FEDERAL RESERVE BULLETIN

VOLUME 36 | *October 1950* | NUMBER 10

RECENT MONETARY AND CREDIT DEVELOPMENTS

When Southern Korea was invaded late in June, output and employment in the United States were close to peacetime record levels, credit had been expanding, and prices had been rising for some weeks. Prospective increases in Government expenditures for military purposes, it was evident, would impose serious strains on both production and prices. The impact of the new defense program would be greater in magnitude and earlier in timing than was suggested by the need for adding some 10 billion dollars of defense expenditures to the Federal budget during the fiscal year 1951 and somewhat more later. The greater and more immediate impact arose from the rapid increase in expenditures of businesses and consumers in anticipation of shortages of civilian goods and of advances in prices.

The needs of the situation were indicated by the President in his Midyear Economic Report, dated July 26, 1950, in the following statement:

> "First of all, for the immediate situation, we should rely in major degree upon fiscal and credit measures. These general measures can be helpful not only in restraining inflationary pressures, but also in reducing the civilian demand for some specific products, such as automobiles and housing, thus making available for necessary military use a larger proportion of an already short supply of some critical materials. The more prompt and vigorous we are with these general measures, the less need there will be for all of the comprehensive direct controls which involve the consideration of thousands of individual situations and thus involve infinitely greater administrative difficulties and much greater interference with individual choice and initiative."

On the fiscal side, an increase in taxes has been enacted and other tax increases are being considered. The Treasury has raised the limits for purchases of Series F and G savings bonds by certain classes of institutional investors and banks in the early part of October, November, and December 1950. Further details concerning the special offering appear on pages 1291-92 of this BULLETIN. A new campaign is also being inaugurated to promote sales of Series E bonds, especially through payroll savings plans. Additional sales of savings bonds will help to absorb funds that might otherwise be available for civilian spending.

MEASURES ADOPTED BY THE FEDERAL RESERVE

On the monetary and credit side, the authorities of the Federal Reserve System—the Board of Governors and the Federal Open Market Committee—on August 18, 1950, agreed upon a policy to place curbs on overall inflationary credit expansion. In line with

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this decision, the following actions have been taken by the Federal Reserve:

(1) Discount rates have been raised from 1½ to 1¾ per cent at all Federal Reserve Banks in order to discourage borrowing by member banks of additional reserves to support further credit expansion.

(2) Open market operations have been directed toward the aim of discouraging sales to the Federal Reserve of short-term United States Government securities, including sales by banks to obtain funds for extending other types of credit.

(3) Early in August the Board of Governors joined with other Federal and State bank supervisory agencies, including the Home Loan Bank Board, in a statement requesting the voluntary cooperation of banks and other lenders in restricting their lending and investment activities.

(4) Effective September 18, under authority of the Defense Production Act, the Board of Governors again placed consumer instalment credit under regulation.

(5) Effective October 12, the Board of Governors, under authority of the Defense Production Act and with the concurrence of the Housing and Home Finance Administrator, placed under regulation credit not extended, insured, or guaranteed by the Federal Government for constructing, purchasing, and financing new houses. At the same time, the Federal Housing Administration and the Veterans Administration issued new regulations designed to produce a similar tightening of credit under Federal programs. Regulation X of the Board appears on pages 1314-21, and the joint statement of the Board and the Housing and Home Finance Administrator on pages 1284-86, of this BULLETIN.

(6) Effective October 16, the Board stiffened the regulatory limits on consumer instalment credit by increasing the minimum down payments and reducing the maximum maturities on certain instalment credits, and by lowering the price below which down payments are not required. The Board's statement appears on pages 1281-83, and the amendment to Regulation W on pages 1308-09, of this BULLETIN.

BANK CREDIT EXPANSION

Expansion of bank credit, which had begun to accelerate in May, continued at a very rapid rate after June. Commercial banks increased their total loans by an estimated 4 billion dollars in the third quarter and their holdings of State and local government and corporate securities by about 800 million dollars. The expansion since June in credit to private borrowers and to State and local governments, which has been in part seasonal, has exceeded that in any peacetime period of similar length. Much of the recent sharp expansion in loans reflects commitments made before restrictive credit policies began to be imposed. Some of the expansion may have reflected anticipation of future needs.

Businesses, as the chart shows, have been especially heavy borrowers in recent months, as they have anticipated shortages of materials and increases in prices as well as provided for seasonal needs. Bank loans to business have accounted for more than half of the over-all loan expansion in the past three months. The increase in business loans has been substantially greater than in the same period of 1946, the previous record year.

Credit extended by banks and other lenders to purchasers of houses has been a large factor in the recent expansion of private credit. New loans on small residential properties during the first nine months of 1950 are estimated at slightly less than 11 billion

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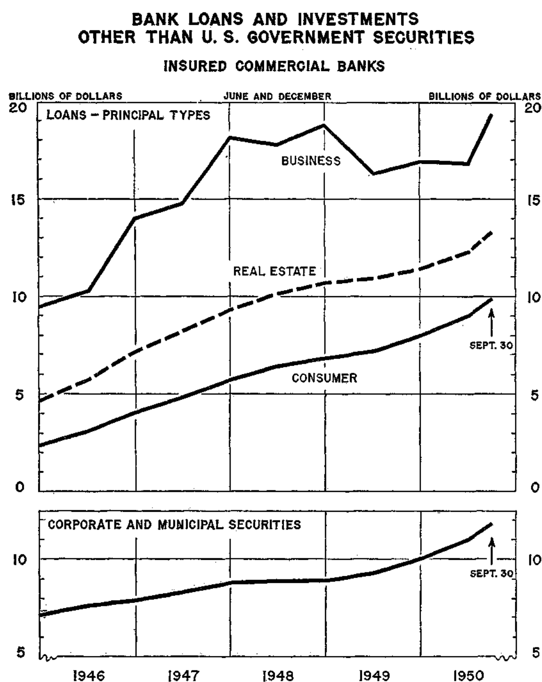

All insured commercial banks in the United States. Figures for June 30 and Sept. 30, 1950, are partly estimated. Business loans include commercial and industrial loans, open-market commercial paper, and acceptances. Agricultural loans and loans for purchasing or carrying securities are not shown. Municipal securities include State and local government obligations.

dollars, or an annual rate of almost 14.5 billion compared with roughly 11 billion in each of the past three years. Reflecting a more rapid expansion in new debt than in repayment of previously contracted loans, mortgage debt outstanding on 1-4 family houses increased nearly 2 billion dollars in the third quarter compared with an increase of less than 4 billion during the entire year 1949. Loans of commercial banks on homes and other real estate increased during this three-month period by about 900 million dollars, which was about as much as in the preceding six months.

