

*A review by the* **Federal Reserve Bank of Chicago**

# Business Conditions

**1951 November**



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# Taxes: third round since Korea

*Increases in personal, corporate, and excise taxes will raise the Federal Government's receipts by about 5.7 billion dollars and just about balance the budget for the current fiscal year.*

CONGRESS has added to the nation's tax bill again, for the third time since the outbreak of the Korean war. Most taxpayers will soon feel the impact of the tax increases which took effect November 1, as withholding takes a bigger bite out of pay checks and prices of liquor, cigarettes, gasoline, automobiles, and most home appliances rise to reflect higher excises. It was the need for higher taxes to offset the inflationary pressures generated by soaring defense spending that forced Congress to shoulder the unpleasant assignment of raising taxes again. As usual, during the eight months of debate and discussion, the controversy centered as much on who was to pay as on how much was to be raised.

The final product, the Revenue Act of 1951, is expected to produce 5.7 billion dollars in new revenue, as compared with the revised administration request for a tax bill increasing the Government's total receipts by 10 billion. Because the legislation was so recently enacted, a much smaller increase will be collected during the fiscal year ending next June 30, but this should be nearly enough to balance the Government's cash income and outgo. For the next fiscal year, however, receipts may fall short of expenditures by 10 billion dollars or more, depending on how fast defense expenditures increase.

## 1950 and 1951 tax bills

The new tax boosts are in addition to two tax bills enacted in the latter part of 1950—the Revenue Act of 1950 which increased personal and corporate income tax rates, and the Excess Profits Tax Act which further increased the corporate tax rate as well as imposed the excess

profits tax. Together the two 1950 bills added about eight billion dollars annually to revenue. The higher tax collections resulting from these acts in the first half of this year were an important factor in the temporary abatement of inflationary pressures during the past spring and summer.

The bulk of the added revenue produced by last year's legislation comes from corporate taxes. The new law taps this tax base again, but not as hard as last year—the combined corporate income tax rate is raised five percentage points, from 47 to 52 per cent, which compares with the 38 per cent prevailing during most of the postwar period. The excess profits tax credit was reduced from 85 to 83 per cent of 1946-1949 income, thus increasing the tax yield by about 120 million dollars per year, but the 21 additional excess profits tax relief provisions which were enacted will offset this.

Personal income taxes were raised last year, too. The method employed was to eliminate the reductions from World War II tax rates which had been granted in 1948. This had the effect of raising taxes by 17 per cent in the lowest bracket, and slightly less than 10 per cent for the top income levels. This year Congress imposed a flat addition of 11¾ per cent of present taxes for most taxpayers (11 per cent for the first \$2,000 of taxable income). For married persons with incomes above \$57,600, the increase is 9 per cent of net income after present taxes, somewhat less than the flat rate for lower income persons.

Excise taxes will provide a significant share of the additional revenue. In the 1950 laws, this source was not used, except incidentally, largely because the Revenue Act of 1950



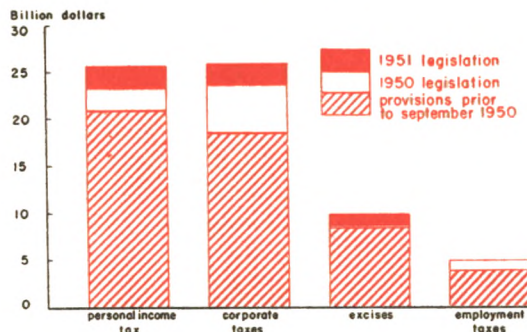
started its life as an excise tax reduction bill, providing the first major reductions from war-time rates. This section of the bill was shelved after the events of June 25, 1950. This year, however, there was ample time to consider further mining of this traditionally rich tax vein. The excises which have been the big producers over the years—those on liquor, cigarettes, and gasoline—will yield the bulk of the 1.2 billion dollars in added receipts expected from this source. Higher taxes on cars, automotive products, and other consumer durables, likewise a popular tax base of long standing, should prove a double-edged weapon: they will maintain, perhaps increase, tax revenue from this source even in the face of defense-required cuts in output, and will help offset the pressure of high demand on the reduced supply of these products.

### Who pays the taxes

Despite all the controversy regarding who should be hit and how, the new tax law makes little change in the distribution of the tax burden. The tax committees of Congress were presented with a variety of plans for increasing personal income taxes. The administration's proposal was for a four-percentage-point increase in each bracket rate. Since the existing rates are much higher for top-bracket incomes, this would have had the effect of raising tax liabilities much more percentagewise for low income taxpayers than for persons with high incomes. A proposal by the Committee for Economic Development for a flat-rate defense tax on incomes after present taxes would have had an even greater effect in this direction. The provision finally adopted largely maintains the existing degree of progression—all taxpayers will face about the same percentage increase, except for a few in the very high brackets, who even before the new law were liable for taxes in excess of half of their incomes.

A tax administration proposal which would have had important effects on the equity of the tax system was the suggested withholding of

*Revenue increases due to the new law will come from most major tax sources, including excises*



taxes, at a 20 per cent rate, on dividends, interest, and royalties. Although passed by the House this was not included in the final bill. Because of the existence of withholding on wages and salaries, taxpayers whose income consists primarily of wages and salaries generally pay the full tax due on their incomes. Treasury studies indicate that enforcement problems are most severe with regard to other taxpayers—those receiving income from investments and those whose earnings consist largely of the net incomes of unincorporated businesses, farms, and professions. The lack of aids to enforcement comparable to withholding on wages and salaries tends to divide taxpayers into a group in which compliance is nearly complete and one in which the extent of compliance is much more uncertain. Continued efforts to improve enforcement for this group probably will attract considerable attention in the next few years, considering the high level of tax rates.

