

BUSINESS CONDITIONS

A REVIEW BY THE FEDERAL RESERVE BANK OF CHICAGO



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Dairy Farmers Look Ahead

Reach Record Production — But Cautious of Future

The dairy industry, like other agricultural enterprises, has undergone a tremendous expansion during the war years. The expansion of output of milk and milk products has been brought about by an increase in the number of milk cows kept and in the output of milk per cow. Shortages of labor and of feed, as well as the maladjustments in prices of these factors, have given the dairy farmer many difficult problems to deal with in meeting the production goals called for by the war. Demands of the war for milk products for the military services and for lend-lease have necessitated significant changes in consumption patterns for dairy products. The utilization of milk has been for many months under substantial regulation in order to achieve the type of production needed to meet war needs. Good prices and satisfactory outlets have encouraged farmers to expand dairying operations. Considerable enthusiasm has been developed in past months for the purchase of purebred herd animals, including bulls, heifers, and calves of both sexes. With the approaching end of a part of the warfare some farmers are beginning to ask whether the prices being asked for some of these animals can be supported by the prospects for the dairy industry in the months and years that lie ahead.

HERDS AND PRODUCTION EXPANDED

At the beginning of the war in 1939 there were a little over 24.5 million head of milk cows on farms in the United States. As the war has progressed the total has expanded rather gradually to a total of 27.6 million head on farms at the beginning of this year, with an expected further expansion to nearly 28 million for the beginning of 1945.

The total production of milk has risen from an average of 104 billion pounds in the prewar years, 1935-39, to a peak production of 119.2 billion pounds in 1942. Estimates for 1943 indicate 117.7 billion pounds, while the figure for 1944 probably will be somewhat under last year. Since 1933 the production of milk per cow has been increasing each year until the peak in 1941 and 1942 was reached. For 1939 the production was 4,589 pounds. For the peak years an average of 4,740 pounds per cow was produced. Comparing production in the peak year, 1942, with the performance for 1939, it is found that an increase of about 11 per cent in total milk production was achieved by an increase of 7 per cent in numbers of cows on farms and an increased output per cow amounting to about 3 per cent. For the current year 12 per cent more cows will yield only about 9 per cent more milk than in 1939 because the output of milk per cow will be about 3 per cent less. The trends in these three series are shown on the accompanying chart I.

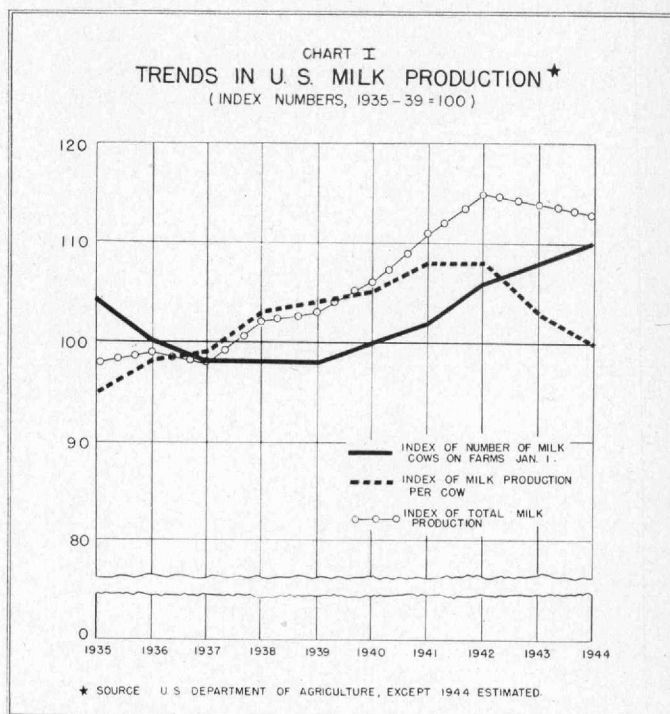
WAR NEEDS LEAVE LESS FOR CIVILIANS

In spite of the expanded output of milk and milk products civilians received a smaller total of milk supplies in 1943

and 1944 than has been consumed in any year since 1929, with less than 100 billion of the approximately 117 billion pounds produced in each of the two years going to civilian consumption. With rising incomes in recent years added to the increasing importance of milk in the average consumer's nutritional evaluation of diets, demand for milk and its products is at an all-time high level. To some considerable extent the price controls have kept the prices of milk and milk products below the level which such demand would normally set, and this has tended to accentuate the demand situation and to create additional problems in providing supplies needed for the war.

In the latter part of 1942 and during 1943 distribution controls were extended over the utilization of milk until they covered about three-fourths of the total milk production. During much of 1943 sales of fluid milk were unrestricted and the sales rose to a record high. However, late in 1943 sales in many areas were limited to the level of June of that year, and fluid milk byproducts, such as chocolate milk, cultured buttermilk, and cottage cheese were limited to 75 per cent of June sales.

Cream consumption was reduced or limited under food distribution orders which set a maximum of 19 per cent fat content of cream and limited sales to three-fourths of June 1943 sales. This permitted consumption by civilians at a level about one-fifth below the high consumption of



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Outlook for Midwest Industry

Varied Conversion Problems, Record Civilian Demand Ahead

After the close of the war in Europe, Midwest industries will begin a period of conversion to peacetime production which is expected to last for more than a year and to be much more extensive than the original shift to war production because of the far greater industrial facilities which will be involved. Two of the Seventh District's leading war industries, aircraft and ordnance, will steadily decline during and after the Japanese phase of the war. The automobile industry promises again to lead peacetime manufactures in this district followed by food production, very important in both war and peace.

Industries which also appear certain to experience substantial reductions in production from current levels after V-E (Victory in Europe) day include chemicals (explosives), iron and steel, and nonferrous metals. In contrast and indicative of the forthcoming shift in industrial emphasis, production soon after the war in Europe is likely to equal or exceed present levels in electrical machinery including electronic equipment, rubber products, furniture and finished lumber products, leather, building materials, paper, petroleum, and printing and publishing. Many of these latter industry groups are now filling large Government orders, but all have heavy backlogs of civilian demand which should require exceedingly high outputs for at least one to two years. Once these demand backlogs have been liquidated, production levels will adjust downward to more normal demand levels influenced considerably by prevailing incomes.