Even before the Korean crisis banks and other lenders were financing a marked expansion in consumer buying, especially of durable goods through the extension of instalment credit. After June consumer instalment credit increased more sharply. The expansion of about 1,200 million dollars in the third quarter compared with 800 million in the same period of 1949, and the amount outstanding at the end of September exceeded 13 billion dollars, about one-third above the level 12 months earlier. Consumer loans by commercial banks increased about 900 million dollars in the third quarter, thus matching the growth during the entire last half of 1949.

Banks have also added substantially to their investment in corporate and State and local government securities in the past three months. Commercial bank portfolios of these securities increased by an estimated 800 million dollars, which was equal to the increase in the first half of this year. The bulk of the purchases were State and local obligations.

Money Supply

Recent growth in bank credit has added considerably to the money supply. During the third quarter of 1950 the total of currency and bank deposits held by individuals and businesses increased more than 2 billion dollars to a new peak level of about 172 billion. As shown in the chart on the next page, this rapid rate of increase almost equaled that of the third quarter of 1947—a period of substantial inflation. The increase would have been much more rapid had not nonbank investors, particularly business corporations, drawn upon growing cash balances to purchase a large volume of Government securities from the banking system during this period.

Increased spending in the economy since midyear has been financed in part by more active use or turnover of money. After rising almost steadily during the first half of the year, the turnover of demand deposits at

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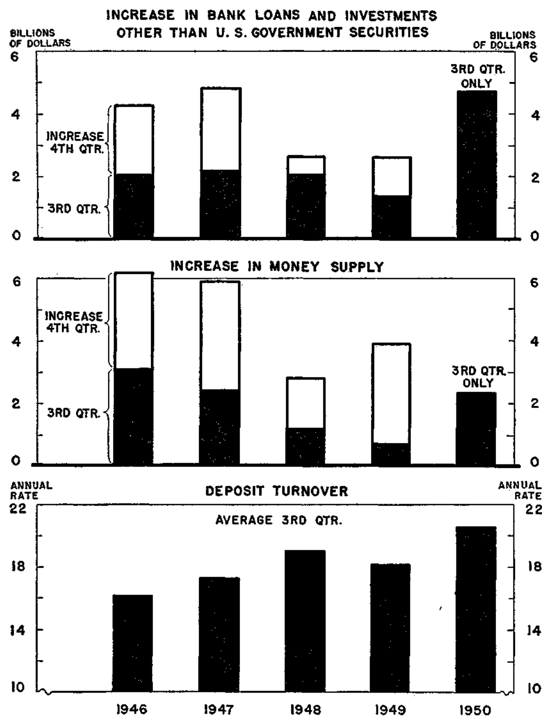

Loans and investments other than U. S. Government securities include figures for all commercial banks in the United States; third quarter of 1950 is partly estimated. Private money supply data include total deposits adjusted at all banks and currency outside banks. Adjusted deposits are total deposits less interbank and U. S. Government deposits and cash items reported as in process of collection; third quarter of 1950 is partly estimated. Deposit turnover data are averages of monthly figures for July, August, and September of the ratio of debits to the level of demand deposits, excluding interbank and U. S. Government deposits, at weekly reporting member banks in leading cities outside New York. September 1950 is partly estimated.

banks in leading cities outside New York accelerated during the third quarter. In that period, as the chart shows, deposits were more active than in the corresponding quarters of any postwar year. The rate of use of deposits is now higher than at any time in more than a decade but is still low relative to the 1920's. The existing volume of deposits could be the basis for a considerable further increase in spending without the creation of additional money.

One factor in the recent increase in spending has been the reduction in certain types of liquid asset holdings by individuals. During the third quarter time deposits at commercial and mutual savings banks declined by approximately one-half billion dollars, redemptions of savings bonds exceeded purchases by about one-third billion, and shareholding at savings and loan associations were also drawn down. In the same period of last year savings deposits showed little change, while purchases of savings bonds exceeded redemptions, and shareholdings at savings and loan associations showed a substantial increase. In recent weeks, however, there has been some slackening in the reduction of total liquid asset holdings by individuals.

Shifts in Holdings of Government Securities

Commercial banks acquired large aggregate amounts of United States Government securities during the war period, and the proportion of short-term securities to total bank holdings has expanded in recent years. As shown in the accompanying table, which gives the principal types of assets held by the various classes of member banks, these banks on June 30, 1950, held liquid secondary reserves amounting to about 47 per cent of total deposits, compared with ratios of about 34 per cent in 1947 and 1948. This increase has resulted primarily from a shift in the maturity distribution of bank holdings of Government securities. The outstanding amount of all marketable Government securities maturing within five years was 58 per cent of the total marketable debt on June 30, 1950, compared with about 40 per cent in June of both 1947 and 1948.

The large proportion of short-term securities held in excess of customary liquidity needs, the relatively low yields on short-term securities, and the increased availability of other loans and investments together have resulted in recent months in intensifying a tendency by banks to sell short-

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LIQUIDITY POSITION OF MEMBER BANKS

Balance sheet item or date	All member banks	Central reserve city banks in— New York	Chicago	Reserve city banks	Country banks
A. Balance sheet items as of June 30, 1950 (in billions of dollars)					
Assets					
Cash assets other than required reserves	14.0	1.9	0.5	5.6	5.9
U. S. Government securities					
Short-term [1]	43.7	8.0	2.3	16.1	17.3
Long-term	12.1	2.3	0.9	4.4	4.5
Loans and other securities	47.0	9.3	2.1	18.2	17.4
Liabilities					
Deposits	122.7	23.2	6.4	47.2	45.9
Capital	9.5	2.3	0.5	3.3	3.4
B. Liquidity position[2] as a percentage of deposits					
June 30, 1950	47	43	44	46	51
Dec. 31, 1949	48	46	45	47	52
June 30, 1948	34	26	28	34	39
June 30, 1947	34	27	30	33	39
June 30, 1941	38	42	39	37	37

[1] Securities maturing within five years. Most of these issues were due or callable within two or three years.
[2] Liquidity position includes all cash assets plus short-term Government securities (maturing within 5 years), but does not include required reserves.

term Government securities, particularly Treasury certificates and short-term notes, and to shift to loans and corporate and municipal securities.

