the speculative pressure that had been associated with anticipated devaluation. But the rise of many local currency prices behind the devaluation screen, together with the automatic increase in the local prices of imports from the dollar area, created an uneasy situation in which the devaluing countries experienced a renewed risk of inflation. While it appeared likely, and desirable, that American imports would be stimulated over the long run by the new currency relationships, the fourth-quarter rise of our total imports of goods and services represented an annual rate of less than ½ billion dollars. Total exports of the United States fell by only a slightly larger amount; and it was impossible to determine how much of this reduction was attributable to the price changes brought on by devaluation, as against the effects of increased import restrictions in some of the more hard-pressed countries.

A second series of measures in the international field, less dramatic than devaluation but possibly of greater eventual significance, gained momentum during the year. Through the General Agreement on Tariffs and Trade, import duties and other restrictions were relaxed on an important segment of the merchandise traded among some twenty-four countries. Moreover, members of the Organization for European Economic Cooperation agreed, with limited exceptions, to conduct at least half of the trade among themselves on open general licenses. And toward the close of the year, the OEEC was again endeavoring to construct a mechanism for multilateral clearing of payments among member countries. From such measures may come a cautious but continuous widening of the scope for relatively free trade, which should help to sort out inefficient uses of resources, to encourage larger-scale production, and generally to stimulate industrial productivity in all of the affected countries.

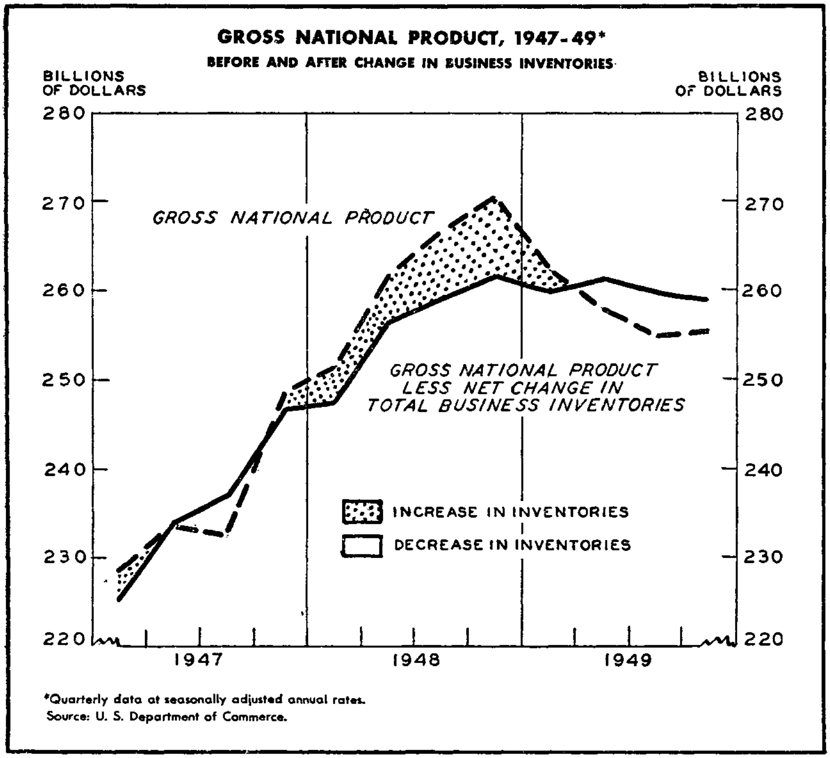
In its annual report for 1949 the Council of the OEEC forcefully pointed out that the exports of all countries need greatly increased access to the markets of the United States, and indicated that Europe is likely in any event to face a continuing (though perhaps "manageable") dollar deficit after the Marshall aid program ends in 1952. These are critical issues for the future. Morever, it is important, as we succeed in expanding imports, to avoid the inequity of placing the full burden of readjustment in the international position of the United States upon a limited few domestic concerns or industries. Yet it is unlikely that other countries can earn dollars to pay for a continued large volume of exports from this country without exerting some competitive impact upon individual producers in this country. To an extent, American capital export may provide dollars with which to close the longer-run hard-currency gap. The President's Point Four program for technical assistance and investment in the underdeveloped areas, announced at the beginning of the year, was received eagerly throughout the world as an indication of forward American planning to this end. But it would be dangerous to expect too much on this score. Emphasis is rightly placed, so far as direct investment is concerned, upon the flow of private capital. It will be difficult, however, to enlarge American capital exports above the one billion dollar (net) annual rate of 1949 while the rewards to capital are still substantial at home, the political and economic risks of investment abroad are great, and the rewards for such risky investment, when successful, are so largely reduced by taxes. Yet ways must be found, both to raise our imports and to increase the outflow of private capital, if many of the successes thus far achieved in rehabilitating the production and trade of the world are not to shrink away after 1952.

In retrospect, 1949 was a year of modest progress toward most of our economic objectives—domestic and international. By safely weathering the first threat of a long anticipated postwar recession, and by continuing to demonstrate the potentialities for growth and adjustment of a vigorous enterprise economy, the United States was fulfilling in substantial measure the heavy responsibilities of leadership that world events during the first half of the century had placed upon it.

National Economic Trends in 1949

The magnitude of the economic fluctuations which occurred during 1949 is apparent only in monthly or quarterly data for certain sectors of the economy. In some lines, gains in the latter part of the year canceled out the poor showing of the first half. Declines in output and employment in particular industries or localities during the year often coincided with the reaching of new peaks of activity in other industries or localities. As a result, most of the business indicators covering the economy as a whole during 1949 compared favorably with 1948, and hardly reflected the readjustments that had taken place during the year. The value of all goods and services produced in 1949 (the gross national product) was estimated at 257.4 billion dollars, only 2 per cent below the 1948 total. Since there was some decline in prices during the year, the over-all physical volume of activity was probably even closer to the 1948 level. Total employment averaged 58.7 million persons during 1949, compared with 59.4 million in 1948, a decline of about 1 per cent. Personal income, at 209.8 billion dollars, was nearly as great as in 1948, and actually a somewhat greater amount of wages and salaries was paid out in 1949.

The gross national product declined from the record (seasonally adjusted) annual rate of 270 billion dollars in the fourth quarter of 1948 to 255 billion in the third quarter of 1949 and remained practically unchanged in the last quarter. The decline was caused almost exclusively by a change in inventory policy, motivated by slackening of consumer demand and falling prices in many lines. As indicated in the accompanying chart, production was increasingly stimulated during 1948 by the demand for goods to build up inventories. In the fourth quarter of 1948, businessmen were adding to their inventories at the rate of 9 billion dollars a year. In 1949, this situation was reversed. Distrib-



utors and manufacturers generally tended to cut down their stocks, and in many instances production was curtailed while orders were filled out of inventories. During the last three quarters of 1949 inventories were reduced at an average annual rate of 4 billion dollars. In this way it was possible for the actual flow of goods and services to consumers, business, and government to be maintained close to the 1948 peak throughout 1949, despite a drop in over-all production amounting to 15 billion dollars (annual rate) or 5½ per cent, between the fourth quarter of 1948 and the fourth quarter of 1949.

While the reduction in inventories took place at all levels of manufacturing and distribution, the decline in production was centered in manufacturing and mining. During the first half of 1949, the Federal Reserve index of industrial production declined steadily, and in July it reached a low (partly seasonal) of 161, which was 17 per cent below the October-November 1948 peak of 195. The inventory curtailment was accomplished in many instances through a drastic reduction of new orders or even the cancellation of old ones. Many business enterprises had started 1949 with a sizable backlog of unfilled orders, but soon found that their backlogs had been substantially reduced. This, together with the curtailment of output by some factories which were working off their own inventories, resulted in many cases of shortened work-weeks, temporary plant shutdowns, and layoffs. Unemployment more than doubled between October 1948 and July 1949, reaching a peak of 4.1 million persons in the latter month.

By July, however, wholesalers, retailers, and some manufacturers appeared to have largely completed working off their excess stocks and to have started increasing their purchases to cover current needs. In a few cases, stocks had been cut too sharply and were inadequate to meet the seasonal rise in demand. As a result, buying was intensified, and a shortage of goods for immediate delivery developed in certain textile and apparel lines, where producers were not fully prepared for the influx of orders. In the last quarter of 1949 labor disputes reduced the output of coal, steel, and aluminum, leading to the depletion of fabricators' stocks. When steel production was resumed, the pressure of demand lifted operating rates to near-capacity levels.

Despite these sharp fluctuations in production, the nation continued steadily to consume goods and invest in housing at near-record rates, while investment in capital goods was curtailed only moderately. New plant and equipment expenditures of nonagricultural producers were reduced from 19.2 billion dollars in 1948 to 17.9 billion in 1949, but this decline was only slightly greater than had been anticipated at the start of 1949. Agricultural and noncommercial capital expenditures remained at the high 1948 level, and so did the construction of new homes. Residential building lagged behind the 1948 rate during the first half of the year, but was maintained at a record-breaking rate during the second half and was an important factor in the business recovery. A new record total of 1,025,800 dwelling units was started in 1949, compared with 931,300 in 1948 and the previous peak of 937,000 units in 1925. There was a decline of 2 billion dollars in "net private foreign investment" (i.e., in the excess of sales of goods and services to foreign countries over purchases from abroad), but there was a rise in Federal, State, and local government expenditures for goods and services, from 36.7 billion dollars in 1948 to 43.4 billion in 1949. More was spent not only for Federal foreign aid, defense, and farm price-support programs, but also for public works programs, particularly at the State and local level.

Personal consumption expenditures were, on the whole, remarkably stable during 1949, and the annual rate of consumption in every quarter of 1949 was approximately equal to the 1948 total of 179 billion dollars. While personal income was 1 per cent less than in 1948, the real purchasing power of consumers was higher in 1949. The lower rate of personal income taxes which was in effect throughout 1949 resulted in a net drop in personal taxes of 2.5 billion and a slight increase in disposable income. In addition, the somewhat lower level of consumers' prices prevailing in 1949 meant that consumers could purchase a somewhat greater volume of goods and services than in 1948, while at the same time they were able to maintain their rate of net personal saving (at about 12 billion dollars, or 6 per cent of disposable income). The high level of spending was based in part on a continued expansion in the amount of consumer credit outstanding. On the other hand, there were indications that the rise in consumer and mortgage debt was accompanied by a corresponding increase in the volume of liquid assets in the hands of consumers. As in the two previous years, however, by far the largest part of individual savings was invested in tangible assets, such as homes, farm equipment, and unincorporated businesses.

Although consumers' expenditures remained relatively stable throughout 1949, there were considerable variations among the different types of expenditures. The sharp rise in automobile sales, particularly in the second half of the year, was the most notable feature of the retail trade picture in 1949, and was in fact an important sustaining influence for the whole economy. The 1949 output of passenger automobiles and trucks reached a new peak of 6,238,000 units, well above any previous year. In July, when industrial production as a whole was at its lowest point of the year, automobile factories broke the weekly production record set more than twenty years earlier. The boom in sales of television receivers gained momentum during 1949, although there was a summer setback, perhaps only partly seasonal in character. Sales of other types of durable goods lagged substantially behind 1948 during the early part of 1949, but recovered subsequently. Total expenditures on all types of durable goods were the highest on record, both in dollar volume and as a percentage of disposable income. Nondurable goods expenditures, on the other hand, were 3 per cent lower than the 1948 record, although much of the decline, particularly in the case of apparel and food, may be attributable to lower prices.

Expenditures on housing rose, because of higher rents and the greater number of units available. In general it may be said that the sale and distribution of goods has become more competitive. For many items, 1949 was the first full year of a buyers' market in nearly a decade.

The decline in prices which had begun in the latter half of 1948 continued during 1949. The general level of wholesale prices was 7 per cent lower at the end of 1949 than it had been a year earlier. As grain prices dropped sharply in February, prices of farm products in general fell and then recovered somewhat; they declined further in the latter half of the year, primarily because of lower livestock prices. The net reduction during 1949 in the prices of farm products was 13 per cent, while food prices, which followed a similar pattern, declined 9 per cent. Other wholesale prices, taken as a whole, declined about 5 per cent in the first half of 1949 and thereafter remained stable. Prices of metals and metal products declined during the first half of 1949, when nonferrous metal prices dropped sharply, but stabilized during the second half of the year. A similar pattern of marked weakness in the first half and firmness in the second half of 1949 was shown by prices of building materials, while textile and chemical prices (with some exceptions) continued to decline, though at a slower rate, during the latter months of the year.