The transition from war to peace will be accompanied by considerable unemployment, virtual permanent closing of numerous specialized war plants, substantial population shifts to different job areas, and changes within the labor force. It seems probable, however, that with orderly disposition of Government plants and equipment and adequate provision for private acquisition of useful facilities, Midwest industry will emerge from the war favorably situated to pursue a vigorous program of peacetime manufacturing. The sharp and enduring adjustments certain to come, nevertheless, will be mitigated by diversity of industry and extensive manufacturing experience including conversion from peace to war production.

Although new industrial facilities valued in excess of four billion dollars have been built and installed in the Seventh District since the outset of the defense program in 1940, as described in the August 1944 issue of *Business Conditions*, current estimates are that probably only half of these new facilities will find immediate peacetime use. Instead of a gain of from 30 to 35 per cent in district industrial capacity during the war, the net gain after conversion is likely to be closer to 15 per cent.

War Mobilization Director James Byrnes stated on September 9, 1944 that conclusion of the war with Germany would be followed by a general reduction in national war

output of about 40 per cent. It seems likely, however, that because of the relatively high importance of products being manufactured in the Midwest for use in the Pacific war, the impending war production cut here may be somewhat smaller at first than in the nation as a whole. Nevertheless, with more than 2.2 million persons now engaged in munitions employment alone in the Seventh District, any important general cutback necessarily will affect sharply, if only temporarily, hundreds of thousands of workers and thousands of industrial firms. Employment prospects in the Seventh District during and immediately after conversion will be considered in a future *Business Conditions* article.

POSTWAR INDUSTRIAL OUTPUT

Many Seventh District manufacturers, besides meeting war production schedules, are now hurriedly preparing to resume production of civilian goods after an interval of three or more years. Although backlogs of demand for consumers' and producers' goods now exceed all previous levels, it appears likely, nevertheless, assuming continuation of roughly the present price level, that the general dollar volume of industrial output at the end of the first full year following total victory will be at least moderately below present production which is about 70 per cent for the armed forces and lend-lease. Even the exceedingly high over-all production of civilian goods, anticipated as soon as manpower and materials can be released without hindering the war effort, is not expected to equal the production which has resulted from the stimulus of war demand for industrial products. Most specialized war goods are not in substantial demand in peacetime, and many war production facilities will not lend themselves to peacetime use.

Peacetime prospects are obviously most favorable for industries with a heavy backlog of civilian demand and industrial facilities readily convertible to peacetime use, and which require materials likely to be in abundant supply immediately after the fall of Germany. Many individual firms will also be influenced during conversion by local manpower supply conditions, complex problems of war contract settlements including interim financing, disposal of surplus products and equipment and use of Government-owned plants, and the speed with which marketing channels can be re-established.

SEVENTH DISTRICT TRANSITION PROSPECTS

An appraisal of the prospects of Midwest industries emerging from a period of intensive war production obviously must be tentative and limited to general trends. Moreover, it is necessary to consider industries in groups of similar manufactures which individually may differ sharply.

To estimate the prospects of Midwest industries during the remaining months of war and the period immediately

thereafter, several related criteria have been used: (1) peacetime (1939) value of product, (2) wartime (1943) estimated value of product, (3) volume of war supply contracts, (4) wartime expansion in productive facilities, (5) estimated average time required to convert war plants to peacetime production, (6) importance of Government ownership of plants and equipment, (7) probable proportion of wartime facility growth to be used in civilian output, (8) the seriousness of wartime surpluses affecting civilian production, (9) estimated level of demand from V-E day to the end of the war against Japan, and (10) estimated level of demand during the first full year after the Japanese capitulation. Data have been compiled from Government statistics and statements issued by industrial groups, supplemented by interviews with industry leaders.

In the five District States, Illinois, Indiana, Iowa, Michigan, and Wisconsin, industrial production, which rose from 13.5 billion dollars in 1939 to an estimated 33-35 billion in 1943, or about 150 per cent, has continued at or near record wartime levels during 1944. The Seventh District has received 39 billion dollars in major nonfood war supply contracts along with more than four billion dollars in new industrial facilities since mid-1940. Assuming availability of manpower and materials, the average Seventh District war plant suitable for peacetime production, when permitted, probably can be converted to making some civilian goods in less than three months. In several industries, such as leather, paper, textiles, food, and stone, clay, and glass, whose products are similar or identical in war or peace, most plants will be able to shift to civilian manufactures in less than one month. Many large-scale manufacturers of aircraft parts and ordnance items and related war products, however, will require extensive retooling before undertaking new production and may be delayed if specialized machine tools are not available when needed. In addition, the flow of parts from subcontractors must be synchronized, which will be time consuming. As obviously no simultaneous shift from war to peace output will occur among all industries or all plants within an industry, the conversion period now beginning may well extend for eighteen months or two years, although the conversion time required by individual plants and industries may be comparatively short.

The Federal Government has financed about 80 per cent of all new wartime facilities in the Seventh District. The Government, moreover, has almost exclusive ownership of the new facilities not expected to find peacetime use, estimated at about 50 per cent of the total expansion. Disposal of Government-owned plants, equipment, and surpluses of finished products looms as a large problem in the district. If conversion is delayed and unemployment threatens to result from this cause, however, prompt public and private action on the matter will be mandatory.

SHIFTS IN WARTIME AND CIVILIAN DEMAND

Although future demand estimates are subject to wide margin of error, available evidence points to a demand well above what can be produced during the Japanese phase of

the war for virtually every industry, except food, primarily serving civilian requirements. Industrial products which have bulked large during the war, such as aircraft, ordnance, steel (indirectly shipbuilding), chemicals (explosives), and nonferrous metals, however, will have sharp drops in demand during this period, although production will remain substantially above prewar levels.

During the first full year following total victory some further significant demand shifts can be expected for the products of Midwest industries. Greater balance probably will be achieved between demand and supply conditions for many civilian goods and some heavy demand backlogs will begin to disappear. War goods will be in negligible demand and most conversion to be undertaken very likely will be completed. These general prospects for Midwest industry have been derived from a summary of the application of the foregoing criteria to the individual industry groups. The prospects for the transportation equipment, food, and ordnance groups are considered in further detail below. Other leading industry group prospects will be discussed in the November issue of *Business Conditions*.

