AUGUST, 1946

LIBRARY
AUG 7 1946

BUSINESS CONDITIONS

A REVIEW BY THE FEDERAL RESERVE BANK OF CHICAGO

Banks Expand Consumer Instalment Financing

Increased Competition Looms for Credit Business

The post V-J Day upsurge in consumer credit now foreshadows a period of intense competition among finance companies and many banks for the retail instalment credit business developing as a result of increased output of automobiles and other major consumers' durable goods.[1] Their prewar campaign to become the major consumer instalment financing agency interrupted by wartime shortages of goods to be financed, banks in most sections of the Seventh Federal Reserve District and the nation are expressing a strong determination to obtain an increasing proportion of the gradually rising volume of retail instalment paper. Finance companies, however, with longer experience and well-established dealer contacts in this credit field are confident of their ability to retain prewar dominance in retail instalment financing.

Well before the end of the war, several uniform financing plans were developed by interested bank and nonbank groups for use by banks in strengthening their individual postwar drives for instalment credit business. These plans are limited to the retail instalment *sale* credit sphere, where banks made less prewar progress and face greater postwar problems than in instalment *cash lending* in which banks are the dominant lenders.

Finance companies, which in the prewar period held over two-thirds of all retail instalment paper in the hands of financial institutions, have responded to announced bank competition by reducing rates and strengthening dealer relationships through which virtually all of their sale credit business originates. Extensive campaigns are being launched to induce consumers to finance their purchases through dealers rather than directly with banks and other institutions.

AUTOMOBILE INSTALMENT FINANCING MARKET

Automobile instalment financing in the prewar period accounted for at least three-fourths of all agency financed retail instalment paper and therefore receives primary attention here. Finance companies and banks in turn held about nine-tenths of all agency financed prewar instalment sales of automobiles, including not only instalment sale credit originated by automobile dealers and sold to credit agencies but also instalment cash credit extended directly to consumers for the specific purpose of buying automobiles.

Consumers who buy automobiles on credit allow dealers to make the necessary arrangements with a financing agency or borrow money from a financing agency and pay cash to automobile dealers. The first method, under which the dealer becomes the key figure in originating the financing transaction, for many years has predominated in automobile instalment financing for several reasons: (1) convenience to consumers in buying and financing their automobiles in the same place and, in the immediate years after World War I, lack of alternative sources of credit; (2) dealer interest in arranging the financial transaction because of their participation through a discounting process in the financing charge as well as in the premium on fire, theft, and collision insurance which form an integral and profitable part of each automobile instalment sale; (3) a noticeable general tendency of buyers to do little or no "shopping around" among dealers or other available sources of credit to find the least expensive financing arrangements, both because financing is regarded as incidental to the credit purchases of automobiles and also because of a common desire to avoid publicity in incurring debt; and (4) generally small influence of variations in finance charges upon the size of credit buyers' monthly instalment payments.

Finance companies, largely born on the wave of the post World War I growth of the automobile business, have developed close relationships with automobile dealers because of the latters' general inability to become financially self-sufficient, and because of the initial unwillingness of banks to enter the instalment field. In addition to sharing finance and insurance charges with dealers, finance companies typically offer other services designed to get the bulk of each dealer's business, including providing loans to dealers for sales-service facilities, financing the dealer's new and used cars from the time of acquisition to the time of sale—wholesale financing or floor planning—and giving dealers finance and insurance forms, collection services, and financial advice. Some banks are now providing many of these services.

Automobile manufacturers themselves are also interested in how the credit purchases of their products are financed. Since dealers have long been required to pay cash at the time automobiles are shipped from the factory, strong and well-established finance companies have added to manufacturer convenience and have reduced dealer risks. Credit financing being an integral part of over 60 per cent of the automobiles sold before the war, manufacturers in the past have stated a preference for uniform and nation-wide financing arrangements in the purchases of their cars. Manufacturers, moreover, have realized the profitability attached to financing.

As a consequence, each of the three largest automobile manufacturers became interested after World I in its own finance company and sought with increasing success to have dealers channel automobile paper to the respective member of the "Big Three", as these nation-wide finance companies were soon termed. Manufacturer interest and the advantages of large-scale operations (a) in meeting dealer wholesale financing needs, (b) in getting required capital to operate in the 1920's and early 1930's, a period in which most com-

(*Continued on Page 8*)

[1]Unless otherwise specified, the term "banks" refers to commercial banks and the term "finance companies" to sales finance companies. All references to credit are to consumer instalment sales financing.

Digitized for FRASER
http://fraser.stlouisfed.org/
Federal Reserve Bank of St. Louis

Deposit Behavior in the Transition

Metropolitan Banks Show Declining Industrial Accounts

Bankers throughout the country since V-J Day have been watching with considerable interest for signs of a reversal in the spectacular wartime deposit expansion. Recent surveys made by the Federal Reserve System reveal that the process of readjustment to peacetime conditions has had a noticeable, but as yet minor, effect on the volume and distribution of bank deposits.

The most important facts brought out by the surveys show that deposits of individuals and businesses in the nation have continued to rise since the end of the war although at a slower rate, and that rural banks have continued to gain deposits more rapidly than banks in metropolitan areas. The smaller growth, or even decline in some cases, in deposits in metropolitan banks is attributable to the decline in deposits of manufacturing and mining concerns which accompanied the termination of war contracts and reconversion to civilian production.

In the period which roughly approximates World War II, December 31, 1941, to June 30, 1945, total commercial bank deposits (excluding interbank deposits and cash items in the process of collection) rose 100 per cent to a level of 137.7 billion dollars. From June 30, 1945, to January 31, 1946, these deposits advanced another 12 billion dollars, and though obscured by the effects of the war loan drives, the rate of growth was apparently maintained. More recently, however, cash retirements of Governments have contributed to a fairly substantial drop in deposits. Future deposit behavior depends to a considerable extent upon the origin of these deposits and the nature of their wartime growth.

