

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

# Business Conditions

**1952 August**



## **Contents**

Report on the Federal Reserve	2
TV curbs lifted	4
Tapping the securities markets	10
Farm assets	15
A big harvest	16
<b>The Trend of Business</b>	<b>8-9</b>

# Report on the Federal Reserve

## *Patman Subcommittee scrutinizes System organization and policies. Spotlight on relationships with Treasury.*

A NEW SET OF FINDINGS concerning the framework of the nation's monetary management has been laid before the Congress and the public. The source: the final report of the Congressional Subcommittee on General Credit Control and Debt Management, chaired by Representative Wright Patman of Texas.

The Subcommittee's report, released early in July, was the fruit of more than a year's deliberations. Primarily under consideration were the Federal Reserve System and the U. S. Treasury—the respective policymakers in the monetary and debt management fields—but the findings and conclusions are of significance to the entire financial community.

Besides making numerous recommendations regarding monetary and debt management, the Subcommittee made two tangential suggestions—that nonmember banks should be required to maintain the same reserves as member banks and gain equal access to Federal Reserve Bank loans; and that domestic convertibility of money into gold not be restored.

### **Questions and answers**

The widespread importance of the study was recognized in the Subcommittee's first major step—mailing lengthy questionnaires to some 1,200 respondents in financial businesses, universities, and government. From these the Subcommittee reaped a harvest of 1,300 crowded pages of fact and considered opinion. Three weeks of hearings served further to define the areas of agreement and disagreement. Guided by this mass of material, the Subcommittee came up with its own appraisal, liberally sprinkled with minority qualifications and dissents.

The primary aim of monetary policy was considered to be influencing movements in

money and credit so as to contribute to high-level employment and stable prices. Against this background, the Subcommittee wrestled with three basic questions. How effective has monetary policy been in furthering these objectives? How effective can monetary policy become? What changes in organization and scope are necessary in order to gain the optimum in effectiveness?

The Subcommittee's answers are carefully phrased. For example, the post-Korean price rise “. . . might have been moderated somewhat by the earlier adoption of a more restrictive monetary policy. But the use of monetary measures sufficiently powerful to have averted most or all of the rise probably would have had consequences even more undesirable than the rise itself.”

On the other hand, in looking ahead the report states: “We believe that general monetary, credit, and fiscal policies should be the Government's primary and principal means of promoting the ends of price stability and high-level employment . . . [monetary policy] must be used with caution, however, in order to insure that measures taken to halt an inflation do not aggravate a subsequent period of depression, and vice versa.”

### **The issue of “independence”**

The thorniest issue facing the Subcommittee was one which has become popularized under the heading of the “independence” of the Federal Reserve System. The chief Federal Reserve weapons for restraining inflationary credit expansion tend to raise the cost and reduce the availability of *all* credit, including that extended to the Federal Government. This makes the Treasury's borrowing and reborrowing more

costly and more difficult and may have effects on holders of outstanding Government securities which are undesirable from the viewpoint of the Treasury. Thus during periods of inflation the aims of monetary policy and debt management can be in partial conflict.

In the search for methods to resolve such conflicts in the public interest, the Subcommittee heard a wide range of comments. Some vigorously defended the present arrangement; others proposed changes. One suggestion was the legislative divorcement of all overlapping monetary and debt management responsibilities; another, the establishment of a new top-level council with power to frame general financial policy and rule on all agency differences.

The final Subcommittee report remarked: "The independence of the Federal Reserve System is desirable, not as an end in itself, but as a means of contributing to the formulation of the best over-all economic policy. In our judgment, the present degree of independence of the System is about that best suited for this purpose under present conditions."

But the Subcommittee was impressed by the need for "increased understanding of each other's problems" among Government agencies. "We recommend that a consultative and advisory council . . . be established on an experimental basis by executive order. Such a council would have no directive powers over its members."<sup>1</sup>

The report recommended other changes in the machinery for administering monetary policy. To improve the effectiveness of the present policy-making body, the report suggested that the number of members of the Board of Governors be reduced from 7 to 5, their salaries increased, their terms reduced from 14 to 6 years, and that they be made eligible for re-appointment. To strengthen ties between the System and Congress, the Subcommittee rec-

<sup>1</sup>Membership of the council, as suggested by Mr. Snyder, would include the Secretary of the Treasury, the Chairman of the Board of Governors of the Federal Reserve System, the Director of the Budget, the Chairman of the Council of Economic Advisors to the President, and the Chairman of the Securities and Exchange Commission.