To some extent during this year corporations and other nonbank investors have purchased short-term Government securities, especially bills and savings notes. In the first seven months large amounts of long-term bonds were also purchased by a broad group of nonbank investment institutions, including particularly numerous pension and trust funds. Most of these securities were supplied from the Federal Reserve portfolio, although life insurance companies sold some bonds. Individuals added to their holdings of savings bonds. These net additions to holdings of Government securities were made while nonbank investors generally were placing large amounts of funds in mortgages and in other securities. The following table shows estimates of changes in holdings of various types of Government securities by the principal investor groups during the first seven months of this year. During August and September, for which complete figures are not yet available, commercial banks continued to sell Government securities in substantial amounts in order to obtain funds to increase loans and other investments. There was also some net retirement of securities by the Treasury. The Federal Reserve bought a large portion of the securities sold by commercial banks. Corporations apparently continued to increase their holdings of savings notes and Treasury bills.

CHANGES IN HOLDINGS OF UNITED STATES GOVERNMENT SECURITIES, BY TYPE OF INVESTOR

DECEMBER 31, 1949—JULY 31, 1950

[In billions of dollars]

Type of security	Total outstanding	Federal agencies and trust funds	Federal Reserve Banks	Commercial banks	Nonbank investors
Marketable public issues:					
Bills	+1.3	(1)	−0.7	−0.5	+2.5
Certificates and notes	+0.7	(1)	+2.1	−0.8	−0.5
Bonds:					
Bank eligible	−2.0	(1)	−0.2	−0.7	−1.0
Bank restricted	......	+0.1	−2.1	+0.1	+1.9
Nonmarketable public issues:					
Savings bonds	+0.9	(1)	......	−0.1	+0.9
Savings notes	+1.0	......	......	(1)	+1.0
All other	−0.2	......	......	−0.1	−0.1
Special issues	−1.4	[2] −1.4	......	......	......
Total	+0.4	−1.4	−0.9	−2.1	+4.8

[1] Less than 50 million dollars.
[2] Reflects redemption of 2.8 billion dollars of issues to meet the National Service Life Insurance dividend and increase in other special issues.
NOTE.—Figures may not add to totals because of rounding.

FEDERAL RESERVE OPERATIONS

Bank reserves, which provide the basis for expansion in deposits and the volume of money, have been supplied principally by Federal Reserve purchases of Government securities in the open market. Since the first quarter of the year, when there was a seasonal contraction in deposits and consequently in required reserves of banks, both reserves and Federal Reserve holdings of securities have increased.

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The Federal Reserve has generally purchased certificates and other issues approaching redemption. At the same time, the System has sold substantial amounts of long-term bonds to supply investment demands and has also sold some shorter term issues for which there were market demands. During the second quarter of this year net purchases supplied funds for a 300 million dollar increase in the required reserves of member banks.

MAJOR FACTORS AFFECTING MEMBER BANK RESERVES

[In billions of dollars]

Changes in	1950		
	First quarter	Second quarter	Third quarter
Factors affecting bank reserves:			
Federal Reserve holdings of U. S. Government securities:			
Bills	−0.9	−0.1	−2.4
Certificates and notes	+0.4	+1.6	+5.4
Bonds	−0.8	−0.8	−1.8
Total	−1.3	+0.7	+1.2
Gold stock	−0.2	(1)	−0.7
Money in circulation	+0.6	−0.1	(1)
Treasury deposits at Reserve Banks	−0.2	+0.1	−0.2
Other factors	+0.2	−0.4	+0.4
Member bank reserves, total	−0.9	+0.3	+0.8
Required reserves	−0.4	+0.3	+0.4
Excess reserves	−0.5	−0.1	+0.4

[1] Less than 50 million dollars.

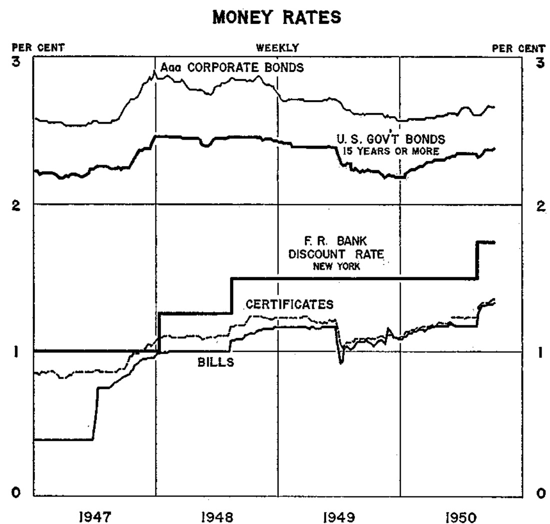
NOTE.—Signs before figures indicate effect on bank reserves. Detailed figures may not add to totals because of rounding.

The net result during the third quarter of Federal Reserve operations and of other factors in the demand for Federal Reserve credit was an increase of 1.2 billion dollars in total Federal Reserve holdings of Government securities. Additions to reserves from these purchases were offset in part by a 700 million dollar outflow of gold, and there were other factors affecting reserves, largely of a temporary nature. On a net basis bank reserves were increased about 800 million dollars.

MONEY RATES

Short-term money rates have tended to stiffen during most of this year, reflecting growing credit demands. This trend was moderated by Federal Reserve purchases of short-term securities, but some rise occurred in rates on bills and certificates. Rates on three-month bills, which were about 1.10 per cent at the end of 1949, rose to about 1.17 per cent by June, while the one-year rate rose from 1.10 to 1.23 per cent. In the latter part of August and in September yields on short-term securities increased by about ⅛ of 1 per cent. Yields on new Treasury bills were at 1.32 per cent by the end of September and on securities with one year to maturity about 1.35 per cent. In October these yields rose further.

