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DEPOSITS

by

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Fluctuations in total bank deposits are similar to fluctuations in total assets. The comparisons which have been made between the two prewar and war periods with respect to trends in total assets are also true with respect to total deposits. The only difference between the two periods relating to all deposit accounts which I wish to stress is the protection provided since January 1934 by deposit insurance.

Total bank deposits may be divided into three major groups: deposits owned by other banks; those owned by the United States Government; and those owned by business and individuals, including State and local governments and clubs and other mutual associations.

The proportion of total deposits owned by other banks varies from year to year, but this variation is not extreme and has been altered little by wartime developments.

United States Government deposits, except in wartime, are a small part of total deposits, and also small relative to the amount of business and personal deposits, amounting in most of the peacetime years to less than 2 percent of the amount of business and personal deposits. However, since war is a business of the national government and absorbs a large part of the nation's economic energies the amount of United States Government deposits increases with great rapidity in wartime. In June 1918, about four years after the beginning of World War I and less than a year and a half after our entry into that war, the amount of United States Government deposits was 24

times as large as the figure in June 1914. In June 1945, about six years after the beginning of World War II, and three and one-half years after our entry into that war, United States Government deposits were 31 times as large as in June 1939. With the termination of hostilities these deposits were rapidly reduced.

Personal and business deposits, except in war periods, comprise approximately four-fifths of total bank deposits. The amount of these deposits is of great economic significance, because they constitute by far the major part of the circulating medium, or money, which is used in transacting the nation's business. It is this group of deposits which deserves most attention in comparing similarities and differences between the two prewar periods and the two war periods, and in noting changes which occurred in the period subsequent to World War I. Further, it is the total amount of business and personal deposits, rather than the amounts in demand and in time accounts, which I wish to emphasize. Both in 1909 and in 1946, 71 percent of business and personal deposits were in demand accounts and 29 percent in time accounts. Between these years, substantial changes occurred in the relative movements of demand and time deposits, but those changes were related primarily to modifications of banking law and custom rather than to wartime conditions or basic economic developments.

If you look at the chart for business and personal deposits, you may note that the upward slope of the line for the 5-year period prior to World War II is a little steeper than that for the 5-year period prior to World War I. In the earlier period, from June 1909 to June 1914, the average

increase per year in business and personal deposits was almost 6 percent, which is slightly higher than the calculated normal rate of growth.

Over a period of nearly a century the average annual increase in the physical output of the United States has been between  $3\frac{1}{2}$  and 4 percent per year. There has also been a tendency, for at least a century, for business and individuals to hold, as the years go by, larger balances in their bank accounts relative to their expenditures for the output of the economy. The trend in output of goods and services and the trend in use of money together give us an estimate of the normal or needed rate of growth of money, and therefore of bank deposits, of about 5 percent per year. Without this growth it is not possible for the people of the nation to continue to purchase the expanding output of the economy at prevailing prices.

In the 5-year period preceding World War II, from the middle of 1934 to the middle of 1939, the average rate of growth in bank deposits was slightly over 8 percent per year. While this appears to have been high relative to the normal rate of growth it was desirable in view of the fact that the five years prior to 1934 had been a time of sharp monetary contraction. After the banking collapse, an increase in deposits at more than a normal rate was needed, in order that the physical output and business transactions of the nation would increase sufficiently to recover from the depths of the great depression.

One other point is worth noting in the comparison of the two prewar periods. The annual change in deposits in the pre-World War I period was more stable than in the pre-World II period. In the former, the annual rate of

growth ranged from a maximum of 9 percent to a minimum of 2 percent; in the latter, the range was from an increase of 16 percent to a decrease of nearly 2 percent. The year of contraction, from June 1937 to June 1938, is notable because it was followed by the sharp business depression of 1937-1938.

In both war periods business and personal deposits increased at rates far above the normal 5 percent per year. In the case of the first World War the average annual change, from the middle of 1914 to the middle of 1919, was  $12\frac{1}{2}$  percent; in the second the average annual change, from the middle of 1939 to 1946, was  $13\frac{1}{3}$  percent. The total increase during the five years of World War I was 80 percent, and during the seven years of World War II 140 percent.

When we turn to the postwar periods we must be careful to avoid the assumption that changes in bank deposits subsequent to World War II are likely to be similar to those subsequent to World War I. The 14-year period from 1919 to 1933--as is shown by the irregularities of the line for deposits on the chart--was a period in which the quantity of bank deposits was erratic. The forces which produced the changes in bank assets and in deposits during this period were in no sense necessary postwar developments.

From June 1919 to June 1920 business and personal deposits increased 15 percent; from June 1920 to June 1921 they decreased 7 percent. The rise was accompanied by price inflation; the swift contraction by a severe fall in the price level and by business depression.

During the 7-year period from the middle of 1921 to the middle of 1928 business and personal deposits increased by an average of 6 percent per

year, the same as the average of the 5-year period preceding World War I. This period of increase in deposits at slightly above the normal rate was accompanied by business recovery from the depression of 1921 and the maintenance, with only slight interruptions in 1924 and 1927, of a high level of business activity.

From the middle of 1928 to the middle of 1929 the change in business and personal deposits was negligible. Business activity continued at a high level for approximately a year after cessation of growth in the volume of bank deposits, but turned downward a few months before the stock market crash in the autumn of 1929.

From June of 1929 to June of 1933 business and personal deposits were reduced by 40 percent; a normal change would have been a growth of more than 25 percent. The sharpest rate of decline occurred from 1931 to 1932 when the contraction was 23 percent. This terrific shrinkage in the circulating medium made it impossible for the people of the nation, in view of their habits of use of money, to purchase the normal volume of output except at a drastic reduction in the price level. We know that the inevitable fall in prices occurred, though it was irregular and business costs did not drop as rapidly as the prices at which output could be sold. Under these conditions business enterprises were forced to close or lay off a large proportion of their employees.

A brief concluding comment may be made regarding the importance of maintenance of a reasonable rate of growth in the amount of bank deposits and therefore in the amount of bank assets. When the prices of goods and

services have become adjusted to the volume of the circulating medium which was produced by the nation's banking system during the war, the most essential condition for maintenance of what we used to call "prosperity" and what in recent years we have come to call "full employment" is a normal rate of growth--about 5 percent per year--in the deposits owned by business and individuals. If this rate of growth is maintained, we will have no reason to fear business depression; if it is not exceeded we have no reason to fear price inflation.