TRANSPORTATION EQUIPMENT

Aircraft — Aircraft now constitutes the largest industry in the transportation equipment group which also includes shipbuilding, automobiles, railroad equipment, and motorcycles. Aircraft and ordnance manufacturers face the most serious and extensive conversion problems among all Midwest industries. Of very minor importance in the district before the war, production of aircraft and parts has increased steadily, especially during the past year, to attain first rank.

The district aircraft industry is expected to experience a sharp cutback in demand after the war in Europe which will gradually reduce over-all production by a third or more, and following the fall of Japan to a small fraction, perhaps less than 15 per cent, of the record wartime level.

About one and one-fourth of the four billion dollars spent for expansion of facilities in the district have been for aircraft and parts. More than half of the new aircraft facilities have been constructed and installed to make engines. These engine plants with their extensive machinery probably will have a greater degree of peacetime usefulness than aircraft assembly plants. As a result, the industry in this area has somewhat more favorable prospects for conversion than in other sections which do largely combat aircraft assembly work.

No more than fifty per cent of the district aircraft industry's new wartime facilities probably will be converted to peacetime use. In some instances the very large size and temporary construction of plants may impede private acquisition and production. Whatever conversion does occur, however, frequently will require from four to six months or more because of the extensive structural and equipment changes which are likely to be needed.

Shipbuilding — Shipbuilding on the Great Lakes and the principal rivers also has grown because of the critical ship-

ping shortage which existed early in the war and which has persisted until quite recently. With some reduction in ship construction already in effect, and heavier cuts impending, it appears obvious that shipbuilding facilities in the district will continue to decline in importance, particularly as the Japanese phase of the war draws to a close. Some postwar demand is expected for small pleasure craft and a few larger commercial vessels, but these will probably prove to be insignificant compared with the highest wartime production.

Automobiles—The automobile industry, the district's peacetime leader, has lost much of its identity during the war because many automobile producers have expanded and converted their plants to produce aircraft and parts and many heavy ordnance items as well as military vehicles. Although the requirements of the armed forces and lend-lease for motor vehicles have been very large, actual automobile production, chiefly trucks and jeeps, is estimated to have declined from first to seventh rank among district manufactures. The automobile industry has had the eighth largest wartime expansion in industrial facilities among district industries.

While many conflicting estimates have been made, it seems probable that some civilian automobile production will be possible after a conversion period of about five months. Full industry conversion probably cannot be achieved in less than a year. Because of the extensive Government-owned facilities used by automobile manufacturers to produce war products other than motor vehicles, speed in providing for the postwar use of these facilities, including the removal of surplus equipment and inventories, will be necessary to expedite reconversion. The demand for automobiles is generally conceded to be heavier dollarwise than any other civilian consumer durable good. There will be a very heavy market for all automobiles which the industry can produce both during, and for several years after, the conclusion of the war with Japan.

Railroad Equipment—Railroad equipment, another component industry in the transportation equipment group, also appears to have very favorable immediate postwar prospects. Although a good deal of railroad equipment has been built during the war for use of the armed services both in this country and overseas, much of the freight and passenger equipment in regular use has deteriorated badly. Both replacement demand and requirements for new, improved equipment will be large for at least a year or more after cessation of hostilities in the Pacific area.

FOOD PRODUCTS

Among district peacetime manufactures, food products nearly equaled in value the production of automobiles and equipment, the largest industry group. The tremendous food requirements during wartime for the armed forces, lend-lease, and civilians, along with important price rises and favorable supply conditions, have raised the value of food production in the district to twice the prewar level, placing food in district wartime manufactures second only to the combined transportation equipment group.

Prewar food manufacturing facilities have been used largely to produce the record food output in the district, and comparatively small additions of new plants and equipment since 1940 have been almost entirely privately financed. Within the food group, meat packing is the largest industry, followed by bakery products, butter, canned and dried fruits and vegetables, candy, and cheese.

While some severe civilian food shortages have occurred since the outbreak of war, food supplies, in general, have been adequate. In recent months food inventories have begun to reach unprecedented levels with the strong possibility that following the war in Europe many surplus supplies will exist. Comparatively little is known about the magnitude of food stocks in the hands of consumers which will be used when shortages no longer restrict possibility for replenishing domestic holdings. Impending food surpluses will have a depressing effect upon food manufactures during the Japanese phase of the war and thereafter until excesses are removed and renewed demand requires a high level of production. Conversion difficulties will be at a minimum in the food products industry group, and wartime facilities will ordinarily lend themselves immediately and easily to peacetime use to the extent that demand requires.

ORDNANCE AND ACCESSORIES

This industry group has had an outstanding war record in the Seventh District, rising from an obscure position in 1939 to a high ranking surpassed only by transportation equipment and manufactured food products. Tanks are the largest single ordnance item followed by heavy ammunition and heavy guns.

Facility expansion for ordnance production in the Seventh District has been second only to transportation equipment, amounting to more than 900 million dollars since 1940. Except for some tank building facilities, most of these ordnance plants, particularly those for ammunition and special guns, are likely to have little short-run or long-run postwar value from a private business standpoint. At wartime values, probably two-thirds of the ordnance facilities in the district may be classified as useful principally for standby purposes after the war. Inasmuch as the Government owns almost all of these facilities, the disposal problem will be largely one of deciding the extent to which it will be in the public interest to maintain these plants and equipment for security reasons.

Because of the different types of war equipment required in the Pacific area compared with European war zones, and because of the shifting requirements of modern warfare, large-scale ordnance production obviously will continue throughout the Japanese war although materially below present levels. Following the end of hostilities, ordnance production should decline to a level only sufficient to supply the requirements of the armies of occupation, and later the peacetime American armed forces.

Crop Prospects Brighten

Feed Prospects Further Improved

A surprising improvement in feed crop prospects, especially for corn, was shown by the September 1 crop report of the U. S. Crop Reporting Board. The estimated crop of all corn is expected to be 3,101 million bushels, an even larger crop than the 3,076 million bushels produced last year.

With the larger crop of oats and grain sorghums harvested this year, the total production of feed grain concentrates will be about 2 million tons larger than the production of 1943, 117 million tons compared with 115 million for last year. In view of the expected smaller numbers of livestock to be fed during the feeding season beginning October 1, the feed situation will be materially relieved. With the improvement in crop prospects, the total of production and stocks will offer a supply nearly 5 million tons larger than the anticipated total of 112.3 million tons shown on page 6 of the August issue of *Business Conditions*. This improvement is due solely to the increased expectations for corn resulting from plentiful rains in the critical areas during August.