MONEY RATES



Corporate bond yields, Moody's Investors Service. For Treasury bills, rate is average discount on new issues during week. Beginning in June 1950, Treasury certificate series is based on 9-12 month note issues. Latest figures are for week ending Oct. 14.

Long-term Treasury and high-grade corporate bonds have followed somewhat different courses. Yields on long-term Treasury bonds, which were at extremely low levels at the end of 1949, increased in the first half of 1950 by about ⅛ of 1 per cent with the

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adoption by the Federal Reserve of a program for selling Government bonds to meet the strong investor demand for these securities. In this period corporate bond yields rose only slightly. Since June yields on both high-grade corporate and long-term Treasury bonds have fluctuated moderately, but in late September and early October they were slightly above the June level.

Average rates on business loans made by banks in leading cities in the first half of September were somewhat lower than in the same period of June. Since mid-September, however, a number of large city banks have announced increases in their rates on business loans of about ¼ of 1 per cent.

FEDERAL RESERVE ACTION UNDER THE DEFENSE PRODUCTION ACT OF 1950

REGULATION OF CONSUMER INSTALMENT CREDIT
(Regulation W, effective September 18, 1950)

Issuance of Regulation W[1]

Under the authority of the Defense Production Act of 1950, the Board of Governors today reinstituted regulation of consumer instalment credit through Regulation W effective at the opening of business September 18, 1950.

The Regulation covers automobile instalment credits of $5,000 and less and other instalment credits of $2,500 and less. Except that home improvement credits are now covered and terms are generally tightened, the Regulation is in much the same form as the Regulation which expired June 30, 1949.

The limitations initially established are:

Down payments of at least one-third, and maximum maturities of 21 months for automobiles.

Down payments of at least 15 per cent, and maximum maturities of 18 months for appliances: refrigerators, food freezers, radio or television sets, phonographs, cooking stoves, ranges, dishwashers, ironers, washing machines, clothes driers, sewing machines, suction cleaners, air conditioners and dehumidifiers.

Down payments of at least 10 per cent, and 18 months maximum maturity for furniture and rugs.

Down payments of at least 10 per cent, and 30 months maximum maturity for home repairs, alterations or improvements.

Following the past policy of placing fewer restrictions on small credits, the new Regulation does not contain down payment requirements for articles costing less than $100 although, unlike the former Regulation, maturities are limited.

Instalment loans for the purchase of any listed article carry the same limitations that apply to the instalment sale of the article; other instalment loans are limited to a maximum maturity of 18 months.

In establishing the initial terms the Board took into account the prevailing practices and terms in the trades affected. There has been a material relaxation of instalment credit terms during the past year or more, and the requirements of the Regulation are substantially tighter than the terms now widely offered.

In the automobile field the great majority of recent instalment sales of new cars and late model used cars are reported as having been financed on substantially easier terms, either as to down payments or maturities or both, than permitted by the new Regulation.

Similarly, many instalment sales of appliances and furniture are reported as having been made

[1] Statement to the Press on Sept. 8, 1950, for release on the following day. For complete text of the Regulation, see the Federal Reserve BULLETIN for September 1950, pp. 1177-85.

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FEDERAL RESERVE BULLETIN

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RECENT MONETARY AND CREDIT DEVELOPMENTS

Monetary expansion, which had been at a very rapid rate in the last half of 1950, was interrupted in the first half of 1951 and the volume of privately held deposits and currency declined somewhat. This development was the result primarily of a large surplus of Treasury cash receipts over expenditures and a gold outflow, both of which occurred in the first few months of the year, and some slackening in bank credit expansion during most of the second quarter.

Demand for credit continued very large in the first half of this year, and availability of credit at banks and at other lending institutions was brought under increased restraint by a series of measures adopted by the Federal Reserve System and the Treasury. Stronger limitations were put on the availability of bank reserves for credit expansion by increases in member bank reserve requirements and particularly through the adoption of a more restrictive Federal Reserve open market policy. The latter action was taken to hold to a minimum the monetization of the Government debt and to encourage lenders to retain their Government securities rather than sell them in order to lend to private borrowers.

These measures for curtailing general availability of credit were supplemented by a voluntary credit restraint program through which banks and other lending institutions cooperate to restrict nonessential credit. Regulations limiting the terms for consumer instalment credit, stock market credit, and certain kinds of mortgage credit, most of which were in effect at the beginning of the year, also restricted the use of credit in these areas.

Expansion of the private money supply is likely to occur in the second half of 1951 for seasonal business reasons and as the Treasury draws on the large cash balance which it held at midyear to pay for the growing volume of defense production. The amount of any additional monetary growth will depend largely on the extent to which bank credit is used for financing either private expenditure programs or Government defense spending.

CHANGES IN THE MONEY SUPPLY

Total private holdings of deposits and currency declined about 2.5 billion dollars in the first half of 1951. This development, which was due partly to seasonal factors, followed an exceptionally large increase in the second half of 1950 and a period of stability in the first half of 1950 prior to the Korean outbreak, as is shown on the chart on the following page.

Most of the contraction was in privately held demand deposits. These declined over 2 billion dollars in the first half of 1951 as compared with a drop of less than a billion dollars in the same period a year ago and an increase of over 7 billion in the last half of 1950. Time deposits rose slightly, reversing the decline that accompanied the consumer buying wave last summer. Currency out-

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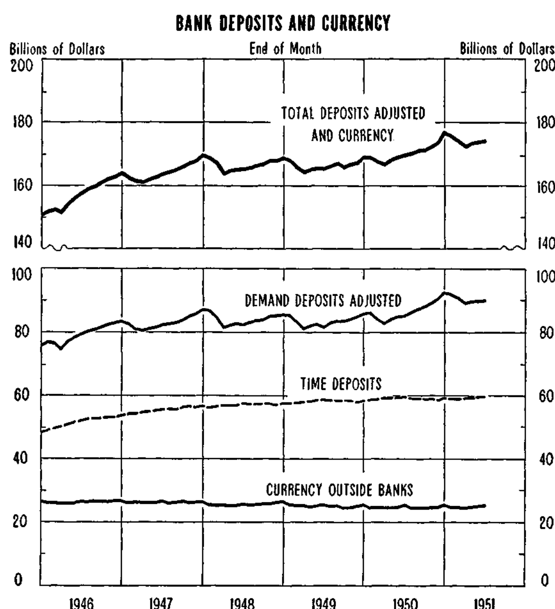

Data partly estimated by Federal Reserve on dates other than June and December. Demand and time deposits partly estimated on June and December dates through December 1946. Demand deposits adjusted exclude interbank and U. S. Government deposits and cash items in process of collection. Time deposits include those in Postal Savings System and in mutual savings banks as well as in commercial banks, but exclude interbank deposits. Data are for end of month, 1946, and last Wednesday of month thereafter except for June and December call dates. Data subsequent to December 1950 are preliminary. Latest figures are for June 27, 1951.

side banks declined by about the usual seasonal amount for the first half of the year.

