MINUTES OF THE MEETING OF THE FEDERAL ADVISORY COUNCIL

November 13, 1949

The fourth statutory meeting of the Federal Advisory Council for 1949 was convened in Room 932 of the Mayflower Hotel, Washington, D. C., on Sunday, November 13, 1949, at 2:00 P.M., the President, Mr. Brown, in the Chair.

Present:

Charles E. Spencer, Jr.	District No. 1
W. Randolph Burgess	District No. 2
Frederic A. Potts	District No. 3
Sidney B. Congdon	District No. 4
Robert V. Fleming	District No. 5
J. T. Brown	District No. 6
Edward E. Brown	District No. 7
W. L. Hemingway	District No. 8
Henry E. Atwood	District No. 9
James M. Kemper	District No. 10
J. E. Woods	District No. 11
Reno Odlin	District No. 12
Herbert V. Prochnow	Secretary

A complete list of the items on the agenda and the conclusions of the Council are to be found in the *Confidential Memorandum to the Board of Governors from the Federal Advisory Council,* which follows on pages 41, 42 and 43.

The meeting adjourned at 5:38 P.M.

HERBERT V. PROCHNOW
Secretary.

MINUTES OF THE MEETING OF THE FEDERAL ADVISORY COUNCIL

November 14, 1949

At 10:00 A.M., the Federal Advisory Council reconvened in Room 932 of the Mayflower Hotel, Washington, D. C.

Present: Mr. Edward E. Brown, President; Messrs. Charles E. Spencer Jr., W. Randolph Burgess, Frederic A. Potts, Sidney B. Congdon, Robert V. Fleming, J. T. Brown, W. L. Hemingway, Henry E. Atwood, James M. Kemper, J. E. Woods, Reno Odlin and Herbert V. Prochnow, Secretary.

The Council reviewed its conclusions of the previous day regarding the items on the agenda and sent to the Secretary of the Board of Governors the *Confidential Memorandum* which follows on pages 41, 42 and 43, listing the agenda with conclusions reached by the Council. The *Memorandum* was delivered to the Secretary of the Board of Governors at 12:35 P.M. on November 14, 1949.

The meeting adjourned at 12:20 P.M.

HERBERT V. PROCHNOW
Secretary.

MEMORANDUM TO THE BOARD OF GOVERNORS FROM THE FEDERAL ADVISORY COUNCIL RELATIVE TO THE AGENDA FOR THE JOINT MEETING ON NOVEMBER 15, 1949

1. What is the Board's opinion on the proposal now being urged to make currency redeemable in gold coin, and, specifically, what is the Board's opinion of the Reed Bill now before Congress which is designed to accomplish that purpose?

While the Council does not consider it feasible or desirable at the present time to make currency convertible into gold coin, it believes convertibility is a desirable objective of our monetary policy. The Council also believes it would be advisable to have a thorough study made to determine what preliminary steps should be taken toward this objective. In view of continuing public uncertainty regarding the power of the Secretary of the Treasury, one of the preliminary steps should be the revision of the Gold Reserve Act of 1934 to make it clear that the power to change the price of gold resides only in the Congress. Facing as we are the danger of a creeping inflation, the right to redeem currency in gold coin on demand would act as some check on a possible further deterioration in the purchasing power of the dollar.

2. The Board would like to have the current views of the members of the Council regarding probable economic and business conditions during the next three to six months.

The Council believes that production and employment will remain at a high level in the months immediately ahead. There will probably be some decline in farm incomes and a decrease in private capital expenditures, but Federal deficit financing, insurance and bonus payments to veterans, capital expenditures by states and municipalities, and increasing industrial costs due to wage increases and pension programs (which will make for higher prices) will probably result in an over-all inflationary pressure in the economy.

3. What suggestions does the Council have to make regarding System credit policy during that period?

With the prospect for active business and with the inflationary forces now evidencing themselves, the Council believes the policy of the Reserve System should be toward firmer money. Through the use of open market operations and the re-discount rate, the Reserve System has ample powers to meet presently foreseeable problems.

4. Does the Council have any further comments to make with respect to the December financing?

The viewpoint of the Council is the same as that expressed in its memorandum to the Board on September 20, 1949, which was as follows:

> "The Council believes that the Treasury's announcement that it proposes to issue notes to refund the bonds coming due in December is a step in the right direction. As the program develops, it should include refunding into both intermediate and longer-term issues. Too large a proportion of the Federal debt is now in short-term securities, especially when considered in connection with the amount of savings bonds outstanding and with the steadily shortening maturities of the present long-term issues."

5. The Board has been asked to submit to the President the legislative program affecting the Federal Reserve System which the Board desires to have considered at the forthcoming session of Congress. The formulation of the Board's views on that matter is now in process and it would be glad to have any advice or recommendations that the Council might wish to make in that connection.

The Council is not advised as to what legislative program the Board may desire to have considered at the forthcoming session of Congress. However, the Council has discussed with the Board various legislative proposals on different occasions.

The Council has previously approved the following legislative proposals:

(a) *Bank holding company legislation*—The Council has on many occasions urged the passage of bank holding company legislation, and is now in favor of the passage of such legislation.

(b) *Capital requirements for admission of state banks to membership in the Federal Reserve System, and for authority over the establishment of out-of-town branches of state member banks*—In its memorandum to the Board on September 20, 1949, the Council favored H.R. 5749. The Council is still of the same opinion.

(c) *Purchase by the Federal Reserve Banks of government obligations directly from the Treasury*—In its memorandum to the Board on March 11, 1947, the Council made the following statement:

"The Council recommends that authority be given for a period of three years to make direct purchases up to 5 billion dollars from the Treasury. The Council believes that it would be advisable to review the matter again at the end of three years to determine if there had been any abuse of the power and also to determine whether the power should be further continued or be permitted to lapse. The Council cannot but be mindful of the fact that historically and in various countries direct borrowing by a government from the central bank has been a common vehicle of inflation."

The Council now recommends a renewal of this authority for a period of three years.

(d) *Modification of limitation on the cost of Federal Reserve Branch buildings*—The Council in the past favored, and now favors, repeal of paragraph 9, section 10, of the Federal Reserve Act.

The Council has expressed opinions on other legislative matters, as follows:

(1) *Section 13b*—In connection with Section 13b of the Federal Reserve Act, the Council stated in its memorandum to the Board on September 20, 1949:

"The Council is opposed to two government agencies having lending or guarantee powers in the same field and therefore would not favor giving additional guaranteeing powers to the Federal Reserve Banks in the industrial field."

The Council is still of the same opinion.

(2) *Consumer credit*—The Council has in the past stated that it does not believe the Board should in time of peace have powers over consumer credit. The Council remains opposed to the granting of such powers to the Board.

(3) *Possible changes in the law with respect to bank reserves—*

(a) The Council, as stated in its memorandum to the Board on September 20, 1949, is "unanimously of the opinion that neither the Board of Governors nor any Federal agency should have authority to fix the reserve requirements of non-member banks."

(b) The Council believes that changes in reserve requirements should be used rarely and only for adjustment to basic changes in the monetary situation. In dealing with the question of bank reserves, it has often been forgotten that to build and preserve a sound banking system banks must have earnings sufficient to enable them to accumulate capital and pay adequate dividends. There should, therefore, be an upper limit on reserve requirements. The Council believes that the limits now in the law are as high as are tolerable, and give the Board sufficient power, with their other present instruments of policy, to deal with any foreseeable situation.

6. Are there any matters in connection with the questionnaires sent out by the Douglas subcommittee of the Joint Committee on the Economic Report that the Council would like to discuss with the Board?

Two members of the Council have been asked to testify before the Douglas subcommittee of the Joint Committee on the Economic Report. It is not possible in this written memorandum for the Council to express an opinion on all of the questions in the questionnaire of the Douglas subcommittee. Members of the Council will be pleased to comment on any of the questions, should the members of the Board desire their viewpoints.

