BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM

Office Correspondence

Date February 24, 1970

To Board of Governors

Subject: Statement of Board's Position on Selective Credit Controls

From Sherman J. Maisel

2/24/70

Attached for Board approval is a draft statement of the Board's position on authority contained in the Credit Control Act of 1969 to impose selective credit controls.

The Office of Emergency Preparedness has asked that a member of the Board's staff present such a statement to OEP's Retail Advisory Committee on March 4, 1970. The Retail Advisory Committee is a group representing the retail industries (other than food and automobiles) that advises OEP on problems relating to the administration of a price control program. 3/4/70

The draft statement, which I regard as a routine response to a request for the Board's position, sets forth the provisions of the Credit Control Act, outlines very briefly the Board's previous experience in administering selective credit controls, describes the argument for supplementing general monetary controls with selective controls, and summarizes Chairman Burns' recent testimony before committees of the Congress.

Attachment.

See
MINUTES
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See statement as presented by M. Grimwood on 3/4/70

Files

February 19, 1970

Governor Maisel — Board Position on Selective Credit Controls

Gordon B. Grimwood

2/19/70

The Economic Stabilization Division, Office of Emergency Preparedness, has scheduled a meeting with its Retail Advisory Committee (on price controls) for March 4, 1970. The Committee has asked that someone from the Board present a brief statement at that meeting with respect to the Board's position on the Credit Control Act of December 23, 1969. A list of the members of the Advisory Committee is attached.

I have drafted a short statement (also attached) which sets forth the provisions of the Act, outlines very briefly the Board's experience in administering selective credit controls, describes the basic issues, and summarizes Chairman Burns' recent statements before committees of the Congress. The draft might serve as the basis for a statement by whoever you may wish to designate to respond to OEP's request.

I am circulating copies of the draft to Messrs. Holland, Partee, Molony, and Cardon for comments and suggestions.

Attachments 2.

cc: Messrs. Holland
Partee
Molony
Cardon

GBG:dch

DRAFT:GBG:dch
February 19, 1970

On December 23, 1969, the President signed Public Law 12/23/69 filed Pocket
91-151, the major purpose of which was to extend the authority of Federal financial agencies to control rates paid by banks and other financial institutions on deposits and other forms of borrowing. However, Title I of the Law also restores authority, originally contained in the Defense Production Act of 1950 but lapsed, for the Board of Governors to organize and to administer a voluntary effort among financial institutions to restrain extensions of credit during times of inflationary pressure.

Title II of Public Law 91-151, entitled the Credit Control Act, gives the President the authority, whenever he determines that such action is necessary or appropriate for the purpose of preventing or controlling inflation generated by the extension of credit in an excessive volume, to authorize the Board to regulate and control any or all extensions of credit. The range of controls that the Board might impose under this authority is very broad.

In signing Public Law 91-151 the President remarked that he had not requested this authority and did not intend to use it.

The Federal Reserve Board has used selective credit controls on three occasions in the past: control of consumer instalment credit during World War II and for a brief period in 1948-1949; and control of consumer instalment and real estate credit during the Korean conflict. The Board also administered a voluntary credit restraint program between March 1951 and May 1952.

During World War II and the Korean conflict the selective credit controls supplemented direct controls over prices and wages, which obscured the effectiveness of such controls as anti-inflationary measures. Controls over consumer instalment credit were re-instituted by Joint Resolution of Congress in September 1948, in the absence of direct controls, because of price increases following the elimination of direct controls after World War II. However, in retrospect it appears that the controls were imposed just at the point of a cyclical easing in economic activity. Prices began to turn downward in August 1948. The consumer credit regulation was eased in January 1949 and again in March, and was allowed to expire in June 1949.

It is difficult to assess the effectiveness of the voluntary credit restraint program because it was a qualitative rather than a quantitative control -- that is, it emphasized the purpose of the proposed credit rather than imposing a ceiling within which over-all credit extension should be contained. The effort was to reallocate "non-defense connected" credits to "defense connected" uses. As a consequence there is no definitive way to measure whether the program succeeded in meeting its objectives.

The consensus of men connected with the administration of the program was that it had had some over-all effect on restraining bank credit. On the other hand, over-all bank credit rose very rapidly while the program was in effect. In the meantime, many manhours were consumed by committees, from the local to the national level, who were wrestling with the definitional problems. These problems, together with the large number of institutions involved, led to competitive pressures which seriously eroded the program. Certain types of credit were exempted from the program by executive order in March 1952, and the entire program was suspended two months later.

Generally speaking, there are two reasons to consider supplementing general monetary controls with selective credit controls. Either the general controls are not being effective (there are several, possibly conflicting objectives against which "effectiveness" might be judged), or the controls are having an uneven effect as among different sectors of the economy. The second reason is dominant at the moment, with housing, State and local governments, and small businesses singled out as sectors bearing an undue share of the burden of current restrictive monetary policy.

In testimony before the House Banking and Currency Committee on February 7, 1970, Chairman Burns rejected the idea of changing general monetary controls in such a way as to restructure credit flows to any particular sector of the economy. Such action, he said, would require offsetting open market operations of a magnitude that would lead to a weakened market for Treasury securities. He even more emphatically rejected any suggestion that funds for the affected sectors should be made available by the Federal Reserve in addition to a level of money and credit that would otherwise be appropriate for the nation as a whole. Such a policy, he said, could lend to a disastrous inflation.

With respect to the authority contained in the Credit Control Act, Chairman Burns said that he had always believed that the existence of such authority on a stand-by basis was helpful and desirable. His tentative opinion was that selective credit controls should not be imposed at the present time. He said, however, that he had an open mind on this subject and that he would be ready to change that opinion if the evidence changed.

Chairman Burns reaffirmed this position while testifying before the Joint Economic Committee on February 18, 1970.