TABLE 1
COMPARISON OF FACTORS AFFECTING COMMERCIAL BANK DEPOSIT EXPANSION
(In billions of dollars)

	Dec. 31, 1941 to June 30, 1945	June 30, 1945 to Dec. 31, 1945
Factors increasing deposits:		
Increase in commercial bank holdings of U. S. Government securities	62.3	6.5
Increase in commercial bank loans	2.0	2.4
Increase in credit extended by Federal Reserve Banks	19.9	2.8
Total	84.2	11.7
Factors decreasing deposits:		
Decline in commercial bank holdings of securities other than U. S. Government securities	.5	—.6[1]
Increase in money in circulation	15.5	1.8
Decline in monetary gold stock	2.5	.1
Increase in bank capital	1.5	.3
Other factors, net influence	.4	.1
Total	20.4	1.7
Net increase in total deposits at all commercial banks	63.8	10.0

[1]Negative sign indicates increase in this factor, with an increasing effect upon deposits.

Note: Deposit figures exclude interbank deposits and cash items in process of collection.

CAUSES FOR DEPOSIT GROWTH

There are three major ways in which our total money supply—deposits and currency—may be expanded: (1) by an inflow of gold, (2) by purchase of securities by the Federal Reserve Banks from nonbankers, or (3) by an expansion of commercial bank credit. Whether an increase in the money supply is in deposits or in currency in circulation depends on the preferences of individuals and businesses as to the form in which they choose to keep their liquid assets. The war brought with the expansion in the money supply a shift in the relative importance of these two types of money, the ratio of currency outside banks to demand deposits adjusted reaching in December 1945 the highest level since 1900, except for the period of the banking crisis in 1932-33.

Unlike the World War I situation, when the deposit expansion was primarily the result of expansion of loans, added deposits during the recent war were largely created by the banks as a result of the increase in the amount of Government securities held by the banking system. In order to make up the difference between its annual spending of roughly 100 billion dollars per year and receipts (excluding borrowing) of about 50 billion dollars per year, the Federal Government was forced to borrow from individuals, businesses, and banks. Insofar as the Government's borrowing requirements were not met by individuals and businesses, banks purchased Government securities. In purchasing new Government securities, they paid the Government with a deposit balance to the credit of the Federal Government. As the Treasury spent these funds, the new deposits were, in effect, merely transferred from the account of the U. S. Government to individuals and businesses who received the Government checks and whose deposits were increased as the Treasury's new balances were reduced. The same result would have obtained had banks purchased Government securities in the open market or loaned money directly to borrowers.

Deposits did not expand by precisely the same amount as the increase in commercial bank holdings of Government securities because some of the other factors which affect deposit volume were also in operation. In Table 1 these factors are shown together with their effects on the magnitude of bank deposits for the war period, December 31, 1941, to June 30, 1945, and for the six-month period, June 30, 1945, to December 31, 1945. A comparison of these two

Digitized for FRASER
http://fraser.stlouisfed.org/
Federal Reserve Bank of St. Louis

periods indicates a definite, significant shift during the last six months of 1945 in the importance of the various factors which influence deposit growth. The change from a war to a peace economy during the second half of 1945 initiated a revival of "private" bank credit. In the latter half of 1945, expansion in bank Government security holdings was still the dominant influence upon deposit growth, the Victory Loan taking place in December 1945; but commercial bank loans and investments other than U. S. Governments, for the first time since the early war period, represented a significant factor in deposit growth.

For deposits in the nation as a whole to decline further—total deposits have declined in some areas since the beginning of 1946—it would be necessary for commercial banks to reduce their holdings of Government securities, since the increase in this factor was primarily responsible for the deposit expansion. A decline in bank holdings of Governments could occur if Federal receipts exceeded expenditures and the surplus used to reduce debt held by the banks. It is also possible that the demand for securities by nonbankers might, either directly or through refunding operations, draw Governments out of the banks. With the prospective continuation of debt retirement in the coming months, there is a strong possibility that total deposits will show some decline. The magnitude of such a decline would depend primarily on the distribution of the retired securities as between bank and nonbank holders.

Several possible developments, however, might operate to further expand deposits. For instance, expansion of bank loans, which has already begun to operate in this direction, might be an important force. If businesses liquidate any of their Government security holdings, banks may absorb them. Reductions in savings bonds holdings, to the extent that they would be refinanced through security sales to banks, would increase deposits. Any of those factors which will change banks' cash or reserve position—primarily a decrease in money in circulation—might cause a further expansion in deposits. Currency in circulation did decline by about 500 million dollars in the first five months of 1946; although higher prices, increased wages, and greater business activity may operate in preventing any considerable return of currency.

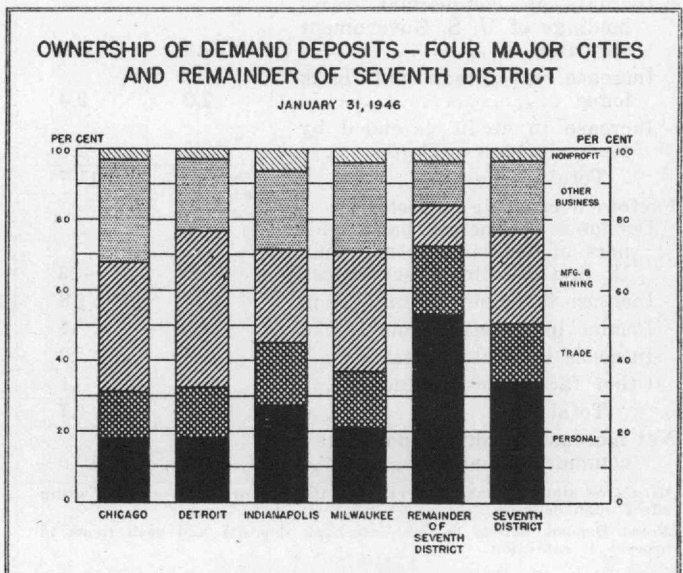
REGIONAL DEPOSIT SHIFTS

All factors considered, it does not appear that deposits of individuals and businesses in the nation as a whole are likely to decline materially. More probably they will tend to rise even further although at a slower rate. It is very probable, however, that certain regions may lose part of their deposit gains as a result of changes in some of the elements which affect deposit volume in a given locality. Although for the United States as a whole the wartime growth of deposits and its acceleration have been caused by the factors already mentioned, varying rates of gain in different areas cannot be attributed to relatively larger or smaller purchases of securities by the banks in these areas. Regional differences in deposit growth stem from the distribution of the banking system's deposits and reflect mainly two factors: first, the spread between receipts and expenditures in the various regions, and second, the manner in which individuals and businesses choose to hold their liquid assets. Two areas with equal income may have different rates of deposit growth because different proportions of liquid assets are held in the form of bank balances, currency, or Government securities.