MINUTES OF THE MEETING OF THE FEDERAL ADVISORY COUNCIL

November 14, 1949

At 2:20 P.M., the Federal Advisory Council convened in the Board Room of the Federal Reserve Building, Washington, D. C., the President, Mr. Brown, in the Chair.

Present: Mr. Edward E. Brown, President; Messrs. Charles E. Spencer Jr., W. Randolph Burgess, Frederic A. Potts, Sidney B. Congdon, Robert V. Fleming, J. T. Brown, W. L. Hemingway, Henry E. Atwood, James M. Kemper, J. E. Woods, Reno Odlin and Herbert V. Prochnow, Secretary.

President Brown presented Mr. Frank Garfield of the staff of the Board of Governors, who spoke on "Economic Prospects."

HERBERT V. PROCHNOW
Secretary.

MINUTES OF JOINT CONFERENCE OF THE FEDERAL ADVISORY COUNCIL AND THE BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM

November 15, 1949

At 10:45 A.M., a joint conference of the Federal Advisory Council and the Board of Governors of the Federal Reserve System was held in the Board Room of the Federal Reserve Building, Washington, D. C.

Present: Members of the Board of Governors of the Federal Reserve System:

Chairman Thomas B. McCabe; Governors M. S. Szymczak, Ernest G. Draper, R. M. Evans, James K. Vardaman, Jr., and Lawrence Clayton; also, Mr. S. R. Carpenter, Secretary of the Board of Governors.

Present: Members of the Federal Advisory Council:

Mr. Edward E. Brown, President; Messrs. Charles E. Spencer Jr., W. Randolph Burgess, Frederic A. Potts, Sidney B. Congdon, Robert V. Fleming, J. T. Brown, W. L. Hemingway, Henry E. Atwood, James M. Kemper, J. E. Woods, Reno Odlin and Herbert V. Prochnow, Secretary.

President Brown stated for the record that the Council approved unanimously the report of its Sub-committee on F.D.I.C. assessments, which is found on pages 36, 37 and 38, of these minutes. The Chairman of the Board was given a copy of the statement.

President Brown then read the first item on the agenda and the conclusions of the Council as given in the *Confidential Memorandum to the Board of Governors from the Federal Advisory Council,* as printed on pages 41, 42 and 43, of these minutes.

Chairman McCabe reported that all members of the Board agreed with his statement on gold as given in his reply to the questionnaire of the Douglas Sub-committee, and that he believes there is substantial agreement between the Council and the Board on this subject.

Dr. Burgess replied that while there is agreement as to the present situation, there is a real difference as to the long term, the Council believing that the right of convertibility should eventually be granted to our citizens.

President Brown then read the second agenda item and the conclusions of the Council as recorded in the *Confidential Memorandum* previously mentioned.

President Brown read the third agenda item relating to credit policy, and the conclusions of the Council in the *Memorandum* which is a part of these minutes.

Chairman McCabe stated that the effects of devaluation in this country were almost nil, and much less than expected.

President Brown then read the fourth item of the agenda and the conclusions of the Council as given in the *Confidential Memorandum* previously cited. Chairman McCabe asked what the Open Market Committee should do. Dr. Burgess replied that the Federal Reserve System should sell some bonds.

President Brown read the fifth item on the agenda and the conclusions of the Council as expressed in 5a in the *Memorandum* mentioned above.

Chairman McCabe inquired if the Council would support the holding company bill when the hearings start, perhaps early in the next Congress. He pointed out that the Council at its meeting with the Board in September had made one exception on the question of exempting wholly-owned trust companies. President Brown replied that he believed the Board could rely on the support of the Council on this legislation.

President Brown then read item 5b and 5c as given in the *Memorandum* mentioned. In connection with 5c, Mr. Fleming suggested it would be helpful for the Council to know what use the Federal Reserve System had made of its right to purchase government obligations direct from the Treasury. Chairman McCabe agreed to furnish the information.

President Brown then read item 5d as given in the *Memorandum.*

A lengthy discussion on Section 13b of the Federal Reserve Act followed between members of the Council and the Board.

President Brown read item 5(2) as given in the *Memorandum.*

President Brown asked if there were any other proposals the Board intended to submit to Congress. Chairman McCabe replied that the Board had not prepared its full program, but that some ideas are mentioned on page sixty-one of the printed reply of the Chairman to the Douglas Sub-Committee.

President Brown then read the sixth agenda item and the conclusions of the Council as given in the aforementioned *Confidential Memorandum.*

Governor Szymczak stated that the establishment of a Monetary Commission may be one result of the work of the Douglas Sub-Committee. Dr. Burgess inquired if the Board still favors a Monetary Commission. Chairman McCabe replied that the Board was on record for it.

It was agreed that the next meeting of the Council would be held February 19-21, 1950.

The meeting was adjourned at 1:20 P.M.

HERBERT V. PROCHNOW
Secretary.

NOTE: This transcript of the Secretary's notes is not to be regarded as complete or necessarily entirely accurate. The transcript is for the sole use of the members of the Federal Advisory Council. The concise official minutes for the entire year are printed and distributed later.

H. V. P.

The Secretary's notes on the meeting of the Federal Advisory Council on November 13, 1949, at 2 P.M., in Room 932 of The Mayflower Hotel, Washington, D.C. All members of the Federal Advisory Council were present.

The Council approved the Secretary's notes for the meetings of the Council held in May and September 1949.

REPORT OF THE SUB-COMMITTEE OF THE FEDERAL ADVISORY COUNCIL ON FDIC ASSESSMENTS.

E. E. Brown commends the sub-committee for its report. The Council unanimously approved the report.

Fleming reports briefly off-the-record on the present status of the various proposals regarding FDIC assessments and coverage.

WHAT IS THE BOARD'S OPINION ON THE PROPOSAL NOW BEING URGED TO MAKE CURRENCY REDEEMABLE IN GOLD COIN, AND, SPECIFICALLY, WHAT IS THE BOARD'S OPINION OF THE REED BILL NOW BEFORE CONGRESS WHICH IS DESIGNED TO ACCOMPLISH THAT PURPOSE?

E. E. Brown asks Atwood to comment on this item on the agenda.

Atwood states that a director of his bank had raised the question with him.

E. E. Brown. Do any members of the Council believe it would be desirable to permit convertibility into gold coin at once? Brown calls attention to the address which Burgess made at the American Bankers Association convention at San Francisco on October 31, 1949. In that address Burgess stated, "There is a group of people today asking for the restoration of the full gold standard immediately in the United States. Today we have a dollar that is convertible into gold for foreign governments and central banks; these people are asking for the same rights to hold gold for our own citizens. In principle I believe these people are right, though I think they are wrong in their timing, and overemphasize the immediate benefits. The gold standard is an international system and calls for basically sound money in many countries before it will work. When European and world monetary reconstruction has restored free convertibility at least among the principal currencies, the time will be ripe to readopt the principle of an unrestricted gold standard here. If you try to force the pace by resuming gold payments before the foundations are laid through government policies on the budget, on credit, and on prices, the gold released may simply move out into hoards and become the tool of the speculator. Gold payments are only part of the building of sound money, and they are in a sense the capstone of the arch. If you put on the capstone before the structure is sound, the arch collapses. Gold payments are the seal of approval of good money." E. E. Brown says that the Council may not favor immediate convertibility, although it may favor it for the long pull.

Atwood states that the director of his bank reviewed a recent Treasury statement which showed an increase in the deficit and other trends which were not reassuring in relation to our fiscal policies. The director believed it was important to permit convertibility so United States citizens could convert part of their property into gold. If enough citizens converted, it would warn the government that the people did not have confidence in the fiscal policies of the government.

E. E. Brown asks each member of the Council for an expression of opinion.

Odlin favors convertibility eventually, but believes it is not now practicable.

Fleming believes it would be untimely at present.

Woods agrees with the comments Burgess made in his address. He does not believe convertibility is desirable at present.