## Official Documents

The following materials pertaining to the completed study by the Subcommittee on General Credit Control and Debt Management can be obtained from the Superintendent of Documents, Government Printing Office, Washington 25, D. C.

"Monetary Policy and the Management of the Public Debt," Replies to Questions and Other Material for the Use of the Subcommittee on General Credit Control and Debt Management. 2 vols. 1302 p. Senate Doc. 123. \$4.25.

"Monetary Policy and the Management of the Public Debt," Hearings before the Subcommittee on General Credit Control and Debt Management of the Joint Committee on the Economic Report, March 10-31, 1952. 993 p. \$2.25.

"Monetary Policy and the Management of the Public Debt," Report of the Subcommittee on General Credit Control and Debt Management of the Joint Committee on the Economic Report. 80 p. Senate Doc. 163.

ommended that the accounts of the Board of Governors be audited by the General Accounting Office and that the annual budgets of both the Board and the Reserve Banks be presented to appropriate Congressional Committees for their information.

On other lesser issues, the Congressional body reached fairly specific conclusions. On the basic questions, however, the report bore the marks of compromise. This was necessarily so, for the subject matter was complex and the testimony often conflicting.

### Differences persist

Some important differences in emphasis could not be resolved. Illustrative of these was the minority statement of Senator Douglas of Illinois, himself the chairman of a similar Subcommittee less than three years ago. Among other things, he differed in his estimate of what monetary policy could have accomplished in the immediate post-Korean period: "I believe that prompt and determined action,

quite within the range of practical policy, would have materially altered people's expectations regarding the desirability of holding or spending money . . . and would thus have materially dampened down the inflationary oscillation that actually occurred."

Senator Douglas also demurred with regard to the sometimes-expressed wish for mutual advisement and sharing of responsibilities on the part of the Treasury and the Federal Reserve: "It seems clear to me that we will have a better end result, and that the Treasury and the System will be better neighbors in the long run, the less they invite themselves in to play in each other's backyards."

Viewing the report's recommendations as a group, Douglas described them as individually not of fundamental importance, but collectively "dangerous" in the absence of a policy mandate. To his mind, therefore, the "most urgent and paramount business" in the field of monetary policy is the preparation of a Congressional directive setting forth a clear differentiation between System and Treasury responsibilities and a general "norm of action" to guide Federal Reserve policy.

The differences in opinion noted above may not appear startling. Yet within the intricacies of credit and fiscal policy, variations in degree can span the difference between expected beneficial and detrimental results. Discussion is further complicated by the fact that incontestable historical evidence of the correctness of any *short-run* policy is hard to come by. Such proof must always draw in part upon the hazy world of "what might have been."

When viewing the long run, however, the Subcommittee was able to reach agreement. It expressed its conviction that changes in the money supply, and hence the monetary policies which can temper such changes, have an important influence upon prices in the long run. But the particular "mix" of short-run influences which must add up to this long-run effect was not, and probably never can be, unanimously defined.

## TV curbs lifted

*"Unfreezing" of TV channels promises to boost station numbers and set sales. Biggest if: can new transmitters bear the high costs?*

FOR ALMOST FOUR YEARS, the number of television transmitting towers dotting the nation's landscape has remained unchanged. The growth in station numbers soon will be resumed, however. On July 1, the Federal Communications Commission ended the Government's ban on channel allocations and started processing applications to construct new transmitters.

A tenfold expansion in telecasting facilities in the Midwest could occur with the channels allocated to this area. Whether such growth will take place depends upon economic factors. The primary question is the capacity of advertising and other revenue to support the large and growing cost of programs and facilities.

### Growing pains

When the so-called "freeze" was imposed, the industry was growing by leaps and bounds and important developments in electronic technology were underway. Color TV appeared to be just over the horizon but technology was still struggling with the problem of its transmission. In the face of all these changes, the Commission was dissatisfied with the plan it had been following in assigning channels. It decided, therefore, to call "time out" to reappraise the problem. Only a limited number of channels could be made available and mistakes in allocation would be difficult to correct.

A similar crisis arose in the early days of radio broadcasting. In 1922 available wave lengths had become so crowded that interference between stations was common. In an attempt to bring some order out of the chaos the Second National Radio Conference was called. As a result of its recommendations, additional

wave lengths were made available to the industry, stations were classified as to the quality of service rendered, and zones were established as the basis for frequency assignments in order to reduce interference.

