

Resum

September 20, 1937

CURRENT BUSINESS SITUATION

Prospect

Many divergent elements in the domestic and foreign situation make for uncertainty in the business outlook. Taking a long view, it seems that we are still in a period of broad recovery which will lead within a year or two to a level of activity substantially higher than that prevailing this year and also considerably above 1929. Output of durable goods is likely to increase considerably, particularly for all types of private construction, and output of nondurable goods is also likely to expand further. Many of the unsound elements which led to the depression after 1929 are not present in the current situation and there do not appear to be other factors sufficient to cause a prolonged downswing. Any decline from current levels of Federal spending would probably reflect improved business conditions and would not be likely to cause a decline in activity.

In the more immediate future, it seems that the current period of readjustment may continue for a few months, with little change in industrial output. Payrolls, dividends, and agricultural income have increased further this year and the volume of retail trade has been at least maintained. Industrial production has been maintained through a period of reduced buying and declining raw material prices. The Board's seasonally adjusted index was 114 in June and July and probably 117 in August compared with 118 in the spring months. In some industries the volume of unfilled orders

continues substantial. The foreign situation holds many uncertainties but appears likely to be an element of strength rather than weakness. On the other hand, maladjustments have developed between costs, prices, and incomes in some lines, notably in residential building. Wage rates in the building industry and also in manufacturing generally have continued to advance in recent months and the question as to whether goods can be sold in such volume and at such prices as to support further increases in wages appears to be more sharply defined than last winter, when the volume of buying was large at whatever prices were asked. Also, the volume of unfilled orders on manufacturers' books has been generally reduced from the unusually high level reached this spring. Altogether it seems likely that, although the long-term outlook is for further substantial recovery, there may be little change in the volume of industrial production, employment, commodity prices, and trade during the next few months.

Retrospect

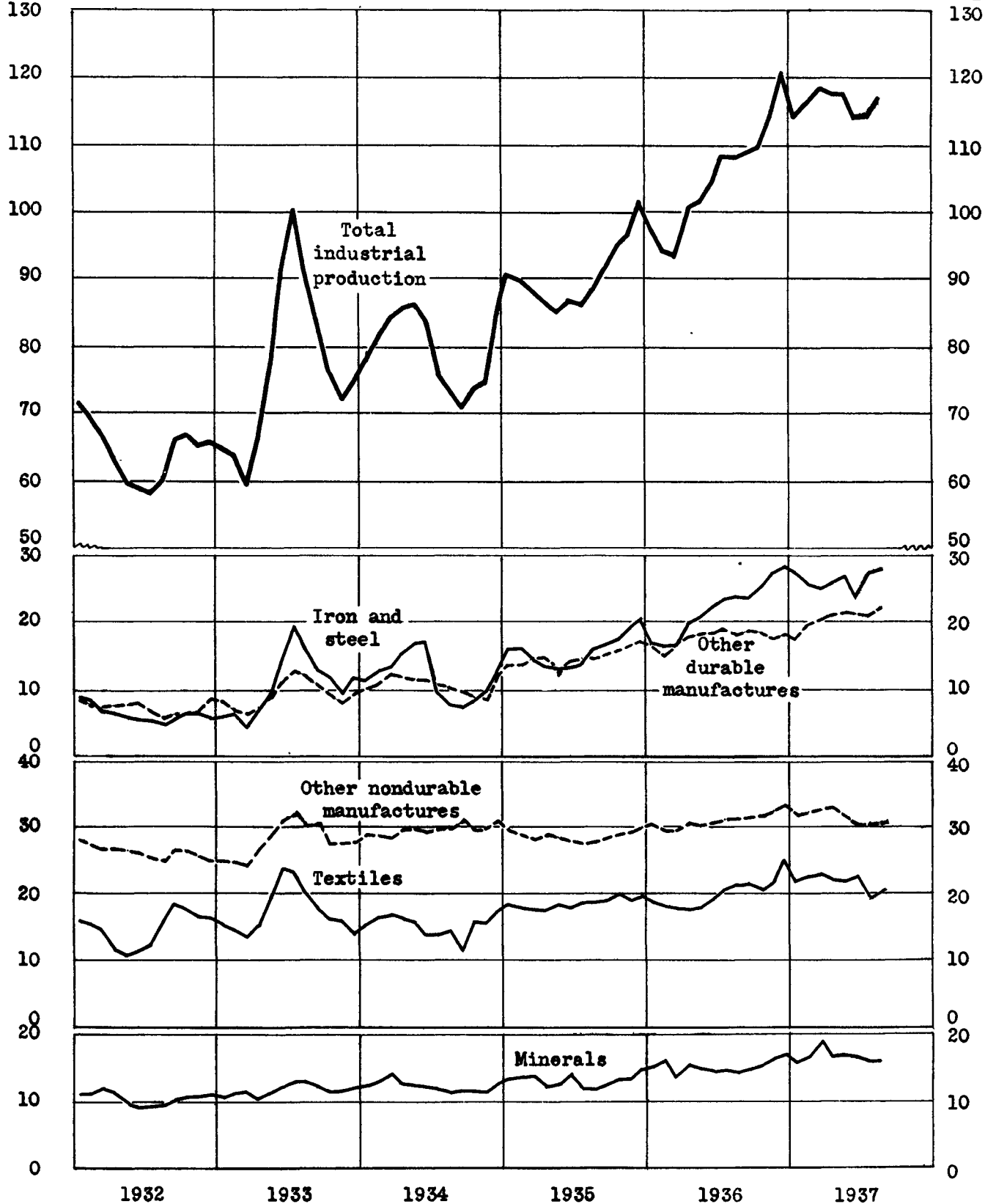
To see current developments in perspective it is desirable to review briefly the various stages of recovery to date. In 1933 and 1934 recovery proceeded irregularly from an extremely low level, with sharp changes in volume of production, prices of commodities and securities, and many other elements in the situation. This is shown for industrial production in the attached chart. In these years the Federal Government was taking a very active part in affairs, reviving the banks, taking over many real estate loans on homes and farms, devaluing the dollar, curtailing agricultural output, increasing wage rates, shortening hours, and spending large sums for relief and other activities.