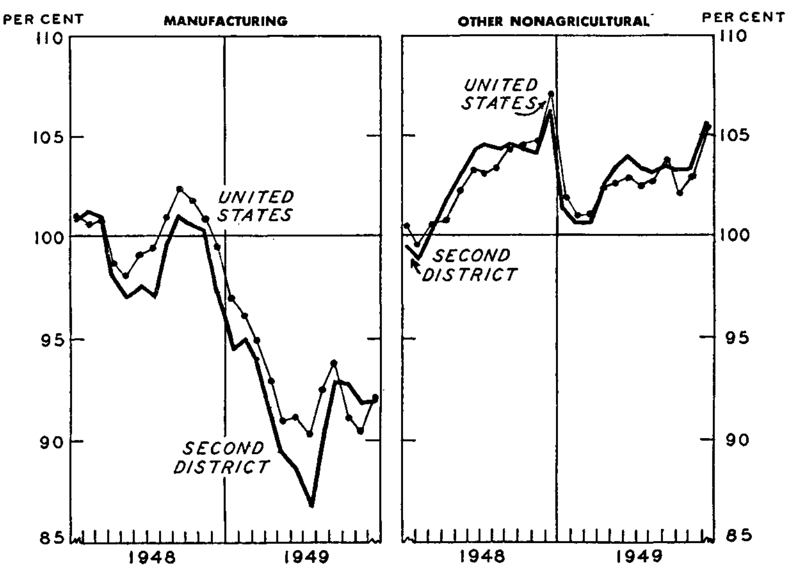
Prices of primary commodities declined much more sharply than prices of finished goods and services. At the end of 1949, the daily index of spot prices of 28 basic commodities tabulated by the Bureau of Labor Statistics was 31 per cent below its postwar peak, and the weekly index of wholesale prices showed an 11 per cent decline from its 1948 postwar high. Retail prices of commodities, however, were down only 6 per cent from their postwar peak, on the whole, while rents and some services continued to advance.

Work-spreading, through shorter work-weeks and staggered layoffs, probably was instrumental in keeping the volume of unemployment from rising higher than it did during the decline in business in the early part of the year. In July, when the number of unemployed, at 4.1 million, was the highest since January 1942, there were also an estimated 1.7 million persons working less than 15 hours a week and 0.3 million people temporarily laid off from their regular jobs. To a large extent, the increase in unemployment was attributable not only to a decline in employment, but also to the failure of new job opportunities to keep pace with an expanding labor force. For the year as a whole, the decrease in employment averaged only 0.7 million, but unemployment increased 1.3 million.

Economic Trends in the Second District

In general, business in the Second Federal Reserve District followed the national pattern of recession and revival during 1949. As the accompanying chart indicates, declines in employment in the District were centered almost entirely in manufacturing, while the number of workers in other nonagricultural industries was practically unchanged from the 1948 level. New York State appears to have fared better in the matter of employment during 1949 than some other parts of the country. Factory employment in New York State averaged 6 per cent lower than in 1948, whereas in the rest of the country the decline was 8 per cent. On the other hand, New Jersey and Connecticut, parts of which are in the Second District, experienced declines in manufacturing employment of 11 per cent and 14 per cent, respectively. On the whole,

NONAGRICULTURAL EMPLOYMENT, SECOND DISTRICT AND UNITED STATES
(1947 average = 100 per cent)



Source: Second District computed by the Federal Reserve Bank of New York from data furnished by the Departments of Labor of the States of New York, New Jersey, and Connecticut; United States computed from data of U. S. Bureau of Labor Statistics.

nonmanufacturing industries made a slightly more favorable showing in this District than in the rest of the country.

According to preliminary estimates made at this bank, income payments in the Second District during 1949 totaled approximately 34 billion dollars, the same as in 1948, whereas in the country as a whole, personal income was somewhat lower in 1949 than in 1948. The slightly more favorable showing in the income of this District arises partly from the more stable nature of this area's economy. On the one hand, farm income, which dropped more than one fifth in the country as a whole and accounted for most of the national decline in income, is a relatively small part of this District's income; the drop in farm income in this District therefore had relatively little effect on the District's total income. On the other hand, an exceptionally large proportion of manufacturing in the Second District is devoted to the production of apparel and other consumers' nondurable goods, which in times of recession generally decline less than durable goods.

To a considerable extent, the fact that the 1949 decline in factory employment was relatively smaller in New York State than in the country as a whole may reflect the circumstance that some of the readjustment process in this State had already been accomplished. Data from the State Department of Labor show that the postwar peak in factory employment in New York was reached back in November 1946. In the country as a whole, factory employment did not reach a peacetime peak until September 1948, almost two years later. During the first half of 1949, the policy of inventory curtailment particularly affected this State's dominant apparel industry, but in the second half of the year that industry was especially stimulated by the restocking movement of the period. At the end of 1949, the apparel industry was the only major industry in the State to employ a greater number of workers than a year earlier. Producers of some nondurable goods, notably food processors, textile mills, and printers, made sizable cuts in their working forces during 1949, but over nine tenths of the year-to-year decline in factory employment occurred in durable goods industries. The reduction in durable goods employment in New York State amounted to 10 per cent, while in nondurable goods the decline was less than 1 per cent. Manufacturers of primary and fabricated metals, machinery (both electrical and nonelectrical), and transportation equipment accounted for the bulk of the layoffs.

The sharper declines in factory employment in New Jersey and

Connecticut were mainly attributable to the greater concentration of durable goods industries in those areas. In New Jersey, the metals and machinery industries laid off large numbers of workers; and in the case of electrical machinery manufacturers, employment was cut by nearly one fourth. In the nondurable goods group, factories producing chemicals, textiles, and rubber products also employed fewer workers in 1949.

Largely as a result of layoffs by manufacturing concerns, two areas in this District, Bridgeport and Utica-Rome, were among the 12 "critical" industrial areas listed by the Federal Government in August. (These areas were so designated because unemployment exceeded 12 per cent of the total labor force in each area.) In both areas there has been some improvement since, but unemployment remains high.

Residential construction in the District reached a high level during 1949. The number of new dwelling units started in the New York metropolitan area alone was 102,000 units, or approximately one tenth of the national total. This represents an increase of more than one third over 1948, when 74,000 dwelling units were started. In New York City itself, residential building was stimulated during the first half of 1949 by a large volume of public housing projects; private building lagged during the first half of the year but increased sharply in the second half. During the year as a whole, 43,390 dwelling units were started in New York City, of which nearly one half were publicly financed. Although the number of one and two-family homes started in the City dropped sharply, apartment house units begun in 1949 numbered more than twice as many as in 1948. In Westchester and the Northern New Jersey counties, there was also a sharp rise in apartment building, while on Long Island increased construction of smaller, lower-priced, single-family homes accounted for much of the rise in activity. New housing in the rest of the Second District outside the metropolitan area totaled about 25,000 units. Various types of nonresidential construction in the District also increased during 1949. An increase in the construction of schools, churches, stores, and office buildings more than offset declines in the erection of factories and institutional buildings.

Agriculture in this area was affected by the extremely dry weather in the early summer of 1949 and by declines in farm prices. Cash receipts from crops produced on New York State farms in 1949 were 16 per cent less than in 1948, and receipts from milk and other livestock products declined 11 per cent. Potatoes accounted for nearly two thirds of the fall in crop receipts, since potato acreage was restricted and the Government price-support level was one-third lower than in the previous year. Pastures generally were poor, and hay output was one-fourth less than in 1948. Although dairy farmers had to rely more heavily on purchased feeds, milk production rose about 10 per cent over 1948.

Retail sales in this District were, on the whole, well maintained during 1949. As in the rest of the country, increased sales by automobile dealers offset declines at other types of retail outlets. With the major exceptions of food and of passenger car sales, trends in consumption and distribution in the District are generally indicated by the statistics of department store sales. According to figures collected by this bank, sales of department stores during 1949 declined 7 per cent in dollar volume from the 1948 record level, marking the first drop in dollar sales in a decade. Unit sales in all probability showed a smaller decrease, for some part of the loss in dollar volume reflected a decline in the level of prices. Dollar sales were reduced somewhat more in this District than in the country as a whole, but the difference was not of significant proportions. Within the Second District, Westchester County was the only area where stores reported a gain in sales for 1949. Buffalo, Niagara Falls, and Poughkeepsie reported decreases of 4 per cent. The decline in New York City was slightly greater than that in the rest of the District, and the sharpest drop in sales—9 per cent—occurred in Binghamton.

Federal Reserve Credit Policy

The character of the credit problems facing the Federal Reserve System changed markedly during 1949, and credit policy was altered to meet the new situation. Late in 1948 the inflationary pressures which had persisted throughout most of the postwar period began to show signs of abating. Not long after the turn of the year it became clear that credit demands had lessened considerably. Bank loans to business were falling and institutional investors had reduced or reversed their large-scale selling of long-term (restricted) Government securities for the purpose of reinvesting the funds in private securities. In fact, purchases of long-term restricted Government securities by some types of investors, which had started near the end of 1948, continued on an increased scale during much of 1949. The gold inflow, which had been adding to member bank reserves at an average annual rate of more than 1½ billion dollars since the end of the war, was reduced to a trickle; indeed, a net outflow of gold set in late in 1949.

In retrospect, the reasons for the decline in the rate of economic activity and in prices during the first half of 1949 are clear enough; they are reviewed elsewhere in this report. As a result, loans by banks to business fell off as inventories declined and demands for long-term capital to finance investment expenditures slowed down. In addition, the postwar rise in consumer expenditures ceased its rigorous upward trend as the more pressing needs of buyers began to be satisfied.

The change in the business situation was accompanied by (though only partly the cause of) a considerable shift in the Treasury's position with respect to disbursements and receipts. In the calendar year 1948, a cash surplus of 8 billion dollars, used largely to retire Government debt obligations held by the Federal Reserve System, had exerted an important restraint on the ability of banks to expand credit, and on the money supply, since these funds were not returned to the income stream. In 1949, however, Treasury cash disbursements to the public exceeded cash receipts by about 1.3 billion dollars, reflecting in part the "built-in" flexibility of the Treasury's cash budget, i.e., the tendency of tax receipts to decline and of expenditures (unemployment payments, for example) to rise in times of reduced business activity. The Treasury's net payments to the public in 1949 were outweighed (in so far as their effect on the money supply is concerned) by a net addition to the

Causes of Changes in Deposits and Currency*

(In millions of dollars; (+) or (−) indicates effect on volume of deposits and currency)

Year	Treasury net cash income or outgo	Bank loans	Nonbank holdings of U. S. securities	Bank holdings of other securities	Gold and foreign accounts	Bank capital accounts	Other	Total
1945	+35,751	+ 4,347	−20,400	+ 1,016	− 214	− 899	+ 967	+20,568
1946	− 989	+ 5,286	+ 7,000	+ 914	+ 817	− 818	+ 1,001	+13,211
1947	− 6,797†	+ 7,354	− 500	+ 1,232	+ 3,029†	− 588	+ 2,274	+ 6,004
1948	− 8,012	+ 5,172	+ 1,000	+ 699	+ 1,240	− 531	− 457	− 889
1949	+ 1,259p	+ 1,600e	− 2,000e	+ 1,200e	+ 58	− 650e	− 467e	+ 1,000e

* Includes: demand and time deposits adjusted (other than U. S. Government) and currency outside banks.

† Adjusted for payment of United States quota in International Monetary Fund.

p Preliminary.

e Estimated by the Federal Reserve Bank of New York.

Source: Treasury cash income or outgo and nonbank Government security holdings derived from *Treasury Bulletin;* all other data, Board of Governors of the Federal Reserve System.