Interdistrict shifts in deposits took place during the war primarily as a result of three principal factors: (1) location of war industries that led to a different geographical distribution of activity during the war; (2) the location of military establishments; and (3) the large increase in farm income, with a combination of large crops and high prices for those crops. The largest wartime purchaser and spender, that is, the United States Government, raised funds through taxation and the sale of securities to a greater extent in certain districts, notably New York, than it returned by way of expenditures to those districts. On the other hand, other regions, particularly in the South and West, with heavy new war industries and concentration of army camps, were the recipients of a larger volume of Federal funds than were removed from those districts. The tendency of industry and trade to resume prewar patterns after the war is rather generally expected to be accompanied by at least a partial reversal of the wartime flow of deposits between geographic regions—that is, from the South and West to the East.

Within districts, the percentage expansion of demand deposits of individuals and businesses in rural banks was greater than in metropolitan banks. As shown in Table 2, in the six-month period following July 31, 1945, these deposits in the combined four major cities in the Seventh District actually declined, whereas in banks in the remainder of the District they rose 11 per cent. It should be added, however, that comparisons of total deposit changes, rather than of demand deposits of individuals and businesses alone, tend to show urban banks in a more favorable position as bankers' balances and United States Government deposits, which are held mostly in urban banks, increased considerably in the six-month period.

Termination of war contracts, reconversion difficulties,



Digitized for FRASER
http://fraser.stlouisfed.org/
Federal Reserve Bank of St. Louis

TABLE 2

COMPARISON OF CHANGES IN DEMAND DEPOSITS OF INDIVIDUALS AND BUSINESSES, FOUR MAJOR CITIES IN THE SEVENTH DISTRICT

(Amounts in millions of dollars)

Area	Change Dec. 31, 1941 to July 31, 1945		Change July 31, 1945 to Jan. 31, 1946	
	Amount	Per Cent	Amount	Per Cent
Chicago	+1,435	+ 57.9	+ 60	+ 1.5
Detroit	+ 582	+ 88.7	— 81	— 6.5
Indianapolis	+ 151	+ 84.8	+ 6	+ 1.8
Milwaukee ..	+ 207	+ 92.4	— 14	— 3.2
Remainder of District ..	+2,464	+138.0	+469	+11.0
7th District total	+4,839	+ 90.9	+440	+ 4.3

strikes, the relatively greater impact of tax payments, and the Victory Loan in the metropolitan areas combined to restrict deposit growth in urban centers. One other element, not common to the actual war period, also tended to restrict deposit gains in the urban banks in the July 31, 1945, to January 31, 1946 period. Large investors, both individuals and businesses, recognized that the Victory Loan was the last major Treasury financing for some time, and so bought heavily in the drive and, even more significantly, failed to sell in any great volume either previously purchased issues or those obtained in the Victory drive.

CHANGES IN DEPOSIT OWNERSHIP

The Federal Reserve Bank of Chicago's most recent survey of deposit ownership, in which 326 reporting banks participated, provides further, more specific information on the shifts which have occurred since the end of the war in demand deposits of individuals and businesses in the Seventh Federal Reserve District. For the District as a whole these demand deposits rose 4.3 per cent from July 31, 1945, to a level of 10.6 billion dollars on January 31, 1946. This compares with a gain of approximately 6.4 per cent for the entire nation. This relatively small change in the District's deposits reflects not so much deposit stability since the end of the war but some major counteracting shifts in deposit ownership within the District.

In Table 3, percentage changes for the six-month period in demand deposits by ownership groups are shown for the four major cities in the Seventh District, the remainder of the District, and the Seventh District as a whole. The most significant change revealed by the figures is a substantial reduction in manufacturing and mining accounts. These deposits dropped approximately 500 million dollars, or more than 15 per cent, in the period covered, constituting one of the first major declines in wartime deposits of any group. Seventh District reductions in manufacturing and mining accounts paralleled to a considerable extent behavior of these deposits throughout the country, Dallas being the only one of the twelve Federal Reserve Districts whose industrial deposits did not decrease. For the United States as a whole, these deposits dropped 2.3 billion dollars or 13 per cent. The explanation of this sharp deposit decline is, of course, related to the change to a peacetime economy. Although the nation's industrial production reached its wartime peak in the latter part of 1943 and declined a little in 1944, the greatest drop, as measured by the index of industrial production of the Board of Governors of the Federal Reserve System, took place immediately after July 1945. Therefore, the July 1945 to January 1946 period covers some of the first repercussions of the end of the war on heavy industry. Renegotiation of Government contracts, income tax payments, repayments on "V" loans, as well as expenditures for reconverting, all contributed to the drain on manufacturers' cash reserves. Table 3 shows that Detroit, which had a very heavy concentration of war industry, had the largest percentage decline in industrial accounts.

Personal deposits, which comprise a major part, 34 per cent, of all private demand deposits in the Seventh District, continued their upward trend with a gain of almost 13 per cent, as compared with a 15 per cent gain for the entire United States. The expansion in personal deposits which took place between the two survey dates was not as great as that of nonprofit associations, trade, or financial businesses, but is especially significant in view of the fact that consumer expenditures in the United States increased 18 per cent in the last six months of 1945, according to estimates of the Department of Commerce, while total income payments to individuals during the period between the July and January surveys decreased about 5 per cent. Part of the increase in personal deposits is attributable to the seasonal influence upon farmers' balances. But a large portion of the gain in personal deposits was made by individuals other than farmers, and, considering lower consumer incomes and higher consumer expenditure, this would indicate a preference on the part of individuals to keep surplus assets in the highly liquid form of demand deposits. Another important element lies in the inability of people in the period since the end of the war to satisfy many of their demands for new consumers' goods which have been slow in returning to the markets.