INDEX OF INDUSTRIAL PRODUCTION

Adjusted for seasonal variation,
1923-1925 average for total=100

Points in
total index
130

Points in
total index
130



In 1935, with increased assurance of recovery, based partly on growing stability in industrial prices and wages, business expenditures for much needed machinery and equipment increased further, and there was expansion in the volume of building, particularly for residential purposes. Other private construction increased considerably beginning early in 1936. Prices and wage rates generally were maintained with little change during 1935 and through October 1936, and in this period the volume of industrial output increased sharply and almost continuously. With a rising volume of business and declining costs per unit there was a sharp increase in profits. Security prices advanced and, with easy conditions in the money markets, refunding operations were on a large scale and there was an increase in issues floated to obtain new capital. The volume of bank loans expanded, Payrolls increased sharply as a consequence of fuller employment, and throughout industrial communities incomes were generally higher. Farm income was also continuing to expand and the strength of the recovery movement appeared to be very great. The activities of the Federal Government were somewhat less important in this period than in 1933 and 1934 but expenditures continued on a large scale, with the bonus as a special factor in the middle of 1936.

The rapid recovery brought total domestic activity toward the end of 1936 close to the 1929 level and in some industries to higher levels. Temporary shortages of skilled labor appeared in a few lines and also there was prospect of delayed deliveries of some goods. These developments, together with increased demand for commodities abroad, for industrial and armament purposes, resulted last winter in widespread buying of many raw materials and finished products for future as well as current needs.

This buying movement was reflected in sharp increases through the first quarter of 1937 in wholesale prices of raw and semifinished commodities and more moderate increases in finished goods. Wage rates increased materially, reflecting improved economic conditions and more aggressive union activity. The extent of wage increases and of increases in employment and payrolls is shown for manufacturing in the accompanying chart. Production showed a seasonal increase early this year from the levels reached in the latter part of 1936, but a substantial volume of unfilled orders accumulated.

Summary of recent developments

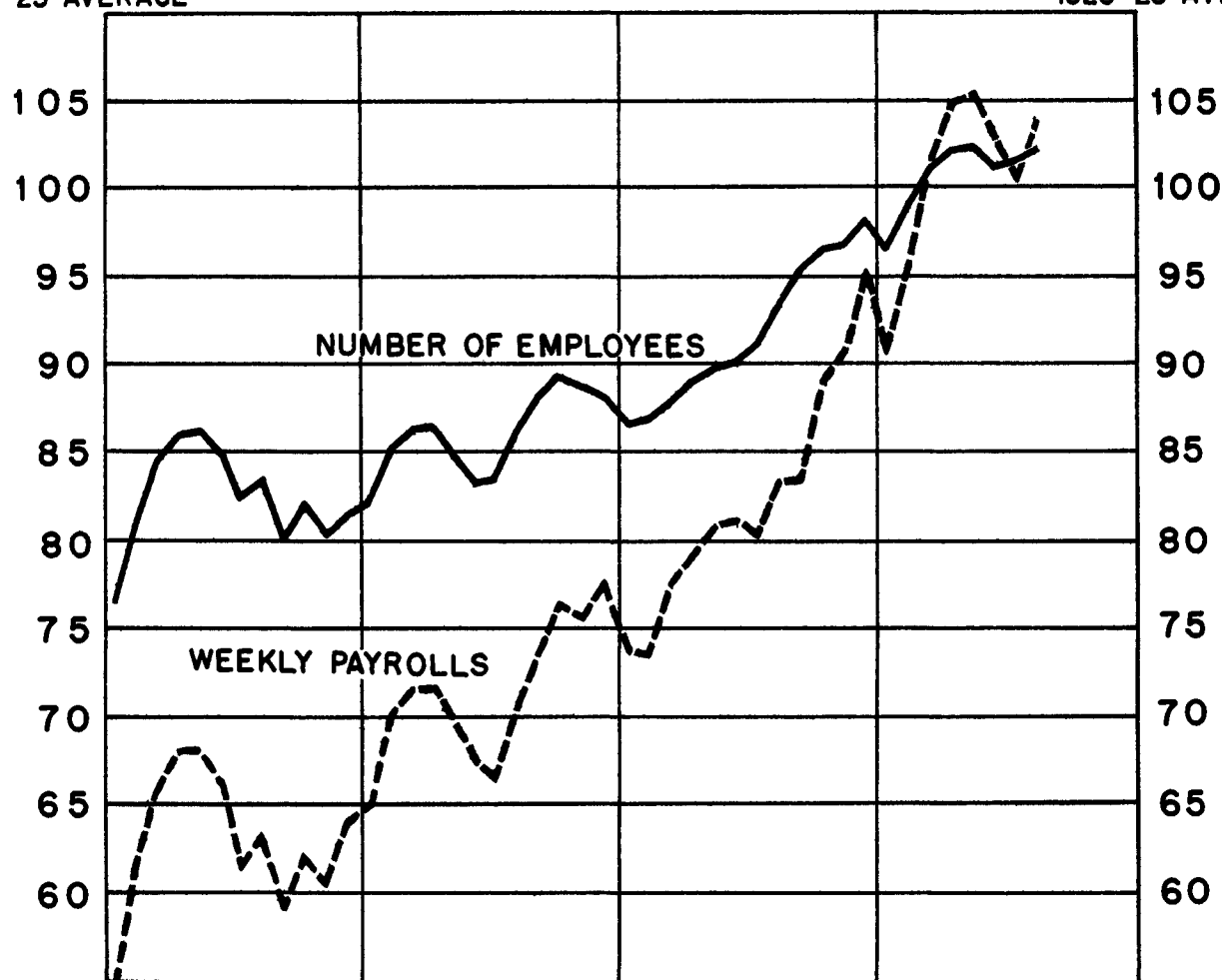
During the past six months buying of commodities by fabricators and distributors has been reduced from the unusually high level of last winter and prices of raw materials generally have declined, but the volume of industrial production has been maintained with little change, partly on the basis of a large volume of orders accumulated last winter. In some industries the volume of unfilled orders continues substantial. Wage rates have shown a substantial rise, particularly in construction and manufacturing. Wholesale prices of finished products, which had increased considerably less than raw materials last winter, as shown in the chart, have continued to advance and increases in wholesale markets have been reflected to some extent in higher retail prices. Rents have continued to advance. Agricultural output this year is substantially larger than last season and larger crops account in considerable part for declines in prices of crops,