Recently, Congress has been quite concerned with another equity problem—situations where the methods and degrees of taxing competing businesses differ because of the different mode of ownership of the enterprise. Last year, Congress provided for the taxation of income of businesses owned by tax-exempt charitable and educational institutions which were clearly un-

related to the functions of the tax-exempt organizations. Rental incomes from the use of "lease-back" contracts by these organizations were also subjected to taxation. This year the major issues in this area concerned publicly owned electric utilities, mutual savings institutions, and cooperatives. The new law repeals the 3 1/3 per cent tax on domestic and commercial sales of electric energy, which did not apply to publicly owned power plants or REA cooperatives. Congress apparently felt that correcting the consequent inequitable treatment of consumers relying on privately owned facilities was worth the loss in revenue.

For the first time, the *retained* income of mutual savings banks, savings and loan associations, and other mutual savings institutions is subjected to the regular corporate tax. However, nearly all savings and loan associations and many savings banks should escape paying this tax through the operation of a clause permitting bad debt deductions of at least 15 per cent of net earnings as long as the bad debt reserves are less than 12 per cent of total deposits. Relatively few mutual savings institutions, especially among the larger ones, have reserves as large as 12 per cent. Farm marketing and purchasing cooperatives are subject to

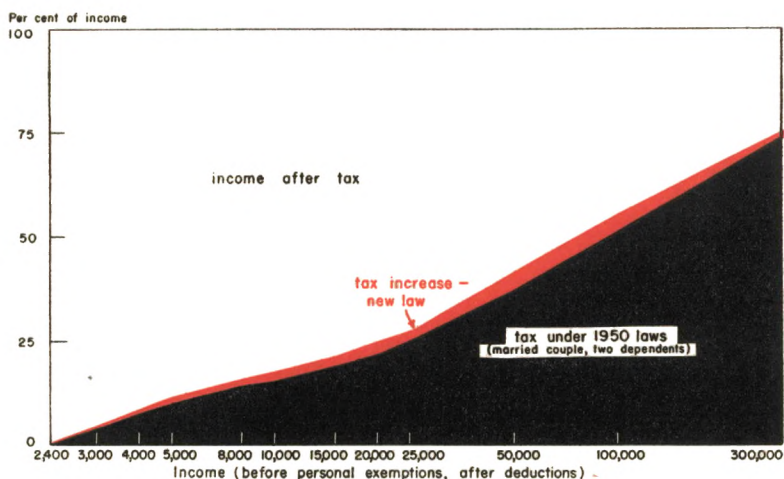
income tax for the first time also, but only on their *unallocated* reserves, which are not very important quantitatively—in fact, the estimated yield is only 10 million dollars annually.

Probably the most novel feature in the new tax law is the taxation of commercialized gambling, which is roughly estimated to produce 400 million dollars in revenue. There are two new taxes—a 10 per cent excise on wagers placed with bookmakers and commercial lottery operators and a \$50 per year occupational tax on all persons receiving or accepting wagers. This provision was strongly opposed, largely on the ground that subjecting such activities to tax in effect sanctions illegal gambling. The Congressional committees rejected this implication, and pointed to the parallel of collecting income tax from illegal as well as legal sources.

The new law contains more technical revisions of the Internal Revenue Code than any tax law in recent years. Despite the technical amendments and the novel features, many problems inherent in a complicated tax structure and a complex economy remain unsolved. Moreover, rising defense expenditures virtually guarantee that the Revenue Act of 1951 will not be the last heard of tax increases.

## Personal income taxes raised again

The relative increase in income taxes is about the same for most income groups, although the biggest increase, as a per cent of income, is for incomes between \$20,000 and \$100,000. Taxes are less than 10 per cent of the income of most married persons earning less than \$4,500.





# More capacity—defense by-product

*Industry is adding more plant and equipment this year than ever before. Total outlays would be even larger, but for bottlenecks and Government restrictions.*

AS MOST BUSINESS INDICATORS tended to stabilize during the past six months, outlays on new plant and equipment continued to surge to new highs. Total private spending on new facilities is expected to be about 25 billion dollars in 1951, 28 per cent more than in 1948, the previous record year. Expansion costs have risen in the past three years, but even in physical volume the gain over 1948 is estimated at one-sixth.

This rate of capital expenditure stems from the general high level of business activity plus special incentives such as accelerated depreciation, direct Government loans and loan guarantees. These Governmental measures are helping to encourage the building of an expanded industrial plant which, it is hoped, will permit sufficient output of arms to deter Red aggression at the same time that the civilian standard of living is maintained at record or near-record levels.

National policy dictates that this expansion job should be undertaken by private industry rather than the Government. Acute shortages of machine tools, structural steel, and electric power which have postponed or delayed many desirable projects are an indication of the success of this program. These bottlenecks coupled with the long-range nature of the plans of basic industries suggests that capital expenditures will remain high for many months. It is probable that outlays in 1952 will, at least, come close to the total for this year.