Deposits of retail and wholesale trade establishments, which represent the third largest segment of the District's private deposits and which for the nation as a whole grew more rapidly than other business balances during the war, rose about 200 million dollars, making approximately the same percentage gain as personal deposits in the six months after July 31. Detroit and the part of the District outside the other three metropolitan areas made the largest percentage gains. The rise in these accounts very likely reflects the building up of cash balances and depletion of inventories in these establishments, resulting from steadily mounting retail sales, especially with the unprecedented spending during the Christmas season of 1945. Deposits of other nonfinancial businesses, which include theaters, restaurants, construction contractors, hotels, service industries, and the business deposits of professional groups, increased even more rapidly than trade deposits in all the metropolitan areas, except Indianapolis, as well as in the remainder of the District. Accounts of financial businesses, including insurance companies, real estate firms, brokers, and savings and loan associations, showed gains of almost 20 per cent, as did

Digitized for FRASER
http://fraser.stlouisfed.org/
Federal Reserve Bank of St. Louis

TABLE 3

ESTIMATED CHANGES IN OWNERSHIP OF DEMAND DEPOSITS OF INDIVIDUALS AND BUSINESSES, ALL BANKS IN FOUR MAJOR CITIES AND THE REMAINDER OF THE SEVENTH DISTRICT

July 31, 1945 to January 31, 1946

Ownership Classification	Percentage Increase or Decrease (—)					
	Chicago	Detroit	Indianapolis	Milwaukee	Remainder of Seventh District	Seventh District Total
Manufacturing and mining	—13.4	—21.6	—12.3	—19.1	—13.4	—15.3
Public utilities ..	— .3	8.6	— 3.8	—21.2	1.7	— .2
Retail and wholesale trade	8.2	15.8	12.9	2.1	16.8	13.2
All other nonfinancial business	14.2	27.2	3.1	21.0	24.2	19.5
Insurance companies	20.5	——	17.9	59.5	17.7	19.9
All other financial business ..	20.3	.9	28.3	11.8	31.3	20.4
Trust funds of banks	22.4	15.5	23.5	4.3	15.4	19.8
Nonprofit associations ..	7.6	42.6	6.9	29.9	24.3	18.5
Personal, including farmers....	18.8	1.5	7.1	1.7	12.9	12.8
All accounts	1.5	— 6.5	2.3	— 3.4	11.0	4.3

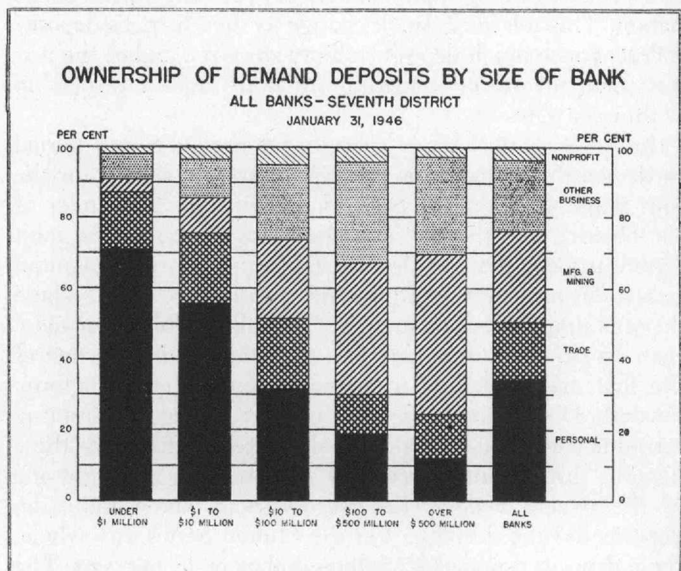
deposits of nonprofit associations. Public utility deposits were the only accounts outside of manufacturing and mining to show a decline in the period, but this decline in no way approached the magnitude of the industrial deposit reduction.

In the accompanying charts, two distributions of deposit ownership are shown for Seventh District banks as of January 31, 1946, after the described shifts had taken place. One chart compares deposit ownership in the four major cities and the remainder of the District. The other compares ownership of all deposits in the District by size of bank. As would be expected, deposits in the metropolitan areas, which constitute over 55 per cent of the District's deposit total, are heavily concentrated in manufacturing accounts. Unlike the Seventh District area outside the major cities, where over 50 per cent of demand deposits of individuals and businesses are held by individuals, less than one-fourth of the demand deposits in the four major cities are in personal accounts. Trade accounts constitute a somewhat smaller proportion of demand deposits in the four cities. Variation in deposit ownership patterns in large and small banks, as would also be expected, is considerable. Over 70 per cent of deposits in the smallest banks—those with total deposits of individuals and businesses under one million dollars—are held by individuals; the larger the bank, the smaller is the relative importance of personal deposits. Thus in the three largest banks in the District with deposits over 500 million dollars, personal deposits accounted for only about 12 per cent of the total. In smaller banks, also, the major part of business deposits belong to unincorporated firms, whereas in the eight largest banks, corporations, primarily manufacturing and mining concerns, account for almost 93 per cent of nonfinancial business deposits. Corporate deposits, it might be added, declined between July 1945 and January 1946 as a part of the drop in manufacturing and mining accounts.

DEPOSIT OUTLOOK

It is still too early to determine with any great degree of accuracy whether new trends in deposits have already set in since the end of the war or how greatly peacetime conditions will affect deposits in the future. As indicated above, trends in total deposits for the nation as a whole will be influenced primarily by the volume of banks' earning assets. To the extent that banks hold Government securities which are retired by the Treasury, the volume of public credit extended by banks will tend to decline, with a decreasing effect upon deposits. Anything which would cause a shifting of Government securities from nonbank to bank ownership, however, or any further increase in private credit extended by banks will tend to raise deposits. Even if the volume of deposits should level off nationally, there is still the possibility of important deposit shifts between districts resulting from possible shifts in business and production activity accompanying the readjustment to peace. Whether the Seventh District will share in any regional gains will, of course, depend upon its balance of payments with the rest of the country.

Within the District, the next survey of deposit ownership may show further shifts among the various types of deposits. What seemed to occur between July 1945 and January 1946 was a drop in deposits of industrial concerns, which drew upon their bank balances to meet expenses incurred in adjusting to peacetime production. Balances of individuals as well as other types of businesses showed gains almost commensurate with the drop in industrial deposits, so that there was no net outflow of funds to other districts. Thus, banks whose deposits are largely owned by individuals and nonindustrial businesses continued to gain deposits during the period in which the large metropolitan banks were experiencing a shrinkage. If the time is not far off when consumer goods become available in greater volume, consumers may draw more heavily upon their bank balances to pay for these goods. Once production approaches current demand, the shift of deposits may turn from personal to business balances.