In the five states of the district, however, production this year will be about 7 per cent less than the output for 1943. The crop will be smaller, according to the September 1 estimates, in all of the states of the district except Michigan. The following table gives the estimates of the two years by states.

Corn production in the other states of the Corn Belt, however, is nearly 30 per cent larger this year than last. Minnesota, Missouri, Nebraska, Kansas, Kentucky, and South Dakota all show substantial increases in the estimates for this year. Only Ohio shows a decline of about 18 per cent. Production in these seven states is estimated to be 1,244 million bushels for 1944 as compared with 985 million bushels in 1943.

In general, corn production outside of the Corn Belt showed substantial declines from last year. The declines were particularly marked in some of the southern and

southeastern states which are fairly important corn producing areas.

The national total acreage expected to be harvested this year is nearly 3 per cent larger than that of 1943. In the five states of the district the current year's acreage for harvest is expected to be about 7 per cent larger. Over the country acreage changes from last year ranged from an increase of one-sixth for some states to a decrease of nearly one-fifth for others.

In spite of unfavorable weather during the large part of the growing season it does not appear that acreage abandonment will have been proportionally any greater than it was last year. However, since these figures cover corn for all purposes, it is quite probable that a proportion larger than that of last year will have to be assigned to lower uses, such as cutting for silage.

A national average yield of 31.8 bushels is forecast. This represents a slight decline from the 32.5 bushels yield per acre of 1943. In the five states of the district the average yield this year will be down to about 45 bushels, compared with 52 bushels for last year. The average yield for Iowa is indicated at 52 bushels as compared with 59 bushels in 1943 and a drop of 5 bushels from 50 to 45 is indicated for Illinois. On the other hand several Corn Belt states outside the district show substantial increases. South Dakota, Nebraska, and Kansas production per acre is up more than one-third above last year with increases of 8.5 to 9.5 bushels.

Yields in the Corn Belt states outside the district show an indicated rise from 31 bushels last year to 37 for the current season. Throughout the Corn Belt as a whole the yield of corn this year at 41 bushels is the same as it was in 1943.

The five states of the district last year produced 47 per cent of the U. S. crop on 29 per cent of the nation's total acreage harvested. This year the indicated production will amount to only 43 per cent of the U. S. total on 30 per cent of the acreage. The 12 states of the Corn Belt* produce about four-fifths of the total crop on less than two-thirds of the total acreage devoted to the crop in the nation.

Soybean production on September 1 was estimated to total 179 million bushels, or 8 per cent less than the 196 million bushels produced in 1943. The total crop of soybeans for beans is expected to be down in all principal states except Missouri. In Illinois and Iowa, the two principal producing states, production is indicated to be down about 6 million bushels with 66 and 37 million bushels respectively for Illinois and Iowa anticipated for this year, in contrast to 70 and 39 million bushels respectively for 1943.

*In the order of their production: Iowa, Illinois, Nebraska, Minnesota, Missouri, Indiana, Ohio, South Dakota, Kansas, Wisconsin, Kentucky, and Michigan.

TOTAL PRODUCTION, ALL CORN
(In millions of bushels)

	1943	1944
Illinois.....	426.6	410.8
Indiana.....	210.4	169.3
Iowa.....	640.7	590.0
Michigan.....	52.9	57.8
Wisconsin.....	108.9	107.2
Total — five states	1,439.5	1,335.1

Bank Reserve and Deposit Changes

Excess Reserves Show Downward Trend

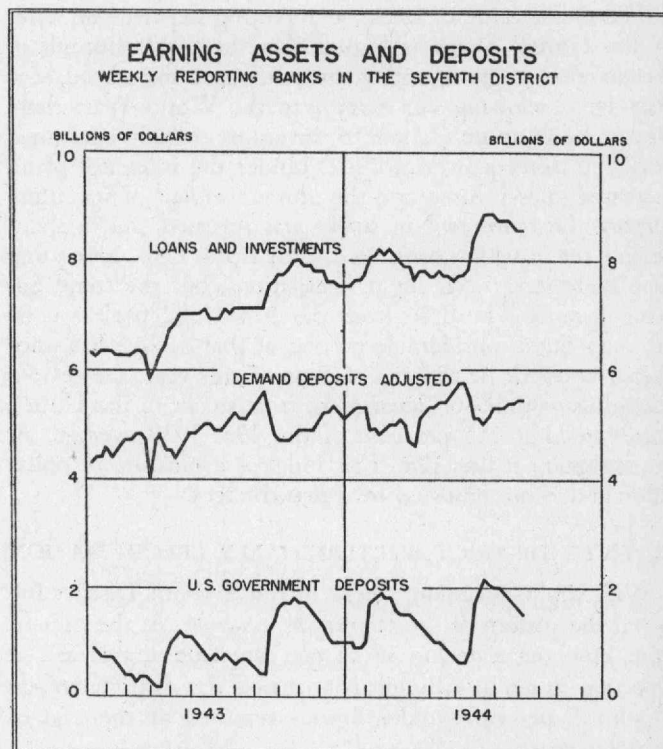
Since the end of the Fifth War Loan Drive in July, the money market has been dominated by Treasury expenditure of war loan account balances built up during the Fifth War Loan. Unlike deposits owned by the public, U. S. Government war loan deposits of commercial banks are not subject to reserve requirements. For this reason required reserves tend to rise between war loan drives, when the Treasury is financing part of its expenditures by withdrawals from war loan accounts and there is a consequent shift in commercial bank deposits from U. S. Government to private account. Also, member bank reserves tend to be reduced through expansion in money in circulation and outflow of gold. Because of the drain on reserve balances through increased demand for currency and gold outflow, and the increase in required reserves, member bank excess reserves tend to decline between war loan drives. Consequently, those banks which have no excess reserves, or which do not wish to reduce the amount of excess reserves they carry, sell Government securities or, in some cases, borrow to replenish or add to their reserve deposits with the Federal Reserve Banks.