## **Basic manufacturing leads**

The years 1946-50 saw a total of over 84 billion dollars worth of new plant and equipment put in place. In a sense, the tremendous

total for 1951 is merely the high point in a six-year, continuous capital spending boom. However, certain developments in the current picture reflect the impact of the defense program.

A larger proportion of all capital outlays are going for new construction than was true in previous years. Second, more of the spending is being done by large firms in the basic industries. Finally, the share of total spending, earmarked for manufacturing facilities is larger and the commercial and miscellaneous category smaller than was the case in any previous postwar year. Outlays of commercial establishments probably will be less than they were in 1948, as a result of NPA restrictions on this type of activity.

## **Expansion in the Midwest**

In most years the five District states, Illinois, Indiana, Iowa, Michigan, and Wisconsin, account for about 24 per cent of the nation's total manufacturing. This is about the proportion of war contracts which are being filled in these states. Michigan, Indiana, and Illinois are among the top seven states on the basis of military contracts awarded. Much of this work is being done in existing plants. Nevertheless, District industry is expanding rapidly.

Of the 9.5 billion dollars worth of projects of all types approved for accelerated depreciation, the District states account for about 17 per cent of the total which can be allotted to particular areas. Many plants which will produce steel, aluminum, and chemicals are being located with an eye to the advantages of ocean transportation and the availability of raw materials or power. Specifically, steel capacity in the Chicago area is rising less rapidly than



that of the country as a whole. Some important new facilities are being located near salt water ports to gain access to new sources of ore in Labrador and Venezuela.

Nevertheless, 1.2 billion dollars worth of certificates have been awarded for facilities in District states. As in the case of war contracts Michigan, Illinois, and Indiana account for most of this total. Among the larger facilities for which rapid write-off permits have been granted in this area are public utilities, steel, aircraft engines and parts, and chemicals.

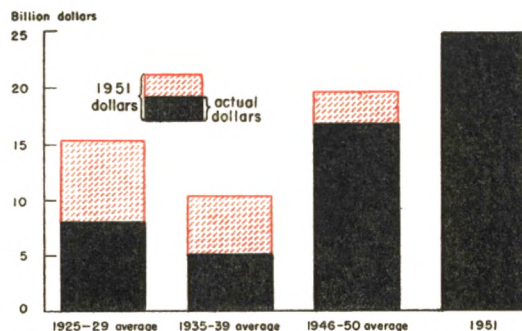
The total picture for manufacturing expansion may be brighter for the District states than is indicated by awards of certificates of necessity. For the first eight months of 1951, according to F. W. Dodge, contract awards for new factory buildings in the District jumped 130 per cent over 1950. This compares with a 95 per cent increase (excluding atomic energy awards) for all the 37 states tabulated by this agency. In the case of public utility contracts, the increase for the District also exceeds that for other states. The District's share of commercial building contract awards, on the other hand, declined more from last year than was true for the other states.

### Dispersal and defense

In battle areas vehicles and riflemen are required to "keep an interval" so as to offer a less concentrated target for enemy fire. During the past year there has been a growing demand that this principle be employed in locating new factories. For the first time in history our great industrial complexes are vulnerable to aerial attacks in the case of full-scale war. There is "no known defense against the atomic bomb except space."

The Government possesses powerful means of inducing dispersal of defense-related industry in the various monetary and material aids which are being offered to encourage desirable private expansion. According to a Congressional Committee which studied the problem, however, too many of the certificates of neces-

## Capital spending—larger than ever!



sity which allow rapid amortization cover projects to be located in large metropolitan areas, close to other, similar facilities.

In recent months, Defense Mobilizer Wilson and President Truman have called for a greater effort on the part of management and mobilization agencies to reduce industrial concentration. This program has brought protests from spokesmen representing older industrial areas, who believe that their regions will be affected adversely. These fears have been quieted to some extent by statements that there is no intention to scatter new plants in remote districts—sites 10 to 20 miles from existing concentrations should leave a sufficient margin of safety. It is not desired that the dispersal program should necessitate manpower migration. On the contrary, attempts are being made to locate new facilities in localities where a labor surplus exists.

Fortunately, some degree of dispersal is being achieved without special incentives. Industry has its own dollars and cents reasons for placing new plants some distance from existing concentrations. The congestion of a large city creates transportation problems. Sites beyond the built-up areas cost less, usually carry a smaller tax bill, and permit the acquisition of additional land for parking areas or further expansion. The results of this movement away from the city are evident in the number of new

plants which may be seen along the highways and rail lines emanating from most of the larger metropolitan areas. Increasingly, the search for "lebensraum" has placed new facilities in smaller towns well away from the big cities.

The past two decades, and particularly the postwar years, have witnessed a continuing relative shift from the older industrial areas to less developed regions. Facilities have been located with closer regard to easy access to raw materials or markets, adequacy of labor supply, and cheap power. This trend has worked in favor of the South, Southwest and Far West.

### The machine tool bottleneck

Not since early 1942 have machine tools figured so prominently in the news. The shortage of these "machines that make machines" is even more troublesome today than it was nine years ago. Currently, order backlogs would take 22 months to fill at present rates of production in contrast to 13 months at the World War II peak.

The situation has been alleviated to some extent by the Government's offer to defense contractors of free use of tools from the World War II stockpile. Unfortunately, the machine tools most in demand for use in the production of jet aircraft are new types.

A number of steps have been taken to speed up deliveries of machine tools. These include adjustments of price ceilings, special priorities on materials, help with manpower problems, and orders for the Government's pool from which special defense needs are being supplied. Large manufacturing firms which have their own facilities for producing machine tools are participating in the program.