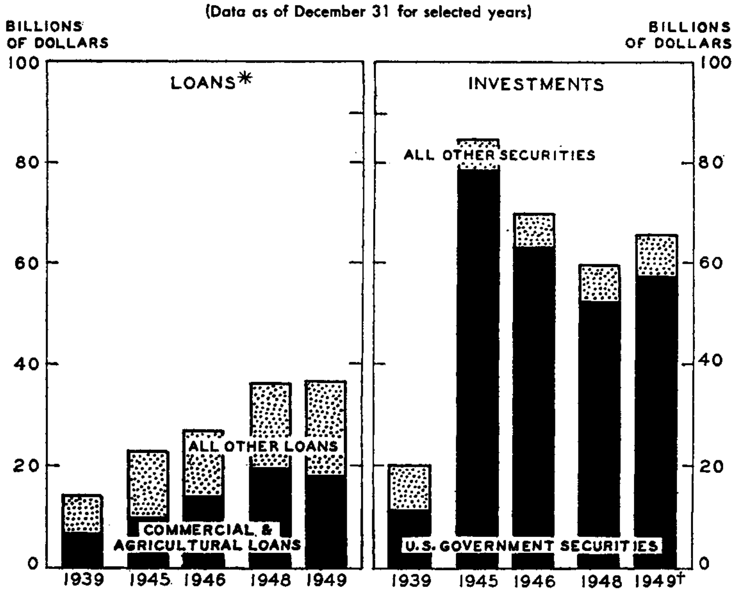
holdings of Government securities by nonbank investors. Nevertheless, the money supply available for the public's use at the end of the year, in the form of demand deposits and currency, was slightly larger than at the beginning.

As a result of the sustained demand for new homes, real estate loans at the banks increased. This increase, together with an expansion in consumer loans, was greater than the decline in loans to business; total bank loans rose, therefore, although the rise was modest compared with that of other postwar years. Bank purchases of securities other than U. S. Government obligations increased during the year and this had an expansive effect on deposits and currency.

None of the forces at work in the economy during 1949 operated evenly throughout the year. For example, the Treasury had its usual cash surplus in the first part of the year, although the surplus was smaller than in recent years. Later the Treasury's expenditures rose and its receipts declined so that net cash disbursements of considerable size resulted. Business inventories and bank loans to business started

MEMBER BANK LOANS AND INVESTMENTS

(Data as of December 31 for selected years)



*Beginning June 30, 1948, various loan items are reported gross, i.e., before deduction of valuation reserves.
†Estimated.

to fall early in the year, but a reversal took place in late summer. At the start of the year, however, these later changes in trend could not be clearly foreseen. In each of the more recent postwar years uncertainties had arisen in the first half, price weaknesses had developed and the rate of growth in bank loans had slackened, but later in each year, inflationary pressures had reasserted themselves. Early in 1949, however, a repetition of these developments appeared sufficiently unlikely to justify the easing of credit restraints in some measure.

The retirement by the Treasury of System-held Government securities was reduced, not only because of the diminished amount of funds available to the Treasury for such purposes, but also because of a desire to relax pressure on the reserve positions of member banks. The System also took other steps to avoid being "too late" in meeting a possible turn of the economic tide. Consumer credit terms were eased in recognition of the slowing down of demand for consumer durable goods such as household appliances. At the end of the first quarter of the year the Board of Governors acted to permit greater use of credit in security transactions by reducing margin requirements, under Regulations T and U, from 75 per cent to 50 per cent. Some further relaxation of restraint upon credit expansion was effected in the second quarter of 1949. In this period, the decline in the volume of bank credit to business had accelerated and the fall in business inventories had become pronounced. At the same time unemployment continued to rise, while prices of basic commodities declined further. In response to these and other indications of a declining level of economic activity, there was a further easing of consumer credit terms by the Board of Governors in April. Late in the same month a lowering of member bank reserve requirements was announced by the Board, to take effect early in May. The percentage of reserves required to be held against demand deposits was lowered by 2 points in the case of central reserve city banks and by 1 point in the case of other banks, while the reserve requirement against time deposits was reduced for all banks by ½ per cent. This action, which freed about 1.2 billion dollars of reserves, was followed by a strong demand for Government securities on the part of the banks. The System met the demand for short-term Government securities and Government bonds by sales from the Open Market Account, and thus prevented a sudden rise in prices and decline in yields. Commercial bank purchases of medium-term issues were supplied mainly by nonbank investors, who in turn bought long-term restricted issues indirectly from the Reserve Banks.

Toward the end of June, in view of the impending expiration of the temporary powers granted to the Sytem under the "anti-inflation act" of August 1948, the Board of Governors announced another reduction in reserve requirements. This reduction brought the required reserve percentages to the levels which constitute the permanent upper limits now permitted by law, except in the case of central reserve city banks, whose reserve requirements were already below the limit.[1] At the same time the Board had to terminate the control of consumer credit which it had been exercising through Regulation W under authority of the temporary legislation of 1948.

On June 28, the day preceding the announcement of the lowering of reserve requirements, the Federal Open Market Committee issued the following statement:

> "The Federal Open Market Committee, after consultation with the Treasury, announced today that with a view to increasing the supply of funds available in the market to meet the needs of commerce, business, and agriculture it will be the policy of the Committee to direct purchases, sales, and exchanges of Government securities by the Federal Reserve Banks with primary regard to the general business and credit situation. The policy of maintaining orderly conditions in the Government security market and the confidence of investors in Government bonds will be continued. Under present conditions the maintenance of a relatively fixed pattern of rates has the undesirable effect of absorbing reserves from the market at a time when the availability of credit should be increased."

Following this statement, the Open Market Account, which had been supplying securities to the market rather freely, temporarily stopped its sales. In the absence of increased private demands for credit, however, member banks undertook to invest, quickly, the 800 million dollars of reserves freed by the reduction in reserve requirements, and prices of all Government securities were bid up sharply. Market rates on Treasury bills, which had hovered near 1.16 per cent during most of June, fell abruptly to 0.78 per cent early in July, and yields on the longest certificates of indebtedness dropped from an average of 1.20 per cent to slightly below 1.00 per cent. It became apparent that, unless additional supplies of securities were made available to the banks, so large an amount of reserves could not be released

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[1] After this reduction, the reserve requirements of member banks were as follows: against demand deposits: 24 per cent for central reserve city banks, 20 per cent for reserve city banks, and 14 per cent for other member banks; and against time deposits, 6 per cent for all member banks.

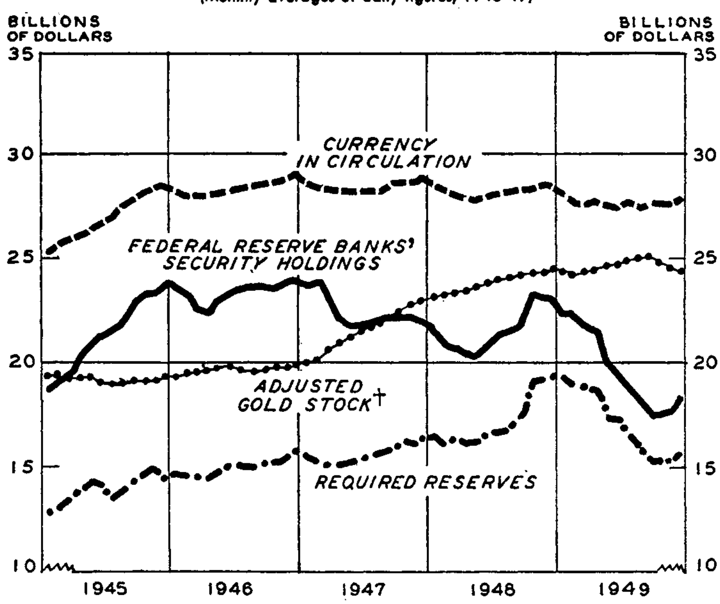
without creating "disorderly" markets. The Reserve System then acted to supply Treasury bills and certificates to meet the demand. By this means the increase in excess reserves was absorbed, at least temporarily, with a stabilizing effect on the market.

A third series of reductions in member bank reserve requirements was announced by the Board of Governors early in August. The reductions were made effective in instalments during that month and ending on September 1. Altogether the reductions amounted to 2 percentage points in the required reserves on demand deposits and 1 percentage point on time deposits for all classes of member banks; and released a total of about 1.8 billion dollars of reserves. The series of small reductions facilitated adjustments by the banks and the Reserve System to the new situation, and avoided the disturbances in the money market which had been found likely to result from a single large release of reserves.

As on previous occasions, member banks invested in Government securities most of the additional funds made available to them. The

MAJOR FACTORS AFFECTING MEMBER BANK RESERVE POSITIONS

(Monthly averages of daily figures, 1945-49)

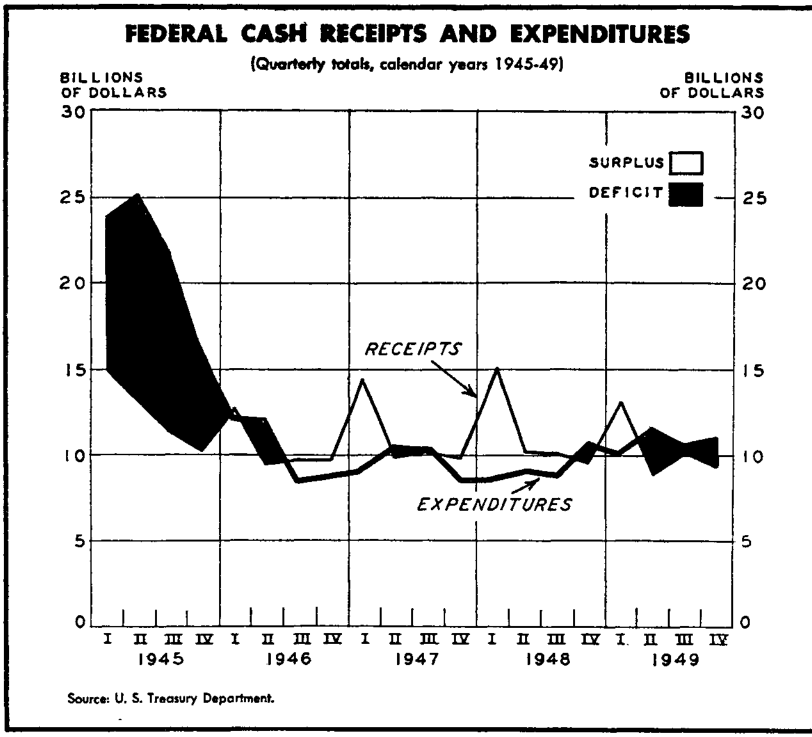


†Gold stock adjusted for foreign account balances with Federal Reserve Banks and for a payment to the International Monetary Fund in 1947 as part of the United States subscription.

Federal Open Market Committee adopted practices designed to facilitate the adjustment. Considerable amounts of maturing Treasury bills in the System Open Market Account were allowed to run off without replacement, which resulted in larger allotments of the weekly issues of new Treasury bills to other bidders. In addition, the Treasury increased its offerings of bills by 100 or 200 million dollars a week for several weeks in August and early September, partly to meet the excess of Government expenditures over receipts, and total Treasury bills outstanding were increased by an aggregate of 800 million dollars in this period. Finally, corporations and other investors made substantial sales of short securities in the market in order to purchase Treasury Savings notes, yields on which were attractive compared with those on short-term marketable issues. The total supply of Treasury bills available in the market from all these sources proved to be greater than the commercial banks were prepared to absorb. There was some fear at the time of a further decline in interest rates, and the banks tended to show a preference for the longer maturities of Treasury certificates of indebtedness. Consequently, the Reserve Banks made certificates available to the market and absorbed some of the supply of bills.

Until the latter part of the summer, little expansion of bank loans followed the successive reductions in member bank reserve requirements. The first effect was to increase the secondary reserves (the liquidity) of the banks and their total earning assets, as they purchased Government and other securities with the released reserves. In the July-September period, however, the decline in bank loans first began to slacken, and then was followed by an upturn; in September member bank commercial, industrial, and agricultural loans expanded rapidly. The rise continued at a slower and irregular pace until the end of the year.

The tendency toward business recovery gained momentum during the autumn, despite the interruptions to production caused by the coal and steel strikes. Prices of industrial products, in a number of instances, became firmer. Meanwhile, the money supply (demand deposits and currency outside banks), which in the second quarter had recovered part of the seasonal reduction in the first quarter, rose considerably further in the latter half of the year. Consequently the year as a whole showed a small net increase, following the 2 billion dollar reduction in 1948. The principal factor in the increase after the first quarter was the cash deficit of the Treasury. In the last three quarters, cash outgo of the Treasury was swollen by payments to farmers



for crop price supports and by rising unemployment benefits. As a result of the enlargement of expenditures and a (partly seasonal) fall in receipts, Treasury cash income, which had exceeded outgo by almost 3.2 billion dollars in the first quarter of 1949, fell short of receipts by about 4.4 billion dollars in the remainder of the calendar year.