Although the amount of money held by individuals and businesses decreased somewhat during the first half of 1951, the rate of its use continued to increase. Turnover of demand deposits at banks in leading cities outside New York has been at the rate, after adjustment for seasonal variation, of 22 times a year, which is higher than at any time since 1937. Turnover began to increase with the expansion of economic activity early in 1950 and accelerated sharply after the Korean outbreak, as is shown in the chart. The rate of turnover of deposits is still much lower than it was in the 1920's.

The decline in the privately held money supply in the first half of the year reflected primarily the favorable developments in the fiscal position of the United States Government, a gold outflow, and a combination of restrictive credit and debt management measures. During the six-month period Government cash receipts from the public, including receipts of Government agencies and trust funds, exceeded expenditures by about 6.8 billion dollars. The surplus was built up in the first quarter of the year when receipts from corporate and individual income taxes were greatly in excess of expenditures. While this is a customary seasonal development, the excess was much larger this year than in other recent years. Over 4.6 billion dollars of the cash surplus was used in a way which tended to reduce the private money supply over the first half of 1951. A substantial amount was retained in the Treasury's cash balance, which increased over 3 billion dollars during the period. The rest of the Government surplus —3.7 billion—was used for debt retirement. About 1.6 billion of this was reflected in a reduction in bank portfolios and had a contractive effect on the volume of money, as is

MAJOR FACTORS AFFECTING THE MONEY SUPPLY

[In billions of dollars; partly estimated]

Factor	1951—First half	1950		
		First half	Second half	Year
	(Sign indicates effect on money supply)			
Bank loans and investments other than U. S. Govt. securities[1]	+3.9	+3.5	+9.5	+13.0
Bank holdings of U. S. Govt. securities[2]	−1.6	−1.7	−2.0	−3.6
Treasury deposits	−3.0	−0.7	+1.1	+0.4
Gold stock	−1.0	−0.2	−1.5	−1.7
Other factors	−0.8	−0.7	−0.1	−1.0
Privately held money supply, total[3]	−2.5	+0.2	+7.0	+7.1
Demand deposits adjusted	−2.4	−0.7	+7.2	+6.5
Time deposits adjusted[4]	+0.3	+1.1	−0.5	+0.6
Currency outside banks	−0.4	−0.2	+0.2	([5])

[1] Commercial and mutual savings banks.
[2] Commerical and mutual savings banks and Federal Reserve Banks.
[3] Excludes deposits and currency held by banks and the U. S. Government.
[4] At commercial and mutual savings banks and the Postal Savings System.
[5] Less than $50,000,000.

NOTE.—Changes are based on data for Dec. 31, 1949, June 30, 1950, Dec. 30, 1950, and June 27, 1951. Estimates for June 27, 1951 are preliminary. Figures may not add to totals because of rounding.

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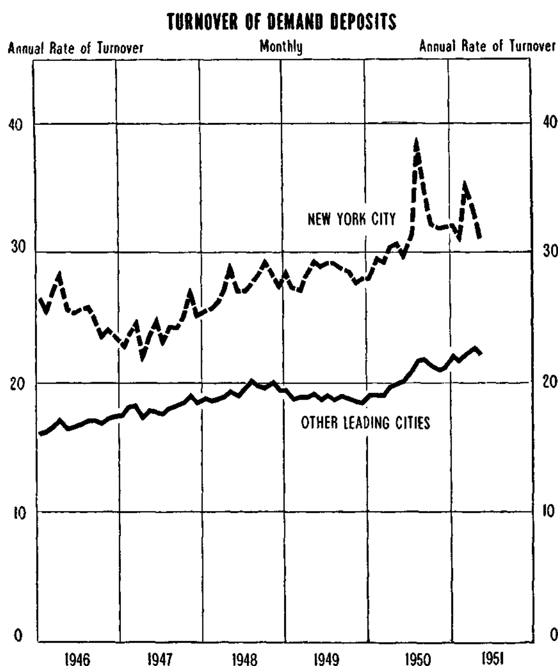

Turnover rates are seasonally adjusted and are compiled by the Federal Reserve Bank of New York. Deposits used are monthly averages of demand deposits, except U. S. Government and interbank deposits, as reported weekly by member banks in leading cities. Latest data are for May 1951.

shown in the table. Private nonbank investors also reduced their holdings of Government securities about 2 billion dollars. Government cash surplus used ultimately for retiring this debt was thereby returned to private balances.

A decline in the gold stock of the United States exerted a further contractive influence on the money supply. The gold outflow, which had been under way since late 1949, accelerated in the second half of 1950 and reached a peak in the early months of 1951. Since April, however, it has nearly ceased. The outflow of gold since 1949, arising from the net flow of dollar payments to foreigners throughout the period, had been due basically to a marked increase in United States imports and to an expansion in the outflow of private capital from the United States, while the downward adjustment of United States financial aid to foreign countries proceeded more slowly. In addition, there was in the first quarter of 1951 some movement by foreign monetary authorities to convert accumulated dollar balances into gold. The change since April has reflected both the reappearance of a large export surplus from this country and a tendency for foreign countries to keep dollar accruals in the form of dollar balances or securities rather than in gold.

Contractive effects on the private money supply of the large Treasury cash surplus and the gold outflow in the first quarter of 1951 were offset in part by a continued expansion of bank credit to borrowers other than the United States Government. Following an exceptionally rapid increase in the last half of 1950, bank loans and bank investments in State and local government securities increased considerably further during the first quarter of 1951, a period of the year when such credit usually shows little change or declines somewhat. The expansion slackened in the second quarter although there were substantial increases late in this period.