Despite the risk of boom and bust characteristic of the machine tool industry many producers currently are expanding their facilities. Several important firms located in Rockford, Milwaukee, Detroit, and Chicago have announced their intention to increase capacity. To aid these undertakings, V-loan guarantees, ordinarily intended only for working capital

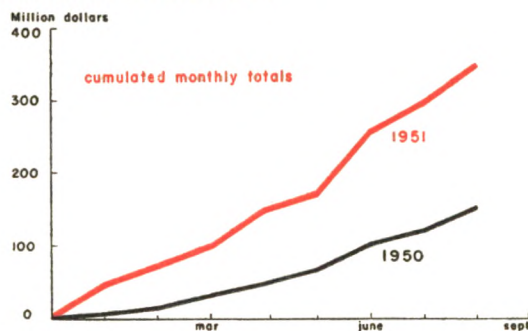
purposes, have been extended to cover capital loans to machine tool builders.

### Trouble for the future?

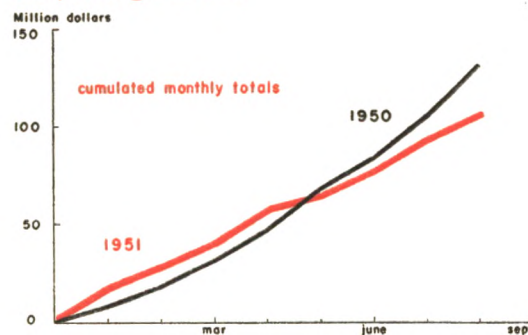
The multitude of new industrial plants springing up throughout the nation give a promise of a stronger, wealthier America. Judging by past experience, however, there is good reason for apprehension concerning the effects upon the economy of "anticipatory buying" of capital goods. Great fluctuations in capital outlays have always accompanied the swings of the business cycle. Perhaps, however, the drop in these expenditures in future years may be less than some observers anticipate. There is still

—continued on page 15

### Manufacturing construction contracts are far ahead of last year in the Seventh District . . .



### . . . while commercial awards are falling behind





# THE Trend OF BUSINESS

OUTLAYS FOR DEFENSE PROCUREMENT are expected to reach a plateau by next summer—well above the present rate. Between now and then, therefore, the nation will undergo the greatest strains of the projected rearmament program. Despite persistent evidence that a renewed general price uptrend may be in the offing, there is some possibility that the next nine months can be weathered without a severe inflationary upsurge.

Optimists currently point to the remarkably stable price situation which has prevailed since early last March. The longer this trend continues the better are the chances for longer-run stability. Most wholesale and retail prices of finished goods have remained relatively dormant during this period despite a mounting Federal deficit in recent months. In the first quarter of 1952, heavy tax payments assure that Treasury receipts will exceed disbursements, thereby reducing spending power of business firms and individuals, at least temporarily. Meanwhile, business inventories are high, and consumers, well stocked with durables, are displaying an unexpected disposition to save a large proportion of their current income.

Opposed to this rosy view of the future which is based mainly on the present and recent past are the hard facts of the growing inflationary potential. Mounting Government spending and the accompanying stiffer cutbacks in non-defense production combined with record individual income and enormous liquid asset holdings provide the groundwork from which another explosive price rise could develop. In previous periods of heavy buying producers were able to meet increased demand with ex-

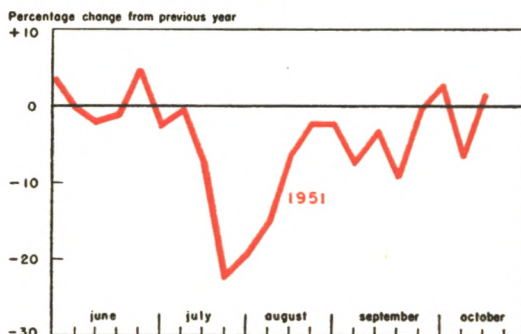
panded output of consumer goods. The growing transfer of resources to defense-connected industries, however, will prevent a similar response in the months ahead.

**Wholesale prices** of nonfarm commodities rose slightly, early in October, reversing a half-year trend. Spot raw material prices are still well below their post-Korean peaks, but there have been some increases recently, wool being the principal example.

The outlook for consumer prices in the immediate future is one of relative stability. Little change is expected for food, but rents are continuing a steady, gradual rise. A number of processors have received approval for price increases which will be relayed to the consumer when such action is warranted by market conditions.

**Sales** at District department stores are recovering from their low summer levels. This increase, however, has been somewhat less than might have been expected seasonally. Sales of

## District department store sales near year-ago levels





apparel have been relatively strong, but appliances continue to move slowly. In the case of television, volume has been only half that of last year.

Total department store sales have been running about equal to year-ago figures. Higher prices indicate that physical volume may be somewhat lower. The trend of sales in major District cities has not differed greatly from the District as a whole with the exception of Detroit. There, retailers have been faring somewhat worse than those in other large cities, reflecting a significant amount of conversion unemployment.

**Total business inventories**, seasonally adjusted, declined in August for the first time since the outbreak of the Korean war. This development was entirely the result of attempts of trade firms to bring stocks into line with current sales. In fact, manufacturers' inventories continued to rise throughout the summer. There is some belief that over-all inventory liquidation will continue. In the Chicago area, however, purchasing agents are reporting that they are ordering further ahead in an attempt to prepare for a pickup in business activity.