From the Fifth War Loan peak of about 1 billion 560 million dollars on July 12 excess reserves of member banks in the nation declined more or less regularly to approximately 900 million dollars on September 20. Required reserves increased by more than 1 billion 300 million dollars between these two dates, while reserve balances were augmented by over 600 million dollars.

In the Seventh District, excess reserves averaged 188 million dollars in the first half of July and by the first half of September had declined to 130 million dollars. Reserve balances increased slightly in this period from an average of 1 billion 986 million dollars to 2 billion 31 million dollars, while required reserves expanded from 1 billion 797 million dollars to 1 billion 901 million dollars. Country banks accounted for about two-thirds of the decrease in excess reserves for the district, declining from an average of 137 million dollars in the first half of July to 97 million dollars in the first half of September. Excess reserves of reserve city banks decreased from 40 million dollars to 26 million dollars, and Chicago central reserve city banks from 12 million to 7 million dollars.

DEPOSITS DECREASE

After reaching a new all-time high of 64 billion 231 million dollars on July 12, total deposits-adjusted¹ of weekly reporting banks in the United States declined rather steadily to 61 billion 605 million dollars on September 20, a decrease of 2 billion 626 million dollars over the period. U. S. Government deposits decreased 5 billion 620 million dollars as



a result of net Treasury withdrawals from war loan accounts, and domestic banks drew on their balances carried with the weekly reporting banks to the extent of 448 million dollars. Adjusted demand deposits and time deposits increased by 3 billion 41 million dollars and 411 million dollars, respectively, as funds disbursed by the Treasury were deposited in weekly reporting banks.

Four factors account for the failure of adjusted demand and time deposits to expand to the same extent as the reduction in U. S. Government deposits. Loans of weekly reporting banks declined from 12 billion 330 million on July 12 to 10 billion 946 million dollars on September 20, most of the decline occurring as a result of the repayment of loans for purchasing or carrying securities. Money in circulation increased from 22 billion 531 million dollars on July 19 to 23 billion 558 million dollars on September 20, and the monetary gold stock decreased approximately 160 million dollars to 20 billion 885 million dollars on September 20. Also, there was probably some redistribution of funds from city to country banks, as part of Treasury expenditures in outlying areas were made with funds withdrawn from city banks, and, particularly in September before the quarterly income tax date, as business funds were withdrawn from New York City to other parts of the country.

¹Total deposits less cash items in process of collection.

Inventories Above Prewar Level

Shifting Composition of Department Store Stocks

The dollar value of stocks at reporting department stores in the United States is higher than at the beginning of the defense program, and is currently running ahead of a year ago. Following our entry into the World War, there was a rapid accumulation of inventory which continued until the third quarter of 1942. Under the influence of an increased sales volume and the announcement of inventory control, the movement in stocks was reversed, and a sharp decline set in which continued until April 1943. Since that time there have been slight fluctuations, but the trend has been upward. The drop from the June 1942 peak was 60 per cent, but a considerable portion of that decline has since been recovered. At the end of June of this year, the seasonally adjusted index of department store stocks in the United States stood at 155 per cent of the 1935-1939 average. At the low point it was 128. This index is a measure of dollar value and is not adjusted for price changes.

SEVENTH DISTRICT SUBSTANTIALLY BELOW NATION

With slight deviation, stocks in the Seventh District followed the pattern of the country as a whole. At the present time, however, a decline of 11 per cent from a year ago at reporting stores in Chicago has carried the district total to a point 5 per cent under figures reported at the end of July last year.

Department stores have been in an unusually good position to maintain inventories. They are outlets for a wide variety of goods, and can shift from items no longer available to those still being manufactured. Their inventories at the present time, however, include stocks that would sell only at greatly reduced prices after the war.

Store owners made it a practice to accumulate inventories as long as it was possible. They did this to support the increased sales volume and to protect themselves against shortages which they felt would develop. As a result, stock assortments have become unbalanced in many lines. Both dealers and customers are inclined to take what they can get. It is important, therefore, in looking at the dollar value of inventories to remember that the composition of the stock has changed. Formerly, stocks were made up of both hard and soft lines, whereas, today the hard lines have been eliminated or materially reduced. Such items as electrical refrigerators, radios, and major household appliances have almost disappeared and this decline in the dollar value of inventories has been offset by increases in stocks of wearing apparel and other soft goods.

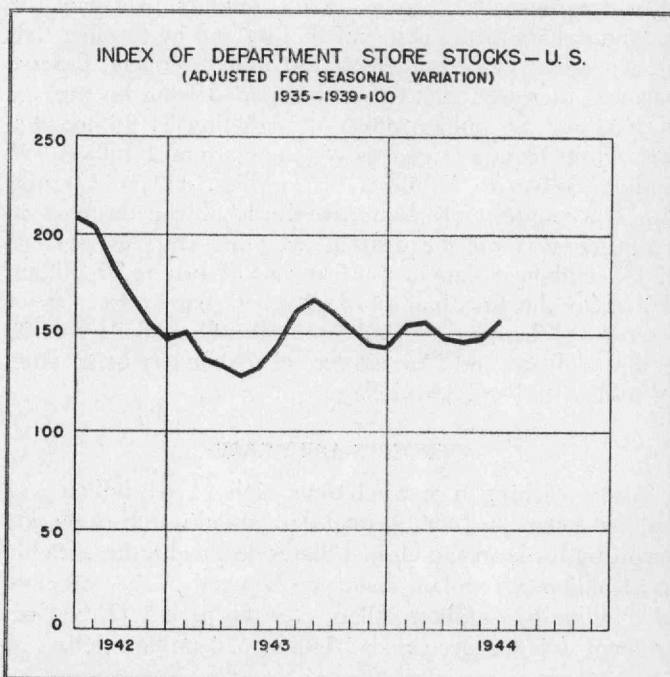
OUTSTANDING ORDERS INCREASING

This attempt to maintain inventory position is also reflected in the movement of outstanding orders. The value

of such orders increased steadily from the last quarter of 1942 until July 1943, and then declined until January 1944. By the end of July of this year, the value of outstanding orders had reached approximately the high point of a year ago. Although these figures are seasonal in nature, they do reveal both the increased volume of orders being placed by stores and the greater replacement cost.