Congdon is inclined to believe it is not desirable now.

Burgess states that in view of continuing uncertainty regarding the power of the Secretary of the Treasury, the Gold Reserve Act of 1934 should be revised to make it clear that only the Congress has the power to change the price of gold. Clarification of the present law is a preliminary step toward convertibility.

Potts does not believe this is the time to permit convertibility. He favors it for the future.

Kemper favors it for the future and believes the sooner it comes the better it will be. However, at the moment it is perhaps not practical in view of world conditions. Kemper would favor planning for it now as a sound objective of our monetary policy.

Hemingway believes the Council might state that it favors convertibility eventually and would recommend a study to determine what steps are necessary to accomplish it.

J. T. Brown does not think it would be practical immediately, but it is highly desirable to take the steps necessary to accomplish it eventually.

Spencer thinks there would be a run on gold if convertibility were permitted now. This would be especially true if people thought the gold price might be increased. Convertibility is not desirable immediately, but it is a sound future objective.

Atwood calls attention to the fact that we are in a time of peace and prosperity and are running a substantial Federal deficit. He agrees with Hemingway that a study should be made to determine what steps are necessary to bring about convertibility.

Burgess agrees with Hemingway's suggestion. In principle Burgess favors convertibility as one of the limitations on a central bank. The Board of Governors continually asks for removal of limitations and more powers. Gold convertibility is one of the essential parts of a sound monetary policy.

E. E. Brown. The Council may state that it is not feasible or desirable at the present time to make currency convertible into gold coin. However, the Council believes it is highly desirable constantly to work toward a policy of making currency convertible into gold coin at the earliest time international conditions will permit. In view of the continuing public uncertainty regarding the power of the Secretary of the Treasury, one of the preliminary steps should be the revision of the Gold Reserve Act of 1934 to make it clear that the power to change the price of gold resides only in the Congress.

Odlin does not think it would be practical if it were done immediately.

Atwood asks whether there might be a run on gold.

Burgess states that it is very possible that there might be a run on gold.

Hemingway. Recognizing that convertibility is a desirable objective, definite steps should be taken to work for it.

E. E. Brown believes the country is in a creeping inflation, and convertibility would tend to stop it. The Council might state that it believes conversion of currency into gold coin is a desirable step to prevent a steady deterioration in the purchasing power of the dollar.

THE BOARD WOULD LIKE TO HAVE THE CURRENT VIEWS OF THE MEMBERS OF THE COUNCIL REGARDING PROBABLE ECONOMIC AND BUSINESS CONDITIONS DURING THE NEXT THREE TO SIX MONTHS.

E. E. Brown asks the members of the Council for their views.

Odlin states that inflationary elements may be in the ascendancy in the immediate future, but he is disturbed about the longer term.

Fleming. We have had an inventory deflation, but have now moved out of it. With the large amounts of money which will probably be spent in the months immediately ahead, plus the inflationary effects of the coal and steel strikes, business should be active.

Woods. Although inflationary elements are at work, he believes there may be some falling off in prices in the next six months. The cotton yield has been bountiful. The last estimate gave Texas 5.6 million bales, or about 38 per cent of the total for the country. Oil production is up. The wheat crop has been large. Business in his district is generally good.

Congdon. Business is comparatively good in his area with the settlement of the strikes. The automobile and tire industries look good. He is inclined to expect rather good business in the months immediately ahead.

Potts. His district was probably as hard hit as most areas because of the steel and coal strikes. There are some sore spots because of the devaluation of foreign currencies, with the locomotive industry as one example where foreign competition has become more difficult.

Kemper. The outlook is for an upturn in volume. Retail trade is better. Business generally looks good.

Hemingway. Conditions are spotty in his district. Business is somewhat lower in volume and considerably lower in profits than it was a year ago.

J. T. Brown. His district has little cotton compared to the past. Retail sales are up, but profits are down, which indicates inventories are being sacrificed. He trusts that the situation in his district does not indicate the pattern.

Spencer. Retail sales are beginning to increase. The Christmas trade should be substantial. Manufacturing has started to pick up. The shoe industry is in better condition, and textiles are better. He expects a large volume of retail trade and manufacturing.

Atwood. Farm income will be down this year over last year, but the farmer is still prosperous. Business generally is very good and is better than any year except possibly 1948.

Burgess. It looks like good business in the months immediately ahead. Private capital expenditures may decline somewhat, but veterans' insurance and bonus payments, as well as deficit financing, give an overall inflationary effect.

E. E. Brown expects good business. The steel strike may mean some readjustment downward for some weeks. However, the steel companies are swamped with orders. Retail trade is down somewhat, but business will probably be active over the next six months. Profits may be down a little, but no real decline in business appears probable in the months immediately ahead. The Council may state that the volume of production and employment remain high, although there may be some shading of profits. Deficit financing and wage increases in the form of pensions may cause inflationary pressures. The result is that business will probably be active in the next three to six months.

Fleming. The Council may say that the ultimate effects of devaluation are not yet clear.

WHAT SUGGESTIONS DOES THE COUNCIL HAVE TO MAKE REGARDING SYSTEM CREDIT POLICY DURING THAT PERIOD?

Burgess. The Federal government may have a deficit of over $5 billion. Heavy bonuses for veterans, and large expenditures by state and local governments are all being made possible through financing at extremely low interest rates.

E. E. Brown. With deficit financing and higher prices, interest rates should not be lowered. (At this point there was an off-the-record discussion on interest rates.)

Burgess. With greater business activity, large expenditures by national, state and local governments, a substantial government deficit and heavy spending for veterans' payments, sound central bank policy requires higher interest rates.

E. E. Brown. With a large government deficit, with insurance and bonus payments to veterans and with wage increases through pensions, the Council may say that it believes the policy of the Board and the Open Market Committee should not be one of cheapening money, but of firming interest rates.

Burgess. The inflation comes from the government.

E. E. Brown. The Board has ample powers over reserves. The System should use open market operations and the rediscount rate, and these instruments are ample to meet presently forseeable problems.

DOES THE COUNCIL HAVE ANY FURTHER COMMENTS TO MAKE WITH RESPECT TO THE DECEMBER FINANCING?

Fleming states that in answer to this question the Council might repeat the comments which it made to a similar question in the September meeting.

E. E. Brown says the Council may say that its attitude is the same as that expressed in September as follows:

"The Council believes that the Treasury's announcement that it proposes to issue notes to refund the bonds coming due in December is a step in the right direction. As the program develops, it should include refunding into both intermediate and longer-term issues. Too large a proportion of the Federal debt is now in short-term securities, especially when considered in connection with the amount of savings bonds outstanding and with the steadily shortening maturities of the present long-term issues."

THE BOARD HAS BEEN ASKED TO SUBMIT TO THE PRESIDENT THE LEGISLATIVE PROGRAM AFFECTING THE FEDERAL RESERVE SYSTEM WHICH THE BOARD DESIRES TO HAVE CONSIDERED AT THE FORTHCOMING SESSION OF CONGRESS. THE FORMULATION OF THE BOARD'S VIEWS ON THAT MATTER IS NOW IN PROCESS AND IT WOULD BE GLAD TO HAVE ANY ADVICE OR RECOMMENDATIONS THAT THE COUNCIL MIGHT WISH TO MAKE IN THAT CONNECTION.

Atwood believes the Council may have to express its opinion on specific items of legislation.

Burgess states he will testify shortly before the Subcommittee of the Joint Congressional Committee on the Economic Report.

E. E. Brown says that he will testify later. For the information of the Council, he expects to testify as follows: (1) He will comment on the overall relationship of the Treasury and the Federal Reserve System. He believes the central bank must be responsive and go along in general with the administration in power, but the central bank must have an independent status which will enable it to offer strong objections when necessary. The Board should not be a department of the Treasury. The Council has expressed itself on this, and Brown is in agreement with the Council's previous statement. (2) Reserve requirements should be flexible. The upper limit should be at a point where banks can live and make a profit. The Board should not have powers that will permit the Board to put banks out of business. It is already impossible to sell bank stock, except at a price below its liquidating value. He believes the Board has ample power over reserves now. (3) The Board should not have control over the reserves of non-member banks. The greatest restraint on arbitrary action of the Board is the power of a bank to leave the System.