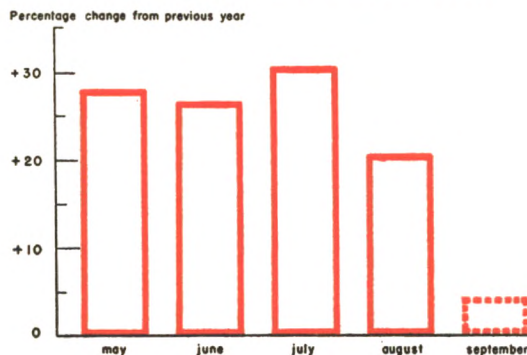
**Industrial production** rose between July and September to the approximate level which prevailed in the first half of the year. During this period output of producers' durable equip-

ment and munitions increased while consumer goods, generally, showed little change. Total factory production probably will rise further in the coming months. Deliveries of military hard goods are slated to step up rapidly, while consumers' durables are expected to hold close to present levels. Current output of most types of appliances is about in line with the new NPA restriction orders. Automobile production is slated to decline from a 4,400,000 annual rate now, to a 3,800,000 rate early in 1952.

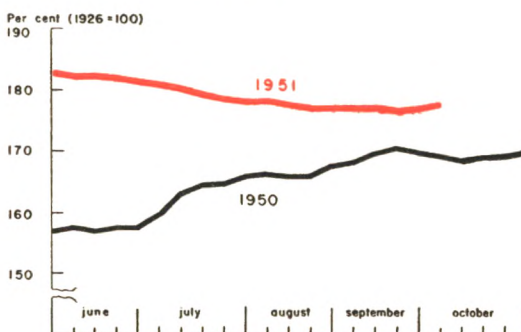
**Manpower** in most District centers is proving to be a limiting factor in attempts to increase essential production. Continuing claims for unemployment compensation have been dropping in Wisconsin and Iowa, and are at a low level in Illinois and Indiana. In Chicago, office help, engineers, and skilled metal workers are in seriously short supply.

The Detroit area, which has been hit hardest by the curtailments in the production of consumer durables, is the major exception. Unemployment rose to 88,000 in September, an amount more than 50,000 greater than a year ago. Attempts are being made to speed up defense work there and in other Michigan cities in order to make use of the available manpower. Continuing unemployment claims in the state as a whole dropped steadily in the month of September.

### **District department store inventories working down to 1950 levels**



### **Wholesale prices stop declining and turn up slightly**



# The check routing symbol

*Odd little fraction pilots billions of checks across the nation.*

TAKE A LOOK at the upper right-hand corner of one of your blank checks. In all probability you will see there a fraction like the one circled below. Those figures, meaningless to the layman, help oil the wheels of the world's biggest and most efficient check collection machine.

An estimated five billion times a year, depositors make out checks on their deposit accounts. Some of these are redeposited by the recipients in the same bank upon which the checks were drawn. A great many others are accepted for deposit by other banks in the same community, and can be presented for payment by the original bank via the local clearing house. Between one-third and one-half of the total volume of checks written, however, moves out of the city, out of the state, and even across the nation. From these far-flung points, each check must be brought back to the bank upon which it was drawn for final payment.

Facilitating such long-distance transmissions of checks is one of the most important services performed by the Federal Reserve System. Over one-fourth of the total personnel of the twelve Federal Reserve Banks is engaged in this function. In performing such an immense job accurately and speedily, a key tool is the numerical check routing symbol, developed by the American Bankers Association and the Federal Reserve System late in World War II.

The purpose of this Symbol is to tell check sorters, at a glance, the identity, location, and proper check collection route to the bank on which the check is drawn. In the numerator of the fraction, the number preceding the hyphen indicates the location of the bank. Numbers 1 through 49 are assigned to major cities; numbers 50-99 apply to states and U.S. territories. Chicago, for example, is 2, Mich-

igan outside Detroit is 74. The number following the hyphen identifies the specific bank in the locality.

The denominator of the fraction indicates the Federal Reserve Bank or branch through which checks payable by the individual bank should be sent. The first part of the number denotes the Federal Reserve District within which the bank is located (numbered from 1 to 12). The following figure indicates whether checks should be mailed to the Federal Reserve head office (number 1) or a branch in that District. A denominator, 71x, for example, indicates the Federal Reserve Bank of Chicago; 72x would mean its Detroit branch. For banks in eastern Michigan outside Detroit, checks can be mailed to either the head office or the Detroit branch of the Federal Reserve Bank of Chicago, and this fact is signified by using a 6 for the second digit.

The final figure in the denominator is a dual-purpose one. A zero means that credit will be given to the collecting bank's reserve account as soon as the check is received by the appropriate Federal Reserve office. Any other final number signifies that reserve credit will be deferred because the paying bank is far enough away from the Federal Reserve office so that one or more days will elapse before the check can be physically presented to that bank for payment. In addition, if a "deferred availability" number (a final number other than zero) appears, it also indicates the District state within which the paying bank is located. In the Seventh District, a final number of 1 signifies Illinois; 2, Indiana; 3, Iowa; 4, Michigan; and 5, Wisconsin.

These same principles are applied as consistently as possible to checks of all par clearing banks and to certain special-purpose checks



as well. Thus, checks of the Treasurer of the United States or of Federal Reserve Banks carry a symbol denominator of 000—meaning that they are payable in any Federal Reserve District, at any Federal Reserve office, with immediate reserve credit given.