Recent Measures of Credit Restraint

Measures for combating inflation by restraining credit expansion were undertaken shortly after the outbreak in Korea in mid-1950 and were broadened in the first half of 1951. Action has been taken along several lines to restrict the total volume of credit available, to limit the demand for certain kinds of credit, and to channel into essential areas such credit as is available.

To restrict the availability of bank reserves for loan expansion, changes were made in the Federal Reserve discount rates and open-market operations in the second half of last year. These measures were greatly strengthened by several actions taken in the first half of 1951. In January reserve requirements of member banks were raised

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to their upper legal limits except at central reserve cities. This increased by about 2 billion dollars the amount of reserves member banks were required to keep. It absorbed the nearly 1 billion dollars of new reserves that banks acquired through a post-Christmas return of currency from circulation and also put banks under pressure to sell Government securities in order to adjust their reserve positions. These sales further reduced the volume of Government securities, particularly short-term issues, which banks could sell or cash at maturity in order to expand their loans.

Early in March the Treasury and the Federal Reserve announced that an agreement had been reached with respect to debt management and monetary policies to be pursued in furthering their common purpose to minimize monetization of the public debt and at the same time to assure the successful financing of the Government's requirements. In accordance with this agreement, the Treasury offered in exchange for the two longest-term 2½ per cent restricted bonds an issue of nonmarketable bonds with a longer term and a higher interest coupon and with the privilege of conversion into shorter-term marketable 1½ per cent notes. The purpose of this offering was to encourage long-term investors to retain these Government securities and thus minimize monetization of the public debt through their liquidation. Of the total of 19.7 billion dollars of the restricted Treasury bonds of 1967-72 outstanding, 13.6 billion were converted.

While the Treasury acted to immobilize part of the publicly held debt, the Federal Reserve took steps to check the sale of marketable Government securities to the Reserve Banks. The System closely limited its purchases of short-term securities to what was essential in connection with short-run money market adjustments. Following this change in System open market operations, rates on short-term Government securities rose irregularly in March and April and reached levels in mid-May about ¼ to ⅜ of 1 per cent above those prevailing early in the year.

During most of April and in May Federal Reserve open market operations tended to reduce the volume of bank reserves and to keep banks under pressure to maintain their reserve positions. Some selling of short-term Government securities by banks as well as substantial sales of Treasury bills by the Federal Reserve were absorbed by nonbank investors. By the end of May member bank excess reserves were at very low levels and banks were borrowing heavily from the Federal Reserve Banks to maintain their reserve positions, as is shown in the chart.

Several debt-management moves made by the Treasury in May had important anti-inflationary effects in the credit market. In mid-May the Treasury announced that it was not exercising its privilege of calling for payment on September 15, 1951, the 8 billion dollars of 2 per cent bonds first callable on that date and maturing two years later. This step, which reflected the fact that under the prevailing interest rate structure the Treasury could gain little or no advantage by refunding the bonds at this time, greatly reduced the volume of Government securities to be refunded in the second half of 1951. At the same time the Treasury announced the offering of a new savings note with yields ranging from 1.44 per cent for six months up to 1.88 per cent for the full three-year investment. These yields were about ½ of 1 per cent higher than those on the old savings note. Late in May the Treasury offered a 1⅞ per cent 9½ month certificate maturing April 1, 1952, in exchange for the 10 billion dollars of mar-

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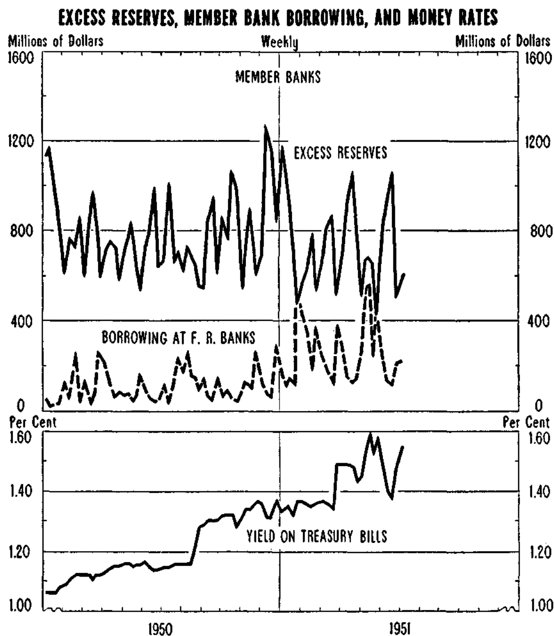

Data are averages of daily figures for week ending Wednesday. For excess reserves data are partly estimated and are preliminary subsequent to June 13, 1951. Weekly figures of borrowings may include small amounts of Federal Reserve Bank discounts and advances for nonmember banks and others. For Treasury bills rate is average of daily mean yield on the longest outstanding issue. Latest data are for week ended July 4, 1951.

ketable securities maturing on June 15 and July 1. This offering, which was priced so that the maturing issues commanded a moderate premium in the market, was well received by investors and in total about 95 per cent of the maturing securities were exchanged for the new issue.

Bank reserve positions eased temporarily in early June. Excess reserves increased, banks were able to repay borrowings at the Federal Reserve, and yields on short-term Government securities declined. This change resulted from a combination of factors, including a large temporary reduction in the Treasury balance at the Federal Reserve and Federal Reserve System purchases of maturing Government securities largely from corporate holders who needed cash for tax and dividend payments. The sharp decline in the Treasury balance was caused primarily by a transfer of funds between the Treasury account at the Reserve Banks and its tax and loan accounts at commercial banks in connection with the redemption for cash of outstanding Series D savings notes and the subsequent use of these funds to purchase the new savings note.

After mid-June member bank excess reserves declined reflecting both a drain on bank reserves as the Treasury balance at the Reserve Banks was rebuilt and an increase in total required reserves. The latter was due largely to an increase in deposits which occurred as corporations sold short-term Government securities to banks to rebuild balances drawn down by quarterly tax and dividend payments. Early in July bank excess reserves were around the minimum levels the banking system seems to want for operating purposes, bank borrowings at the Federal Reserve were up somewhat from the low volume of mid-June, and yields on Treasury bills were at about the levels reached in mid-May.