The industry boomed and by 1927 radio was available to every home in the nation. But with this growth came a growing dissatisfaction with the disposition of scarce wave lengths and the practices that congestion produced. To remedy this situation Congress established the Federal Radio Commission, forerunner of the Federal Communications Commission. The new body was given broad authority to classify and license stations, assign operating frequencies, determine operating time and power, and make regulations to prevent interference. Primarily as a result of the exercise of this increased authority, the number of stations dropped from 681 in 1927 to 606 in 1929. This experience with radio has enabled the Federal Communications Commission to avoid, in the developmental period of TV, some of the problems that beset radio.

### TV a postwar industry

Between the end of 1946 and the spring of 1951, the television industry grew tremendously closely paralleling that of the radio industry in its heyday. Two hundred thousand sets were produced during 1947. In 1950, only three years later, 7 million came off the assembly lines. Broadcasting activity boomed along with the sale of sets. Total advertising revenues of 8.7 million dollars in 1948 had increased over tenfold by 1950. Nevertheless, climbing costs kept most stations in the red until 1951.

Employment provided by the television industry can only be roughly estimated. In the Chicago area, which accounts for about one-half of the nation's TV set production, the radio-television industry employs more individuals than do the mail order or meat packing industries. Due chiefly to increased TV production, employment in the radio-television industry rose rapidly during the latter part of 1949

and by November 1950 had reached a peak of 53,000 workers. During 1951, primarily due to the decline in demand for TV sets, employment fell to 44,000 in May. Currently, somewhat fewer than this number are working in the industry in the Chicago area.

Television currently dominates the home appliance industry. In 1946, when only about two million dollars worth of TV sets were sold, TV sales contributed a smaller dollar sales volume than did any other home appliance. By 1949, however, when sales approached one billion dollars, only refrigerator sales exceeded those of television. During 1950, sales of TV sets reached their peak—almost two and a quarter billion dollars. Last year, although the dollar volume of sales fell by one-third, TV was still by far the best selling appliance. Manufacturers' sales of the major household electrical goods during 1951, valued at retail, were as follows:

	(millions)
Television .....	\$1,500
Refrigerators .....	1,120
Washing machines .....	727
Lamp bulbs and tubes .....	501
Home freezers .....	378
Ranges .....	343
Vacuum cleaners .....	231
Home radios .....	229

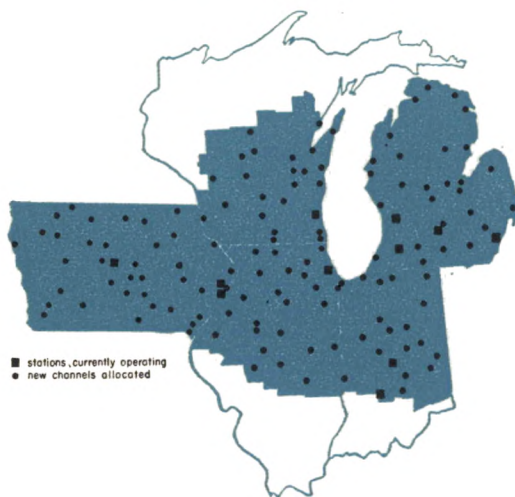
SOURCE: *Electrical Merchandising*.

### New market for TV sets

The 1948 "freeze" order automatically imposed a temporary limit upon the potential number of viewers. In succeeding years, swelling set production and sales cut sharply into that restricted market. As a result, since 1951 the term "saturation" has appeared with increasing frequency in explanation of the decline in demand for TV sets.

There is little question but that the order has affected the character of the industry's growth. For example, it has been estimated that in District cities which have TV broad-

*Most of the District's residents will be in range of TV if full use is made of channels allocated*



casting facilities, from 32 per cent to 74 per cent of the families have sets. Most of the telecasting facilities of the large cities are reaching considerably more than one-half the potential set owners. In Milwaukee, almost three-quarters of the maximum number of families have sets.

For the U. S. as a whole, however, only about one out of three homes is equipped with television. It is obvious that a large first purchase market exists in communities not now served by nearby stations. And each passing year will add to the replacement market in both old and new TV areas. Set makers can look forward to replacing many small tube sets and beyond that to color and other technological changes which will stimulate repeat purchases.