FACTORY EMPLOYMENT, HOURS, AND EARNINGS

PER CENT OF
1923-25 AVERAGE

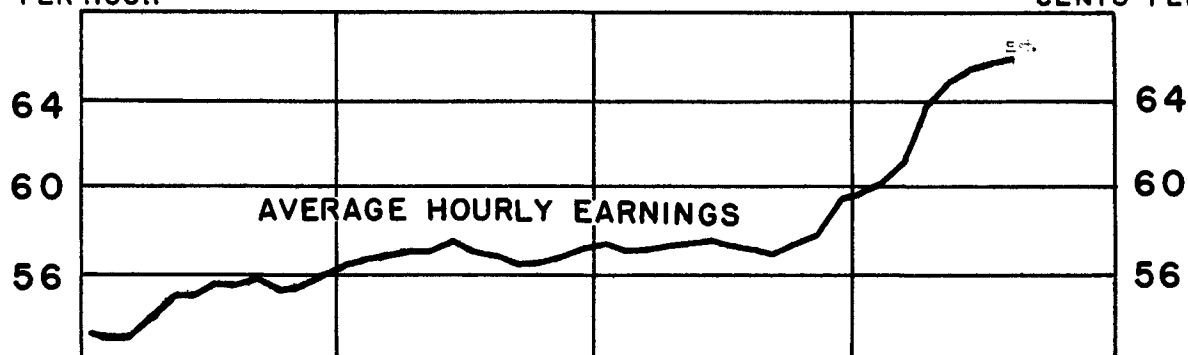
WITHOUT SEASONAL ADJUSTMENT

PER CENT OF
1923-25 AVERAGE



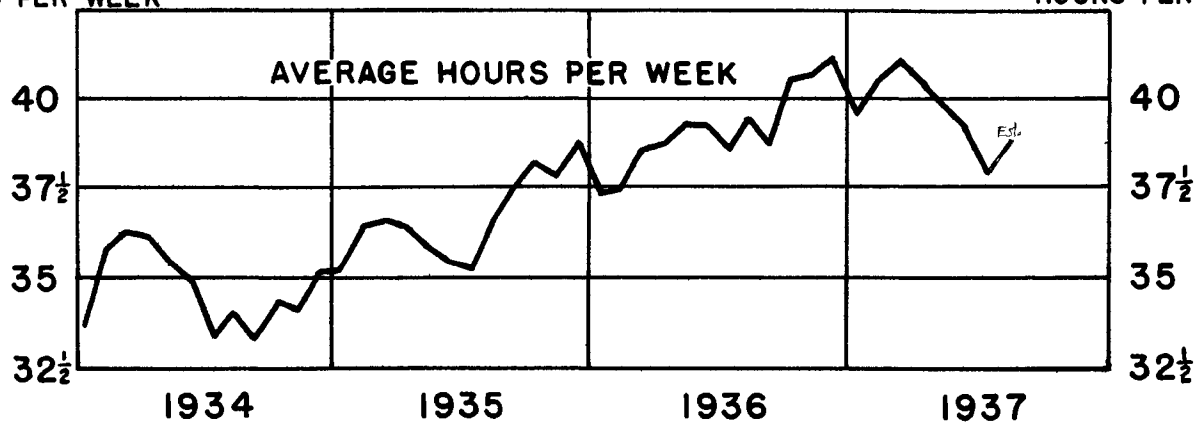
CENTS PER HOUR

CENTS PER HOUR

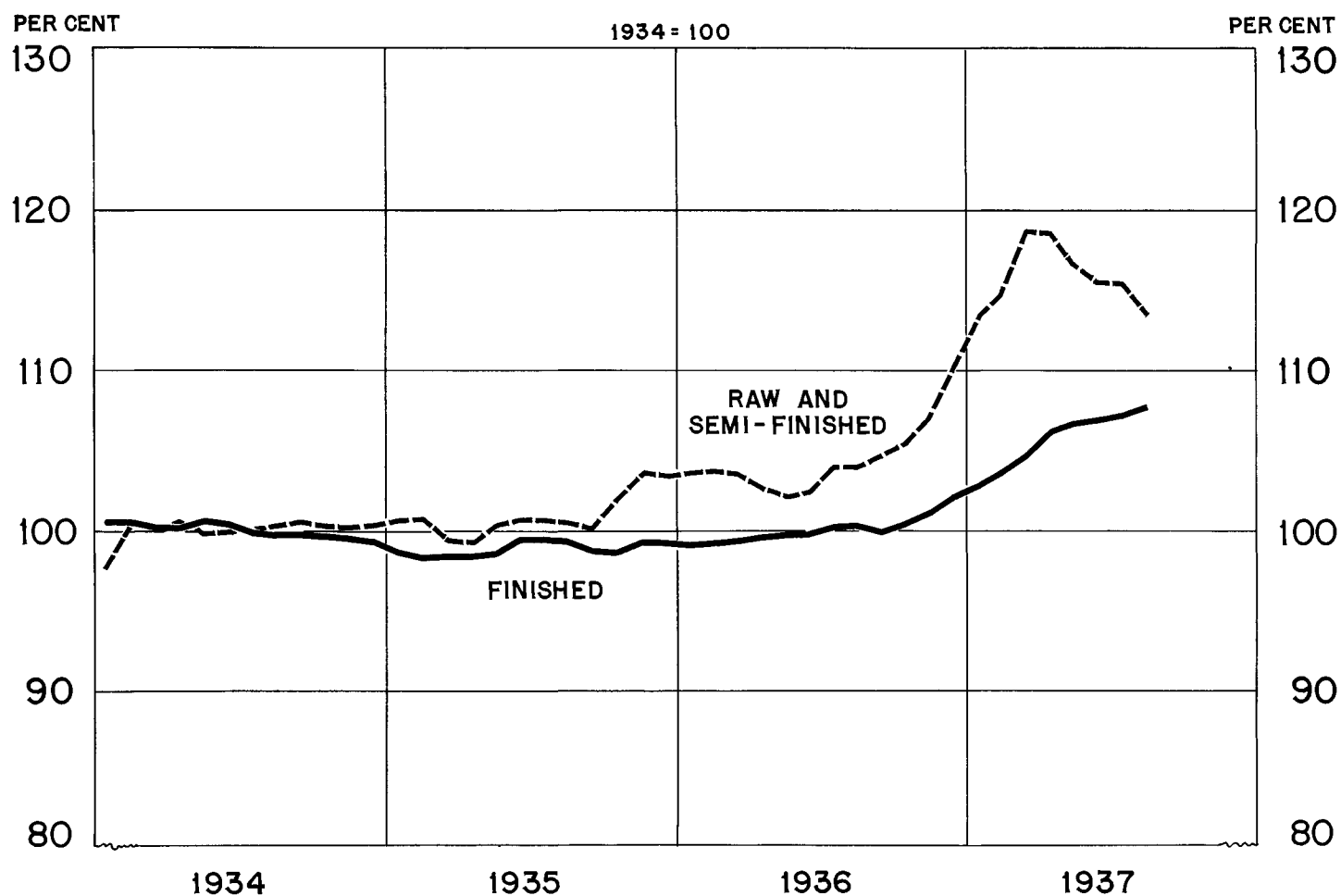


HOURS PER WEEK

HOURS PER WEEK



WHOLESALE PRICES OF COMMODITIES OTHER THAN FOODS AND FEEDS



Federal Reserve Classifications
Bureau of Labor Statistics Data

while livestock prices have continued to advance. Incomes have been quite generally higher this year in both industrial and agricultural communities. There has been a decline in the number of unemployed and government relief expenditures have shown a decrease.

Since last autumn many of the relationships between costs and prices and between prices and incomes have been altered considerably and currently the new relationships are being tested. The rise in costs and prices has been an important factor in checking the growth in residential building, which was apparent in 1935 and 1936. Although other private construction has increased further and public construction has continued in substantial volume, the total volume of construction continues much smaller than in the 1920's.

While industrial activity has been generally maintained at the levels reached toward the end of last year, security prices have shown considerable decline and the volume of new capital issues has been reduced. Bank loans, however, have continued to increase.

The effects of world developments on the domestic business situation have been mixed, with increased orders from both raw material and industrial nations a factor sustaining activity, and war threats being a disturbing element, particularly in the security markets.

Prices

The general index of wholesale prices for the week ending September 11 was at 86.8 percent of the 1926 average, 1.5 points lower than at the peak in the first week in April and about 6 points higher than at the beginning of the sharp upward movement early last November.

The course of wholesale prices since 1934 is shown in two accompanying charts. The first shows that the price rise last winter was general for crops, livestock, and other commodities but that the movements since the beginning of April have been different, with a sharp decline for crops, a further increase for livestock, and little change for other commodities as a group. The decline in crops reflects primarily the prospect of considerably larger crops this season, particularly for cotton, grains, and potatoes. The further advance in livestock and livestock products is due largely to reduced supplies as a secondary result of droughts, and to sustained demand on the part of consumers. This year's large feed crops probably will result in a larger production of livestock products and by next spring prices of these products may decline.