Burgess says that he will comment upon essentially the same points. He wishes to add that in various states, including New York, the state banking board has the power to change reserve requirements to keep them in line with those fixed by the Board of Governors.

E. E. Brown will state in his fourth point the idea that the examining of banks should be done by some agency other than a policy making agency. The Comptroller's office has had the longest experience in examing banks.

Woods asked Burgess whether the Banking Board of New York State must fix reserve requirements the same as those of the Federal Reserve System.

Burgess replies that the Banking Board may use its own judgment. In connection with McCabe's reply to the questionnaire of the Douglas Subcommittee, McCabe makes no reference to the fact that banks should have adequate earnings. Burgess thinks the Board might advise the President that the Board does not wish to recommend additional banking legislation and can get along satisfactorily with present legislation.

E. E. Brown states that the Council is already on record on legislative matters like Regulation W, authority over reserves of non-member banks, Section 13b, and bank holding company legislation.

Fleming thinks the Board should advise the Council what legislative program it has in mind so the Council can discuss the program.

J. T. Brown reports that the Board has sent a telegram to the Federal Reserve Bank of Atlanta asking for opinions on various legislative proposals. J. T. Brown reads the list of legislative items mentioned in the telegram.

Congdon believes the Council should state specifically where it stands on various legislative proposals.

E. E. Brown says that the Council may state that it is difficult to make specific comments to the Board when the Council does not know what legislative proposals the Board anticipates submitting to the President. However, the Council may state that in the past it has expressed opinions on various legislative proposals, and it may then list the proposals.

Burgess believes the Board would be wise if it did not ask for authority over the reserves of non-member banks. The Council should also emphasize that banks should be permitted to earn a living. The question of bank reserves is one of the most important.

E. E. Brown. On the question of reserves, the Council may state that it does not approve giving the Board power over the reserves of non-member banks, and that it is opposed to any increase in the reserve requirements of member banks. The Council may add that it would be pleased to consider any specific plan but would oppose any proposal if it necessitated an increase in the maximum reserves. The Council may also say that it has previously dealt with the matter of buying government securities directly and recommends at this time renewal of that power for three years.

ARE THERE ANY MATTERS IN CONNECTION WITH THE QUESTIONNAIRES SENT OUT BY THE DOUGLAS SUBCOMMITTEE OF THE JOINT COMMITTEE ON THE ECONOMIC REPORT THAT THE COUNCIL WOULD LIKE TO DISCUSS WITH THE BOARD

E. E. Brown. The Council may state that two of its members have been asked to testify before the Douglas Subcommittee. The Council cannot in a brief written memorandum express an opinion on all of the questions asked by the Douglas Subcommittee. Members of the Council will be pleased to comment on any of the questions, should the Board desire their viewpoints.

The meeting adjourned at 5:38 P.M.

THE COUNCIL CONVENED AT 10 A.M. ON NOVEMBER 14, 1949, IN ROOM 932 OF THE MAYFLOWER HOTEL, WASHINGTON, D. C. ALL MEMBERS OF THE FEDERAL ADVISORY COUNCIL WERE PRESENT.

The Council prepared and approved the attached Confidential Memorandum to be sent to the Board of Governors relative to the agenda for the joint meeting of the Council and the Board on November 15, 1949. The Memorandum was delivered to the Secretary of the Board of Governors at 12:35 P.M. on November 14, 1949. It will be noted that each item of the agenda is listed with the comments of the Council on the item.

The meeting adjourned at 12:20 P.M.

CONFIDENTIAL

MEMORANDUM TO THE BOARD OF GOVERNORS
FROM THE
FEDERAL ADVISORY COUNCIL
RELATIVE TO THE AGENDA FOR THE JOINT MEETING
ON NOVEMBER 15, 1949

1. What is the Board's opinion on the proposal now being urged to make currency redeemable in gold coin, and, specifically, what is the Board's opinion of the Reed Bill now before Congress which is designed to accomplish that purpose?

While the Council does not consider it feasible or desirable at the present time to make currency convertible into gold coin, it believes convertibility is a desirable objective of our monetary policy. The Council also believes it would be advisable to have a thorough study made to determine what preliminary steps should be taken toward this objective. In view of continuing public uncertainty regarding the power of the Secretary of the Treasury, one of the preliminary steps should be the revision of the Gold Reserve Act of 1934 to make it clear that the power to change the price of gold resides only in the Congress. Facing as we are the danger of a creeping inflation, the right to redeem currency in gold coin on demand would act as some check on a possible further deterioration in the purchasing power of the dollar.

2. The Board would like to have the current views of the members of the Council regarding probable economic and business conditions during the next three to six months.

The Council believes that production and employment will remain at a high level in the months immediately ahead. There will probably be some decline in farm incomes and a decrease in private capital expenditures, but Federal deficit financing, insurance and bonus payments to veterans, capital expenditures by states and municipalities, and increasing industrial costs due to wage increases and pension programs (which will make for higher prices) will probably result in an over-all inflationary pressure in the economy.

3. What suggestions does the Council have to make regarding System credit policy during that period?

With the prospect for active business and with the inflationary forces now evidencing themselves, the Council believes the policy of the Reserve System should be toward firmer money. Through the use of open market operations and the re-discount rate, the Reserve System has ample powers to meet presently foreseeable problems.

4. Does the Council have any further comments to make with respect to the December financing?

The viewpoint of the Council is the same as that expressed in its memorandum to the Board on September 20, 1949, which was as follows:

> "The Council believes that the Treasury's announcement that it proposes to issue notes to refund the bonds coming due in December is a step in the right direction. As the program develops, it should include refunding into both intermediate and longer-term issues. Too large a proportion of the Federal debt is now in short-term securities, especially when considered in connection with the amount of savings bonds outstanding and with the steadily shortening maturities of the present long-term issues."

5. The Board has been asked to submit to the President the legislative program affecting the Federal Reserve System which the Board desires to have considered at the forthcoming session of Congress. The formulation of the Board's views on that matter is now in process and it would be glad to have any advice or recommendations that the Council might wish to make in that connection.

The Council is not advised as to what legislative program the Board may desire to have considered at the forthcoming session of Congress. However, the Council has discussed with the Board various legislative proposals on different occasions.

The Council has previously approved the following legislative proposals:

(a) Bank holding company legislation--The Council has on many occasions urged the passage of bank holding company legislation, and is now in favor of the passage of such legislation.

(b) Capital requirements for admission of state banks to membership in the Federal Reserve System, and for authority over the establishment of out-of-town branches of state member banks--In its memorandum to the Board on September 20, 1949, the Council favored H.R. 5749. The Council is still of the same opinion.

(c) Purchase by the Federal Reserve Banks of government obligations directly from the Treasury--In its memorandum to the Board on March 11, 1947, the Council made the following statement:

"The Council recommends that authority be given for a period of three years to make direct purchases up to 5 billion dollars from the Treasury. The Council believes that it would be advisable to review the matter again at the end of three years to determine if there had been any abuse of the power and also to determine whether the power should be further continued or be permitted to lapse. The Council cannot but be mindful of the fact that historically and in various countries direct borrowing by a government from the central bank has been a common vehicle of inflation."

The Council now recommends a renewal of this authority for a period of three years.

(d) Modification of limitation on the cost of Federal Reserve Branch buildings--The Council in the past favored, and now favors, repeal of paragraph 9, section 10, of the Federal Reserve Act.

The Council has expressed opinions on other legislative matters, as follows:

(1) Section 13b--In connection with Section 13b of the Federal Reserve Act, the Council stated in its memorandum to the Board on September 20, 1949:

"The Council is opposed to two government agencies having lending or guarantee powers in the same field and therefore would not favor giving additional guaranteeing powers to the Federal Reserve Banks in the industrial field."

