~~CONFIDENTIAL~~ Fed Res Bd August 9, 1950

RECENT ECONOMIC CHANGES

Since the outbreak of hostilities buying has increased sharply from the advanced levels reached in the second quarter and prices have risen considerably further. Seasonally adjusted purchases of goods at department stores rose 20 per cent in July -- an unprecedented increase for one month. Buying of major appliances in the third week of July reached a rate which was triple the level prevailing in June. In the fourth week of July, purchases of these and other department store goods showed little abatement. Likewise, demand for passenger cars and new houses has been maintained at peak rates and in excess of the supply available. Buying, however, of such foods as sugar and coffee apparently has declined to more normal levels during the past two weeks. Business purchases of materials and orders for capital equipment also expanded sharply in July. Orders for new freight cars, for example, increased to 30,000 from 2,200 in June.

This general upsurge in buying has been in anticipation of a return to wartime shortages of civilian goods and a resumption of generally advancing prices. The buying has been financed by high and rising levels of consumer and corporate incomes, by an accelerated expansion in bank loans to business and credit extensions to consumers for purchasing durable goods and homes, and by the spending of liquid assets. Partial data indicate some recent reduction in savings bank deposits. Also, the redemption of Series E Government savings bonds exceeded purchases by 50 million dollars in July, while last July people bought considerably more bonds than they cashed.

These increases in demand have stimulated activity in those lines which had not already been at current capacity levels in June. In manufacturing, further increases in output of such goods as textile, petroleum, and machinery products are possible and expected during the third quarter but production of these and other finished goods is limited by the supply of such basic materials as steel, nonferrous metals, lumber, cement, and rayon. Output of fuels and other minerals are rising and the Board's total index of industrial production in August is likely to be about 205 per cent of 1935-39 -- up 3 per cent from the peacetime record level in June and up one-fifth from a year ago.

Construction activity continued to rise in July and the volume of new contracts awarded indicates that building activity will be sustained at record levels in August. Prices of building materials have advanced further since June to new highs and property values are again rising.

Total nonagricultural employment has increased considerably and is close to the record level reached in mid-1948. Unemployment is still about 1 million greater than at that time reflecting the increase in the labor force. Average hours worked indicate that a substantial amount of overtime is being put in, particularly in the durable goods industries.

Agricultural production will be down somewhat this year. Total crop production was expected earlier to be 6 per cent below last year's large volume and recent crop developments have shown little improvement. Carryovers of basic crops, however, are larger than last season and stocks of livestock products are greater. Farm marketings of livestock products are running somewhat above last year's level.

Altogether, production of these and other goods and services were at record levels and rising before the Korean crisis. At the same time, however, over-all demands were also at advanced levels and rising. Consumer demands for automobiles and other durable goods were exceptionally active, reflecting the rising level of employment, the stimulus of the large veterans insurance dividends, and the widespread use of credit on easy terms. Consumer credit outstanding increased by about 550 million dollars in June to a level of 19.6 billion dollars. Mortgage and other credit similarly increased sharply. Business demands for inventories were expanding further and earlier plans for expenditures on plant and producers equipment were being revised upward. Government stockpiling activities were being stepped up, and various other developments, especially in the international sphere, also were expanding demands for goods in this country and abroad.

As a result of these upward pressures, wholesale prices, especially of imports, metals, lumber, and livestock, rose considerably in April and May and in June the consumers' price index increased further by 1 per cent. The upsurge in buying since that time has been followed by sharp rises in prices, especially of raw materials and foods. Basic commodities have risen 16 per cent and on August 8 were 25 per cent higher than in March. The sharpest advance has been in rubber to 61 cents per pound as compared with 29 cents in June and 20 cents in March. All commodities at wholesale by August 1 had risen 5 per cent in five weeks and were 8 per cent higher than in March. Wholesale prices of farm products and foods were up 12 per cent from March and industrial commodities, 5 per cent. Retail food prices now are nearly 10 per cent higher than in March and the total of consumer prices -- including controlled rents -- is probably up 4 per cent.

Since August 1 prices of domestic basic commodities have leveled off. Buying interest in these commodities has been reduced by actual and prospective increases in market supplies and growing sentiment for Federal action to curb inflationary developments. Prices of rubber and other imports, however, have continued to advance, scrap metal prices are now rising, and additional increases have occurred in prices of manufactured goods.

Division of Research and Statistics,
Board of Governors, Federal Reserve System.

Recent Changes in Prices

Series	Percent rise to Aug. 1, 1950 from:		
	Week ending		1948
	June 24	March 18	monthly highs
Consumer Prices			
All items	2	4	-1
Foods	4	9	-3
Apparel	0	0	-8
Rent	0	1	4
Wholesale Prices			
All commodities	5	8	-3
Farm products	8	12	-12
Grains	1	2	-35
Livestock	10	23	-12
Foods	8	13	-8
Other commodities	3	5	0
Textile products	8	7	-4
Chemicals	6	4	-14
Building materials	4	8	2
Metals and metal products	1	3	0
28 Basic commodities	15	23	-14
Selected items:			
Rubber	84	171	
Lard	39	41	
Print cloth	28	28	
Hides	26	28	
Tin	25	27	
Hogs	19	43	
Cocoa	18	71	
Wool tops	17	30	
Cotton	13	20	
Coffee	13	18	
Sugar, raw	7	12	
Steers	5	6	
Wheat	3	0	
Zinc	0	47	
Copper	0	22	
Steel scrap	-2	39	

Note: Compiled from B.L.S. data. August 1 consumers prices estimated by Federal Reserve.