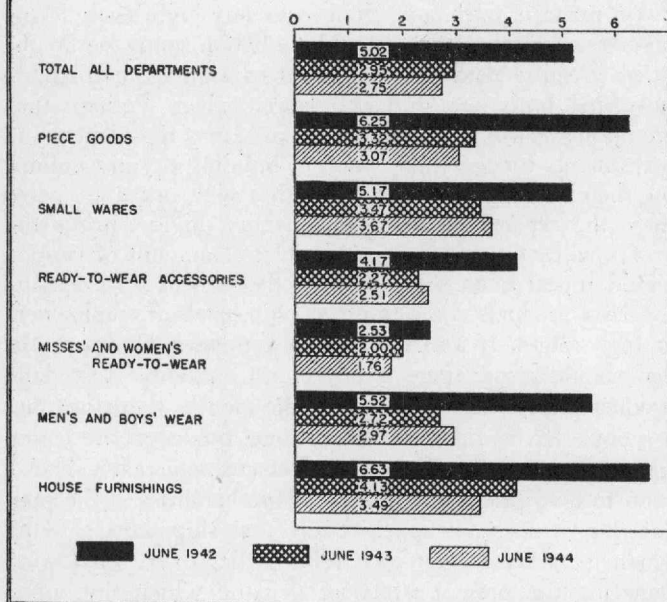
Given sufficient buying power, a consumer will buy all those goods which he heretofore had only dreamed of possessing. Such articles as fur coats and jewelry which the average consumer feels are out of his price range in normal times, are demand items in department stores now. As shortages of those goods which the store normally carried developed, such luxuries were stocked and customers bought them.

Substitute goods, however, have been warily stocked by department store merchants. Even though the public now buys items which would warrant prewar scorn, such as paper garbage cans, make-shift household appliances, and victory undergarments, they are not likely to do so in the postwar. Many merchants have been reluctant to stock such items since they know that they will become "dead" goods when the standard merchandise is again available. They must have something to sell but they are hopeful that their stock of such goods will be thin when conversion comes. Nevertheless, they must continue to buy "war" goods and are prepared to take their loss when clearances are necessary.



SOURCE: FEDERAL RESERVE BULLETIN

STOCK TO SALES RATIOS DEPARTMENT STORES IN THE SEVENTH DISTRICT



THE SEVENTH DISTRICT SITUATION

Values of inventories on hand in reporting stores in this district are currently running 5 per cent below a year ago. Stocks of reporting stores in principal cities rose in values ranging from 2 per cent in Detroit and Indianapolis, to 12 per cent in Milwaukee. The Chicago decline was 11 per cent.

Because stocks in some department stores suffered a more serious depletion than the others, it is natural that the character of the department store inventories should change. When sources of supplies of most durable goods were closed, department stores saw that they could no longer sustain the importance of home furnishings, household appliances, and similar sections. Consequently, in order to maintain sales of goods that were available, it was necessary to counter-balance thin stocks in such departments by adding to the weight of nondurable goods. Thus apparel, small wares, and similar kinds of goods now constitute a large portion of total department store inventories. Apparel departments had no decline in dollar volume of stocks even when other departments in the stores were down to rock-bottom levels.

In fact, in June 1943, which was the low point in the total volume of stocks, ready-to-wear apparel departments gained 12.8 per cent over the previous June. In the same period, total store inventories declined 20.2 per cent. In order to keep pace with the demand for those articles of apparel for which the consumer had expressed a preference, inventories of furs, ready-to-wear clothing, and like items which have been always relatively easy to obtain were added to consistently.

Piece goods sections gained in stock value. Evidently some consumers sought to evade the higher prices of ready-to-wear apparel by making their own clothes. Consumers,

too, did some trading up, for basement stores have consistently lost volume in both sales and stock. The prevalent consumer's belief seems to be that in wartime one must pay high prices to obtain standard quality goods.

STOCK-SALES RATIOS DECLINE

In view of rising sales, it has been impossible for stores to accumulate stocks sufficiently high to maintain stock-sales relations. In the Seventh Federal Reserve District, stocks on hand at reporting department stores, at the end of June 1944, were 2.75 times the June sales. On the same date a year ago, they were 2.95, and in 1942 they were 5.02.

Because department stores in the Seventh District have materially increased their financial liquidity during the war period, they will be able to replace depleted stocks of goods and victory products as soon as such replacements are available. This buying to replenish inventories, in addition to the backlog of demand by individual consumers, will stimulate business activity after the war.

FIGURES DO NOT TELL FULL STORY

No set of inventory figures can reveal the underlying problems facing the management of department stores during this critical war period. Neither physical count nor dollar value of stocks on hand even begins to disclose the situation with respect to the future of merchandising. At the present time, merchandise managers are actuated by the same forces as those which motivate the consumer. The merchandise man buys what he can get and hopes for the best. If he does not buy wartime quality he will have nothing to sell to his customers. If he becomes overstocked and is caught with a sizable inventory when standard articles are available he faces a shrinkage of dangerous proportions.

The volume of outstanding orders in relation to sales is not strictly comparable with ratios during normal times. Sources of supply have changed, and the time and dependability of delivery are uncertain factors. Even if the suppliers can furnish the goods with a reasonable degree of promptness, transportation difficulties may intervene and seriously handicap the retailer.

Ratios of stocks to sales must also be understood in the light of present conditions. A stock-sales ratio that would be ample in peacetime may be inadequate today and dangerously high tomorrow. Insofar as the retailer is concerned, a gradual reconversion to the manufacture of consumers' goods will be a blessing in that it will give him an opportunity to convert his stocks without serious loss.

Another aspect of the present inventory situation is revealed in the balance sheet. Under ordinary conditions cash and Government securities account for one-third of total current assets, receivables account for one-third, and inventory makes up the remainder. As a result of wartime operations, the cash position of the stores has increased at the expense of receivables and inventories. Higher taxes have made it prudent for management to carry a higher percentage of their funds in the form of marketable securities.

DAIRY FARMERS LOOK AHEAD

(Continued from Inside Cover)

1942. Perhaps most interest has been aroused in consumers by the butter situation, partly because the pinch of rationing and short supplies has been most sharp in the case of butter. Consumption of 12 pounds per capita in 1943 and 1944 has been the lowest in several decades, and substantially lower than the 16.7 pounds average consumption in the five years, 1935-39. The most important point to be emphasized is that the butter situation is largely the result of the strong demand for fluid whole milk. Fluid outlets have been relatively more attractive than butter manufacture, which has resulted in a substantial diversion from butter manufacturing to whole milk sales.