The Council is still of the same opinion.

(2) Consumer credit--The Council has in the past stated that it does not believe the Board should in time of peace have powers over consumer credit. The Council remains opposed to the granting of such powers to the Board.

(3) Possible changes in the law with respect to bank reserves--

(a) The Council, as stated in its memorandum to the Board on September 20, 1949, is "unanimously of the opinion that neither the Board of Governors nor any Federal agency should have authority to fix the reserve requirements of non-member banks."

(b) The Council believes that changes in reserve requirements should be used rarely and only for adjustment to basic changes in the monetary situation. In dealing with the question of bank reserves, it has often been forgotten that to build and preserve a sound banking system banks must have earnings sufficient to enable them to accumulate capital and pay adequate dividends. There should, therefore, be an upper limit on reserve requirements. The Council believes that the limits now in the law are as high as are tolerable, and give the Board sufficient power, with their other present instruments of policy, to deal with any foreseeable situation.

6. Are there any matters in connection with the questionnaires sent out by the Douglas subcommittee of the Joint Committee on the Economic Report that the Council would like to discuss with the Board?

Two members of the Council have been asked to testify before the Douglas subcommittee of the Joint Committee on the Economic Report. It is not possible in this written memorandum for the Council to express an opinion on all of the questions in the questionnaire of the Douglas subcommittee. Members of the Council will be pleased to comment on any of the questions, should the members of the Board desire their viewpoints.

THE COUNCIL CONVENED IN THE BOARD ROOM OF THE FEDERAL RESERVE BUILDING AT 2:20 P.M. ON NOV. 14, 1949. ALL MEMBERS OF THE COUNCIL WERE PRESENT TO HEAR FRANK GARFIELD OF THE STAFF OF THE BOARD OF GOVERNORS SPEAK ON THE SUBJECT, "ECONOMIC PROSPECTS".

Mr. Garfield prepared the following summary of his remarks:

ECONOMIC PROSPECTS

Next six weeks

With the steel strike settled last week and coal mines operating again, industrial production -- output at factories and mines -- for the whole month of November may be estimated at 168 per cent of the 1935-39 average as compared with 163 in October and 173 in September. The rate in December may be over 175 if the coal mines continue to operate and the advanced levels reached in many lines after recovery in August and September are maintained. So far these advanced levels -- in the output of textiles, paper, furniture, household appliances, lumber, and other building materials -- are being largely maintained. Auto assemblies are declining from the peak level reached this autumn, owing in part to model changeovers. Heavy demand for steel, including substantial orders to replenish inventories depleted during the six-week strike, will probably bring output to a level close to capacity and higher than at any time since early spring.

Immediate prospects for commodity prices are fairly uncertain. Advances have occurred recently in prices of carpets, tires, some grades of lumber, copper, and steel scrap; somewhat earlier there were increases in numerous textile items. Coffee has shown a spectacular advance on crop news from Brazil. Strong demands for finished steel and added pension costs at least make very unlikely any price reductions such as purchasing agents for steel consumers were looking forward to last summer. On the other hand, in agriculture large crop supplies tend to prevent price advances and currently prices of hogs are declining seasonally under the impact of heavy marketings. Imports of goods, which were at a low level this summer, have been increasing lately, bringing more downward pressure on the price structure at numerous points. In consumer markets meat prices have been declining lately; rents, however, have continued to advance.

The gross national product figures, if available monthly, might show a rise with increased production at steel mills and coal mines but on a quarterly basis they will probably show little change from the third to the fourth quarter. They indicated a decline from the second to the third quarter, at least partly because the low point of the decline in activity from the end of 1948 was in July, the first month of the third quarter.

Levels at year-end

What sort of levels will activity and prices be at as the old year ends and the new begins, four years and four months after V-J Day? At that time population will be at a new high, close to 150 million and 16 per cent above the 1935-39 average. The number employed will be up over a third, industrial production three-fourths, and all production almost that much. Reflecting price as well as production increases, gross national product will be at an annual rate of about 255 billion, roughly three times the 1935-39 average. In the price field, wholesale quotations are up 90 per cent, consumer prices nearly 70 per cent, and farm land values over 100 per cent. In general, then, production levels will be very high in comparison with prewar and fairly high in relation to peacetime capacity. Prices also will be at levels very much higher than before the war, up much more than the prices of the 1920's were from pre-World War I levels.

The levels indicated for the year-end are moderately below the 1948 peaks, 2 per cent for total employment, 10 for industrial production and wholesale prices, 3 for consumer prices, 4 for farm land values. There have been sharp adjustments in particular commodity prices in various periods (wheat and corn in 1948, nonferrous metals in the spring of 1949) and in particular production activities (textile yarns and fabrics in 1948 and early 1949, machinery production from the end of 1948 to the middle of 1949); they have occurred serially, however, within a general framework of high demand and activity. The decline this year was more widespread than earlier postwar reductions in activity but important advances to new record levels were occurring in the automobile and housing industries at the time when numerous other activities were reaching their low points.

First half of 1950

The view most widely held by System economists attending the meeting of the Current Business Developments Committee in Dallas three weeks ago, and also by other economists, has been that production in mid-1950 would be at or slightly below the level of the third quarter of 1949 and that commodity prices would be somewhat lower. It has been noted that the recent strikes might result in marked fluctuations in activity meanwhile.

Each economist has his own peculiar way of looking at the prospects but there has been considerable agreement on the view that demands for plant and equipment, for new housing, and for autos would decline, at least moderately. Commonly note is made also of the downward pressures on prices exerted by large supplies of crops and increasing marketings of livestock. Increased foreign competition is expected, particularly abroad. On the other hand, state and local expenditures on needed schools, highways, and the like are expected to continue expanding and Federal outlays are expected to rise somewhat further. It is in the first half that most of the National Service Insurance Dividend payments, amounting to 2.8 billion dollars, will be made and while there is a wide difference of opinion as to the importance of this, no one doubts that it will be in the direction of strengthening consumer demand, at least temporarily. Because the downward pressures mentioned are expected to exceed upward pressures, prices are expected to be stable or declining and this is expected to mean that changes in inventories held by business enterprises will not be important. This would be in sharp contrast to the situation in most of the postwar boom period when considerable production went into such inventory accumulation. A neutral position would differ moderately from the situation which has prevailed beginning in the second quarter this year, with inventories declining somewhat as production has been somewhat below consumption.

Those who held this general view of prospects do not expect a return to peak levels, partly because they think that many of the stimulating effects of the shortages of goods and the abundance of money created during the war are of a temporary nature. They believe the deferred demands have been largely met and that the price-cost-income adjustments which have occurred have not been adequate to assure full production and employment on a continuing basis. They think that the end of the latest decline came quickly this summer, partly because of various Government props to income, -- such as the agricultural price support program and the foreign aid program. They point out that efforts will be made to restrict acreages of many important crops in 1950 and that farm cash receipts may show a decline of 10 per cent, following a similar decline in 1949.

Another view of prospects is that activity will return to peak levels and that prices will be at least maintained. This is still a minority view but inquiries concerning this possibility have been increasingly frequent lately.

One argument is that once a revival is under way it is likely to gain momentum. The revival this past summer is regarded as primarily self-generating rather than stimulated by any war scare or special Government programs. The strength of demand for autos and housing during a period of fairly widespread weakness in markets is regarded as evidence that there are some deferred demands yet to be met, and that, with judicious price adjustments, markets are still available for a very large volume of output. On the outlook for capital goods, the position is that basic needs are very great -- consumption is high, obsolescence is very rapid, and wage rates are higher than ever; that costs of new equipment are not likely to decline enough to make waiting worthwhile, and may even increase if steel prices are advanced; that funds are readily available from large retained earnings or other sources; and that, consequently, in a period of revival, outlays for plant and equipment are likely to be in very large volume. Inquiries concerning the possibility of devaluation of the dollar suggest that some of those expecting higher activity are thinking in terms of rising prices and inflation.