### **Telecasting to the nation**

The "unfreeze" order offers potential TV facilities for almost all sections of the nation which do not now have them. In addition to the 108 TV transmitters currently operating in the United States, the Commission will permit

the construction of 2,053 more. They will be located in about 1,300 communities, two-thirds of which will be one-station towns.

On the other hand, cities such as Chicago, San Francisco, Oakland, and Los Angeles are allowed up to 10 stations apiece. Thirty stations now in operation will have to change their channels, although none will be forced to move to the new ultra-high-frequency band from the very-high-frequency band where they currently operate. Of the 2,053 new assignments, 12 per cent have been set aside for non-commercial, educational purposes.

In the Seventh District the Commission has provided that in 135 localities approximately 200 new transmitters may be erected. This is an impressive addition to the 16 stations now operating in 11 communities.

The new channel allocations are the product of over three years of work by the Commission. The allocation of channels to specific cities was in accord with the following two objectives: first, to provide at least one channel service to all parts of the U. S.; second, to provide as many cities as possible with at least one TV broadcasting station.

### **The educational channels**

One of the most controversial parts of the allocation order is the provision for 243 educational channels. The Commission recognized the claims advanced for universities to their own TV outlets in lieu of purchased or donated time from commercial stations.

Response to the reservation in Chicago of Channel 11 for educational purposes indicates the interest in this aspect of telecasting. Very shortly after this reservation was tentatively made in 1951, the Illinois Institute of Technology filed a statement with the Commission supporting the reservation. At about the same time, a "Working Committee for Developing the Use of Channel 11 for Education in Chicago" was formed. It includes the major colleges and universities in the city plus the Chicago Public Schools, the Art Institute of

Chicago, the Chicago Historical Society, and the Museum of Science and Industry.

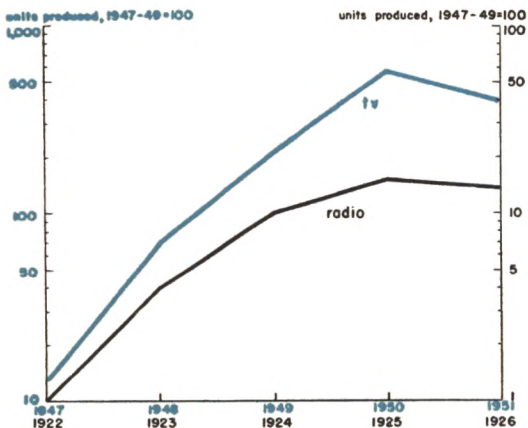
These groups are exploring the possibility of financing, programming, and operating an educational TV station on a cooperative basis. The Committee believes that such a station would reach at least 60 per cent of the population of Illinois.

### Stations come high

When will these new channels go on the air? Some delay will occur in the processing and hearing of applications before the FCC. Additional time will be consumed in station construction. But the ultimate factor influencing both timing and extent of development is an economic one. Full telecasting facilities are very expensive.

Many of the smaller towns which now have radio stations and which have been allocated a TV channel may not be able to support a television station for some time to come, even though they are currently supporting radio broadcasting facilities. Likewise, there is considerable question whether all of the larger cities will be able in the near future to support the maximum number of outlets allotted them.

### *Early growth of television production parallels that of radio*



Estimates of the cost of building telecasting facilities vary considerably, depending upon the type of station contemplated. There appears to be agreement, however, that it would be extremely difficult at present to construct facilities of minimum standards for less than \$150,000 and such equipment would not permit the use of live shows or films. Its programs would have to come from the networks. The success of such a setup is problematical.

It is generally felt that the minimum facilities required for profitable operation must provide for film as well as network presentations. Cost of constructing such a station is estimated to be at least a quarter of a million dollars. Facilities which provide for live shows, originating both inside and outside the studios, and the use of filmed and network programs runs upward from half a million dollars.

Costs of operating TV stations are considerably greater than those of operating comparable radio stations. Although it is difficult to generalize about costs, there appears to be general agreement that it would be difficult to operate even the minimal facilities mentioned previously for less than \$30,000 per year. Operating costs more than double when filmed programs are added and exceed half a million dollars when live programs are produced.

These factors may hold the construction of new telecasting facilities to a slower pace than commonly expected. Only a few new stations may come into operation within the next 9 to 12 months. In the District the first ones to go up probably will be in larger cities such as Peoria and Des Moines which currently have no TV facilities.