Just how useful this "numerical shorthand" can be is best illustrated by reviewing the travels of a typical check. Suppose that a man in Kankakee writes out a check for 100 dollars on his local bank. Provided that bank pays checks drawn upon itself at full face value, the check will bear the routing symbol 70-xxx over 711.

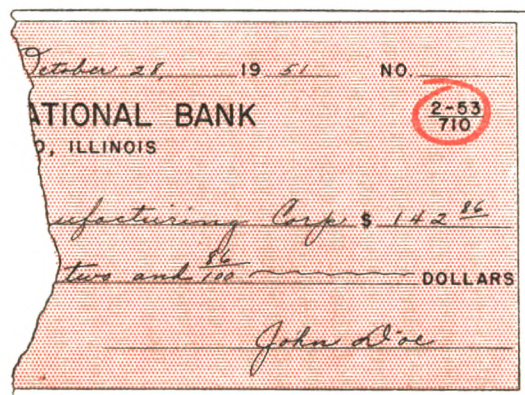
If the depositor mails the check to a San Francisco firm in payment of a bill, that firm will deposit the check in its own bank, receiving deposit credit contingent upon final collection of the check proceeds. As the San Francisco bank sorts through the day's receipts of checks, the routing symbol on the Kankakee check will show that it is an out-of-city item which can be appropriately collected through the Federal Reserve System. The commercial bank can thus send the check to the Federal Reserve Bank of San Francisco the next morning, where it will receive deferred credit in its own deposit account.

A second reference to the routing symbol, by the Federal Reserve Bank employees, will reveal that the check should be collected

through the Federal Reserve Bank of Chicago. In a matter of hours, the check is on its way by air. In the Chicago Reserve Bank other check sorters again note the routing symbol, and accordingly arrange to send the check to the Kankakee bank for final payment. Upon receipt of the check in Kankakee, the local bank will make payment either by authorizing the Chicago Federal Reserve Bank to debit its deposit account, or by draft instructing one of its Chicago correspondent banks to transfer 100 dollars to the Reserve Bank on its behalf. Within a few days after the check is received in San Francisco, the transfer of funds from depositor to depositor and bank to bank will have been completed. And three times the check routing symbol will have saved sorters from a time consuming search through the location and check routing lists covering the nation's 19,000 banks and branches.

It is impossible to set a dollar-and-cents value upon the countless hours and errors thus saved in the sorting, mailing, and crediting of checks. In the Federal Reserve Bank of Chicago, where 900 people are engaged in handling over a million checks daily, the costs savings are naturally very large. Advantages accrue to even the smallest bank and to all depositors as well, for checks received and checks drawn upon their accounts are thereby cleared with a minimum of delay. Mis-sorts and miscalculations of reserve credit are greatly reduced. That these advantages are important is attested by the fact that 49 per cent of the banks in this country adopted check routing symbols when they were first introduced in 1945. Today 82 per cent of the nation's checks are thus identified, and in the five Seventh District states 74 per cent of the checks drawn carry these symbols.

It is hoped that this trend toward more widespread use will continue, for the sooner all banks, individuals, and corporations arrange to place such numbers on their checks, the sooner will the ultimate advantages of faster presentation at lower cost be realized.





# Contrasts in home financing

*Chicago and Detroit show wide differences in mortgage practices.*

AN AVERAGE FAMILY wanting to buy a new home in and around Chicago had better have from \$2,000-\$4,000 more cash for down payment than would be needed in the Detroit area. In addition, if future experience follows the recent past, their mortgage will be from \$500 to \$1,000 larger, and the monthly payments will average \$10-\$15 more. These facts, revealed in a recent study by the United States Bureau of Labor Statistics<sup>1</sup> highlight the extreme differences in home building and home financing in the two major centers of the Seventh Federal Reserve District. Probably no other metropolitan areas in the nation provide greater contrasts in this important segment of economic activity.

Here are further Chicago-Detroit comparisons brought to light by the survey:

Mortgages in Chicago were for a shorter term of years.

Average interest rates in Chicago were  $\frac{1}{4}$  to  $\frac{1}{2}$  per cent higher.

FHA and VA guarantees were used less in Chicago.

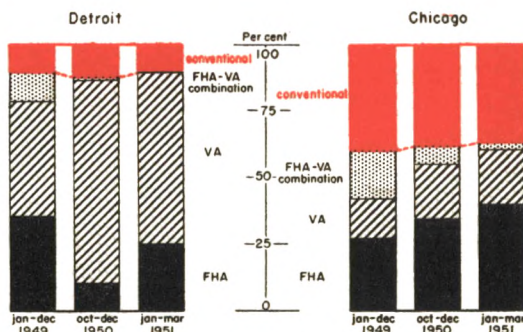
Average prices of new houses in Chicago were \$3,000 to \$4,000 higher.

## Single homes dominate building

During the periods covered by the BLS study—fall 1949 and the winter of 1950-51—a total of 28,600 new dwelling units were built in Detroit and 18,500 in Chicago. In both cities the majority were one-family houses, erected for sale by speculative builders. In

<sup>1</sup>The BLS study includes dwelling units completed during the last half of 1949, the fourth quarter of 1950, and the first quarter of 1951, which were purchased or rented within two or three months after the end of each survey period.