A third view, for which it is now difficult to find a defender, has been that an important decline in activity would be under way before the end of the first half. In this view, postwar adjustments have been quite inadequate (note the contrast with 1920-21) and neither producers nor consumers (at home or abroad) will continue in the market indefinitely at current price levels. The current revival in some of the nondurable goods lines is regarded as partly speculative and not fully warranted by sales of finished products to ultimate consumers; while department store sales of household appliances and furniture have shown some recovery, apparel sales are at rather low levels. On capital expenditures, it is argued that the railroads and many manufacturing industries have already curtailed outlays considerably, that many other postwar programs are nearing completion, and that the incentives for undertaking new programs are not adequate to prevent a continuing decline in this area for some time.

Alternative interpretations of recent events

One way to check on the plausibility of various views is to take a look at recent important events and see which way they may be expected to push things from previously established and known positions. In the past two months there have been many important developments.

1. The strikes have clearly reduced stocks of steel and coal and the settlements will raise production costs somewhat. A period of heavy purchases of steel may well provide a stimulus even though some of the demands will be of a temporary sort. The idea that steel production will be at capacity for six months -- a guess of three months might be more realistic -- certainly seems to provide a basis for confidence and forward commitments quite different from that in a period of declining steel output, such as the second quarter of 1949. An alternative view is that however beneficial capacity operations for a time may be, the postponement of price reductions or the substitution of price increases for steel (and perhaps other products) may be harmful, restricting purchases of final products.

2. Announcement of atomic explosion in Russia. This appears to have contributed to such actions as Congressional agreement on a larger appropriation for arms aid to Europe; Congressional removal of restrictions on spending procedure of the Atomic Energy Commission; and the pushing of plans for economic integration of Western Europe. It has also led to much talk, some apparently more serious than before, concerning the possibility of international control. Continued active participation in world affairs seems likely to mean substantial U. S. expenditures in one form or another for a long time to come and more rather than less in the first half of 1950.

3. Devaluation. This can be viewed as having had little effect; an index of dollar prices of eight materials imported from the

sterling area, using the 1948 average as 100, on November 11 was at 85, down only 7 points from the September 15 figures and up 1 point from the June average. Declines in imported finished goods since September 15 have been fairly limited also. Two months, however, is a very short period for the effects of devaluation to appear and some of the more important effects may appear in the export markets temporarily held by the United States in the postwar period. The whole foreign trade adjustment process now occurring as a result of devaluation, and also of reductions in trade restrictions, may exert more downward influence on business in the United States during the first half of 1950 than many anticipate. Meanwhile costs of imported goods in devaluing countries have been greatly increased; in the United Kingdom, for example, cotton is up 24 per cent and most nonferrous metals are up 30 per cent. How successful the efforts to prevent further inflation abroad and put trade on a more sustainable basis may be is yet to be determined.

4. October housing starts at 100,000. This is the sixth month in a row with starts at or close to 100,000. The October figure last year was 73,000. The indicated total for 1949 is 1,000,000 units as compared with 931,000 last year. There can be no question that the record is one of great strength in the residential building field even though some of the volume has been achieved by lowering prices and by building smaller houses. Financing arrangements, both for rental housing, which has been built in considerable volume this year, and for owned housing, have been eased to a point which seems to some economists to be unsound but for the immediate future a high level of activity in this field seems assured.

5. U. S. passenger car production at 489,000 (estimate) in October and about 5,100,000 for the year. October output is below the August-September peak rate but is much higher than had been generally anticipated. Total for year will be above 1929 by 10 per cent or more and above 1948 by 30 per cent. Meanwhile output of replacement parts has declined but the record for the industry is a very impressive one and it has been achieved in the face of many declines in the economy. Stocks of passenger cars in the hands of dealers have increased but the proportion of output going into dealers stocks has been very small and generally dealers are not overstocked. This is another field where price adjustments (higher trade-in values and lower used-car prices) have helped to increase volume. The big question is how long consumers will remain in the market and what additional inducements they may be offered. About 35.7 million passenger cars will be in use by the end of the year. This is 6.1 million more than in 1941 but 14 million of the 35.7 million are over 10 years old whereas in 1941 only 5 million fell in this group. Also, highways are being crowded -- discouraging some potential car buyers as well as encouraging expansion of highway programs. In the first half of 1950, however, it now appears that output may continue at a very high level.

6. Freight car deliveries at 4,500 in October. Such deliveries have been declining rapidly from a peak of over 10,000 a month early in the year and backlogs of unfilled orders are down from 120,000 a year ago to 17,000. This is a reminder that backlogs of orders in many lines have been sharply reduced and also that there are real problems in connection with capital expenditure programs. Freight car loadings before the strikes were running 20 per cent below a year ago and a reduction in business of this amount is very discouraging to capital outlays. Only a few inquiries for freight cars have been received lately. Orders for diesel locomotives continue in substantial volume -- because they make possible large savings in operating expenses.

7. Man-hours in machinery industries in September 3 1/2 per cent above August and July. Is this a reversal of the downtrend which had brought man-hours in these industries down over 20 per cent since December? Or is it just a seasonal rise in output of household appliances, which are included along with industrial machinery of all sorts? For the moment it does seem to mean an end to the steady decline here but figures for one or two months are not very persuasive and much of the rise appears to have been seasonal. However, appliance sales at retail (seasonally adjusted) have increased since late last spring. In other (much more important) machinery lines there is not much evidence of any rise; in some quarters foreign as well as domestic demands are expected to show further reductions. How far prospective declines in capital outlays have already been reflected in reduced machinery output is a moot question. (Incidentally, preliminary figures show capital outlays by manufacturing concerns in Philadelphia estimated to be down 24 per cent in the period from October 1949 to September 1950 as compared with the preceding 12-month period.)

8. Relative stability in wholesale prices since early July. One way to look at this is to say that, with devaluation abroad and increased agricultural supplies in this country, little change is an evidence of strength. On the other hand, it may be argued that the volume of business buying was very great in this period and that if prices did not advance on the average (some, like nonferrous metals, did rise somewhat) in this period they are not likely to go up in the near future. Some of the argument that business will be sustained or improve further in the first half is based on the idea that moderate price reductions stimulate consumption. Another part of the argument is based on the idea that because prices are not expected to go lower buyers recently out of the market will reenter it. These positions are not necessarily inconsistent because they may refer to different commodities and markets. As yet, prospects in this field are not very clear but a strong case can be made that the main drift is still downward.

These are only some of the important recent developments -- nothing has been said about consumer credit, commercial loans, third quarter profits or the New York elections. Certain of the developments discussed are subject to very different interpretations. Each man will have his own peculiar system of selecting and counting, omitting and duplicating. The view which appeals to me right now is a sort of upper middle view, a view that activity will be a little higher in June of 1950 than in the third quarter of 1949 but not up to the peak at the end of 1948. Prices may be somewhat lower than in the third quarter or at present.

On November 15, 1949, at 10:45 A.M., the Federal Advisory Council held a joint meeting with the Board of Governors of the Federal Reserve System in the Board Room of the Federal Reserve Building.

All members of the Council were present. The following members of the Board of Governors were present: Chairman McCabe; Governors Szymczak, Draper, Evans, Vardaman and Clayton. Mr. Carpenter, Secretary of the Board of Governors, was also present.

REPORT OF SUB-COMMITTEE OF THE FEDERAL ADVISORY COUNCIL ON F. D. I. C. ASSESSMENTS

E. E. Brown states for the record that the Council approved unanimously the report of its Sub-Committee on FDIC Assessments. The Chairman of the Board was given a copy of the statement.