In view of the pronounced change in the business and financial situation in the latter part of the year, the Reserve System modified its aggressive "easy money" policy, and allowed increased demands for credit and currency to exercise a moderate firming effect on the money market during the fall. By the end of November, yields on Treasury bills and other short-term Government securities were pressing against the 1⅛ per cent, one-year rate which had been fixed by the Treasury in its September and October refunding operations. It was in these circumstances that the Treasury had to decide upon the terms for the refunding of its bonds called for redemption on December 15 and of its certificates maturing on that date. The decision was to offer 1⅜ per cent, 4¼-year Treasury notes in exchange for these issues. At the same time it was announced that another issue of 1⅛ per cent, one-year certificates of indebtedness would be offered in exchange for the issue of certificates maturing on January 1, 1950. Prevailing short-term interest rates were maintained during December in order to facilitate the January 1 Treasury refinancing operation.

These developments illustrated the close interrelationship between monetary policy and debt management policy and the need for effective coordination of the policies of the Treasury and of the Federal Reserve System. As the president of this bank stated[2] ". . . the central problem of monetary and credit policies under present conditions . . . . is how to combine effective monetary management with effective debt management . . . . there cannot be a purposeful monetary policy unless the Federal Reserve System is able to pursue alternating programs of restraint, 'neutrality,' and ease, as the business and credit situation may require. Such programs must, as they accomplish an increase or contraction in the volume of credit and a tightening or loosening in the availability of credit, affect interest rates, not only for private credit, but for Government securities. The terms of Treasury offerings for new money, and for refunding issues, must be affected. Yet those effects will, at times, be inconvenient and burdensome to the Treasury in its management of the enormous public debt, and may conflict with otherwise praiseworthy efforts to minimize expenditures for debt service. This is a conflict which will continue to arise, in one form or another, so long as this public debt, huge in relation to our present national income, is with us. It is not a problem which can be solved by demanding more courage or independence on the part of the Federal Reserve System, nor by attacking indiscriminately the Treasury's understandable concern with the cost of servicing the public debt."

The operations of the Reserve System during the latter half of 1949 illustrated and clarified the meaning of the statement in the June 28 announcement of the Federal Open Market Committee that it would "be the policy of the Committee to direct purchases, sales, and exchanges of Government securities by the Federal Reserve Banks with primary regard to the general business and credit situation"; also the statement that "The policy of maintaining orderly conditions in the Government security market" would be continued.

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[2] Midwinter meeting of New York State Bankers Association, January 23, 1950.

Corporate Finance and the Capital Markets

Financing by nonfinancial corporations, in the aggregate, was sharply lower during 1949, reflecting mainly the tendency of working capital requirements to decline during the moderate business recession in the first half of the year. The business adjustment was reflected in figures of corporate finance mainly in a liquidation of inventories and a general strengthening of financial positions. Corporations improved their liquidity through large repayments of debts to banks and smaller repayments to trade creditors, while adding substantially to their cash and Government security holdings. The reduction of inventories released an estimated 3.7 billion dollars of corporate funds during 1949, in contrast to 1948 when an accumulation of inventories required the investment of 6.3 billion dollars.

The liquidation of inventories provided corporations with funds with which to repay debts. Corporate indebtedness to the banks was reduced by about 1.6 billion dollars during the year (compared with an increase of 1.2 billion during 1948), and indebtedness to trade creditors by 0.2 billion. At the same time, funds accruing in Federal income tax reserves prior to payment (and thus available for general business purposes) declined 2.4 billion dollars. Since corporations as a whole increased their cash and bank deposits by 1 billion dollars, their Government securities by 1.5 billion, and their customer financing through open book credit by 0.7 billion, largely offsetting the decline in inventories, current assets were reduced only slightly while current liabilities were reduced substantially. In other words, there was a growth of more than 3 billion dollars in *net* corporate working capital.

Corporations continued, however, to require large amounts of funds for the purpose of financing new plant and equipment. In 1949 the amounts spent for this purpose are estimated to have totaled 16 billion dollars, only 1.3 billion (or 7½ per cent) below the 1948 total.

In financing this huge capital expenditure, and at the same time increasing net working capital, nonfinancial corporations in the aggregate relied somewhat more on the capital markets (relative to their total financing) than in previous years. Somewhat larger depreciation allowances were available to meet part of the corporations' needs for funds, but undistributed earnings, estimated at 7.5 billion dollars, were 40 per cent smaller than in the preceding year, since business corporations in the aggregate increased their dividend payments to stockholders in the face of reduced net profits after taxes. As a result, the volume of corporate financing in the capital market was fairly well sustained, especially in the first half of the year, and approximately 5.1 billion dollars, net, of new security issues (total issues less cash retirements) were offered, compared with 6 billion in 1948.

Despite this relatively greater reliance by corporations on the capital markets to meet their needs for long-term and equity funds, the total funds which they obtained from external sources fell sharply from 9.7 billion dollars in 1948 to 1.4 billion in 1949, as a result of the sharp decline in bank loans and other current liabilities.

A decline in new corporate mortgages accounted for about one third of the decrease (from 7.4 billion dollars in 1948 to 6.8 billion in 1949) in urban mortgage financing. The decrease in urban mortgage financing reflected a slight decline in the value of private construction of all types except utility construction. The small decrease in the amount of residential mortgage financing was due in part to a decrease in new loans for the purchase of existing homes, and apparently also, in part, to an increase in the proportion of new homes in the lower price ranges. (Although 1949 was a record year in terms of the number of new dwelling units placed under construction, it was estimated that the total value of private residential construction in 1949 was slightly below the 1948 total.)

State and local government outlays for roads, schools, housing, hospitals, and other public construction reached new record levels during the year, and were financed largely through borrowing. State and local governments in 1949 raised about 2.9 billion dollars through security issues, or 200 million more than the previous year's record-breaking total, despite much smaller amounts of veterans' bonus issues.

While the aggregate demand for funds declined during 1949, personal savings, as measured by the increase in funds made available to thrift institutions, continued to increase. The supply of other investable funds probably rose, also, due partly to the accumulation of pension fund reserves. This shift in the balance between the demand for and supply of investable funds, compared with 1948, was pointed up by the substantial decline during 1949 in the liquidation of Government bonds by nonbank investors.

Prices of high-grade bonds rose throughout the year, and new corporate bond offerings were generally well received by investors. Total corporate security issues for new money purposes declined about

19 per cent to 4.8 billion dollars[1] during 1949, with the volume of offerings declining sharply in the second half of the year. The decrease for the year as a whole was entirely in corporate bonds. Issues for the retirement of existing indebtedness totaled 875 million dollars, and were somewhat larger than in 1948, owing partly to the decline in interest rates. New security offerings for other purposes (including the purchase of existing plant and equipment, securities of other companies, etc.) amounted to about 370 million dollars as against 235 million in 1948. The volume of securities placed directly with large investors (for the most part, life insurance companies) fell about 16 per cent to 2.6 billion dollars.

Despite the low and decreasing cost of debt capital and the high cost of equity financing in 1949, total common and preferred stock flotations amounted to more than 1.1 billion dollars (about 20 per cent of total new capital issues) and were slightly above the 1948 total. Yields on representative common stocks during 1949 averaged over 6½ per cent, a rate of return which until the past few years has prevailed only in periods of war or depression. Nevertheless, new issues of common stocks rose 120 million dollars to about 735 million, while sales of new preferred issues dropped about 60 million dollars to 430 million.

Stock prices declined during the business recession of the first half of the year and in mid-June fell somewhat below the range of fluctuation which had persisted since September 1946. Trading remained relatively inactive and, even while new low prices were being made, never reached a volume that would indicate general liquidation. Share prices subsequently responded strongly to the improved business prospects in the latter part of the year, and toward the close of 1949 the Dow-Jones average of industrial stock prices, consisting mainly of higher-grade issues, was the highest since August 1946 and came within 6 per cent of the postwar high of May 1946.

The New York Foreign Exchange Market

The outstanding developments affecting the New York market were those leading up to and resulting from the devaluation of the pound sterling from $4.03 to $2.80 in September. While prior to devaluation the spot sterling rate in New York was maintained close to $4.03 through

[1] This figure differs slightly from the 5.1 billion given on page 29 for net new security issues, owing to the fact that the latter includes new security issues for the purpose of purchasing assets of existing businesses and new issues of open-end investment companies.

official support, market sentiment with respect to the pound had been reflected in discounts of as much as 25¾ cents for three months' forward delivery. After devaluation the forward rates were variously quoted at only a slight discount from or premium over the spot rate, and spot quotations were at all times close to the Bank of England's official buying and selling rates.

In the wake of the sterling devaluation, the currencies of all other sterling area countries (except Pakistan) and of various European and other countries (including Canada) were devalued. As shown in the table, most of these countries—with the principal exceptions of Belgium, France, Western Germany, Portugal, and Canada—devalued their currencies to about the same extent as the pound sterling, i.e., 30.5 per cent. Italy made certain changes in its regulations which had the effect of depreciating the lira vis-a-vis the dollar by about 9 per cent, and Argentina, Paraguay, and Uruguay made adjustments in their multiple rate systems. Peru abolished its multiple rate system in November, and since that time all transactions have been effected at a uniform but fluctuating rate. Prior to the autumn wave of devaluations, Mexico had established a new par value of 8.65 pesos per dollar ($0.1156 per peso), after allowing the peso to depreciate to that level from the old parity of 4.855 pesos ($0.2059 per peso) which had existed until July 1948. To the extent that the currencies of the above-mentioned countries are quoted in the New York market, rates here, of course, reflected the changes made abroad.

An important step in the direction of freer foreign exchange trading was taken by Belgium, which established a free market for the United States dollar at the end of November 1949. In Switzerland all dollar transactions have been conducted at the free market rate since the latter part of September 1949; previously there had existed both a fixed official rate and a fluctuating free rate, the latter applying to sales of dollar capital assets and certain other transactions. In both Belgium and Switzerland rates for the dollar during the past few months have been quite stable, and provision has been made for official intervention, if required, to maintain them within certain limits. Some progress towards more normal exchange conditions has also been made by France which, immediately following the sterling devaluation, established uniform exchange rates to replace the previously existing multiple rate system; for most types of transactions the new arrangement represented a depreciation of somewhat over 22 per cent.

Currency Readjustments, September 18 - December 31, 1949*

Country	Monetary unit	Date of devaluation	Value of monetary unit in U. S. cents†		Percentage of devaluation
			Old	New	
Argentina	Peso	October 3	(a)26.80 to 20.26 (b)29.78 to 20.00	(a)26.80 to 11.09 (b)29.78 to 11.11	0.0 to 46.7 0.0 to 46.7
Australia	Pound	September 19	322.40	224.00	30.5
Austria	Schilling	November 22	10.00	(c) 6.94 (d) 4.68 (e) 3.85	30.6 53.2 61.5
Belgium-Luxembourg ‡	Franc	September 21	2.28	2.00	12.3
Burma	Rupee	September 18	30.23	21.00	30.5
Canada	Dollar	September 19	100.00	90.91	9.1
Ceylon	Rupee	September 19	30.23	21.00	30.5
Denmark	Krone	September 18	20.84	14.48	30.5
Egypt	Pound	September 19	413.30	287.16	30.5
Finland	Markka	September 19	(f) 0.6250	(f) 0.4348	30.4
France§	Franc	September 20	(g) 0.303# (h) 0.367#	0.286#	5.6 22.1
Germany—Western	Deutsche mark	September 19	(f) 30.00	(f) 23.81	20.6
Greece	Drachma	September 22	0.01#	0.0067	33.0
Iceland	Krona	September 20	15.41	10.71	30.5
India	Rupee	September 19	30.23	21.00	30.5
Iraq	Dinar	September 20	403.00	280.00	30.5
Ireland	Pound	September 18	403.00	280.00	30.5
Israel	Pound	September 18	403.00**	280.00	30.5
Italy	Lira	September 19	0.1739#	0.1576#	9.4
Netherlands¶	Guilder	September 20	37.70	26.32	30.2
New Zealand	Pound	September 19	(f) 399.96	(f) 277.89	30.5
Norway	Krone	September 18	20.15	14.00	30.5
Portugal	Escudo	September 21	4.00	3.48	13.0
Spain‖	Peseta	October 7	(a) 8.91 to 3.65 (b) 9.13 to 4.00	(a) 8.91 to 2.54 (b) 9.13 to 3.51	0.0 to 30.4 0.0 to 12.3
Sweden	Krona	September 20	(f) 27.82	(f) 19.32	30.5
Thailand	Baht	September 27	10.08	8.00	20.6
Union of South Africa	Pound	September 18	403.00	280.00	30.5
United Kingdom°	Pound	September 18	403.00	280.00	30.5

* In addition to the devaluations shown in the table, Paraguay, Peru, and Uruguay carried out in 1949 readjustments of their multiple-exchange-rate systems that amounted to substantial depreciations for some types of transactions.