THE WHITE HOUSE
WASHINGTON

August 25, 1950

Dear Tom:

I want the members of the Federal Reserve Board and the members of the Federal Open Market Committee to understand that I approved on last Friday afternoon a refunding of United States Government securities involving Thirteen and a Half Billion Dollars ($13-1/2 billion) of issues maturing between now and the late fall.

I understood from my conversation with you over the telephone that this action would have the complete support of all the agencies which have been granted responsibility in that line.

It is of paramount importance that confidence be maintained in the credit of the United States. I have discussed the matter with the Secretary of the Treasury since the Korean outbreak and we are in complete agreement.

I think it is imperative that at the earliest possible moment all operations of the Federal Reserve Board and actions relating to the market for Government securities be so adjusted that outstanding United States Government securities sell at par.

I want the situation maintained as it was when you and I had our conversation the other evening on the action to be taken by the Federal Reserve Board with regard to public credit.

Sincerely yours,

Harry Truman

Honorable Thomas B. McCabe
Chairman, Board of Governors
of the Federal Reserve System
Washington 25, D. C.

THE SECRETARY OF THE TREASURY
WASHINGTON

MEMORANDUM TO THE PRESIDENT

Last Friday afternoon I announced to the market that the \$13-1/2 billion of Treasury bonds and certificates of indebtedness, maturing or called for redemption on September 15 and October 1, would be refunded into 13-month, 1-1/4 percent Treasury notes, which issues have to be approved by you under the provisions of the Second Liberty Bond Act, as amended. In essence and reality, therefore, the offering of Treasury notes is an action undertaken by the President of the United States.

When the market opened on Monday morning, the Open Market Committee of the Federal Reserve System, through its open market operations, established and maintained a pattern of prices on various short-term issues of Government securities which would justify a 1-3/8 percent rather than a 1-1/4 percent rate on Treasury notes of the type offered in connection with the refunding. Their operations, if continued along the lines followed up to now, are untenable because they will force a market failure of the refunding of the \$13-1/2 billion of maturing issues which you approved on Friday.

This matter is one of most serious import because it aims directly at the matter of maintaining confidence in the financial strength of the United States Government. As you know, confidence in our financial strength and stability, both at home and abroad, is of prime importance. I developed this matter fully with the Federal Reserve immediately after the outbreak of the Korean crisis and in my letter of July 17, a copy of which is attached. Years have been spent in building up confidence in this strength and the action of the Federal Reserve at a time when the debt is \$257 billion, and when its successful management is no simple matter, may have serious results in our successful prosecution of the war effort. It is of paramount importance that no uneasiness about the management of the public debt should occur, yet such uneasiness could become wide-spread easily if a loss of confidence should result in the action of the Federal Reserve, and wholesale liquidations of Government securities, particularly savings bonds, could be touched off among non-bank investors.

I mention these matters not to be an alarmist, but with the view of approaching the situation objectively so that I may convey to you the seriousness and possible ultimate effect on our war effort itself, which might result from a financial disturbance of importance.

RECOMMENDATION

It is my recommendation that you advise the Federal Reserve Board that you approved the Treasury refunding announced last Friday, as required by law; and that you advise the Federal Reserve that you intend that all agencies of the Government, with public powers and responsibilities, are to do everything necessary to make this operation a success; and that you are fully aware that there need be no difficulty toward making the present operation a success if it is the Board's intention to do so and the Board takes appropriate action along the lines with which it is completely familiar.

John W Snyder

Attachment

THE WHITE HOUSE
WASHINGTON

My dear Mr. Chairman:

I wish that you would convey to the members of the Federal Reserve Board and other members of the Federal Open Market Committee, that, as required by law, I approved on last Friday afternoon a refunding of United States Government securities involving $13-1/2 billion of maturing issues. It is reasonable for me and the Nation to expect that this action should have the complete support of all the agencies which have been granted public power and responsibility.

It seems to me that under the present circumstances it is of paramount importance that confidence be maintained in the credit of the United States, and that stability be maintained in the Government security market. I understand that the Secretary of the Treasury outlined his views on these matters to you fully immediately after the outbreak of the Korean crisis, and in his letter of July 17.

It is imperative that at the earliest possible moment, all of your operations and actions relating to the market for Government securities be so adjusted that outstanding United States Government securities sell at yields which will make the 13-month 1-1/4 percent issue attractive and insure complete success of the refunding operation. This was essentially the situation in the Government security market that prevailed when I approved the 13-month, 1-1/4 percent issue on last Friday.

Sincerely,

Honorable Thomas B. McCabe
Chairman, Board of Governors
of the Federal Reserve System
Washington 25, D. C.