As TV transmission coverage begins to blanket the nation, advertising revenues and new set sales will expand from present levels. The extremely rapid rate of growth of the early postwar years will not be equaled, however. Despite the freeze on new stations, the industry has been growing vigorously during the past four years. Adolescence passed, TV has taken its place as a major, American industry.

# THE Trend OF BUSINESS

THE COSTS AND EFFECTS of the long steel strike can now be evaluated in the light of developments during the past month. The final toll has not yet been taken, however. Widespread production curtailments will continue in the great steel consuming centers of the Midwest for many weeks after the ending of the dispute. Some large steel users in the automobile, farm machinery, and appliance industries reported that operations had come to a virtual standstill almost a month ago. Other enterprises are only now being pinched for supplies.

Many manufacturing concerns had accumulated extremely large inventories of steel products by the end of May. These firms have maintained operations at peak levels and expect that current rates can be held through the summer. Growing inventory imbalance, however, suggests that few processors may expect to be completely immune from the aftereffects of the strike.

Depleted inventories which need rebuilding and the special priorities on the first steel runs which will be granted to defense contractors may mean that the march toward normalcy, which began earlier this year with the easing of allocations, cannot be resumed for several months. Aside from the immediate steel loss, the stoppage of ore shipments during two of the seven ice-free months has limited summer stockpiling and may cut output late next winter when rail shipments must be relied upon.

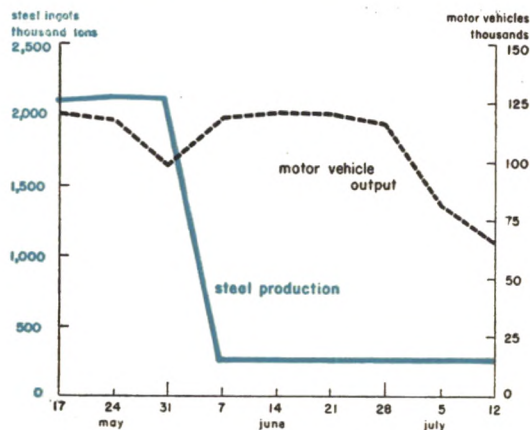
The nation may expect tightness in steel supplies for months to come. By July 25 the steel loss exceeded 17 million tons—about the amount of increase in rated annual capacity in the past two years. A few months ago steel industry officials had predicted that output

would be only 85 per cent of capacity later this year. Assuming these estimates to be correct, it would take almost a full year of capacity operation to make up for two months of lost production.

Although restriction orders were tightened on nonessential steel use shortly after the strike began, defense production has suffered along with civilian output. Makers of tanks, army trucks, shell casings, and a number of other products were forced to cut back about the end of June. Steel shortages particularly of bars and plates began to plague armament makers just about the time that the long build-up stage for certain complicated items had begun to pay off. In the second quarter defense outlays had reached a monthly rate of 4.4 billion dollars, an increase of 40 per cent over a year earlier.

Not all steel production has been cut off dur-

## *Drop in vehicle output lags behind steel decline*





ing the shut down. Thirteen to 15 per cent of capacity has continued in operation—mainly in plants dealing with independent unions. In the Chicago area only the Wisconsin Steel Company, a subsidiary of International-Harvester, maintained production. The benefits to the parent company were limited, however, since a large share of its needs are supplied by finishing mills which were strikebound. In fact, almost all I-H production in early July ceased, although some replacement parts for farm machinery needed for summer and fall harvesting continued to be processed.

**Automobile production** fell off abruptly early in July after a vigorous effort to keep assembly lines moving at maximum rates during the peak selling period. Splicing of narrow sheets and a variety of other expedients kept vehicle production fairly steady at about 120,000 units per week until the drop to 80,000 in the week ending July 5 and 26,000 in the week ending July 19.

In addition, steel troubles have interfered with production schedules on the all-new "Patton 48" tank. Over 2 billion dollars in contracts for this weapon have been awarded to

Chrysler, Ford, Continental Motors, and the Allison and Fisher Body Divisions of GM.

**Manufacturing employment** fell rapidly in the District during June and July. About one-fourth of the 600,000 striking steel workers are located in the Chicago-Gary and Detroit areas; secondary unemployment and the influx of June graduates into the labor force swelled the number of jobless. In mid-July, Michigan unemployment was estimated at 240,000, far exceeding the high point of last December when production was curtailed by allocations and model change-overs.