† In some cases figures are rounded to simplify table.

‡ The Belgian Congo franc remains at par with the Belgian franc.

Rates based wholly or in part on dollar quotations in officially regulated free markets; new lira rate based on September 21, 1949 quotation, French franc on postdevaluation quotations.

§ All local currencies of French dependencies are pegged to the French franc except: (1) the rupee of the French possessions in India, which is maintained at par with the Indian rupee; and (2) the Djibouti franc, which retains its old dollar parity of 0.47 U. S. cents.

** In addition, a rate of approximately 300.00 was used for certain transactions.

¶ The Indonesian guilder remained at par with the Netherlands guilder during 1949; but the Surinam and West Indies guilders retain the old dollar parity of 53 U. S. cents.

‖ Representative rates applicable to specified commodity transactions.

° All local currencies of British dependencies, except British Honduras, have been devalued by 30.5 per cent; the British Honduras dollar has been devalued by 30.0 per cent.

(a) selling rates; (b) buying rates; (c) basic rate; (d) effective average rate; (e) premium rate; (f) middle rate: (g) free rate; (h) commercial rate.

Foreign Economic and Financial Conditions

The countries covered by the European Recovery Program, whose affairs continue to be a focal point of American foreign economic policy, made better internal progress during 1949 than seemed likely a year ago. Nevertheless, improvement in their balance of dollar payments was slow, leaving unanswered the question of their ability to close the "dollar gap" before Marshall Plan aid ends in 1952. The satisfactory rate of advance which these countries had shown in 1948 in meeting their dollar needs faltered during the spring of 1949 under the triple impact of: (1) the American recession, (2) the curtailment of American purchases from some foreign countries whose export prices were considered too high, and (3) the postponement of American purchases from and payments to some countries in the expectation that they would soon devalue their currencies. Some countries, principally the United Kingdom, had to resort to the sale of gold to keep their dwindling dollar balances at a working level.

By the middle of September, Europe's difficulties in closing the "dollar gap", together with rapidly mounting pressure on the British pound sterling, brought to a climax the economic imbalance between the dollar and "soft currency" areas. Led by sterling, a concentrated and unprecedented wave of currency devaluations swept over a good part of the world.

The only noticeable immediate effect of the devaluations was a rise in dollar balances of most of the devaluing countries, some of which converted a part of these increased dollar reserves into gold. Thus, gold and dollar reserves of foreign countries rose in the last quarter of 1949 by about 600 million dollars. In the first few months of 1950, this strengthening of foreign gold and dollar reserves has continued. Aside from this, the only observation that can be made concerning the immediately discernible effects of the currency devaluations of 1949 is that the unspectacular character of postdevaluation developments, up to the end of the year, is to some extent a cause for satisfaction. Among the consequences of an unfavorable nature that might have followed—but did not follow—close upon such widespread and substantial devaluations were a sharp drop in commodity prices in terms of dollars, pronounced repercussions upon the exports and internal economy of the United States, and rapid inflationary spirals abroad. Whether all of these unfavorable possibilities are to be permanently avoided, however, and the potential benefits inherent in the currency readjustments are to be finally realized, will depend in good part upon the progress of the European Recovery Program and upon the economic policies of the individual countries concerned.

The European Recovery Program

The Congress of the United States initiated the European Recovery Program in mid-1948 by appropriating 4 billion dollars for the twelve months from April 1948 to March 1949 and authorizing the Economic Cooperation Administration to borrow 1 billion from the Treasury for the purpose of granting loans to, and providing transfer guarantees for private American investment in, the ERP countries.[1] The program was carried forward in 1949 by a further appropriation of 4.9 billion dollars, of which 1.1 billion was allocated for grants during April-June 1949, and 3.7 billion for grants and 150 million for loans (through the Export-Import Bank) during the fiscal year 1949-50.

Assisted by the inflow of ECA-financed supplies, most of the ERP participants achieved, during 1949, significant increases of production, which contributed in turn to a great improvement in their internal financial stability. Despite less than average rainfall, grain harvests in most of these countries exceeded 1948 and closely approached the prewar average. Many of the ERP nations also reported an important expansion of industrial output during the first half of the year. By the third quarter, however, production was showing a tendency to level off and even to decline somewhat—the result apparently not only of mounting strain on productive capacity but also, in certain instances, of developing sales resistance in domestic as well as foreign markets. Although the year's improvements in output and in the over-all supply position thus were not unqualified, they reinforced the effectiveness of the existing monetary controls. Price levels remained encouragingly stable during the first three quarters of the year. The September currency devaluations touched off a chain of more or less significant price increases, but the economies of most of the ERP participants appear to have withstood the shock of devaluation remarkably well.

Unfortunately, the noteworthy progress achieved by Western European countries in terms of output and internal financial stability has not been accompanied by corresponding improvement in their bal-

[1] The 4 billion dollar appropriation was nominally for the fifteen months ended June 30, 1949, but included authority to the President, which he exercised, to commit the full amount by April 2, 1949.

ances of payments, particularly with respect to the dollar area. During the first nine months of 1949, Western European exports to all markets, in the aggregate, appeared to have stopped expanding, while exports to the dollar area fell off sharply during the first half of the year. In the case of the United Kingdom, the falling off of dollar earnings, accompanied as it was by other adverse developments, became so serious a threat to the British dollar position as to necessitate substantial cutbacks of dollar imports below the austerity levels already prevailing. Although the decline of European dollar earnings was arrested during the third quarter of the year and earnings have since recovered somewhat, the 1949 accomplishment has fallen short of earlier anticipations.

On the other hand, there has been significant progress in restoring intra-European trade. Trade among the ERP countries rose from hardly more than 55 per cent of the prewar level in 1947 to nearly 100 per cent in 1949. The pronounced recovery of European sources of supply has in turn lessened the excessive reliance of Western Europe upon United States goods, thereby facilitating the progressive reduction of ECA assistance.

The expansion of intra-European trade has been assisted by the intra-European payments plans for 1948-49 and 1949-50, under which the ECA has helped to finance the trade surpluses of the intra-European creditors through so-called "conditional" dollar aid grants. During 1949, the efforts of the ECA and of the Organization for European Economic Cooperation (the common agency of the ERP countries) to secure a freer flow of intra-European trade have been directed toward a comprehensive program having as its goal the ultimate unification of the various ERP economies into "a single large market within which quantitative restrictions on the movements of goods, monetary barriers to the flow of payments, and eventually all tariffs would be swept away."[2] The Council of the OEEC in July 1949 called for the progressive removal of quantitative restrictions on intra-European trade. In compliance with this resolution, most of the ERP member nations had, by the close of the year, abolished quantitative restrictions upon roughly 50 per cent of their imports on private account from intra-European sources.

Some progress has also been made in liberalizing the exchange restrictions that have hampered trade among the ERP member nations.

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[2] Address of Paul Hoffman to the Council of the OEEC on October 31, 1949.

Under the 1948-49 payments plan, the "drawing rights" extended by one ERP member to another could for all practical purposes be spent only in the market of the original donor. This rigid bilateralism was relaxed under the 1949-50 payments plan by a provision permitting each country to spend 25 per cent of its drawing rights in ERP markets other than that of the original donor. Proposals now under consideration by ECA and OEEC contemplate further liberalization of payments restrictions through the establishment of a European payments union.

The Currency Readjustments

While these steps toward a large and better integrated European market were being taken, the effects of currency devaluation, expected by many to reduce the need for discriminatory trade arrangements, were only beginning to work themselves out. The devaluations that began on September 18 involved the currencies of thirty-one countries (see page 32) accounting for approximately two thirds of all world trade. The movement started with the United Kingdom at a moment when British gold and dollar reserves had fallen to 1,329 million dollars and were being drained away at an annual rate of almost 1,400 million dollars. The United Kingdom was followed within one week by twenty-three countries, the remaining seven following a little more slowly.

The causes of this currency adjustment were of course more fundamental than the pressure, amounting to a "run," to which sterling seems to have been exposed last summer from traders all over the world. The existence of a very serious imbalance in the international economy was hardly open to doubt. Since the Marshall Plan was approaching mid-passage, intensified efforts to close the "dollar gap" were clearly required. For many months, the question had been debated in this country and abroad as to whether the gap could be closed by internal measures to be taken by the foreign countries concerned, by a further tightening of their direct controls over dollar purchases, or by exchange rate adjustments, and in what combination and what order of timing action should be taken. The issue, however, was largely forced by the mounting drain on the British reserves. Once the United Kingdom had made its decision, a similar course became a practical necessity for a large number of other countries.

The new exchange rate pattern, established with the formal approval of the International Monetary Fund, may be regarded as closer, on the whole, to economic realities than that which prevailed before devaluation. Yet it is by no means certain that each devaluation corresponded to the particular maladjustment that the devaluing country was facing. Nor has devaluation done away with all of the exchange rate practices that the International Monetary Fund considers undesirable. Most countries maintaining multiple-exchange-rate systems, for instance, have continued such practices, and a number of countries have not yet reached agreement with the Fund on uniform par values for their respective currencies.

The course of postdevaluation world trade and commodity prices has reflected the interaction between, on the one hand, the monetary influences set in motion by the currency readjustments, and on the other, the supply position of various commodities, the prevailing competitive conditions, and the world-wide pattern of demand. Three different effects of the devaluations upon world trade, and particularly American trade, could be anticipated. First, the devaluations may tend to curtail the demand for American goods; where this demand has been restricted by direct controls, they may make such controls more effective (or unnecessary). Second, the devaluations may tend to increase the international demand for many of the goods produced in the devaluing countries, since these goods can now compete more effectively. Finally, the devaluations may divert exports of devaluing countries away from soft-currency to hard-currency areas, since the latter have now been made more attractive as markets, although this shift appears to be at least partly counteracted by rising demand from some of the soft-currency areas.

The tendency of foreign countries, after devaluation, to curtail purchases in the American market appears so far to be a good deal stronger than the tendency towards greater sales to this country. During the final quarter of 1949, dollar disbursements of the devaluing countries declined noticeably, although it is impossible to determine whether this was the result primarily of devaluation or of the tighter restrictions against purchases from the dollar area that were initiated in many cases just before devaluation. As to the devaluing countries' exports to the United States, the postdevaluation picture, so far, differs from country to country and from one commodity group to another, but on balance some slight improvements attributable to the devaluations are discernible. From a long-run viewpoint, the currency readjustments have brought the devaluing countries a powerful stimulus to exports and deterrent to imports which—unless offset by renewed internal inflation—

should contribute effectively toward redressing the prevailing international imbalance.

With respect to the repercussions of the devaluations on prices of internationally traded commodities, dollar quotations have proved on the whole to be controlling for those primary commodities and manufactured goods that are still in short supply. As a result, the foreign-currency prices of primary commodities, including those produced in the sterling area, have experienced a rise that has confounded some earlier apprehensions of a widespread price decline. On the other hand, the fact that dollar prices of foreign manufactured goods have declined only moderately does not augur well for a rapid expansion of foreign sales to this country. The price structure of the United States itself has so far been little affected by the devaluations.

In the countries that have devalued, internal prices have risen to a varying extent. In some countries the impact of these price increases has been softened by controls and subsidies, but the increases have unquestionably given a new impulse to the inflationary pressures that still prevail in some European countries, and even more in some other areas. These price advances point to the necessity for continued firm anti-inflationary measures. The inflationary forces inherent in devaluation are likely to prove particularly strong in the present instance because, as already indicated, the internal prices of internationally traded commodities have risen in many cases by the full extent of devaluation and because full employment in most of the devaluing countries has not permitted a significant further expansion of production.

If these inflationary pressures can be successfully checked through monetary and fiscal policies of the countries concerned, a gradual shift toward a better balance of the international accounts of all countries should be attained. The need for such a shift, however, poses important questions of policy for the United States. Under present conditions of abnormally high exports and relatively low imports by this country, exporters, as well as domestic producers who are enjoying a market protected from foreign competition, tend to benefit at the expense of the whole community, which pays for the export surplus through foreign aid. Relief to the taxpayer through reduced foreign aid inevitably involves depriving the exporter or the domestic producer of a part of his markets. The proper apportionment of the burden among the three interested groups will be difficult, and no easy and early solution in terms of private capital exports appears probable.