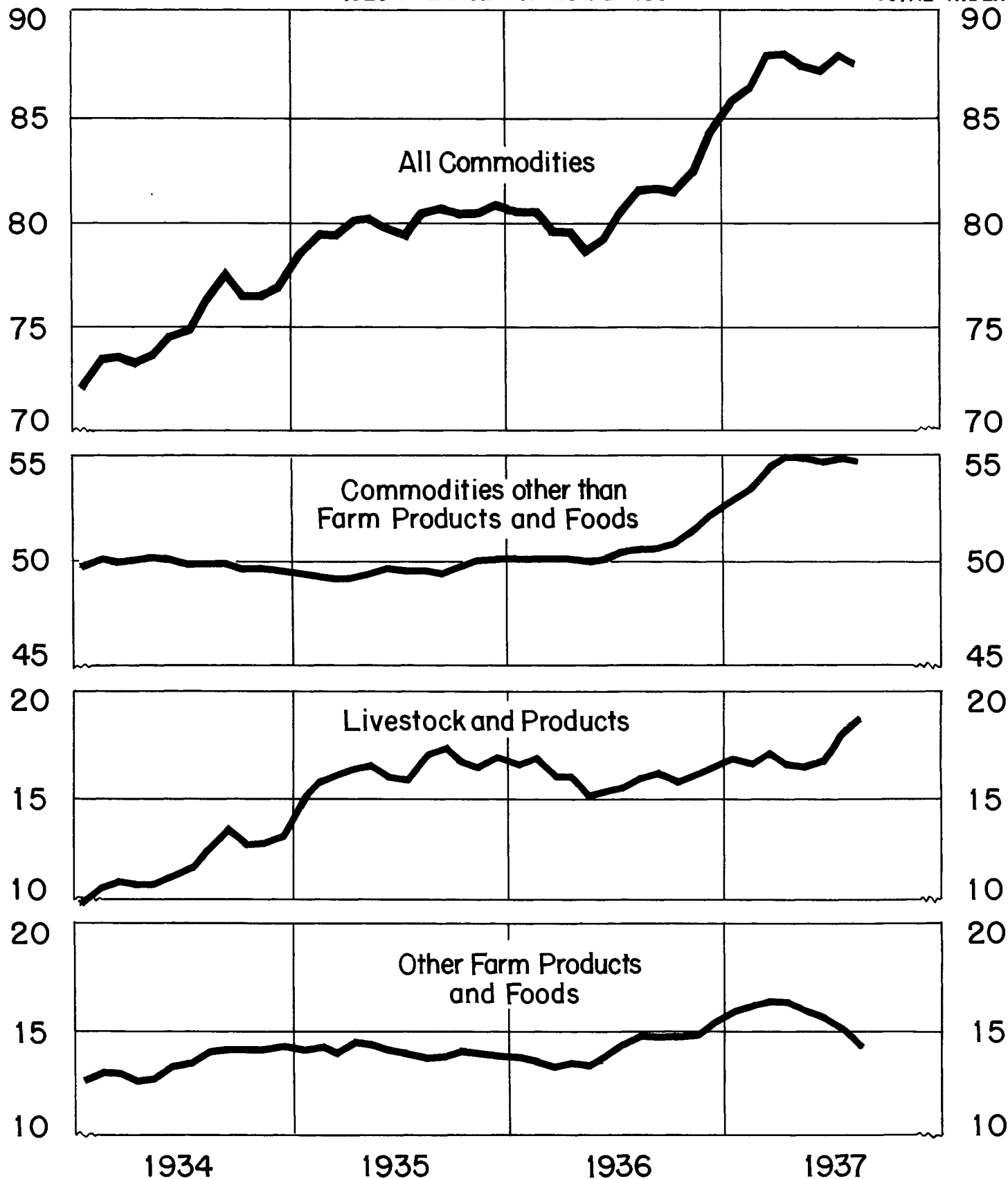
Last winter prices of industrial raw materials and semifinished products increased much more than prices of finished products, as shown in the second chart, but since the beginning of April they have declined, while prices of finished industrial products have advanced somewhat further. Prices of raw and process foods and feeds, on the other hand, have moved closely together, advancing last winter and declining somewhat since then.

WHOLESALE PRICES

POINTS IN
TOTAL INDEX

1926 AVERAGE FOR TOTAL=100

POINTS IN
TOTAL INDEX



The decline in industrial raw and semifinished materials has been considerably smaller than the preceding advance and has reflected largely a decrease in the price of cotton from a peak of almost 15 cents a pound early in April to a level of about 9 cents. Prices of cotton yarns and cloths, rubber, nonferrous metals, and steel scrap^{also} declined substantially from the speculative peaks reached early in the spring and there were smaller decreases in wool, worsted yarns, silk, lumber, paint materials, and anthracite. The decline in raw and semifinished materials to lower levels has reflected reduced buying in this period as well as increases, actual and prospective, in supplies. The latter is particularly the case for cotton. For some other commodities, such as hides, zinc, lead, and wood pulp, supplies have continued low; currently prices for hides and leather are at about the spring peak; wood pulp is higher; and zinc and lead are only moderately lower.