WHAT IS THE BOARD'S OPINION ON THE PROPOSAL NOW BEING URGED TO MAKE CURRENCY REDEEMABLE IN GOLD COIN, AND, SPECIFICALLY, WHAT IS THE BOARD'S OPINION OF THE REED BILL NOW BEFORE CONGRESS WHICH IS DESIGNED TO ACCOMPLISH THAT PURPOSE?

E. E. Brown reads Item 1 on the agenda, as given above, and the conclusions of the Council as submitted in its Memorandum to the Board dated November 15, 1949. All members of the Council are agreed that it is not feasible at present to make our currency convertible into gold coin. Most businessmen are concerned regarding the possibility that the price of gold may be changed. Although the President and the Secretary of the Treasury have said the price would not be changed, there continues to be uncertainty because of the language of the Gold Reserve Act of 1934.

Fleming reads a news letter which states that there may be a loophole in the law that would permit the gold price to be changed.

Szymczak says that the law clearly states the gold price can be changed only by the Congress.

McCabe believes that the big question is whether you want the whole question of gold to be reopened in the Congress. If you ask for a revision of the Gold Reserve Act of 1934, it is possible that the whole question of gold would be debated at length in Congress, and there would be no certainty regarding the outcome of the debate. McCabe reports that all members of the Board agree with McCabe's statement on gold as given in his reply to the questionnaire of the Douglas Subcommittee. McCabe believes that on the price of gold there is substantial agreement between the Council and the Board.

Burgess. There is a real difference of opinion between the Council and the Board, not as to the present situation, but as to the long term. The members of the Council believe that our citizens should eventually be given the right to convert currency into gold. Burgess mentions that the Greek drachma is today being stabilized through sales by the central bank of gold sovereigns in the open market.

McCabe says that in this country people have confidence in their money.

Odlin replies that he questions whether people are confident that their money will not depreciate in value.

McCabe does not believe it is desirable now to raise the question in Congress of the power of the Secretary of the Treasury.

Fleming. The question is not one of whether the present Secretary would devalue or whether the major officials of the present Administration would favor devaluation. They have stated their opposition to devaluation of the dollar. It is a question of whether the law provides any loophole whereby some successor might devalue.

E. E. Brown asks whether it might be possible to get an opinion of the Attorney General which might stop the continuing discussion regarding a change in the price of gold.

THE BOARD WOULD LIKE TO HAVE THE CURRENT VIEWS OF THE MEMBERS OF THE COUNCIL REGARDING PROBABLE ECONOMIC AND BUSINESS CONDITIONS DURING THE NEXT THREE TO SIX MONTHS.

E. E. Brown reads Item 2 on the agenda and the conclusions of the Council as expressed in the Memorandum to the Board which is included in these minutes. Brown assumes that the viewpoint given by Frank Garfield yesterday in his discussion with the Council on "Economic Prospects" represents the opinion of the Board staff. Brown comments that sales of refrigerators, washing machines, vacuum cleaners and even radios are all increasing.

McCabe. The economists of the twelve Federal Reserve banks are meeting in Washington now. One of them said that he thought June 1950 would be about 5 to 15 per cent above the third quarter of 1949. Most of the economists present agreed, although some thought the figures might be even higher. The economists from Cleveland and Chicago were more conservative.

Odlin asks whether the figures were dollar figures and whether the economists were considering possible increases in prices.

McCabe. The figures represent dollar volume.

Odlin states that he had in mind price increases which would make dollar volume larger.

E. E. Brown. There has been a change in public psychology since the Bethlehem Steel settlement. Without in any way questioning the opinions of the economists, Brown feels that the economists necessarily may get their figures a little later than the commercial bankers, because the commercial bankers are in-direct contact with industry. The bankers, therefore, become aware of changed conditions earlier.

WHAT SUGGESTIONS DOES THE COUNCIL HAVE TO MAKE REGARDING SYSTEM CREDIT POLICY DURING THAT PERIOD?

E. E. Brown reads Item 3, as given above, and the comments of the Council as expressed in the Memorandum to the Board which is a part of these notes. The Council is pleased that the rediscount rate was not reduced at the time the Council and the Board discussed the matter in September. The Council believes that in view of present conditions, interest rates should be firmed.

McCabe thinks that the Federal Reserve Bank of New York was concerned in September with the possible effect of the devaluation of foreign currencies. McCabe states that he has noticed the views of the members of the Council and the Board are constantly changing because of changing economic conditions. He wonders what the situation will be in three months.

Spencer. Whatever economic conditions will be, we know they will not be the same.

McCabe. The effects of devaluation in this country were almost nil and were much less than McCabe expected.

Potts asks if there is any talk of difficulties ahead, perhaps in June 1950.

McCabe. Some economists think that there will be difficulties by next summer. However, McCabe thinks that as long as Federal, state and local governments continue spending large amounts of money, there is little likelihood of depression.

Vardaman believes that the effects of devaluation may not be felt for several months. A possible decrease in private capital expenditures may be a deflationary factor, but high wages and increased pensions should lead more businesses to modernize so they can reduce costs.

Fleming. Permission for accelerated depreciation might help modernization.

Spencer. Many businesses are concentrating on improving their inventory turnover. Spencer describes the great improvement in production through modern equipment in the brass industry.

E. E. Brown. The same condition prevails in the oil industry.

DOES THE COUNCIL HAVE ANY FURTHER COMMENTS TO MAKE WITH RESPECT TO THE DECEMBER FINANCING?

E. E. Brown reads Item 4 as given above and the conclusions of the Council as expressed in the Memorandum to the Board as given in these notes. The opinions of the Council remain the same as they were in September, especially in view of the large Federal deficit.

Szymczak. The Council does not indicate that the longer-term bonds should be for banks.

E. E. Brown. No.

Burgess. Some of the addition to the debt should be in longer-term bonds. Interest rates should be firmed to accomplish this objective. Present interest rates are an invitation to states and municipalities to overborrow.

Szymaczak. Increasing reserves might help to correct the situation.

McCabe asks what the Open Market Committee should do.

Burgess. The System should sell some bonds.

E. E. Brown. The System should sell some of the bonds which it now holds. Present low interest rates tend also to cause private borrowers to overborrow. The Council would favor selling restricted issues out of the System's portfolio.

McCabe. The Treasury today would probably hesitate to go beyond a note issue. McCabe does not believe the Council and the Board are far apart in their thinking on this matter.

THE BOARD HAS BEEN ASKED TO SUBMIT TO THE PRESIDENT THE LEGISLATIVE PROGRAM AFFECTING THE FEDERAL RESERVE SYSTEM WHICH THE BOARD DESIRES TO HAVE CONSIDERED AT THE FORTHCOMING SESSION OF CONGRESS. THE FORMULATION OF THE BOARD'S VIEWS ON THAT MATTER IS NOW IN PROCESS AND IT WOULD BE GLAD TO HAVE ANY ADVICE OR RECOMMENDATIONS THAT THE COUNCIL MIGHT WISH TO MAKE IN THAT CONNECTION.

E. E. Brown begins to read Item 5 given above and the conclusions of the Council as expressed in its Memorandum to the Board as given in these notes.

McCabe asks permission to interrupt as Brown reads the comments of the Council on bank holding company legislation. McCabe asks whether the Council will accept the present holding company bill and support it when the hearings start, perhaps early in the next Congress. McCabe says that the Council made one exception at its last meeting on the question of exempting wholly-owned trust companies.

Atwood believes the bank holding company group favors the bill.

McCabe. Would the Council support the bill?

Odlin. The Council is on record many times in support of the legislation.

E. E. Brown believes the Board can count on the Council in support of the bank holding company bill.

E. E. Brown reads points (b) and (c) of Item 5, and the opinion of the Council, as expressed in the Memorandum of the Council to the Board, which is a part of these notes. In connection with point (c), dealing with direct purchases of government obligations by the Federal Reserve banks from the Treasury, Brown believes there have been no abuses of this power, but the Council thinks it advisable to review what actual use was made of the power.

Fleming thinks it would be advisable to see the record of what actually took place under this power.

McCabe agrees to provide the information.