Economic Development Abroad

Some steps to stimulate private American investment abroad and extend technical and financial assistance to economically underdeveloped areas were taken in 1949 as a result of the Point Four proposal advanced by President Truman. In his inaugural address of January 21, 1949, the President called for a ''bold new program for making the benefits of our scientific advances and industrial progress available for the improvement and growth of underdeveloped areas'', and for action ''to foster capital investment in areas needing development''.

A concrete program directed towards these ends began to take shape by midyear. The President requested an appropriation of 45 million dollars from Congress to expand the existing program of technical assistance to underdeveloped areas. At the same time he requested legislation to give the Export-Import Bank authority to start an experimental program of guarantees to United States investors abroad against such risks as inconvertibility of earnings, arbitrary expropriation, and war. In addition, negotiations were initiated for a series of bilateral treaties between the United States and other countries, designed in the main to assure United States investors of ''national'', or at least of ''most-favored-nation'', treatment with respect to their legal position, personnel, and business activities, as well as prompt and adequate compensation in the event of expropriation.[3] Finally, certain recommendations have been made by the National Advisory Council and by the President with respect to the need to eliminate international double taxation and the advisability of reducing United States taxes on income from foreign investment as incentive measures.

In his original proposals President Truman had urged that technical assistance be carried out largely through the United Nations and its specialized agencies. This recommendation gave fresh impetus to the United Nations technical assistance program and led the General Assembly in November to approve a comprehensive plan involving the expenditure of 86 million dollars in the first two years of operation.

Technical assistance which foreign countries actually received during 1949 consisted mainly of surveys of resources and the formulation of development plans. The International Bank for Reconstruction and Development sent a major mission to Colombia, and also missions to

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[3] A "Treaty of Friendship, Commerce, and Economic Development" with Uruguay was signed on November 23, 1949.

various other countries. The United Nations sponsored the Clapp Mission which surveyed the economic potentialities of the countries that had been most directly affected by the Palestine war. Finally, a joint commission of United States and Brazilian technicians completed a comprehensive study (begun in 1948) of the possibilities of Brazilian economic development. These activities were supported by continuing efforts in the underdeveloped countries themselves to draw up development programs which might be within their capacity if supported by a measure of foreign aid. Experience has indicated that over-ambitious plans, unsupported by indigenous administrative and technical skills necessary to carry them out, cannot be made successful by foreign advisors nor by foreign loans or grants. The effectiveness of technical and financial aid from abroad largely depends on the extent to which the governments of the recipient countries adapt their plans to their domestic capacities and then assume a positive role in carrying them out, and in pursuing suitable financial policies while doing so.

The proposals for fostering the flow of private capital abroad give rise to more difficult problems than do the technical assistance programs. Among the difficult problems are the following: To what extent is it appropriate for the United States Government to guarantee private ventures in the foreign field? Granted that such guarantees are appropriate under present circumstances, what risks can legitimately be covered without the likelihood of serious abuse? Should guarantees against foreign currency inconvertibility apply only to the earnings from foreign investment or also to the eventual repatriation of the principal? Are old as well as new investments to be offered guarantees? Can a system of tax incentives to increase the net return on foreign investment be devised without impairing the equity of our tax system?

If all these and other technical problems connected with the creation of special incentives can be satisfactorily resolved, serious obstacles to the outflow of private United States capital remain. The rewards of capital at home are still attractive. The foreign fields that have traditionally attracted the bulk of American direct investment, such as public utilities and mining (including petroleum), are becoming in many countries the prerogatives of the governments. Portfolio investment, as an alternative investment form, has not recovered from the debacle of the 1930's.

The United States Balance of Payments

The balance of payments of this country in 1949 reflected both current economic and financial developments in foreign countries and the year's changes in domestic income and employment. Our exports of goods and services fell from 16.8 billion dollars in 1948 to approximately 15.9 billion in 1949, while imports of goods and services fell from 10.5 billion dollars to 9.8 billion. The export drop was in line with the past three years' decrease in the foreign need for American goods and services. The fall in imports, on the other hand, resulted partly from the decline in domestic business activity during the first half of 1949, and apparently also in part from a temporary postponement of purchases from abroad in anticipation of the September currency devaluations. A moderate decline in the prices of foreign raw materials was also a factor, although prices of certain imports—notably coffee and wool—rose to new high levels. As a result of these divergent developments, the United States current account surplus declined only 0.2 billion dollars, from 6.3 billion in 1948 to 6.1 billion in 1949.

The over-all figures for 1949, however, do not give an adequate picture of developments during the course of the year. In the first six months the annual rate of exports actually exceeded that of the year previous. At the same time imports fell short of the 1948 rate; in particular, imports from Europe declined, thus upsetting previous hopes that the large United States export surplus with that area, financed primarily with ECA funds, would be steadily reduced. The effect of these developments was a rise of this country's January-June surplus on current account to an annual rate of 7.5 billion dollars. In consequence, the flow of Government grants and loans proved insufficient to finance the "dollar gap", and foreign countries again had to tap their dwindling gold and dollar reserves.

In the last six months of the year, this trend toward greater imbalance was reversed. As a result of new restrictions abroad against imports payable in dollars, and of the foreign currency devaluations, United States exports of goods and services fell to an annual rate of 14.5 billion dollars, while this country's disbursements of dollars for merchandise imports and tourist and other services crept upward. The export surplus during the second half of the year was thus reduced to an annual rate of about 4.9 billion dollars, the lowest since the end of the war.

By far the larger part of our 1949 export surplus was financed by the various foreign aid programs, more than 4 billion dollars being expended for the European Recovery Program, 1 billion for Army relief in the occupied areas, and 170 million for aid to Greece and Turkey. Of the total ERP disbursements, 2.6 billion dollars was spent directly in the United States, 1.1 billion was used for offshore purchases in Canada, Latin America, and other countries, and the remainder went for shipping charges.

The contribution of the Export-Import Bank to the financing of the export surplus during 1949 continued on a limited scale. New loan authorizations aggregated 241 million dollars (compared with 138 million in 1948), loans being approved for Afghanistan, Bolivia, Chile, Israel, and Yugoslavia. Gross disbursements amounted to 185 million dollars, but, because of repayments of 144 million, net disbursements amounted to 41 million only.

The International Bank stepped up the volume of new operations in 1949, authorizing loans totaling 219 million dollars to Belgium, Brazil, Colombia, Finland, India, Mexico, the Netherlands, El Salvador, and Yugoslavia. Total loan commitments of the Bank from the beginning of its operations to the end of the year aggregated 744 million dollars. Disbursements in 1949 amounted to 68 million dollars, compared with 199 million in 1948. Sales of exchange (mostly U. S. dollars) by the International Monetary Fund, which aggregated 468 million dollars in 1947 and 208 million in 1948, declined to 100 million in 1949, the chief recipient countries being Australia, Brazil, India, and Yugoslavia.

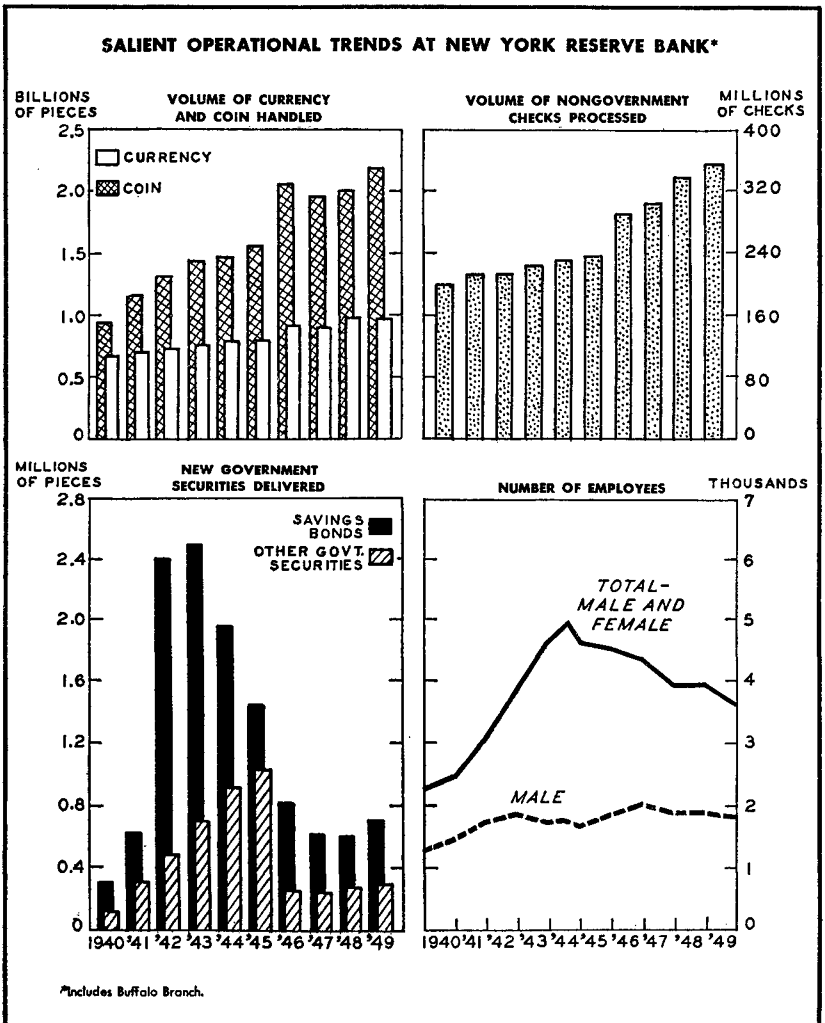
The gross outflow of United States private capital in 1949 amounted to approximately 1,900 million dollars, but a large part of this was accounted for by capital expenditures on American oil properties in Latin America and in the Near East, and by the reinvestment of funds earned by foreign subsidiaries of American corporations. The gross outflow was partly offset, moreover, by an inflow of American capital of about 800 million dollars and a small net increase of foreign-owned long-term investment in this country.

Volume and Trend of the Bank's Operations

Domestic Operations

In 1949, as in other recent years, the volume of the bank's domestic business was substantially above prewar levels. There was some further contraction in fiscal agency operations, but the normal peacetime operations remained near or exceeded the peaks of previous years.

During the war the enlargement of the bank's fiscal agency operations, as well as the assumption of certain temporary work for the United States Treasury, necessitated a large increase in the bank's staff. The accompanying chart shows that peak employment in the bank was attained in July 1944, when the total staff reached 4,940, or approximately double the number employed in the prewar year 1939. During the remainder of the war and postwar periods, employment at the bank contracted; temporary work for the Treasury largely ceased



and the bank promoted efficiency through the use of better techniques and more and better equipment in handling the enlarged peacetime operations. Because of this larger volume of normal work, the decline in employment was not so great or so sharp as the previous rise had been. At the end of 1949, the total number of people employed amounted to 3,611, or about 50 per cent above the 1939 level. The bulk of the wartime rise in employment and of the subsequent decline took place among the women employees of the bank.

Fluctuations in employment have occurred principally in functions set up to facilitate the war effort. The Foreign Funds Control Department was created in 1941 to act, in effect, as the field office of the United States Treasury in administering the controls over the blocked assets of certain foreign countries; the Department was liquidated as of June 1, 1949. The Government Check Department was expanded rapidly during the war and has since operated on a reduced but substantial scale. Fiscal agency operations for the United States Government in connection with the issue, redemption, and exchange of securities expanded and contracted sharply, as did fiscal agency operations for the Reconstruction Finance Corporation. One section of the chart shows the sharp rise and decline in the number of Savings bonds and other Government securities issued through this bank in each year since 1940. The chart indicates that during the peak year (1943) the bank issued 3.2 million individual Savings bonds and other Treasury securities, whereas the annual total is now down to about one million pieces—which is still more than twice the 1940 level.

The growth in volume of two of the most important regular operations of the bank, namely, meeting the public need for currency and coin and facilitating the collection and clearance of checks, is also indicated in the accompanying charts. In 1949, the volume of coin handled, as measured by the number of pieces counted (2.2 billion), was the highest on record and more than double the 1939 volume. The number of pieces of paper currency sorted and counted (968 million) was slightly below the 1948 record high level but still 47 per cent above the 1939 level.