Prices of finished products have continued to advance since early in April, but at a much slower rate than during last winter. These increases have reflected in part earlier advances in material costs and higher labor costs, as well as the larger incomes of consumers.

In recent months, with continued strong demand, prices of durable commodities, including building materials, metals and metal products, and house-furnishing goods, have been generally maintained, as shown in the accompanying table, and in some instances there have been increases and prices for these commodities are substantially higher than last October. In the case of nondurable commodities, current prices are lower than in the spring and only moderately higher than last autumn.

WHOLESALE PRICES

Week ending September 11

	Indexes 1926 = 100	Percentage change	
		April 3, 1937 to September 11	October 31, 1936 to September 11
All commodities	86.8	-2	+7
Farm products	84.5	-12	+1
Foods	86.6	-2	+5
Other commodities	86.0	0	+7
Durable			
Metals and metal products	96.4	0	+12
Building materials	96.4	0	+10
Housefurnishings	92.8	+3	+12
Nondurable			
Hides and leather	108.5	+2	+13
Textile products	75.5	-3	+5
Chemicals and drugs	80.9	-7	-1
Miscellaneous	76.9	-4	+7
Fuel and lighting	79.8	+3	+3

Source: Bureau of Labor Statistics.

Prices of commodities sold in retail markets have increased about 2 percent within the past year and housing costs have shown a considerably larger advance in this period. Food prices are 2 percent higher, reflecting an advance in meats offset in part by a decrease in prices of fruits and vegetables. Retail prices of other commodities are also higher but in recent weeks they have generally shown little change, with declines reported for some items. Prices of most models of automobiles were raised last month and it is expected that further increases will be announced when the 1938 models are introduced.

Industrial production

Industrial activity, which had increased sharply in 1935 and 1936, has shown relatively little change since the beginning of this year, at a level slightly lower than that in 1929. The average of the Board's seasonally adjusted index for the first eight months is 116 as compared with 119 for the year 1929 and 105 for 1936. The preliminary August index is 117.

Output of durable manufactures has increased somewhat further this year and has been substantially larger than a year ago. Output of non-durable goods currently is lower than at the beginning of the year, owing largely to declines in recent months in meat packing and in output of textiles and leather products, but for the year to date has been larger than in the corresponding period last year.

The increased production of durable manufactures this year reflects in considerable part the continued growth in activity in the steel industry, where output has been close to the volume of the peak year 1929. Industries producing automobiles, farm equipment, machinery, household appliances and many other steel products have been operating at a high rate, in many instances using more steel than in 1929. Export demand for semifinished and finished steel products, as well as for pig iron and scrap, has increased sharply. Steel consumption by the railroads, which had been at an extremely low level for a long time, has been considerably larger this year. The demand for steel by the building industry, however, has remained at a low level, reflecting a continued small volume of commercial building.

During recent months operations at steel mills have been based to some extent on unfilled orders accumulated early in the year. While some mills still have a backlog of unfilled orders, continuance of the current high level of activity in this industry, around 80 percent of capacity, will depend in considerable part on the volume of orders received in the near future. Specifications on orders placed earlier have been in steady volume, indicating continued need for steel by manufacturers, and new orders have been increasing gradually. During the autumn months seasonal changes in steel output are small, so that if output is maintained at the current level, the Board's adjusted index of industrial production will not be affected much one way or the other.

As is shown in a preceding chart, activity in the steel industry has been at a higher level than activity in other durable industries as a group. Automobile production has been at a high rate but output of building materials, while increasing somewhat, has still been at a low level.

In the textile industries and at shoe factories a reduced volume of buying during the late spring and summer has been reflected recently in a decline in activity and output now is at about the level prevailing before the large buying movement last winter. Other nondurable goods have shown little change in the aggregate. Marketings of livestock have been very small since early summer, while output of tobacco and petroleum products has continued to increase. Sugar meltings have shown rather wide fluctuations this year, reflecting uncertainties regarding legislation, but the volume for the first eight months was somewhat larger than in 1936.

In August volume of industrial production increased somewhat, following a decline in June and little change in July. Steel production rose slightly further and was close to the high level prevailing before strikes curtailed output in June. Automobile production was maintained in August in much larger volume than is usual in that month preceding the shift to new model production. Lumber output declined, following a period of increase. In the nondurable goods industries output was maintained in August. Production at cotton and silk mills, which had declined in July, showed little change in August and available data indicate that activity in woolen mills was probably sustained, following a sharp decrease in the preceding month. Activity at meat packing establishments increased somewhat from extremely low levels. Crude petroleum production rose further to a new high level, while output of coal showed less than the usual seasonal increase.

Last spring when output of durable manufactures was approaching a level about the same relative to output of nondurable manufactures as in some years preceding declines in activity, some analysts took this fact as a warning that a recession in output was likely. Since last spring durable goods output has shown some further increase, while output of nondurable manufactures has declined. This does not seem to us a disturbing development, however, partly because ^{the} in/recent depression output of durable goods was at an unusually low level for an unusually long time and substantial shortages developed. As indicated in Current Comments, the short-term outlook is for a few months of activity near current levels, with further expansion in output likely in the next year or two.

Construction

The following table shows the value of construction contracts awarded in August and in the first eight months of the year as compared with last year. The increases over a year ago reflect partly higher costs of construction.