Digitized for FRASER
http://fraser.stlouisfed.org/
Federal Reserve Bank of St. Louis

Livestock and Feeds Face Readjustment — II

Recent Developments and Prospectus

Since V-J Day the feed-livestock-meat situation has changed substantially. Military requirements of livestock products have decreased. Export requirements continue large, while civilian demand continued to outrun supplies at ceiling prices. Elimination of the rationing of meats, while continuing price ceilings at levels below the prices at which consumers were willing to take the available supply, resulted in a maldistribution of meats with severe shortages becoming apparent, first in restricted areas, then quite generally.

A product priced below the "free market" level when demand is not limited by rationing tends to be consumed largely near the point of production with less than the normal proportion available for distribution to other areas. That shipped to more distant consumers goes largely to those consumers and areas favored by the highest ceiling prices. More of the product is diverted from "normal" channels of distribution, wherein price regulations were enforced, into channels which circumvent most efforts to control prices.

DEMAND OUTPACES SUPPLIES

Based upon past relationships between income payments and meat prices, it is estimated that with ceiling prices eliminated, the average price of meat at retail during the latter half of 1946 may average at least 20 per cent above recent reported prices, with the better grades and more desirable cuts rising somewhat more. The per capita supply of meats available to civilians in 1946 is expected to be about 147 pounds, compared to 138 pounds in 1945. However, this was inadequate to satisfy the demand under ceiling prices. Civilians would have taken about 165 pounds of meat at ceiling prices if the supply had been available.

Before the end of price ceilings, supplies in 1947 were expected to approximate the 1945 level, declining from the 1946 level, due in large part to the production of fewer hogs as well as marketing them at lighter weights. At this writing it is too early to foresee the effect uncontrolled prices will have on livestock production, but it would appear that given a large corn crop, production of meat animals may be somewhat larger than had been expected, utilizing feeds at the expense of dairy and poultry production and possibly also at the expense of the food relief program.

The demand-supply situation for dairy products is similar to that for meats, although shortages probably are not so great except for butter. However, under controlled dairy prices, the gap between demand at ceiling prices and available supplies was expected to increase during the autumn and winter months of low seasonal production. Production of butter will probably continue at a low level due to the exceptionally strong demand for fluid milk, cream, and ice cream. The recent order prohibiting the sale of whipping cream may increase butter production, but only slightly.

Supplies of poultry and eggs were more nearly balanced with demand at ceiling price levels. Earlier in the year it appeared that prices might fall to support levels due to large supplies. However, a part of the excess demand for meats strengthened the poultry and egg markets. Also, relatively large purchases of dried eggs have been made for British account. With adequate meat supplies available, there would be an abundance of poultry and eggs. Prospects for the 1946-47 period indicate lower per capita civilian supplies of eggs and poultry than during the past twelve months, but materially higher than for the prewar period.

With the end of hostilities, export demand for foods for relief feeding as well as for distribution through commercial channels increased. While meat, dairy products, and eggs continue to be of importance in the picture, primary emphasis has shifted to grains, especially wheat. This is due to the emergency nature of the problem—to provide enough calories to keep large numbers of people alive until more food can be produced, with only minor emphasis given to the massive task of trying to provide diets adequate in all the important nutritional elements—and to the fact that neither supplies of nor production capacity for livestock products were adequate to alleviate the situation quickly. In addition to the time factor, quantity was important. Grains consumed directly by people provide several times as much energy as if fed to livestock and the livestock products consumed by people. If large numbers of people were to be fed, they had to be fed on grains and vegetables.

Feeding ratios for hogs, poultry, and dairy cows were favorable, and livestock production was geared closely to the available supply of grains during the war. The favorable livestock-feed price ratios encouraged heavy feeding, with the result that inventories of feed grains had been reduced to a low level. Disappearance of corn, oats, and barley for all purposes during the last quarter of 1945 and the first quarter of 1946 was unusually large, amounting to 76.7 million tons, equivalent to 1,040 pounds per grain-consuming animal unit on farms, January 1, 1946. This compares to a disappearance equivalent to 960 pounds per animal unit during the corresponding period of 1944-45, and to 900 pounds in the five-year period 1938-42.

The combined disappearance of the three grains during October-December 1945 was 9 per cent greater than a year earlier and 11 per cent greater during January-March 1946 than January-March 1945. April 1 stocks of corn, oats, and barley on farms and at terminal markets totaled 42.3 million tons, 10 per cent smaller than on April 1, 1945, and only slightly larger than on April 1, 1944, when supplies were smallest in recent years. The tonnage of corn and oats on farms on July 1 this year was down 25 per cent from a year ago. Continuation of a relatively high rate of disappearance through August and September will reduce the carry-over of

Digitized for FRASER
http://fraser.stlouisfed.org/
Federal Reserve Bank of St. Louis

feed grains into the 1946-47 feeding year to an exceptionally low level.

FEED PRICES INCREASED

In the face of this tight supply situation it was extremely difficult to extract from the domestic economy the quantities of wheat, corn, and oats required for export. The price structure encouraged heavy feeding of relatively large numbers of grain-consuming livestock. Furthermore, livestock production is, for the most part, a long-time undertaking. Herds cannot be expanded and contracted on short notice without incurring excessive costs.

Recent actions taken by the Government, so far as feed is concerned, included the offer in mid-April to buy corn at a premium from producers, primarily for export, and in mid-May the sharp upward revision of ceiling prices of grains and by-product feeds. Under the Government purchase plan, producers were paid a bonus of 30 cents per bushel above the ceiling price on the date of delivery for corn sold to the Commodity Credit Corporation.

Effective May 13, ceiling prices of grains and by-product feeds were adjusted upward. These increases, amounting to 25 cents per bushel of corn and $7.50 to $14 per ton for the important protein supplement foods, narrowed livestock-feed price ratios sufficiently to make the conversion of feed grains into livestock products a much less attractive operation, particularly for hog and poultry producers and cattle feeders. The hog-corn, beef steer-corn, and egg-feed price ratios, as price control ended, were well below the long-time averages. The butter-fat-feed and milk-feed ratios were more favorable relative to the long-time average ratios for these commodities. However, the large amounts of labor required in the production of dairy products, together with the high farm wage rates, probably will require a relatively more favorable feeding ratio for dairy cattle than for other kinds of livestock to maintain dairy production at a high level. In other words, feed costs are a smaller part of total costs in the production of dairy products than for other kinds of livestock. What the immediate future of these ratios will be is not clear until market price relationships are clarified.