The number of checks of businesses and individuals collected and cleared during 1949 reached a record figure—356 million, or more than one million checks per business day. The number of United States Government checks cleared and collected in 1949 increased by approximately 10 per cent to 44.4 million items, but the dollar volume receded

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

	1949	1948
Number of pieces handled*		
Discounts and advances	2,257	2,720
Currency received and counted	967,773,000	978,239,000
Coin received and counted	2,182,874,000	2,000,994,000 r
Gold bars and bags of gold coin handled	168,000	317,000
Checks handled:		
United States Government checks	44,392,000	40,444,000
All other	356,095,000	338,976,000
Collection items handled:		
United States Government coupons paid	5,729,000	6,162,000
All other	5,570,000	5,634,000
Disbursements as fiscal agent for		
Reconstruction Finance Corporation, its subsidiaries, and Commodity Credit Corporation	28,000	30,000
Issues, redemptions, and exchanges by fiscal agency departments:		
United States Savings bonds	22,907,000	22,597,000
All other United States obligations	2,729,000	3,158,000
Obligations of the International Bank for Reconstruction and Development	16,000	190,000
Safekeeping of securities:		
Pieces received and delivered	4,471,000	4,243,000
Coupons detached	1,711,000	1,551,000
Transfers of funds†	235,000	225,000
Incoming and outgoing mail:		
Registered	407,000	472,000
Ordinary	9,211,000	9,376,000
Amounts handled		
Discounts and advances	$ 12,563,787,000	$ 7,760,124,000
Currency received and counted	6,101,253,000	6,352,616,000
Coin received and counted	175,281,000	160,255,000 r
Gold bars and bags of gold coin handled	2,353,838,000	4,184,698,000
Checks handled:		
United States Government checks	14,854,411,000	20,687,994,000
All other	209,388,256,000	209,221,357,000
Collection items handled:		
United States Government coupons paid	1,428,259,000	1,519,420,000
All other	866,267,000	798,876,000
Disbursements as fiscal agent for		
Reconstruction Finance Corporation, its subsidiaries, and Commodity Credit Corporation	441,120,000	500,266,000
Issues, redemptions, and exchanges by fiscal agency departments:		
United States Savings bonds	2,218,828,000	2,505,974,000
All other United States obligations	221,491,033,000	263,940,171,000
Obligations of the International Bank for Reconstruction and Development	30,636,000	260,023,000
Safekeeping of securities:		
Securities received and delivered (par value)	390,454,757,000	460,507,275,000
Transfers of funds†	132,063,441,000	120,443,671,000

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

† Includes wire and mail transfers; excludes Treasury transfers and Reserve Bank inter-district settlements.

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by 28 per cent, reflecting a decline in the average amount of the individual checks processed. The number and dollar total of Government checks processed in 1949 were only slightly more than two fifths the number and dollar volume processed in the closing war years. Collection items handled (acceptances, notes, drafts, and coupons credited upon collection rather than immediately or in accordance with a time schedule) were in about the same number and dollar volume as in 1948. In the safekeeping function, the number of securities received and delivered was moderately higher than in 1948, but the dollar volume decreased rather sharply. There was an increase in the number of coupons detached from securities held in safekeeping and collected. Transfers of funds (mostly telegraphic) were a little greater in number and 10 per cent higher in dollar volume during 1949.

Foreign and International Operations

Total assets held at the Federal Reserve Bank of New York for foreign and certain international accounts combined rose during 1949 to around 8 billion dollars, or close to the peak reached in February 1947. Gold and dollar assets held for the International Bank and International Monetary Fund declined by a moderate amount, but assets held for foreign central banks and governments increased by 702 million dollars, continuing at a somewhat reduced rate the upward trend which has been in evidence since the latter part of 1947. Despite this upward trend, the total held for foreign accounts alone (4,956 million dollars at the end of 1949) remained considerably below the peak of 6,971 million dollars reached in September 1945. The net increase in foreign assets during 1949, while distributed among all kinds of accounts, was largely in the form of earmarked gold and deposits, which rose by 482 million dollars and 124 million dollars, respectively.

The year 1949 witnessed a decline in loans on gold to foreign central banks. The total of such loans outstanding, which had risen to a record high of 259.7 million dollars in August 1948, receded to 69.5 million dollars by the end of 1949. At the close of 1948 loans were outstanding to four European central banks and one Latin American central bank. Three of these loans were retired in full during 1949, and the other two are expected to be liquidated during 1950. During the year new loans were made to two central banks (and there were several renewals).

The policy of the bank with respect to gold loans remained unchanged, i.e., loans were generally made for an initial period of up to three months to meet temporary (usually seasonal) dollar deficiencies, and renewals were made for limited periods where it appeared that they would serve a useful purpose and were not to be substituted for long-term needs. The loans are fully secured by gold held in our vaults and bear interest at the bank's current discount rate (1½ per cent per annum during 1949).

With respect to foreign correspondent relationships, a regular account was opened during the year for the newly-organized Central Bank of the Philippines, while one wartime account which had been maintained for a foreign government was closed, practically bringing to an end the phase of wartime operations. An account was also opened for the World Health Organization, an agency of the United Nations, the bank acting as fiscal agent of the United States in this case.

The over-all volume of transactions handled for foreign and international accounts in 1949 was somewhat smaller than in 1948. Security transactions and dollar payments and receipts increased, while the number of gold transactions, gold loans, and collections handled declined.

The Federal Reserve Bank of New York continued as the United States depository of the International Bank and the International Monetary Fund. The custody of securities, earmarking of gold, and handling of investments in United States Government securities were among the more important functions executed in this capacity.

Financial Statements

Statement of Condition

During 1949 this bank's total assets showed the first substantial contraction (1,292 million dollars) since 1941. The contraction was caused principally by a moderate reduction in total gold certificate reserves and by a sizable decline in the volume of earning assets, i. e., discounts and advances and Government security holdings.

The decline in total gold certificate reserves, amounting to 146 million dollars, followed three successive postwar years of expansion during which such reserves had increased 2,413 million dollars, or 48 per cent. The principal cause of the 1949 decline was the unfavorable balance of the Second Federal Reserve District, relative to the remainder of the United States, in commercial and financial payments through the Interdistrict Settlement Fund. A contributory influence was the sharp diminution in the net gold inflow from abroad. In 1949, the Treasury's credits to the gold certificate fund of this bank against the net volume of incoming gold offset only a portion of the bank's losses of funds to other sections of the country, whereas in 1947 and 1948, when gold imports were substantial, the gold certificate fund credits were greater than the losses through domestic transfers.

Among the earning assets of the bank, discounts and advances at the end of 1949 were only 23 million dollars — 55 million lower than at the close of 1948. The 1949 year-end total represented almost exclusively loans to foreign central banks; only 1 million dollars consisted of advances to member banks secured by Government securities. The low year-end volume of advances to member banks, however, does not by any means measure the member banks' use of the borrowing privilege. Their average borrowings increased 62 per cent during 1949 to the highest level since 1945.

Reflecting its share of a larger decline for all Reserve Banks, this

Assets of the Federal Reserve Bank of New York
(In thousands of dollars)

Assets	Dec. 31, 1949	Dec. 31, 1948
Gold certificates	$ 7,250,198	$ 7,390,440
Redemption fund for Federal Reserve notes	49,736	55,182
Total gold certificate reserves	$ 7,299,934	$ 7,445,622
Other cash	$ 41,720	$ 42,544
Discounts and advances	$ 23,377	$ 78,700
U. S. Government securities:		
Bills	$ 1,144,483	$ 1,317,805
Certificates	1,487,219	1,457,291
Notes	133,236	189,560
Bonds	1,710,523	2,632,140
Total U. S. Government securities	$ 4,475,461	$ 5,596,796
Total loans and securities	$ 4,498,838	$ 5,675,496
Due from foreign banks	$ 12*	$ 16*
Federal Reserve notes of other banks	24,251	20,331
Uncollected items	546,227	507,096
Bank premises	7,872	8,022
Other assets	23,584	35,252
Total assets	$12,442,438	$13,734,379
* After deducting participation of other Federal Reserve Banks amounting to	$ 26	$ 33

bank's total holdings of United States Government securities decreased 1,121 million dollars to 4,475 million on December 31, 1949, the lowest year-end level since 1943. Most (922 million) of the decline occurred in Treasury bonds and represented primarily the New York bank's portion of System Open Market Account sales made prior to the June 28 announcement of the Federal Open Market Committee (see page 23). Treasury bill and note holdings receded 173 million dollars and 56 million dollars, respectively, during the year, while certificates of indebtedness rose 30 million dollars. The effect upon the bank's Treasury bill holdings of substantial cash redemptions of bills (by System Open Market Account) during the year was largely offset by net market purchases to supply member banks with needed reserves during periods of reserve stringency. The Treasury's refunding of outstanding notes

Liabilities of the Federal Reserve Bank of New York
(In thousands of dollars)

Liabilities	Dec. 31, 1949	Dec. 31, 1948
Federal Reserve notes	$ 5,430,281	$ 5,582,297
Deposits:		
Member bank—reserve account	$ 5,347,438	$ 6,701,274
U. S. Treasurer—general account	255,479	184,745
Foreign	246,250*	209,368*
Other	464,380	430,977
Total deposits	$ 6,313,547	$ 7,526,364
Deferred availability items	$ 446,139	$ 390,868
Other liabilities	2,303	2,670
Total liabilities	$12,192,270	$13,502,199
Capital accounts:		
Capital paid in	$ 72,425	$ 69,333
Surplus (Section 7)	148,149	143,019
Surplus (Section 13b)	7,319	7,319
Other capital accounts	22,275	12,509
Total capital accounts	$ 250,168	$ 232,180
Total liabilities and capital accounts	$12,442,438	$13,734,379
Contingent liability on acceptances purchased for foreign correspondents	$ 3,319†	$ 1,065†
Ratio of gold certificate reserves to deposit and Federal Reserve note liabilities combined	62.2%	56.8%
* After deducting participation of other Federal Reserve Banks amounting to...	$ 520,250	$ 432,276
† After deducting participation of other Federal Reserve Banks amounting to...	7,188	2,264

and bonds with certificates of indebtedness in January, June, and September was the dominant factor increasing this bank's holdings of certificates. In the case of Treasury note holdings, exchanges during the year were more nearly in balance and the decline arose principally from net market sales.

Federal Reserve notes of this bank outstanding in the hands of the public decreased 152 million dollars, or 2.7 per cent, during 1949, compared with a decrease of 184 million dollars, or 3.2 per cent, in 1948.

Member bank reserve accounts declined 1,354 million dollars in 1949 whereas they had risen 1,128 million in 1948. The 1949 reduction reflected the lessened need for reserves by member banks as the Reserve System during the spring and summer reduced the percentages of reserves which member banks are required to hold against net demand and time deposits. During 1948, when credit policy had been directed toward restraining the expansion of bank credit and of the money supply, the Board of Governors had raised reserve requirements, and member banks had had to build up their reserve accounts substantially. Deposits of foreign banks and governments held at the New York Reserve Bank increased 125 million dollars during 1949. The New York bank's share of those accounts (which are participated among the 12 Reserve Banks) together with certain accounts which this bank holds as fiscal agent of the United States, increased by 37 million dollars. The general account of the U. S. Treasurer increased 71 million dollars during the year and "Other" deposits advanced 33 million dollars.

Capital accounts in the aggregate increased nearly 18 million dollars during the year. Approximately 5.1 million dollars of net earnings was added to the regular surplus (Section 7) and 9.8 million dollars was added to reserves included in "Other capital accounts". "Capital paid in", reflecting payments for additional shares by member banks which increased their own capitalization (either by the reinvestment of earnings or by the sale of new capital stock), rose 3.1 million dollars.

As a result of proportionately greater declines in this bank's deposit and note liabilities than in its gold certificate reserves, the ratio of gold certificate reserves to the combined deposit and note liabilities increased sharply during 1949 to 62.2 per cent, the highest year-end ratio since 1943.

Earnings and Expenses

Gross earnings of the Federal Reserve Bank of New York rose

2.4 million dollars in 1949 to a record high of 75.6 million. This rise was occasioned almost entirely by an increase in income from Government securities, reflecting the effect of a greater average volume of Treasury bond holdings (in contrast to the reduced year-end holdings) and also somewhat higher average annual yields on shorter-term Treasury obligations. Total income from advances remained small and approximately unchanged from the 1948 level. A rise in income from advances to member banks secured by Government securities, which reflected both higher rates and a higher average volume, was just about counterbalanced by a decline in income from a lower average volume of loans to foreign banks secured by gold.