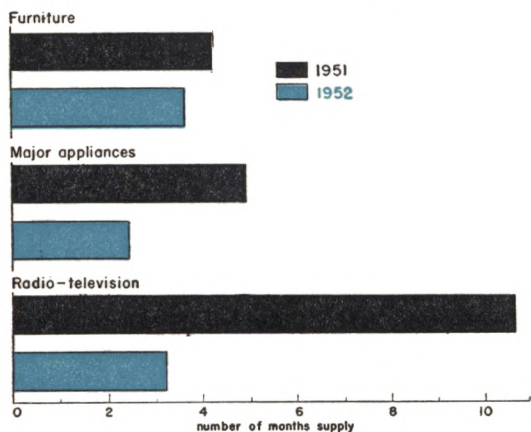
**Retail trade** continued fairly strong into July despite layoffs. Most District department stores reported sales to be near last year's figures. Only in cities such as Gary where affected workers account for 45 per cent of the labor force, did sales drop significantly.

Household appliances were moving at their fastest rate in over a year just at the time when Hotpoint and other makers were forced to close down as a result of steel shortages. District department stores reported stocks of major household appliances to be down 45 per cent from a year earlier at the end of May, whereas sales for the month were up 10 per cent.

**Some higher prices** are doubtless on the way. One immediate effect of the strike will be the 3 to 5 dollar per ton increase in the price of finished steel, but that is only part of the story. Lessened supplies of durable goods in the months immediately ahead together with the revived "fair trade" or "price-fixing" law will work toward discouraging discount selling at retail.

The loss of wages and earnings resulting from the strike will dampen some buying, but lowered supplies of goods probably tip the balance toward inflation. Many of the jobless have been able to maintain spending by drawing down savings. In addition, merchants have been willing to extend credit rather liberally because of the realization that wage payments are certain to be resumed often at higher rates because of overtime necessitated by the layoffs.

### *Inventories fall relative to sales at District department stores*



# Tapping the securities markets

*Corporate offerings are running at a record postwar rate.  
Liquidity and tax considerations uppermost in financial planning.*

THIS YEAR expansion programs and working capital needs combined with lower liquidity and high taxes are causing U. S. corporations to seek a huge volume of new money in the capital markets. Altogether, 2.9 billion dollars of new corporate securities were sold in the January-April period of this year—17 per cent more than in the same months of 1951. Large flotations since April have placed the market well on the road toward beating the 7.7 billion of new issues sold for cash last year.

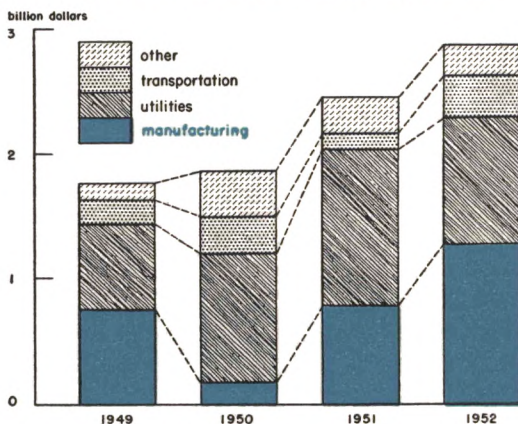
Stocks and bonds are being relied upon more heavily as a source of funds than at any time in recent years. Earnings available for retention are lower and many firms are attempting to avoid additional short-term debt. Bonds continue to dominate the financing picture, but there is evidence that common stock is regaining its long lost place as a major source of new money for industry.

## Expansion lowers liquidity

Almost 70 per cent of the proceeds of this year's new security issues are slated to be used in financing outlays on new plant and equipment. Capital expenditures of U. S. business are expected to set a new record in 1951 of over 25 billion dollars. About half of the total will be made by manufacturing establishments. For this reason, issues of manufacturers are accounting for about 45 per cent of all corporate flotations—a considerably larger proportion than in earlier years. (See chart.)

Most of the remainder of the money from new securities will be used to bolster working capital. Higher prices, larger inventories, and a greater volume of outstanding receivables have caused quick asset holdings of many corporations to appear inadequate. At the end of

## Manufacturers' issues lead uptrend



New corporate security issues, January—April periods

World War II corporate treasuries were well stocked with cash and Government securities. (See chart.) Postwar price inflation and an expanded volume of physical activity brought the ratio of cash and Governments to current liabilities to a low point in 1949. As inventories were worked down and bank debt paid off in that year, the liquidity ratio gradually improved and the better trend prevailed until mid-1950.