## Government guarantees used more in Detroit



Chicago, however, a larger proportion were contract built to the specifications of the owner—21 per cent compared with 9 per cent in Detroit. Construction of rental housing was not of major importance in either area, but the proportion of rental units in Chicago exceeded that in Detroit—12 per cent as compared with 5 per cent.

Although speculative builders dominated home building in both centers, the fact that a larger fraction of the new Chicago homes were built on contract to the owners' specifications illustrates a basic difference in the two housing markets. In Detroit, builders were concentrating more heavily on meeting the housing demand of buyers who had little cash and could make only relatively small monthly payments. To do so, they had to trim costs and make maximum use of the liberal financing terms available under VA guarantees.

Total population in the Detroit metropolitan area is only slightly more than half that of the Chicago area. Yet Detroit has built 130,000 houses since 1946 as against Chicago's total



of 132,000. This means that Detroit has built almost double the number of homes in relation to its population. In large part, however, this difference reflects the greater growth in Detroit during the past decade; total population increased 670,000 as compared with 570,000 in Chicago.

### Where the money comes from

Very few new homes in either Chicago or Detroit required no mortgage at all. As a matter of fact, only 6 per cent of the houses in each metropolitan area were cash deals. On mortgaged houses, however, average down payments were considerably higher in the Chicago area—over \$4,000 compared with \$1,250 in Detroit. The broad average tends to hide other variations since the proportion of homes carrying no down payment at all was very small in Chicago but accounted for about 30 per cent of those built in Detroit.

Down payment money came from past savings in nearly all cases, but the fact that so many Detroit homes were bought without down payment meant that there was considerable difference in average amounts of savings used in the two areas. Nearly 90 per cent of Chicagoans, as compared with 60 per cent of Detroiters, used accumulated savings in the purchase of their homes. Other sources of down payment money include borrowings and gifts from relatives, and sale of nonliquid assets such as real estate.

### Sources of mortgage funds, per cent of total

		Banks	Savings and loan	Mortgage companies	Other investors
Chicago	1949	34	22	31	13
	1950	31	35	15	19
Detroit	1949	18	4	65	13
	1950	7	7	78	8

As for sources of mortgage money, the study shows that wide differences existed. Banks and savings and loan associations accounted for a higher proportion in Chicago, while mortgage companies were by far the most important source in Detroit. In neither city did individuals account for much of the total mortgage lending on new homes.

During the fall of 1949 the Federal National Mortgage Association (Fanny May) was making extensive precommitments to purchase mortgages. Mortgage companies were making use of this outlet because of the then existing shortage of private mortgage funds. More than 70 per cent of all new houses mortgaged in Detroit during the periods of study were financed through mortgage companies, many of which used Fanny May. Less than one-fourth of the new homes in the Chicago area were financed through mortgage companies, and this no doubt accounts for the smaller volume of Fanny May purchases there.

The greater use of Fanny May in Detroit as a source of funds is in some respects a reflection of the markedly higher proportion of guaranteed loans. Both FHA and VA were decidedly more active there than in the Chicago market. Together the two kinds of guarantees covered nearly 90 per cent of new house mortgages in Detroit as compared to approximately 60 per cent in Chicago.

Broadly speaking, it may be said that Detroit

### Prices and down payments differ

	Chicago		Detroit	
	Price	Down payment	Price	Down payment
1949	\$12,900	\$4,000	\$ 9,500	\$1,600
1950	14,400	4,800	10,600	1,600
1951	14,600	4,850*	11,100	1,650*

\*Estimated

## House purchases by income groups, 1949

	Chicago			Detroit		
	Purchases Number	Per cent	Average purchase price	Purchases Number	Per cent	Average purchase price
Under \$3,000	214	4	\$11,600	1,305	13	\$8,000
3,000—4,000	1,661	31	11,000	4,751	45	8,800
4,000—5,000	1,759	33	11,900	2,473	24	9,700
5,000—6,000	720	13	12,400	1,305	12	11,000
6,000—7,500	491	9	16,200	305	3	10,400
\$7,500 & over	457	9	22,000	278	3	20,000
Total	5,382	100	\$12,900	10,528	100	\$9,500

lenders—through greater use of FHA and VA guarantees and larger sales to Fanny May—passed on most of the mortgage risk to the Government. In many cases, of course, Chicago lenders did the same. However, in a greater proportion of cases risk in the Illinois city was assumed by the lender—through conventional loans. And even in cases where Government guarantees were used, they were a smaller part of total cost since buyers made larger proportionate down payments.

### House buyers' income

The over-all spread and level of family incomes are almost identical in Chicago and Detroit, according to the U.S. Bureau of the Census. Yet the distribution of incomes of house buyers in the two cities is significantly different. Families earning less than \$4,000 per year purchased nearly three-fifths of the single-family houses completed in Detroit during the last half of 1949, as compared with 35 per cent of those completed in Chicago. Conversely, families earning \$6,000 or more accounted for only 6 per cent of the house purchases in Detroit as against 18 per cent in Chicago. Moreover, the average prices paid by each income class were substantially greater in Chicago. Builders in the two cities clearly were serving different markets.

By the winter of 1950-51, house costs had risen significantly. Despite this increase, however, about a third of Detroit's new houses were sold to buyers earning less than \$4,000, whereas in Chicago the proportion had declined to 3 per cent. The higher income groups accounted for a larger proportion of purchases in both cities than had been the case in 1949, with more than one-third of Chicago's and one-eighth of Detroit's new houses going to buyers with incomes of \$6,000 or more.