Net expenses increased 900,000 dollars to 17.4 million dollars, reflecting moderate salary increases and generally heavier expenses of operation, including the cost of supplying Federal Reserve currency. After deducting net expenses, current net earnings amounted to 58.3

Profit and Loss Account
For the Calendar Years 1949 and 1948
(In thousands of dollars)

	1949	1948
Earnings	$ 75,640	$ 73,223
Net expenses	17,350	16,467
Current net earnings	$ 58,290	$ 56,756
Additions to current net earnings:		
Profit on U. S. Government securities sold (net)	$ 7,653	$ 1,502
All other	7	4
Total additions	$ 7,660	$ 1,506
Deductions from current net earnings:		
Reserves for contingencies	$ 9,765	$ 9,884
Retirement System (Adjustment for revised benefits)	667	—
All other	3	4
Total deductions	$ 10,435	$ 9,888
Net earnings	$ 55,515	$ 48,374
Dividends paid	$ 4,220	$ 4,142
Paid United States Treasury (Interest on Federal Reserve notes)	46,165	39,809
Transferred to surplus (Section 7)	5,130	4,423
Surplus (Section 7) beginning of year	$ 143,019	$ 138,596
Addition as above	5,130	4,423
Surplus (Section 7) end of year	$ 148,149	$ 143,019

million dollars, or 1.5 million more than in 1948. Additions to current net earnings consisted almost entirely of the net profits on sales of Government securities, and amounted to 7.7 million dollars. Deductions from current net earnings were made for the purpose of adding to reserves for contingencies and for payments to the retirement system, and totaled 10.4 million dollars.

Net earnings after all adjustments but before dividends totaled 55.5 million dollars, or 7.1 million more than in 1948. The usual statutory dividend of 6 per cent, amounting to 4.2 million dollars, was paid to the member banks. Of the remaining net earnings, 46.2 million dollars, or 90 percent, was transferred to the United States Treasury in payment of an interest charge on Federal Reserve notes levied by the Board of Governors of the Federal Reserve System under Section 16 of the Federal Reserve Act. The balance of the year's earnings, 5.1 million dollars or 10 per cent of net earnings after dividends, was transferred to the bank's regular (Section 7) surplus account.

Changes in Membership

Three State banks and trust companies in the Second District were admitted to membership in the Federal Reserve System during 1949. There was a net decline of 13 banks in the District membership, however,

Number of Member and Nonmember Banks in Second Federal Reserve District at End of Year
(Exclusive of savings banks, private bankers, and industrial banks)

Type of bank	December 31, 1949			December 31, 1948		
	Members	Non-members	Per cent members	Members	Non-members	Per cent members
National banks	526	0	100	532	0	100
State banks and trust companies	244	116	68	251	115	69
Total	770	116	87	783	115	87

Changes in Federal Reserve Membership in Second District during 1949

Total membership beginning of year	783
Increases:	
State banks and trust companies admitted	3
Decreases:	
Member banks combined with other members	13
Withdrawals from membership	3
Total membership end of year	770

owing to mergers of 13 member banks with other members and the withdrawal from membership of 3 banks because of the statutory capital requirements for member banks with branches.[1] At the end of the year, there were 770 member banks, which constituted 87 per cent of all national banks, State banks, and trust companies in the District and which held 95.6 per cent of the total assets of all such institutions. All national banks are members and 68 per cent of the State banks and trust companies in this District are also members.

Changes in Directors and Officers

In July 1949, Marion B. Folsom, Treasurer and Director of the Eastman Kodak Company, Rochester, N. Y., was elected by member banks in Group 2 as a Class B director for the term ending December 31, 1950, to fill the vacancy caused by the resignation of Charles E. Adams, Chairman of the Board of the Air Reduction Company, Incorporated, New York.

At a regular election in the fall of 1949, John C. Traphagen, Chairman of the Board of the Bank of New York and Fifth Avenue Bank, New York, was elected by member banks in Group 1 as a Class A director for a term of three years, beginning January 1, 1950, to succeed Winthrop W. Aldrich, Chairman of the Board of The Chase National Bank of the City of New York, whose term expired on December 31, 1949. At the same time, Lewis H. Brown, Chairman of the Board of the Johns-Manville Corporation, New York, was reelected by member banks in Group 1 as a Class B director for a three-year term beginning January 1, 1950.

In December, the Board of Governors of the Federal Reserve System redesignated Robert T. Stevens, Chairman of the Board of J. P. Stevens & Co., Inc., New York, as Chairman and Federal Reserve Agent for the year 1950. William I. Myers, Dean of the New York State College of Agriculture, Cornell University, Ithaca, N. Y., was reappointed Deputy Chairman for the year 1950.

In December also, the directors of this bank appointed Bernard E. Finucane, President of the Security Trust Company of Rochester, a director of the Buffalo Branch for a term of three years, beginning January 1, 1950, to succeed Raymond F. Leinen, Executive Vice President of the Lincoln Rochester Trust Company, Rochester, whose term

[1] The Federal Reserve System has urged modification of capital requirements in such cases to remove this obstacle to membership.

expired on December 31, 1949. George F. Bates, President of the Power City Trust Company, Niagara Falls, N. Y., was also appointed a director of the Buffalo Branch for a term of three years, beginning January 1, 1950. Mr. Bates succeeds C. George Niebank, President of the Bank of Jamestown, Jamestown, N. Y., whose term expired on December 31, 1949. The Board of Governors appointed Edgar F. Wendt, President of the Buffalo Forge Company, Buffalo, N. Y., as a director of the Buffalo Branch for a term of three years, beginning January 1, 1950.

The directors of this bank designated Lewis B. Swift, President of the Taylor Instrument Companies, Rochester, N. Y., as Chairman of the Board of Directors of the Buffalo Branch for the year 1950.

Changes in Officers

Walter C. Warner, formerly Acting Manager of the Credit and Discount Departments, was appointed a Manager, effective June 23, 1949, his assignment to those departments being continued.

Curtis R. Bowman, formerly Manager of the Government Bond and R.F.C. Custody Departments, was appointed Assistant General Auditor, effective October 1, 1949.

James J. Carroll, Manager of the Planning Department, was also appointed Assistant Secretary, effective October 1, 1949.

John J. Clarke, formerly Assistant Secretary, was appointed Secretary, effective October 1, 1949, succeeding William F. Treiber in that office. Mr. Treiber continued as an Assistant Vice President, and Mr. Clarke as an Assistant Counsel.

Marcus A. Harris, formerly Assistant General Auditor, was reappointed a Manager and assigned to the Government Bond and R.F.C. Custody Departments, effective October 1, 1949. He continued in that assignment until January 5, 1950, when he was appointed an Assistant Vice President.

Harold A. Bilby, formerly an Assistant Vice President, was appointed a Vice President, effective January 5, 1950.

Member of Federal Advisory Council

At its meeting on January 5, 1950, the Board of Directors of this bank selected N. Baxter Jackson, Chairman of the Board of Directors of the Chemical Bank & Trust Company, New York, N. Y., to serve during the year 1950 as the member of the Federal Advisory Council from the Second Federal Reserve District.

Directors and Officers

Class	Group	DIRECTORS	Term expires Dec. 31
A	1	JOHN C. TRAPHAGEN Chairman of the Board, Bank of New York and Fifth Avenue Bank, New York, N. Y.	1952
A	2	FREDERIC E. WORDEN Chairman of the Board, and President, The National Bank of Auburn, Auburn, N. Y.	1950
A	3	ROGER B. PRESCOTT President, The Keeseville National Bank, Keeseville, N. Y.	1951
B	1	LEWIS H. BROWN Chairman of the Board, Johns-Manville Corporation, New York, N. Y.	1952
B	2	MARION B. FOLSOM Treasurer and Director, Eastman Kodak Company, Rochester, N. Y.	1950
B	3	JAY E. CRANE Director, Standard Oil Company (New Jersey), New York, N. Y.	1951
C		ROBERT T. STEVENS, *Chairman, and Federal Reserve Agent* Chairman of the Board, J. P. Stevens & Co., Inc., New York, N. Y.	1950
C		WILLIAM I. MYERS, *Deputy Chairman* Dean, New York State College of Agriculture, Cornell University, Ithaca, N. Y.	1951
C		Vacancy	1952

DIRECTORS — BUFFALO BRANCH	Term expires Dec. 31
LEWIS B. SWIFT, *Chairman* President, Taylor Instrument Companies, Rochester, N. Y.	1950
CLYDE C. BROWN President, The Cuba National Bank, Cuba, N. Y.	1950
GEORGE G. KLEINDINST President, Liberty Bank of Buffalo, Buffalo, N. Y.	1951
CARL G. WOOSTER Farmer, Union Hill, N. Y.	1951
GEORGE F. BATES President, Power City Trust Company, Niagara Falls, N. Y.	1952
BERNARD E. FINUCANE President, Security Trust Company of Rochester, Rochester, N. Y.	1952
EDGAR F. WENDT President, Buffalo Forge Company, Buffalo, N. Y.	1952

MEMBER OF FEDERAL ADVISORY COUNCIL

N. BAXTER JACKSON,

Chairman of the Board of Directors, Chemical Bank & Trust Company, New York, N. Y.

OFFICERS

ALLAN SPROUL, *President*
LESLIE R. ROUNDS, *First Vice President*
HAROLD A. BILBY, *Vice President*
HERBERT H. KIMBALL, *Vice President*
L. WERNER KNOKE, *Vice President*
WALTER S. LOGAN, *Vice President and General Counsel*

JOHN H. WILLIAMS, *Economic Adviser*
ARTHUR PHELAN, *Vice President*
HAROLD V. ROELSE, *Vice President*
ROBERT G. ROUSE, *Vice President*
VALENTINE WILLIS, *Vice President*
REGINALD B. WILTSE, *Vice President*

TODD G. TIEBOUT, *Assistant General Counsel*

RUFUS J. TRIMBLE, *Assistant General Counsel*

DONALD J. CAMERON, *Assistant Vice President*
FELIX T. DAVIS, *Assistant Vice President*
NORMAN P. DAVIS, *Assistant Vice President*
MARCUS A. HARRIS, *Assistant Vice President*
SILAS A. MILLER, *Assistant Vice President*

HORACE L. SANFORD, *Assistant Vice President*
WILLIAM F. SHEEHAN, *Chief Examiner*
OTTO W. TENEYCK, *Assistant Vice President*
WILLIAM F. TREIBER, *Assistant Vice President*
JOHN H. WURTS, *Assistant Vice President*

WILLIAM F. ABRAHAMS, *Manager, Security Custody Department*
HARRY M. BOYD, *Manager, Safekeeping Department*
ROBERT H. BROME, *Assistant Counsel*
WESLEY W. BURT, *Manager, Savings Bond Department*
JAMES J. CARROLL, *Manager, Planning Department, and Assistant Secretary*
JOHN J. CLARKE, *Secretary, and Assistant Counsel*
HOWARD D. CROSSE, *Manager, Bank Relations Department*
PAUL R. FITCHEN, *Manager, Cash Department*
WILLIAM A. HEINL, *Manager, Personnel Department*
PETER P. LANG, *Manager, Accounting Department*

SPENCER S. MARSH, JR., *Manager, Securities Department*
MICHAEL J. MCLAUGHLIN, *Manager, Cash Custody Department, and Manager, Government Check Department*
O. ERNEST MOORE, *Manager, Research Department*
FRANKLIN E. PETERSON, *Manager, Collection Department*
WALTER H. ROZELL, JR., *Manager, Foreign Department*
RALPH W. SCHEFFER, *Manager, Service Department*
CHARLES N. VAN HOUTEN, *Manager, Government Bond Department, and Manager, R.F.C. Custody Department*
WALTER C. WARNER, *Manager, Credit Department, and Manager, Discount Department*
ROY E. WENDELL, *Manager, Check Department*
HAROLD M. WESSEL, *Manager, Accounting Department*

WILLIAM H. DILLISTIN, *General Auditor*
CURTIS R. BOWMAN, *Assistant General Auditor*

OFFICERS—BUFFALO BRANCH

INSLEY B. SMITH, *General Manager*
HALSEY W. SNOW, *Cashier*
GEORGE J. DOLL, *Assistant Cashier*
M. MONROE MYERS, *Assistant Cashier*