

FORTY YEARS OF THE FEDERAL RESERVE SYSTEM

by Karl R. Bopp

INTRODUCTION

1. Happy to be here
2. Regret circumstances
3. Pete (J.M.Peterson) a representative of finest in System  
We could ill afford to lose
4. Consideration of life and death leads one to take  
a longer view
5. Many times someone has thought he has had the  
FINAL answer
6. As Mr. Justice Holmes once said:  
To rely (rest ?) on a formula is a slumber, that  
prolonged means death.

Forty years in forty minutes!

I commend to you the 1953 Annual Report of the Federal Reserve  
Bank of Minneapolis - feature article on 40 years of the System

Federal Reserve System arose out of the Panic of 1907  
when you simply could not get money and the call money rate went to 125%

Reserve Banks established so they could create new money and  
reserves in such cases  
Also for seasonal currency needs

In general to adjust the quantity of money and credit to the  
needs of the economy

Essential Nature of Central Banks

- (a) With unused authority to issue currency and reserves  
for member banks to expand
- (b) With a portfolio of earning assets that it can  
dispose of to contract
- (c) Institution operating in the Public Interest

In forty years we have gained increasing comprehension  
of this basic nature

Persistent problems

Objectives  
Instruments  
Guides  
Effectiveness  
Organization

## I. Objectives of Policy

- A. General: promote stable economic progress
- B. Possible specific objectives and their implications
  - 1. Convertibility: expand with more gold - contract when less  
On gold standard: did not prevent panic of 1907 - or  
great depression of 1932
  - 2. Productive credit: seductively appealing  
but how can you tell when productive?  
e.g. 1946 borrow to buy motors for refrigerators  
(The money value not physical quantity of output)
  - 3. A fixed rate of interest: experience 1946 to the accord
  - 4. Stable price level: can we be sure? late 1920's?
  - 5. Full employment: inflationary bias if at any wage rate
- C. Possible conflicts and need for choice or combination  
e.g. last fifteen months
  - 1. We lost  $1\frac{1}{4}$  billion gold
  - 2. Prices - wholesale and retail levels stable but agriculture down
  - 3. Unemployment doubled to 3,745,000

## II. Instruments

- A. Discounting and Discount Rate  
eligibility theory - didn't work out  
Limits? How expand when No one will borrow?  
How contract when no one is borrowing?
- B. Open market  
How contract when you have no portfolio  
- or it is less than excess reserves? 1930's
- C. Changes in Reserve Requirements of member banks
- D. Selective instruments

## III. Guides to current actions

- A. Application of principles to current developments
- B. Time lags
  - 1. In collection, tabulation, and analysis of information
  - 2. Between an act of policy and its effects
- C. Information of past or  
Projections of the future

IV. Effectiveness of operations

- A. Appropriate action a necessary but not a
- B. Sufficient condition to assure stable progress
- C. Effectiveness and the business cycle

V. Organization

- A. Relation to Government
  - Not to executive but to legislature
  - Objection: can't move fast enough
  - Answer: can when necessary
- B. Internal
  - 1. A Federal system
  - 2. Group judgment
- C. Outside criticism and support

VI. Experience and the future

- A. A central banker must work against the current wave of optimism and pessimism
  - Unpopular
  - But not dogmatic - must have an open - not drafty - mind
- B. In the 20's we thought monetary policy all powerful  
In the 30's we concluded it is impotent - fiscal policy everything  
In the 40's we found that to ignore money is dangerous  
Now, in the 50's we remember the 30's and know it is not omnipotent  
we remember the 20's and 40's and know we  
cannot even hope to achieve stable growth  
without appropriate monetary policy
- C. But most important, I believe, is a recognition of the complexity of the problems that confront us, how difficult it is to have sound judgment, the consequences of mistakes - hence humility  
Yet must act on judgment: courage