Changes in Long-term Credit Markets

Availability of long-term credit in the mortgage and the corporate and municipal bond markets was considerably curtailed by developments following the announcement of the Treasury-Federal Reserve agreement in early March. For a number of months the total demand for long-term credit, which has been exceptionally large in recent years, had considerably outstripped the supply of funds for such investment becoming available from new savings and repayment of outstanding loans. Some holders of marketable Government bonds, such as insurance companies and savings banks, had been selling heavily from their portfolios in order to raise funds to meet this surplus demand for long-term credit, and the volume of such sales had been greatly in excess of buying by other private investors. To prevent declines in prices of Government securities, the Fed-

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eral Reserve System had been purchasing the excess of Government bonds offered for sale, thereby increasing both the money supply and the volume of reserves that banks had available as a basis for expansion of their credits. As a result of the Treasury conversion offer for the two longest-term restricted bonds, a substantial portion of the Government bond portfolios of nonbank lenders was immobilized. After the close of the conversion offer, Federal Reserve purchases of bonds were sharply reduced, and bond prices declined in response to selling pressures in the securities market.

At the lower prices and higher yields on Government securities and in view of the greater difficulty of finding buyers, with the changed Federal Reserve policy, lenders have become more reluctant to sell their Government bonds to extend credit to private borrowers. With the curtailment of this inflationary source of funds, savings institutions have begun to limit their new commitments to extend credit, particularly mortgage credit, and these lenders are now matching more closely their new long-term extensions with the funds they have available from new savings and from repayments on old loans. With the change in capital market conditions a number of corporate and municipal financing programs have been postponed, cut back, or canceled. The total volume of such financing, however, is still large.

Selective Credit Controls

Demand for credit of certain types has been restricted by regulation of the terms under which such credit could be granted. Last autumn, under authority of the Defense Production Act of 1950, the Board issued Regulation W establishing minimum down payments and maximum maturities on instalment credits for the purchase of certain durable consumer goods. Under the terms now in effect, the inflationary expansion of consumer purchasing power through increases in consumer instalment credit has been stopped. In the eight-month period October 1950-May 1951, instalment credit outstanding has declined over 400 million dollars. This compares with an increase of about 1.8 billion in the corresponding period a year earlier.

Restraints on certain housing credits were put into effect last summer and early autumn. In July the terms were tightened somewhat on mortgages insured or guaranteed by the Federal Housing Administration and the Veterans Administration. In October under authority of the Defense Production Act, the Board of Governors, with the concurrence of the Housing and Home Finance Administrator, issued Regulation X which limited the credit that could be extended through noninsured mortgages on certain new residential construction. Related measures were announced at that time by the Federal Housing Administration and the Veterans Administration, tightening further the terms of insured and guaranteed mortgages. By steps taken in early 1951 Regulation X was revised to apply restrictions to credit on nonresidential construction and new multi-unit residences not previously covered.

In the first months after their issuance the real estate credit regulations had little effect on the amount of real estate credit extended because they did not apply to credit on a large number of houses already under construction, to credit already committed, or to noninsured credit for purchase of existing houses. More recently the proportion of housing construction subject to the regulations has been rising, and the regulations have become increasingly effective. Partly as

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a result of the regulations and to a large extent because of the tightening in the supply of funds in the mortgage market, private housing starts this spring—although large compared with most earlier years—have shown little of the usual seasonal rise and in April, May, and June were more than one-third below the record levels of the corresponding months a year ago.

Regulation of stock market credit has been a continuing restraint on expansion of this type of credit. In January the Board of Governors exerted a further tightening influence by increasing margin requirements from 50 per cent to 75 per cent of the market value of the securities.

Program for Voluntary Credit Restraint

Measures for restricting the total volume of credit available have been reinforced by the Voluntary Credit Restraint Program, which is directed primarily toward curbing the extension of nonessential credits not covered by selective credit regulations. Under authority delegated by the President under the Defense Production Act of 1950 and after approval of the Attorney General given early in March, the Board of Governors cooperated with representatives of financing institutions in establishing a national Voluntary Credit Restraint Committee. This Committee, which includes representatives of commercial and savings banks, investment bankers, insurance companies, and savings and loan associations, has as a primary responsibility the establishment of criteria for distinguishing between essential and nonessential credit. For this purpose it has issued a series of bulletins covering various kinds of credits. The national committee has also set up regional committees to deal with problems in the various sections of the country.

Through voluntary cooperation of thousands of individual financing institutions under the program, progress has been made in the restriction or postponement of credit not essential to the economy at this time. The national and regional committees have been very active familiarizing lenders with the details of the program. Many requests for advisory opinions regarding specific loans have been sent in by lenders to the appropriate committees. While it is impossible to determine precisely the volume of credit that has been denied, a very large number of loan requests, including several sizable ones, have been delayed or refused by lenders acting voluntarily in accordance with the principles of the program.

Changes in Bank Credit

Expansion of bank credit to private borrowers and State and local governments slackened during most of the second quarter of 1951 after a rapid growth in the first three months of the year and throughout 1950. Total loans at all commercial banks increased by about 2 billion dollars during the first quarter of 1951 and bank portfolios of State and local government securities rose by about 200 million dollars. The expansion in loans in the first three months represented a record peacetime growth for this time of year. During the second quarter of the year, after the Treasury-Federal Reserve accord and the institution of the Voluntary Credit Restraint Program, commercial bank loans expanded by about 1 billion dollars, and bank holdings of State and local government securities showed little change.