The termination of price controls on June 30 permitted grains and other feeds to seek levels determined by demand-supply relationships. Prices rose sharply and, at this writing, still are in a state of flux. The very favorable July 1 Crop Report indicating prospects for a record corn crop and a near-record crop of oats in 1946 promises some relief from the current "tight" feed situation. However, the over-all demand for grain and by-product feeds continues strong, even at higher prices. Wheat millfeed prices have shown some tendency to stabilize at prices $20 to $25 per ton above June 30 ceilings. Oilseed cake and meal prices have been quoted at $20 to $30 above recent ceilings, but offerings have been limited. Relationships between livestock and feed prices will continue unsettled until the feed and livestock markets stabilize. If these markets continue relatively free, livestock-feed price ratios which are somewhat unfavorable to livestock production can be expected to prevail during the period of strong foreign demand for grains for food.

LIVESTOCK PRODUCTION REDUCED

Clearly, some contraction of the livestock industry was dictated by the recent price relationships under price control. This could come in two ways, less intensive feeding or reduction of numbers. The former might be expected to dominate the adjustment in dairy cattle, while both less intensive feeding and reduction of numbers would be important in hog production and cattle feeding. Reduction of numbers would dominate the adjustment in the poultry industry.

Dairy production is a long-time undertaking, and the expense involved in increasing dairy production through increasing cow numbers is large. Also, the number of dairy cows "kept" by most farmers is determined primarily by the amount of hay and pasture produced, not by grain supplies. If the relationship of feed grain to dairy product prices is favorable, more grains are fed; if unfavorable, less grain is fed, but always with roughages providing a large part of the ration. Thus, a scarcity of feed grains is not expected to be a highly important factor in determining the number of dairy cows. Also, with the ending of price ceilings, improved distribution of feed grains may tend to curtail the culling of dairy herds in the hands of the more efficient producers and encourage culling by the less efficient producers.

Feed costs account for about 75 per cent of the total cost of producing hogs. The typical hog ration is predominantly corn, and corn normally provides about 70 per cent of the total tonnage of feed grains. Consequently, a scarcity of feed grains is particularly serious for hog producers. Hog numbers can be increased relatively quickly. It is common for gilts to farrow a litter of pigs at about one year of age. Also, they may be bred to farrow twice each year. Since hog numbers can be increased readily, there is less reluctance to reduce numbers sharply when feed becomes scarce and the hog-corn price ratio is unfavorable. Farmers' reports on breeding intentions indicate a decrease of 16 per cent in the number of sows

SUPPLY AND DISPOSITION OF FEED GRAINS AND CONCENTRATES, YEAR BEGINNING OCTOBER, 1938-45

Item	Average 1938-42	1942	1943	1944	1945[1]
Total supply of concentrates (millions of tons)[2]	147.0	175.1	165.3	161.2	159.1
Total concentrates fed (millions of tons)	115.3	145.7	140.6	133.3	135.0
Uses other than feed (millions of tons)[3]	11.2	12.7	14.0	13.9	13.3
Stocks at end of crop year (millions of tons)	20.5	16.7	10.7	14.0	10.8
Number of grain-consuming animal units, January 1 following (millions)	140.3	159.6	171.1	146.2	146.5
Supply of concentrates per animal unit (tons)	1.05	1.10	.97	1.10	1.09[4]
Utilization of all concentrates for feed per animal unit January 1 following (tons)	.82	.91	.82	.91	.92[4]

[1]Preliminary.

[2]Stocks at beginning of year plus production; includes feed grains, other grains fed, and by-product feeds.

[3]Seed, human food, industry, and exports.

[4]No allowance made for excessive moisture content of much of 1945 corn.

SOURCE: *The Feed Situation*, U.S.D.A., B.A.E., April-May-June 1946, p. 23.

Digitized for FRASER
http://fraser.stlouisfed.org/
Federal Reserve Bank of St. Louis

to farrow between June 1 and December 1, 1946, compared to the corresponding period in 1945, but the price relationships under freer market prices and a bumper corn crop prospect may result in the marketing of fewer bred sows, with farrowings nearly equal to the 1945 volume. Farmers also adjust hog production to feed supplies by varying the weight at which hogs are marketed. As feeds become scarce or high in price relative to the price of hogs, the animals are marketed at lighter weights. This type of adjustment will be an important factor determining the volume of pork production during the coming year.

Cattle feeding is similar to hog production in the type of adjustments to be made to a shortage of feeds. Since cattle are better equipped than hogs to utilize roughages, a larger part of the ration may consist of hay and pasture. However, the fattening process usually involves a ration rich in grains. When grains are scarce or high in price relative to the price of fat cattle, farmers adjust to the situation by feeding fewer cattle and feeding them less grain.

Poultry numbers can be expanded greatly in a single year. The ration consists almost entirely of grains. Consequently, as feed grains become scarce, numbers are curtailed. June 1 estimates indicate that poultrymen culled flocks during May at a rate about 60 per cent higher than average. Culling before May 1 was at about a normal rate. The scarcity of feeds and the desire of producers to adjust their production costs to the less favorable egg-feed ratio by ridding their flocks of the least efficient birds encouraged heavy culling. Also, it reduced the number of chicks hatched.

Production of chickens in 1946 may total 20 per cent less than in 1945, the reduction being largely in broilers. The number of cattle on feed for market in the Corn Belt states as of April 1 this year was 17 per cent less than a year ago. The 1946 turkey crop is expected to be 15 per cent smaller in number than the record crop last year and 10 per cent less than growers intended in January. Also, there are indications the average weight per bird will be less than in recent years.

Production of milk is expected to total at least 2 to 3 per cent less than in 1945. Greatest contraction will tend to occur on those farms and in those areas which normally rely largely on purchased feeds. With a shortage of feeds, more than the usual proportion of grains will be fed on the farms and in the areas where produced, with less being sold for distribution in feed deficit areas. Less favorable livestock-feed price ratios will, of course, facilitate distribution of feed grains, favoring the more efficient producers as to the procurement of feeds.

The extent of the adjustments in livestock operations will be governed largely by four factors: the geographical distribution of existing short grain supplies during the next few months, before 1946 feed grain crops are harvested; prospects for the 1946 corn crop; cost-price relationships under decontrolled prices; and the extent of our commitments to aid in feeding hungry peoples abroad.