In the accompanying chart II the trends in per capita consumption of the principal classes of dairy products are shown. The figures are in terms of index numbers using 1935-39 = 100.

IMPORTANCE OF LEND-LEASE

Figures on Government purchases of milk products for war purposes do not at present lend themselves to a separation of the amounts used by civilians from the requirements of the military services. However, net purchases by the War Food Administration give a fairly accurate picture of the requirements for lend-lease. For creamery butter 1941 purchases were negligible, while in 1942 they absorbed about 2 per cent of production and in 1943 nearly 6 per cent. Net purchases of American cheese constituted 22 per cent of 1941 production, 29 per cent of the 1942 total produced, while for 1943 the figure was 31 per cent.

For evaporated milk net purchases by WFA accounted for 23 per cent of production in 1941, 29 per cent in 1942, and dropped to under 6 per cent in 1943. The production of condensed milk is of minor importance, but net purchases were 10 per cent in 1942 and 56 per cent last year. About one-third of the dried whole milk produced last year went to WFA. Net purchases of "nonfat dry milk solids" (formerly known as dry skim milk) were 10 per cent of production in 1941, rose to 43 per cent for 1942, and to 45 per cent for last year.

OUTLOOK - CAUTION INDICATED

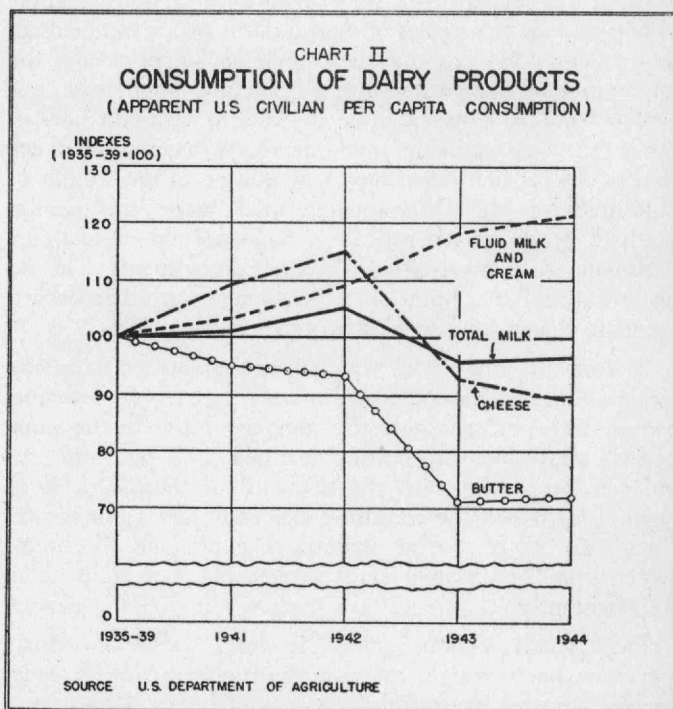
During much of the war period the profitability of the dairy enterprise, in terms of ratios of price of products to prices of feeds in the dairy ration, has been a rather mixed situation. Until very recent months butterfat-feed price ratios have been somewhat below average, while milk-feed ratios have been quite favorable to production and sale of milk. This disparity has tended to become adjusted in recent months. Demand is such that milk prices might be expected to remain at levels somewhat higher than last year. However, an early end to European hostilities may upset these expectations. Feed prices have tended upward, although in July the OPA announced lower ceilings on oats and barley.

Prices for dairy products have been at record high levels and dairy incomes have looked attractive. However, costs,

especially for labor and feeds, have also been at very high levels. As a result of these high costs the gross margins to dairy farmers have not yielded profits as attractive as for some other farm enterprises.

Yet prices of milk have climbed to very high levels. Many observers feel that there is wild inflation going on in the prices recently paid for some types of animals, particularly pure-bred bulls and bull and heifer calves. Perhaps they are unduly alarmist, and the prices paid may represent sound investments for dairymen who are building up and improving their herds. But to the extent that such prices are based upon the expectation that present dairy product prices and profits will continue indefinitely a great amount of caution would appear to be wise. Much of the present high demand for dairy products is the result of high levels of employment at high wages. If an early end to European phases of the war should come, there is no certain guarantee that dairy product prices will not within a few months thereafter face a serious downward adjustment. Some producers are counting on European food relief needs to cushion such a shock—even to hold prices up. In view of probabilities at the present time it does not appear likely that shipments of dairy products to Europe for food relief will go very far toward replacing the present tripod of demand which rests upon the three legs of high civilian incomes, heavy military requirements, and lend-lease shipments. Should the war be followed by very short and not too extensive unemployment the situation will be much more promising.

Meanwhile, many far-sighted dairymen are taking advantage of present high levels of demand for meats to cull out inefficient animals, and where they are building herds are basing their judgment and the prices they pay on fairly modest long-time expectations.



NATIONAL SUMMARY OF BUSINESS CONDITIONS

BY BOARD OF GOVERNORS OF FEDERAL RESERVE SYSTEM

Industrial output and employment showed little change in August. Retail trade was at a new high level for the month. There was a small further rise in retail commodity prices.

Industrial production—Output at factories and mines was 232 per cent of the 1935-39 average in August as compared with 231 for July, according to the Board's seasonally adjusted index of industrial production. Steel production was maintained, while output of nonferrous metals continued to decline. Over-all, activity in the metal fabricating industries continued at the level of the preceding month. There were large increases in output of heavy trucks, tanks, and some other critical ordnance items in August; aircraft production showed little change; while shipbuilding declined.

Output increased in the shoe, woolen and worsted, and paper industries in August following a drop in July which reflected chiefly the curtailment of operations around the Fourth. Output of manufactured foods, after allowance for seasonal changes, declined in August, largely reflecting decreases in output of meats, dairy products, and sugar products. Distilleries were shifted for the month of August from production of industrial alcohol for war purposes and output of about 50,000,000 proof gallons of beverage spirits was reported. Production of other nondurable goods was maintained at the level of the preceding month.

Minerals output in August rose 2 per cent from July, reflecting increases in coal and crude petroleum. Crude petroleum production was at a rate 11 per cent above the same month last year.