CONSTRUCTION CONTRACTS AWARDED

(In millions of dollars)

	August		January-August	
	1936	1937	1936	1937
Total	275	285	1,807	2,100
Public	153	108	946	790
Private	122	177	861	1,310
Residential	69	73	460	623
Other	53	105	401	687
Factories	15	38	124	254
Commercial	22	30	161	211
Other	16	37	116	222

Source: F. W. Dodge data for 37 Eastern States.

Statistics on residential construction and a discussion of movements in materials prices and wages are contained in Mr. Currie's memorandum.

Employment conditions

Employment in nonagricultural activities has increased further this year, although not so sharply as in 1936. This continued increase in the number employed at a time when production and trade have leveled off reflects in part a decline in the length of the average work week. Unemployment has declined further and is currently about 1 1/2 to 1 3/4 millions less than a year ago. Estimates based on National Industrial Conference Board would indicate about 6 3/4 million persons unemployed in July and are probably closer to the fact than the American Federation of Labor estimate of 8,600,000. The shortages of certain types of skilled workers, which some observers regarded as a serious problem last autumn when production was increasing rapidly, have proved to be temporary.

Factory employment has increased considerably further in 1937 and employment on the railroads, in the utility industries, and in trade and service has shown some additional increase when allowance is made for seasonal influences. Employment in the construction industry, however, has shown a smaller than seasonal expansion this summer.

In manufacturing, the principal increases in employment have been at plants producing durable goods, particularly steel, machinery, automobiles, and lumber. Employment in the nondurable goods industries, which had increased considerably last summer and autumn following a period of little change during the previous three years, has shown only seasonal changes during recent months.

Payrolls also have expanded considerably this year, reflecting not only increased employment, offset in part by a decline in average hours, but also a marked rise in average hourly earnings, as is shown for manufacturing on the chart. In the two previous years payrolls had advanced sharply but at that time the increases reflected increased employment and a rise in hours, while wage rates showed little change.

Increases in average hourly earnings since last year have been considerable in industry and trade generally and have been particularly large in industries producing durable manufactures and in construction and mining.

The advance in wage rates has resulted from the higher level of activity maintained since the end of last year combined with aggressive campaigns by labor unions. In many instances strikes or threats of strikes were important in bringing higher wages and in some cases increases were given by employers to forestall increased union activity. The effects of wage rate increases on the volume of output, particularly in residential building, are discussed in another section.

Agriculture

Preliminary estimates by the Department of Agriculture indicate that total cash income, including Government payments of about \$425 million, will be \$9,000,000,000 for the calendar year 1937, an increase of 14 per- cent over 1936 and the largest cash income since 1929. Official estimates indicate that ^{incomes from} crops will be considerably larger than last season, with increased output more than offsetting the decline in crop prices. Live- stock marketings have been lower this year and are expected to continue small the remainder of the year, but livestock prices have advanced sharply, and income from marketings of livestock products is about the same as last year.

The September estimates for leading crops are shown in the accompany- ing table. A cotton crop of 16.1 million bales, representing an increase of 3.7 million over last season, was forecast on the basis of September 1 conditions. Approximately 190 million of the 886 million wheat crop, which is 40 percent larger than that last year, are available for export. Other food crops and tobacco are expected to be substantially greater than a year ago. Prospective production of feed grains will be sharply higher than last season, when output was severely curtailed by the drought, and the supply will be the largest in several seasons, with a greatly reduced number of livestock on farms.

CROP PRODUCTION

(In millions of units)

Crop		Average 1928-32	1936	Indicated Sept. 1, 1937
Cotton	bales	14.7	12.4	16.1
Wheat, all	bushels	864.5	626.5	886.0
Corn, all	bushels	2,554.8	1,529.3	2,549.3
Oats	bushels	1,215.1	789.1	1,136.2
Tame hay	tons	70.1	63.3	74.9
Potatoes, white	bushels	372.1	330.0	403.4
Tobacco	pounds	1,427.2	1,153.1	1,448.9

Source: Department of Agriculture.

Trade and distribution

Distribution of commodities to consumers during 1937 has continued at the level reached at the end of 1936 and has been considerably larger in volume than a year earlier. Increases over last year have been particularly marked in midwestern industrial areas where consumer incomes have been increased sharply by the rapid recovery in activity in the durable goods industries and by advances in wage rates.

The leveling off of trade at department and variety stores, mail order houses, and similar establishments this year, when consumer incomes have continued to increase, may reflect in part an unusually sharp increase in expenditures for travel and recreation.

Freight-car loadings have shown somewhat less than the usual seasonal increase this year, following a substantial rise in 1936.

Foreign trade

Merchandise foreign trade of the United States has expanded further this year, and in the first seven months was about 40 percent larger than in the corresponding period of 1936. Imports have shown a greater increase than exports, particularly in the early part of the year, and the excess of imports has amounted to \$145,000,000 compared with \$24,000,000 in 1936. As compared with the late 1920's, imports this year have been $\frac{4}{5}$ as large while exports have been only two-thirds the level in those years. The rise in exports this year has been the first of any considerable magnitude since the summer of 1933 and has reflected, largely, demand from abroad for semifinished and finished manufactures, particularly iron and steel products, machinery, automobiles, and petroleum products. Exports of raw cotton have continued at a low level. Imports, which had increased steadily during 1935 and 1936, rose sharply in the early part of 1937 and since then have been maintained. The rise in imports has continued to be general with the largest increases reported for industrial raw materials, reflecting increased industrial activity in this country, and for agricultural commodities, reflecting the effects of the drought last year.