E. E. Brown continues reading point (d) of Item 5 of the agenda with the conclusions of the Council, as expressed in the Memorandum of the Council to the Board which is a part of these notes, dealing with the cost of Federal Reserve branch buildings. Brown states that the Board should have power over the construction of its buildings.

Vardaman says the Board has extensive building plans.

E. E. Brown continues reading the comments of the Council dealing with Section 13b, as expressed in the Memorandum of the Council to the Board which is a part of these notes.

McCabe asks whether the Council has read his comments on this subject, as given in his reply to the questionnaire of the Douglas Subcommittee.

E. E. Brown reports that the members of the Council have read McCabe's comments.

McCabe. The Federal Reserve System would not make loans unless banks were interested up to ten per cent. The RFC could only make loans after it was determined that financial assistance was not available from the commercial banks and the Reserve banks. He thinks the Federal Reserve Bank of Philadelphia has done a particularly good job in this respect.

Congdon asks whether situations have developed where a bank in a smaller community has worked with the local Federal Reserve bank to compete with the correspondent bank in a large city? The small bank may desire to have the local Federal Reserve bank take a portion of a loan rather than share the loan with its city correspondent, fearing that the city correspondent may eventually take a part or all of the business from the small bank.

McCabe does not think it would be proper for the Federal Reserve bank to offer this kind of competition by working with smaller banks against city correspondents. The Board would not approve that policy.

Draper agrees.

E. E. Brown states that this has happened in Chicago. A bank, for example, in a community like Waukesha, may go either to Milwaukee or Chicago banks for help in financing a local company. Instead of going to either the Milwaukee or Chicago banks, the Waukesha bank may choose to go to the Federal Reserve Bank of Chicago, in order to avoid losing any of the business of its customer to Milwaukee or Chicago. Brown states also that the policy of the RFC is liberal, and that the Federal Reserve banks would have to be very liberal to get loans in competition with the RFC.

McCabe believes the larger manufacturer would prefer to do business with the large city bank rather than with the Federal Reserve bank as described in the case Congdon mentioned.

Atwood asks whether the Board would refuse the authority it seeks, if a bill passed Congress and left out the provision that the RFC could only lend money provided the commercial banks and the Reserve banks would not make the loans.

McCabe says the reply to the Douglas Subcommittee is the reply of the Chairman and not of the Board. But he does not specifically answer the question as to whether he would decline the authority he seeks if the provision Atwood mentions were omitted from the legislation. McCabe states that the majority of the directors of the Federal Reserve banks represent the banks, and he believes the bankers should prefer to have the authority he requests lodged in the Federal Reserve System.

Spencer would prefer leaving these loans in the other cesspool.

Kemper believes that an important angle is being overlooked in the discussion. He states that it has been said the lending operations under 13b worked out well, but Kemper believes that special consideration should be given to the fact that the loans were made during a war. The conditions now are different. The loans may be made for ten years. When the Federal Reserve System gets into this type of business now it is in a different business with different problems than it faced making loans during the war. It will be competitive with the banks, and the Federal Reserve loan policies will be liberal. Some commercial banks will favor loans in order to build local industries. The banks will take ten per cent and figure they can get out. There will be pressure from Congressmen on the members of the Board of Governors to see that the Federal Reserve banks make the loans.

Draper. Do you think that the Boards of the local Federal Reserve banks would permit such pressure and follow the policy you have outlined?

Kemper. If you are going to make good loans, we have the machinery for making such loans now in the private banking system. The other loans should be in the cesspool of socialized lending.

Evans. If any Congressman spoke to the Board we would simply say we have a decentralized central banking system, and such matters would be handled by the local Federal Reserve banks.

Draper asks whether the Federal Reserve System should have the power to help small businesses.

Kemper thinks section 13b should be repealed.

McCabe believes the Council is making a mistake if it does not seek to shift the emphasis from the RFC to the Federal Reserve System. The Council should offer some alternative instead of opposition. He has watched the trend to the left over the years, and he thinks it would be wise to offer an alternate plan to help the free enterprise system.

Odlin. If the Federal Reserve banks operate the lending function conservatively, then the government would establish another agency to make more liberal loans.

McCabe asks if the Council wishes to defeat a proposal he believes is constructive.

Hemingway inquires whether this lending activity did not originate in a depression. He also asks whether this function is not outside that of a central bank.

Szymczak replies that many central banks make loans and accept deposits.

Odlin. Isn't this the only central bank that isn't broke?

McCabe thinks there is more to this matter than letting the RFC go until it hangs itself with the banking system remaining mum. McCabe adds that we must attempt to preserve free enterprise.

Kemper. We cannot take small steps backward to socialism and think we are preserving free enterprise. Kemper does not believe a central bank properly may lend money to every small business with good ideas when the businesses need venture capital. The losses would be tremendous.

McCabe thinks private enterprise must offer alternative ideas in this trend to socialism, or we may go the way of England and other parts of the world.

Woods states he seems to be the only representative present of small banking. The small banker might even benefit from McCabe's proposal. However, Woods believes that McCabe's proposal would result in unwise expansion of the functions of the Federal Reserve System.

Vardaman inquires as to the propriety of taking banking funds of the System for this function, instead of funds appropriated by Congress.

McCabe states that it is one and the same thing as the funds would come out of the surplus of which ninety per cent now is turned back to the government.

E. E. Brown continues reading point 2 of Item 5 on consumer credit with the opinion expressed by the Council in the Memorandum to the Board which is a part of these notes.

McCabe states that he told the Douglas Subcommittee that he has reviewed the question of consumer credit regulation many times. He does not wish to press the matter. It is largely a question now of someone else urging that these controls over consumer credit be restored. He states a small automobile retailer told him recently he would not mind having Regulation W back.

Vardaman. Does the small retailer want it as a trade regulation?

E. E. Brown states that the small dealers as a rule want Regulation W as a trade regulation. Brown continues reading point 3 of Item 5 on bank reserves with the conclusions of the Council as expressed in the Memorandum to the Board which is a part of these notes.

McCabe states that in his reply to the Douglas Subcommittee he took an idea from J. T. Brown.

J. T. Brown says he noticed the Chairman had taken the idea, and the Chairman had added a little cracker at the end.

McCabe. J. T. Brown has said that all banks might have the same reserve requirements, but the non-members could carry their reserves with their correspondents.

J. T. Brown understands some states have banking boards which may fix reserves at the same percentages required of member banks.

E. E. Brown asks whether there are any other proposals the Board may submit as part of its legislative program.

McCabe. The Board has not prepared its full program. Some ideas are mentioned on page sixty-one of the printed reply of the Chairman to the Douglas Subcommittee.

ARE THERE ANY MATTERS IN CONNECTION WITH THE QUESTIONNAIRES SENT OUT BY THE DOUGLAS SUBCOMMITTEE OF THE JOINT COMMITTEE ON THE ECONOMIC REPORT THAT THE COUNCIL WOULD LIKE TO DISCUSS WITH THE BOARD?

E. E. Brown reads Item 6 and the conclusions of the Council as expressed in its Memorandum to the Board as given in these notes. Brown asks whether the Subcommittee is planning to prepare legislation on the entire field of banking as well as fiscal problems and other related aspects of the economy.

Szymczak believes the result of the Subcommittee's work may be the establishment of a Monetary Commission.

Burgess. Is it fair to ask whether the Board still favors a Monetary Commission?

McCabe. The Board is on record for it.

Congdon hopes if the Board completes a study on reserves and formulates any proposal, the Board and Council may discuss the matter fully.

Burgess. Any such study should include a study on bank earnings. There is no comment on the necessity for adequate bank earnings in the reports on this subject from time to time. Banks now are worth more dead than alive.

Fleming suggests also that it would be helpful if the Council and the Board could work together on any study of the subject of reserves.

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The meeting adjourned at 1:20 P.M.

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It was agreed that the next meeting of the Council would be held February 19-21, 1950.