EXPECT LARGE FUTURE PRODUCTION

Total production of meat in 1946 is expected to approximate 22.6 billion pounds, slightly less than the 22.9 billion pounds produced in 1945, but about 40 per cent above the 1935-39 level. Longer-run prospects, beyond the current emergency relief feeding period, are for a continued high level of production of feeds and livestock and livestock products. Much of the increased production of feed grains during the war years resulted from technological developments in agriculture, such as development and general adoption of higher yielding varieties of seeds, improved hay and pastures, and increased use of fertilizers. The shift from horse to mechanical power will continue and will release more feeds for other kinds of livestock.

All these forces will promote a large production of feeds in the future, possibly equal to or even above the record volume of recent years. With large supplies of feeds, high levels of livestock production are to be expected. Should future feed supplies approximate those of recent years, the per capita production of beef and veal in 1950 would be about 70 pounds and of pork and lard about 91 to 104 pounds, according to U. S. Department of Agriculture estimates. This would provide about the same per capita supply of beef and veal as was consumed during the middle 1920's and in 1941 and 1942. Pork and lard supplies would average about 15 pounds more than consumption during the 1920's and well above per capita consumption of recent years. Greater emphasis upon soil conserving practices may result in relatively greater expansion in cattle and less in hogs and poultry.

READJUSTMENT IN LIVESTOCK-FEED SITUATION

Price relationships during the war favored a rapid conversion of feeds into livestock products, reducing feed inventories to a very low level. With the end of war, greatly enlarged demands for food products for commercial export and for relief feeding in devastated areas added to the high level of civilian demand, no longer held in check by rationing controls, resulted in completely inadquate supplies of food to satisfy existing needs and desires. In an effort to supply emergency food requirements, it was necessary to allocate sizable quantities of grains, which normally would have been used to produce livestock products, for export. The resulting shortage of feed grains dictated a contraction of livestock production.

With highly favorable feeding ratios, it was difficult to extract from the domestic economy the desired quantities of grains for export. Also, there was no assurance that the contraction of livestock production would be made by the less efficient producers. Grain prices were increased to overcome both these problems. Feeding ratios resulted which would have effected the greatest contraction in hogs, poultry, and cattle fattening. The ending of price control may permit meat animals to attract more of the available feed supplies, attenuating the extent of curtailment in meat production at the expense of dairy products.

Finally, there are several influences present in agriculture which indicate the production of large feed supplies in future years. This, in turn, would encourage a high level of production of livestock and relatively large per capita supplies of meats and dairy and poultry products.

Digitized for FRASER
http://fraser.stlouisfed.org/
Federal Reserve Bank of St. Louis

CONSUMER INSTALMENT FINANCING

(*Continued from Inside Front Cover*)

mercial and investment bankers were relatively unacquainted with the automobile financing business, (c) in collecting payments, and (d) in securing repossession, when necessary, of a commodity which moved readily over wide areas, all have tended to favor the "Big Three" as well as relatively large regional finance companies.

Of the total (automobile and non-automobile) retail instalment paper held by the 159 multi-unit and 927 single-city finance companies in existence at the end of 1939, about 89 per cent was held by the 20 largest multi-unit companies, and over 75 per cent was accounted for by General Motors Acceptance Corporation, Universal-CIT Credit Corporation, and Commercial Credit, the finance companies through which respectively General Motors, Ford, and Chrysler automobiles have been largely financed. Thus, when the majority of the banks began their extended "invasion" into the automobile instalment financing field in the middle 1930's their major competition was not, nor is it today, a large number of small locally operated finance companies, but instead a relatively few, large, far flung, well-integrated, and well-operated companies with close dealer relationships. Dealer relationships of the "Big Three" before the war, in fact, were so close that the U. S. Department of Justice was successful in 1939 in outlawing the continuance of certain types of dealer arrangements held to be in restraint of trade.

BANKS SEEK FINANCING

In the middle 1930's what appeared, with some exceptions, to be general bank indifference to retail instalment financing, gradually changed to an attitude of widespread interest, and more banks entered the retail automobile instalment financing field each year after 1934. This changing attitude was influenced by: (1) declining interest rates on a falling volume of business loans and investments, (2) rapid growth in bank deposits and excess reserves as a result of prevailing monetary and fiscal policies and business recovery, (3) increasing need for banks to diversify risks, combined with greater recognition of the profitable experience of finance and small loan companies in extending consumer instalment credit, (4) growing community pressure on banks to provide a rounded producer-consumer credit service, and (5) increasing banker use of the instalment technique as a result of successful experience in making instalment home repair and modernization loans under Title I of the Federal Housing Act passed by Congress in 1934.

The strong dealer-finance company relations very likely will continue to be a compelling factor encouraging the majority of banks entering the automobile instalment financing field to do so directly through the consumer rather than obliquely through the dealer. Direct appeals to consumers, moreover, avoid the necessity of taking all or the bulk of any dealer's retail automobile paper. This practice allows greater selectivity in choice of borrower risks, eliminates the need for engaging in wholesale financing with its low interest return and high risk of loss from possible dealer overstocking and conversion, and requires no sharing of finance charges with dealers. The consumer solicitation method, however, requires greater advertising costs than the dealer solicitation method. Insurance premiums on financed automobiles, a lucrative field for finance company subsidiaries, offer little inducement to banks in some states because of laws limiting or prohibiting banks from acting as insurance brokers.

In several areas, for example, California and New York, banks have used branches with considerable success to facilitate the solicitation of retail instalment sale credit business and to expedite collections and repossessions. In many states, however, branch banking restrictions exist, and there is by no means uniform agreement among bankers, legislators, and others of the importance of branches as an aid in engaging in consumer instalment financing.

POSTWAR COMPETITIVE SITUATION EVALUATED

The fundamental question regarding competition for retail instalment financing in the postwar period appears to be whether the dealer still will be the key figure in automobile financing or whether the consumer will supplant the dealer. Upon the answer to this question may hinge the outcome of plans which the majority of the nation's banks now have to increase their relative importance as a retail automobile instalment financing agency.

Primarily because of their established dealer relationships, finance companies currently appear to have several strong competitive advantages over banks in many areas. The strategic position of dealers will, for a time at least, be strengthened by scarcities of automobiles, and dealers have been made increasingly aware of the advantages of remaining the key figure in consumer automobile financing.

