TIGHT MONEY AND ITS COMMERCIAL BANKING IMPLICATIONS

Panel Discussion before the
Philadelphia Chapter, Robert Morris Associates

KARL R. BOPP - Vice President, Federal Reserve Bank of Philadelphia

WM. R. K. MITCHELL - Chairman of Board, Provident Trust Co. of Philadelphia
Member Federal Advisory Council (rep. 3rd F.R. District)

WILLIAM F. KELLY - President, First Pennsylvania Banking & Trust Company

The Barclay Hotel, Philadelphia, Pa.

October 4, 1956 - 6:15 p. m.

- - - - - - - - - - - - - - -

Karl R. Bopp

Introduction

N.S.F. - Not you - us!

What I have been asked to do:

(1) Give a background on development of tight money

(2) Since Bill Mitchell and Bill Kelly preferred answering questions to giving talks, to ask appropriate questions of them - handed in

(3) Clay Anderson before A.I.B. will give statistical presentation. I shall use precious few figures.

I. If in banking 20 years, have heard of tight money only in the past 4 years on 2 occasions:

1952 - 1953
1955 - date

A. Why not in preceding 15-16 years?

1. From revaluation to World War II
Inflow of gold ↑ supply
Government, business & individual little demand

2. World War II - March 4, 1951
Era of the pegs
Didn't hear of tight money - but of inflation!

B. The Accord and its meaning

No longer tolerate inflation

Direct monetary policy toward full employment of resources at stable prices.
i.e. lean against the wind

Digitized for FRASER
http://fraser.stlouisfed.org/
Federal Reserve Bank of St. Louis

C. An over-all program

Effective demand = flow of goods and services at current average price level

In a flexible economy with great freedom by consumer to spend for one thing or another, a profit - and loss - economy cannot thru monetary policy build a floor under demand for every product e.g. automobiles without inflation elsewhere

Monetary policy can't do the whole job

D. The real test of whether credit is too tight is - are we using our resources fully at stable prices?

Employment release for September
Price Indexes

E. The future:

What will be true next May-June?

Should fear of that close our eyes to what is going on now?

Bi-weekly meetings of F.O.M.C.

II. Money supply for economic growth

A. Perspective

In 1843	Aggregate deposits in U.S.	60 million
1943	Demand deposits adj.	60 billion
End of July 1956		107 billion

By 1966 substantially higher still but how we get there in detail from day-to-day is another question; also from area to area!

B. Recent developments

About 3% a year BUT not every year

Greater in 1954 Less in 1955 Still less in 1956

Why? Briefly, more efficient use of money-velocity

Corporate investment policy

Implications for future cycles and money supply

III. Regional changes - Why is Philadelphia hit especially hard?

A. Expectation of normal national growth in deposits

B. Expectation of sharing normally in that growth

Philadelphia has had an adverse balance of payments

C. Expectation of normal growth in credit demands

D. In 1954 actively seeking new accounts
Opportunity to acquire national customers

E. Where funds have come from
Larger liquidation of investments
Larger borrowings

Digitized for FRASER
http://fraser.stlouisfed.org/
Federal Reserve Bank of St. Louis

QUESTIONS SENT IN IN ADVANCE

For Mr. Bopp:

What factors are responsible for the present tightness of money?

To what extent and in what ways has the Federal Reserve System influenced the situation?

What are the objectives of Federal Reserve monetary and credit policies?

What has been the relative impact of tight money on commercial banks in the Philadelphia Federal Reserve District compared with banks in the other Districts, and what factors have been responsible for the difference?

Has the relative position of the banks in the Third District been changing recently for better or worse?

Wage rates have been rising more or less steadily since World War II, without an accompanying equivalent rise, in the aggregate, in the productivity of labor. This certainly appears to be an inflationary trend and one, which if continued over a period of years would seem to present a real dilemma to the Federal Reserve System authorities in their efforts to combat inflation through control of the money supply. Mounting wage costs have served to stimulate the demand for more labor-saving machinery and for funds with which to finance same. Are higher interest rates going to effectively deter business men from borrowing for such purposes?

There is a vast segment of the money supply in this country which the Federal Reserve System has very little control of, namely, the savings and loan business, the savings banks, the insurance companies, pension funds and labor union funds. Both of these sources might be said to supply long-term capital needs rather than short-term. If these two premises are correct, generally speaking, then how can the system effectively control inflationary trends, long range, in our economy?

For Mr. Mitchell:

What factors should influence a bank's decision regarding tax switches in its bond portfolio?

Will you comment on the basic principles which should motivate bank portfolio management during the present tight money period?

Is this a good time to extend bond maturities in view of the present levels of bond prices?

Should a commercial bank liquidate short, intermediate or long-term securities under present circumstances to provide funds to lend to its customers?

As a commercial banker, what is your view of Federal Reserve monetary and credit policies and their implementation during the recent past with respect to their effectiveness in achieving their objectives?

Digitized for FRASER
http://fraser.stlouisfed.org/
Federal Reserve Bank of St. Louis

For Mr. Kelly:

More attention has been focussed recently upon the subject of compensating deposit balances. What constitutes a proper relationship between credit lines and deposit balances in the case of different types of borrowers, and how can the bank's requirements best be sold to customers?

To what extent should the continuing rise in the operating costs influence interest rates?

In the matter of loan interest rates, is it proper to charge all that the traffic will bear, recognizing that borrowers will give expression to their bargaining power when credit and money rates ease?

Will you comment on some of the customer and public relations aspects of credit rationing?

What general principles should be observed in the rationing of credit during a period of tight money?

Digitized for FRASER
http://fraser.stlouisfed.org/
Federal Reserve Bank of St. Louis