The over-all contrast in financing then is clear. Chicago home buyers paid higher prices; used larger amounts of savings for down payment; carried slightly smaller mortgages in relation to the value of their house; and depended more heavily upon the conventional financing through savings and loan associations and banks. Detroit buyers leaned more heavily upon Government guarantees financed mostly through mortgage companies; put very little of their own money into the house; and carried larger mortgages in relation to the total purchase price. The two cities provide a good example of conservative versus liberal home financing.

Is the Chicago or the Detroit approach the more to be desired? Financial conservatives will contend that Chicago financing has been safer, and more "sound." The less conservative



reaction is that the Detroit building industry has succeeded in achieving lower costs and by liberal financing has been more successful in meeting the demand for new homes.

### **Relaxation of Regulation X**

Housing starts in both cities for 1951 to date are about 30 per cent below the record levels of last year. This decline is about 5 per cent greater than the national drop, but most of the difference is accounted for by public housing in other areas.

It might be expected that starts in Detroit would have declined more than those in Chicago. However, a large fraction of the housing starts during 1951 resulted from commitments which were made in 1950. Recent months have seen a greater decline in Detroit starts and that city probably will record a greater drop for 1951 as a whole than will Chicago.

The recently passed Defense Housing Act has brought about a liberalization of Regulation X and the companion rules covering VA and FHA operations. It is now possible for a veteran to buy a new house priced at \$12,000 with a down payment of \$960, or 8 per cent. He formerly had to pay \$1,900, or about 16 per cent. For nonveterans the down payment on a new \$12,000 house now is \$2,400 as compared with \$3,100 previously. On houses priced below \$12,000 the terms are still more liberal, but there is little change for those priced above \$15,000.

Thus, the easing of the credit restrictions applies primarily to the lower priced houses. Since the Chicago building industry generally has not been successful in producing homes to sell for \$12,000 or less, the more liberalized terms are not likely to be as meaningful to Chicago buyers.

The biggest problem currently facing builders and mortgage lenders in both cities is the dearth of mortgage funds (see *Business Conditions*, June 1951). This shortage of funds is expected to continue throughout the present year and may be eased only slowly through the

first half of 1952. By that time the increased flow of savings, repayments on existing mortgages, and the working off of commitments, should result in the return of a large volume of funds seeking mortgage investment. Until such time, however, the relaxed terms of Regulation X are not likely to make much difference in the level of building in either Chicago or Detroit.

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### **Capital spending** *continued from page 7*

a lot to be done.

Additions to plant and equipment may well be very high relative to previous periods for many years to come. Important types of non-essential outlays are being deferred at the present time. Extensive development over the long-term can be foreseen for new industries such as synthetic fibers, and plastics. New resources such as lignite and taconite are being tapped. Modernization and replacement of outmoded equipment would permit vast segments of industry to cut costs. Electric power use probably will continue to expand faster than industry as a whole.

Finally, the population is rising at a rapid rate while the proportion of workers to total numbers is declining. More of our population will consist of children and pensioners. As a result a continued growth and improvement of our industrial plant is necessary if present living standards are to be maintained and bettered.

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# Currency rise

*People are demanding more coin and paper money—but not primarily for hoarding or illegal use.*

MONEY has been in the news of late. For one thing, the growing coin shortage has attracted much attention. Although neither basically serious nor permanent, it is certainly inconvenient. More disturbing to many has been the persisting rise in the *total* amount of cash held by the public. Memories of abnormal uses and demands for currency during World War II have raised questions as to whether the 1951 rise, too, is not abnormally large and in part related to a resurgence of hoarding, black markets, and income tax evasions.

Money in circulation has risen more than seasonally in every month since March. The total outstanding on October 18 was 28.4 billion dollars, over 1.1 billion higher than a year ago. This is a far cry from the wartime record, when money in use jumped from 11 billion to 28 billion within the space of four years. Nonetheless, the 1951 rise is in sharp contrast to the average 400 million yearly decline of most earlier postwar years.

Among denominations, the half-billion rise in \$20 bills leads the list, but this is a reflection of their large unit value. Percentagewise, the circulation of every denomination from \$20 down to \$1 has increased between four and six per cent since last fall. Coin circulation has risen very slightly more.

In contrast, denominations over \$100 dropped by an average eight per cent, continuing a trend apparent since the early postwar period. This casts little light on abnormal demands, however, since use of large bills has been discouraged by required bank reporting of transfers of the \$50 and higher issues. Some quarters allege that the \$20 bill is now the favorite medium in illegitimate operations.

Even so, the noted evenness of the rise in all commonly used sizes of currency and coin strongly suggests that hoarders, black marketers and the like are not yet absorbing currency in important volume.

Standards for determining what is an "abnormal" rise in total currency are necessarily vague. Within fairly broad limits, cash in use need bear no fixed relation to national measures of income and production. A more useful comparison is between the amount of active purchasing power which people choose to hold in cash and the amount they retain in the alternative money form of demand deposits. By this standard the currency rise has not been disproportionate, for the ratio of cash to demand deposits dropped in the year ended August 1951, as it has in every year since the war.

All things considered, there seems little reason for concern over the rise in currency thus far. Moreover, conventional demands for currency can grow still more, if demand deposits rise and if Federal military spending again channels funds into heavy cash-using organizations and communities.

## *Money in circulation has climbed steadily since March*