Distribution—Value of department store sales, according to the Board's seasonally adjusted index, was larger in August and the first half of September than in the first half of 1944 and averaged 12 per cent above the corresponding period of last year. In the third quarter the index at 90 per cent above the 1935-39 average has been at the highest level on record.

Carloadings of railroad freight were maintained in large volume in August. During the first three weeks in September loadings were slightly less than during the same period a year ago, owing to decreases in all classes of freight except merchandise in less than carload lots and miscellaneous shipments.

Commodity prices—Wholesale prices of farm products and foods showed small seasonal decreases from the middle of August to the middle of September. Maximum prices of such industrial goods as cotton fabrics, cement, and bricks were increased.

Retail prices of food and other cost of living items increased slightly in August and the average of all items was 2 per cent higher than a year ago, according to the Bureau of Labor Statistics index.

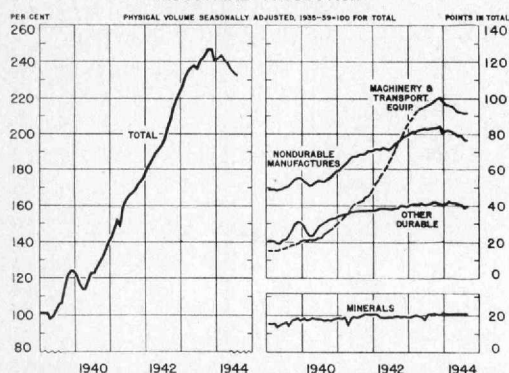
Agriculture—Crop prospects improved during August and the early part of September and harvests of most major crops are expected to be larger than last season. Marketings of livestock products, which were at a record level earlier this year and 15 per cent higher than during the first six months of 1943, have declined in July and August to about the same level as that prevailing last year.

Bank credit—Bank deposits of businesses and individuals, as well as currency in circulation, have increased since the end of the Fifth War Loan Drive. This increase in the money holdings of businesses and individuals is largely a reflection of the expenditures made by the Treasury from its war-loan accounts built up during the drive. Adjusted demand and time deposits at member banks in leading cities increased by nearly 4 billion dollars between the close of the drive and mid-September, or by over three-quarters of the amount of reduction in such funds during the drive. Deposits at non-reporting banks probably increased by nearly 2 billion dollars. Treasury war loan accounts at banks declined by nearly 8 billion dollars.

In the same period loans and investments at weekly reporting member banks in 101 leading cities declined by 2.2 billion dollars. Loans to brokers and dealers for purchasing and carrying Government securities declined to a level approximately equal to that of the pre-drive period. There was, however, a temporary increase in such borrowings in late August and early September presumably associated with market transactions stemming from the Treasury offer to exchange certificates maturing on September 1 and notes maturing on September 15 for new issues. Loans to others for purchasing and carrying securities declined steadily, but on September 13 were still well above the pre-drive level. Government security holdings showed a net decline of 800 million dollars over the period, reflecting mainly substantial bill sales by reporting banks partially offset by some increase in bond holdings.

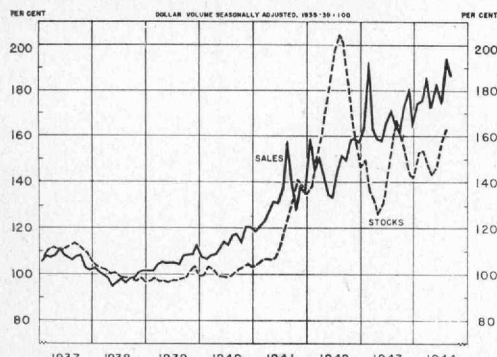
As the result of the increase in deposits of businesses and individuals, the average level of required reserves at all member banks rose by about a billion dollars between the close of the Fifth Drive and mid-September. In addition, a billion dollar increase in money in circulation and some further decrease in gold stock served to absorb reserve funds. Member bank needs for reserves due to these factors were met largely through an increase of 1.7 billion dollars in the Government security portfolio of the Federal Reserve Banks and there was also a slight increase in Reserve Bank discounts. Excess reserves declined from an average level of 1.4 billion at the close of the drive to somewhat less than a billion by early September.

INDUSTRIAL PRODUCTION



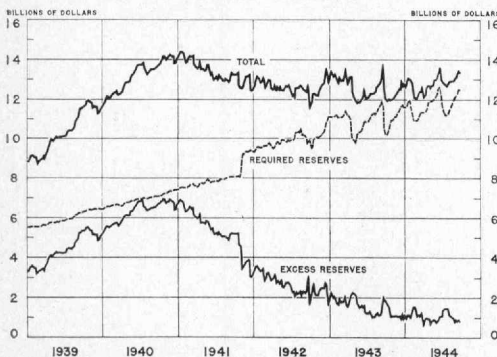
Federal Reserve indexes. Groups are expressed in terms of points in the total index. Monthly figures, latest shown are for August 1944 except total. Latest total figure shown is preliminary for July.

DEPARTMENT STORE SALES AND STOCKS



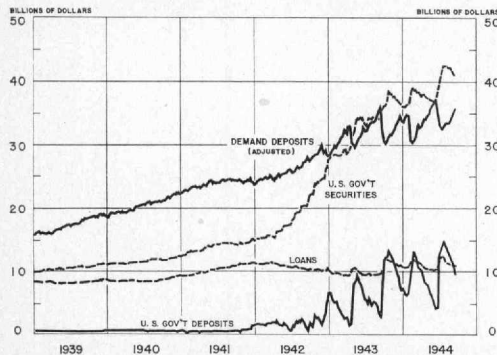
Federal Reserve indexes. Monthly figures, latest sales figures shown are for August 1944, latest stock figures shown are for July 1944.

MEMBER BANK RESERVES



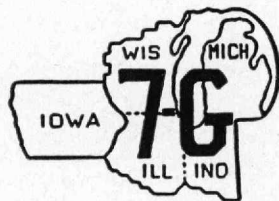
Breakdown between required and excess reserves partly estimated. Wednesday figures, latest shown are for September 20, 1944.

MEMBER BANKS IN LEADING CITIES



Demand deposits (adjusted) exclude U. S. Government and interbank deposits and collection items. Government securities include direct and guaranteed issues. Wednesday figures, latest shown are for September 13, 1944.

SEVENTH FEDERAL



RESERVE DISTRICT