Loans to business enterprises have accounted for nearly all of the increase in total loans at commercial banks since the beginning of the year, as is shown on the chart on the following page. These loans expanded by nearly 2 billion dollars, or about

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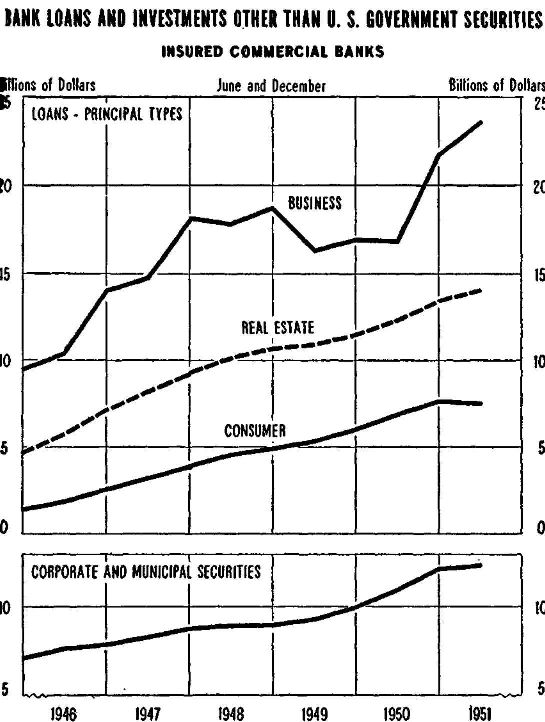
8 per cent in the first quarter. They declined somewhat during most of the second quarter, but not as rapidly as is usual at this season of the year. Late in the quarter there was an increase.

More complete information as to the nature of bank loans being advanced to businesses has been available since early April. At the request of the Voluntary Credit Restraint Committee, the Federal Reserve System has been collecting reports from a group of the largest member banks on the types of businesses that are borrowing or repaying loans and on the purposes of the loans. These banks account for about two-thirds of total business loans at all banks.

The figures indicate that in recent weeks new borrowings have been undertaken mainly to finance direct defense contracts and what may be termed "defense-supporting" activities. Engaged in these activities, in part at least, are manufacturers of metals and metal products and public utilities, including transportation concerns, which have been important borrowers recently, as is shown on the following chart. Defense borrowing was insignificant during the large loan expansion last fall.

BANK LOANS AND INVESTMENTS OTHER THAN U. S. GOVERNMENT SECURITIES

INSURED COMMERCIAL BANKS



All insured commercial banks in the United States. Business loans include commercial and industrial loans, open market commercial paper, and acceptances. Consumer loans exclude single payment loans to individuals of $3,000 and over. Agricultural loans and loans for purchasing or carrying securities are not shown. Municipal securities include State and local government obligations. Latest figures are for June 1951 and are estimated.

Some recent new borrowing, however, has been done by business concerns in industries that are not engaged generally in defense or defense-supporting activities. Loans to manufacturers of textile, apparel, and leather products and to wholesale and retail trade firms have risen in recent weeks. Sales finance companies also have increased their bank borrowing somewhat since early April, mainly to finance increased lending by these companies to automobile dealers and other retailers.

Significant reductions have occurred, however, in the outstanding bank indebtedness of some types of business not engaged in defense activities. Reductions have included seasonal repayments of loans by commodity dealers and processors of agricultural products. Loans to these types of businesses typically increase when the major crops are harvested in the fall and decrease through the rest of the crop year as farm products are consumed. Recent repayments by these types of borrowers, however, have not been so large as their new borrowings last fall. This development, together with the appearance of new defense loans, has prevented a substantial decline in business loans such as usually occurs at this time of year.

Real estate loans at commercial banks, increased about 600 million dollars in the first six months of this year. This compares with increases of around 1 billion dollars in the same period of recent years other than

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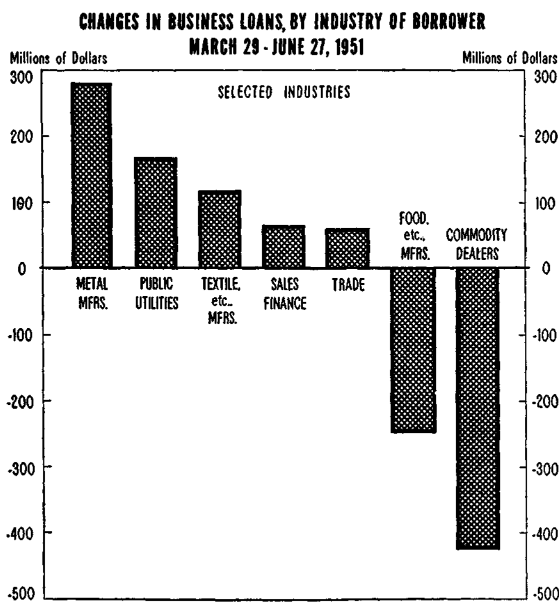

Data reported by over 200 of the largest weekly reporting member banks. Textile, etc., manufacturers includes apparel and leather. Food, etc., manufacturers includes liquor and tobacco.

1949. The smaller growth reflects the effects of general credit controls and the regulations on real estate loans, as well as the fact that many banks are approaching the limits for such loans established either by law or as a result of managerial decision. For the past two years growth in real estate loans has been less rapid at commercial banks than at savings and loan associations, life insurance companies, or mutual savings banks, and the proportion of the total outstanding mortgage debt held by commercial banks has declined.

Bank lending to consumers fell slightly during the first half of this year. This is in contrast to an increase of nearly 900 million in the same period of last year and substantial increases in the corresponding period of other postwar years. All of the decline in the consumer debt at banks thus far this year has been in instalment loans. Single-payment loans to individuals, which are not subject to regulation, have increased.

Monetary Outlook

The interruption of monetary expansion in the first half of 1951 has reflected several factors that are temporary or seasonal in nature. Expansion of the privately held money supply has been resumed in recent weeks and may continue during the second half of the year, partly for seasonal reasons. The large Treasury balance accumulated by mid-1951 will be reduced somewhat over the rest of the year, and as this occurs these funds will also go into the hands of individuals and businesses. The extent of any additional growth in the privately held money supply in the second half of the year will be determined largely, however, by future developments in bank credit, to both private borrowers and the Government.

The Government will need to increase its borrowings during the next six months. To the extent that new funds can be obtained from nonbank lenders, the supply of money will not be affected, but if funds must be borrowed from the banking system, including the Federal Reserve, the effect will be an expansion in the money supply. Business demands for credit may be large in view of prospective plant and equipment expansion, the general over-all pressure currently being exerted on business financial positions, tending to increase the volume of outside financing, and the greater difficulty of obtaining outside funds through capital market channels. On the other hand, inventory expansion should be a less significant factor in bank borrowing than it was last year. Consumer borrowing may be at a rate which will not add significantly to total outstandings. With some further reduction in housing construction, demand for mortgage credit may be very little, if any, greater than can be supplied from current savings available for such investment.

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