While it has not been demonstrated that consumers will assume more of a "shopping around" attitude toward financing than they did in the prewar period, there is some partial indication that such a change may appear. In recent sample surveys of families in Minneapolis, Buffalo, Salt Lake City, and Montgomery, about half of the persons interviewed in the first three cities and 30 per cent in the fourth, said they would rely upon banks to finance any future credit purchases of automobiles *and* home appliances. At the end of 1939, banks in Minneapolis, Buffalo, and Salt Lake City successively held less than 28, 16, and 12 per cent of the dollar volume of then existing instalment paper in the hands of financial institutions. To the extent that the surveys are representative and numbers of persons are an adequate measure of the dollar volume of retail instalment credit, banks in the months ahead will show a marked increase over their 1939 positions in these cities. Because of wide local variations in the extent to which the financing of automobiles and home appliances has been distributed between banks and finance companies in the past, it is not certain that the results of the recent surveys would have been duplicated if the individuals interviewed had been asked to separate their answers for each of the two commodity groups.

In the prewar period, California accounted for less than 10 per cent of all automobile instalment paper outstanding, yet California banks had 20 per cent of the automobile paper held by the nation's banks. These California banks have

Digitized for FRASER
http://fraser.stlouisfed.org/
Federal Reserve Bank of St. Louis

used the same general techniques as finance companies, namely, building automobile dealer relationships and using branches of their own institutions to expedite credit investigation, collection, and repossession. It is reported that these banks and their branches are extending their automobile and other instalment financing business throughout the eleven states west of the Rockies, utilizing both dealer and consumer solicitation methods.

In the area east of the Rockies, banks appear to be placing greater emphasis on the consumer solicitation method in their drive for postwar automobile instalment financing business. A number of these banks as well as some banks on the West Coast are supplementing their previous plans with the Bank and Agent Auto Plan sponsored by the National Association of Insurance Agents. Under this plan, banks in cooperation with insurance agents are continuing their prewar technique of appealing directly to the consumer for business and are relying mainly upon correspondent bank relations to expedite collection. The relatively small volume of retail automobile instalment loans which these consumer-aimed banks developed in the prewar period probably represented the cream of the consumer credit risks. To keep increasing their volume after automobile instalment selling levels off in the postwar period, these consumer-aimed banks necessarily will have to attract higher-risk credit buyers, many without previous bank connections.

Finance companies appear to be well aware of the possibility and implications of increased bank participation in the consumer instalment credit field. As a result, during and since the war several new and adapted competitive measures have been undertaken: (1) a vigorous campaign by the American Finance Conference, trade association of independent finance companies, and the National Automobile Dealers Association to persuade automobile buyers to place their financing and insurance business through dealers, (2) reductions in basic retail and wholesale financing rates by the "Big Three", and (3) statements by leading finance company executives that they are prepared, if necessary, to engage in an extensive promotional campaign to prove to consumers that finance companies can provide financing at the lowest cost available anywhere.

To the extent that consumers become cost-conscious in a detailed sense, the volume of instalment credit business going to banks or finance companies will be influenced much more in the future than in the past by specific rates charged. Specialization and "know-how" built up through more extended experience, stronger dealer contacts as an aid to business promotion and convenience in solicitation, and branches to aid in spreading risks, costs, and repossessions now give the finance companies certain, if only temporary, advantages over many banks entering the field or seeking to extend consumer credit business. The banks' chief advantages would appear to lie in the lower cost of acquiring capital, the possibility of charging some of the expenses of consumer instalment financing against other banking departments, and in general, by improving upon methods now in use by finance companies.

Finance companies normally secure a substantial proportion—often more than half—of their funds through bank borrowing. Banks are expected to continue to lend freely to finance companies in spite of the competitive character of finance company operations. A few large banks which lend extensively to finance companies thus far have not entered the retail automobile instalment financing business.

OTHER RETAIL INSTALMENT FINANCING

The prewar relations between instalment dealers of non-automotive commodities and financing agencies were generally less formal than in the case of automobiles. Not only were many of these sellers less dependent upon instalment sales than were automobile dealers, but many sellers were able to finance all or part of their own retail instalment paper. Contributory factors were relatively better financial positions, lower-priced goods handled, and the fact that manufacturers did not regularly require cash on delivery. The resulting relatively small volume of non-automobile instalment paper reaching financing agencies and the absence of insurance thereon have somewhat lessened interest in soliciting such business. Although prewar instalment selling of other than automotive commodities accounted for slightly less than one-half of all instalment sales, agency financing of these commodities accounted for only about one-fourth of total retail instalment financing.

Expectations of sharply increased postwar sales of household appliances, furniture, and other durable goods are giving rise to a large expansion in allied credit business. As a result, competition among banks and finance companies for this less profitable retail instalment financing business is anticipated to become keen as the goods flow to consumers in increasing quantities.

In contrast to the automobile financing field, the war-formulated bank plans in non-automobile financing are based primarily on building dealer relationships. At least two cooperative plans exist: the National Sales Finance Plan covering an estimated 1,400 banks east of the Rockies, and the Bankredit Time Payment Plan covering many banks west of the Rockies. In addition, many banks have announced similar individual efforts.

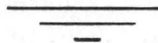
The postwar dealer-aimed plans of "eastern" banks in non-automobile instalment financing and the postwar consumer-aimed plans of these same banks in automobile financing promise to test further the relative merits of the two approaches in postwar consumer credit financing.

At present, with automobiles and other consumers' durable goods still in very limited supply, and with many buyers willing and able to buy available articles with cash, longer range consumer instalment credit financing trends are still quite obscure. It is evident from the foregoing discussion, however, that banks and finance companies intend to strive earnestly for the credit business becoming available. The finance companies cannot expect to win postwar instalment credit contracts without meeting a strong challenge from commercial banks, but it is equally clear that the latter now find themselves in a field in which well-established finance company dominance will not be easily yielded. Until instalment selling levels off, however, all financing groups will experience large increases in business.

Digitized for FRASER
http://fraser.stlouisfed.org/
Federal Reserve Bank of St. Louis

SEVENTH FEDERAL

RESERVE DISTRICT



Digitized for FRASER
http://fraser.stlouisfed.org/
Federal Reserve Bank of St. Louis