New security issues

Securities sold by domestic corporations since June have averaged somewhat less than half as much as during earlier months of this year. The smaller amount reflects in part the usual summer dullness, and in part the continuance of unsettled price conditions in the security markets which culminated in September in a sharp recession to new lows for the year in prices of common stocks and lower grade corporate bonds.

In the spring months unsettled price conditions were accompanied by a decline in the offerings of corporate and other securities for refunding purposes, which had been exceptionally large in the preceding year, but corporate offerings for new capital continued to increase. Since June, however, there has been a substantial shrinkage in offerings for new capital also; in August total security offerings, both new and refunding, were the smallest since the beginning of the recent revival of the capital markets in 1935. It now appears that September will establish another new low for this period.

Some dullness in the capital market is not unusual during the summer months but the psychological effect of the recent break in stock prices may lead to a continuation during the fall months of the small volume of corporate offerings for new capital purposes. This indicates hesitation on the part of corporate managements to secure funds through new security issues in order to expand their operations, and this may delay to some extent expansion of plant and increase of working capital, with a consequent effect on the demand for various durable goods.

Statistics on the volume of capital issues, as tabulated by the Commercial and Financial Chronicle, and on bond yields are summarized in the attached table.

It may be noted:

(1) For the first eight months of 1937 corporate issues for new capital purposes have totalled about \$930,000,000, which is about 30 percent larger than in the corresponding period of 1936. Most of the increase in new financing has occurred in industries classified as "oil" and "other industrial and manufacturing."

(2) Available data indicate that about one quarter of the issues for new capital purposes are intended for expansion of plant and equipment, while a little more than half are designated for increasing working capital.

(3) About 37 percent of this year's new capital offerings have been in the form of common and preferred stocks, as compared to 23 percent during the first eight months of 1936. Security prices in September have been particularly unsettled for those classes of securities which are being offered to secure new capital, that is, for stocks and lower-grade corporate bonds. Bonds offered for new capital are usually given one of the lower ratings when first offered.

In the latter part of March and April prices of common stocks showed the sharpest decline since 1933; in the recovery during subsequent months average prices did not reach their March high and in September there was another sharp recession to new lows for the year. Prices of lower-grade corporate bonds have continued to be weak since their sharp decline last March and were particularly weak in September. Prices of lower-grade railroad and public utility bonds are now at the level of the early part of 1936.

(4) Corporate security issues offered for refunding purposes during the first eight months of 1937 were only about 40 percent as large as in the corresponding period of 1936. While it seems obvious that unstable security prices were a factor in this decline, too much importance may be attributed to it. During the second half of 1936, notwithstanding that long-term interest rates were at their lowest on record, the total amount of corporate refunding was about \$800,000,000 less than during the preceding half of the year. This decrease represented smaller offerings by corporations other than public utility companies. During 1937, however, refunding operations by other corporations have again increased, while public utility refunding declined. Furthermore, corporate refunding is still at a rate substantially above pre-depression years.

(5) It has recently been reported by market observers that plans already announced by various industrial and public utility companies indicate a large volume of refunding to be done before the end of this year. Also, any renewed stability of security prices will probably be accompanied by offerings of securities to repay some part of the \$850,000,000 increase since February in commercial loans of weekly reporting banks, much of which was probably incurred by corporations. Offering of securities to fund such current obligations will be reported as flotations for new capital purposes.

CAPITAL ISSUES, 1936 AND 1937

(In millions of dollars)

	Total	New capital				Refunding			
		Corporate			Other	Corporate			Other
		Total	Bonds	Stocks		Total	Bonds	Stocks	
8 months ending									
Aug. 1936	4,243	695	534	161	488	2,377	2,242	136	682
Aug. 1937	3,106	926	589	338	658	1,045	734	311	477
Quarterly									
1936									
1st	1,467	137	111	26	221	918	896	23	191
2nd	2,139	317	238	79	188	1,173	1,069	104	461
3rd	1,046	315	233	82	183	462	434	28	86
4th	1,561	422	257	165	188	834	789	45	117
1937									
1st	1,485	363	237	125	234	609	390	220	279
2nd	1,093	432	279	153	229	323	274	49	109
3rd (est.) ^{1/}	650								
^{1/} September estimated.									
July and Aug.	528	131	72	59	195	113	71	42	88
July	344	82	39	43	168	57	20	37	36
Aug.	184	49	33	16	27	56	51	6	52

BOND YIELDS 1936 AND 1937

(per cent)

	1936		1937		
	High (Jan.)	Low (Dec.) ^{1/}	Jan. low	April high	Week ending Sept. 18
U.S. Treasury	2.71	2.22	2.27	2.78	2.67
Corporate Aaa ^{2/} :					
Total	3.42	3.09	3.07	3.48	3.30
Industrial	3.24	2.89	2.86	3.35	3.13
Rails	3.70	3.30	3.29	3.69	3.56
Public utility	3.32	3.06	3.05	3.39	3.22
Corporate Baa ^{2/} :					
Total	5.20	4.50	4.46	4.93	5.26
Industrial	4.23	3.91 ^{1/}	3.92	4.26	4.18
Rails	6.36	5.04 ^{1/}	4.97	5.50	6.33
Public utility	5.01	4.50	4.47	5.04	5.27

^{1/} October for Baa rails and November for Baa industrials.

^{2/} Moody's Investors Service.