After the start of the Korean war relative liquidity again suffered as business activity intensified, inventories were increased rapidly, and prices rose. Because of these factors and the higher tax rates, over-all business liquidity has continued to deteriorate.

The Mills plan for accelerated corporate tax payments has contributed to the process. Under this arrangement corporations paid 70 per cent of their 1951 tax liability in the first half of

1952. Next year 80 per cent of the 1952 liability must be paid in the first half. As a result, corporations can no longer rely so heavily as in past years upon the accumulated tax liability as a steady source of funds during years of rising tax accruals. During the second half of 1952 corporations will be accruing taxes much faster than they are paid to the Government. Nevertheless, financial managers cannot safely tie up a large portion of these funds in physical assets.

The attempt to improve working capital positions provides an incentive for security financing—to acquire funds through stock or long-term bonds and notes. Bank borrowing is often undesirable since the great bulk of bank loans are current liabilities. During the period from the start of 1952 to July 16, business loans of weekly reporting banks in the Seventh District declined by 152 million dollars or 6 per cent in contrast to a rise of 202 million or 9 per cent in the same period of 1951.

There are indications that some businesses prefer to undergo some financial stringency rather than take on additional short-term obligations. Requests for bank loans for meeting tax payments fell considerably below expectation at large Midwest banks in March and June of this year.

Another compelling reason for the move toward securities has been the decline in the amount of funds generated by business internally. Despite record pretax profits in 1951, retained earnings of corporations dropped 30 per cent from the 13.6 billion dollar total of the previous year mainly as a result of higher taxes.

This year a combination of taxes and high costs, a desire to maintain or raise dividend distributions, and lower sales in some lines may drop profit retentions further to something over 8 billion dollars. Depreciation charges have been rising rapidly and undoubtedly will surpass undistributed profits as a source of funds. In any case, these two major internal sources of funds combined will finance a

smaller portion of requirements in 1952 than in any previous postwar year.

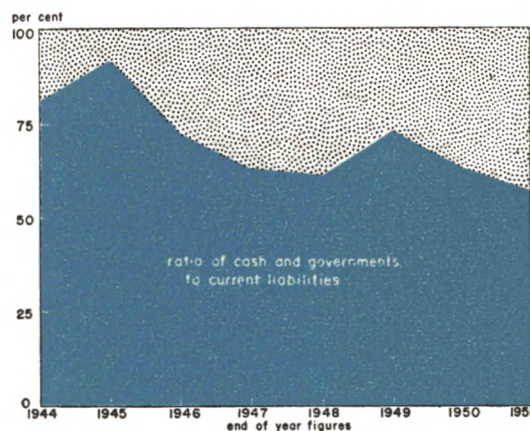
### Common stock more common

Since corporate assets began expanding rapidly after mid-1950, a growing number of firms have been coming to the market with new common stock issues. In the first four months of 1952, about 500 million dollars worth were sold—about 18 per cent of the total dollar value. This proportion was only 12 per cent in the first quarter of 1951.

From the supply side common stock financing is more appealing to many corporations at the present level of stock prices than any time since 1946. Although the financial position of business in general remains strong, most corporate executives are desirous of keeping debt accumulations within bounds. In connection with one recent stock issue, it was announced that a portion of the proceeds would be used to retire bank debt.

One reason for heightened demand for stocks is that more individuals currently are “in the market” than at any time since 1946. Partly, these investors are responding to the broad publicity given to stocks as an inflation hedge. Of equal importance, however, is the simple

### Corporate liquidity ratio declines



fact that since mid-1949 average stock prices have risen 35-40 per cent.

Individuals taking their first "flyer" in the market are often ready to jettison their holdings at the first storm warning. Fortunately, a stabilizing influence has appeared in the growing amount of investments in equities made by institutions. Pension funds and to a lesser extent insurance companies have been buying common stocks. Other institutional investors such as universities and churches are finding the higher yields on stocks increasingly attractive as they struggle with rising costs.

Nevertheless, some of the new stock issues offered this year found the market inhospitable. In several cases selling syndicates had to be broken up and prices allowed to find their own level, despite the fact that substantial blocks of

securities remained in the hands of dealers.

A good level of stock prices is not always sufficient to permit large flotations to be absorbed easily. New issues usually fare well only in a rising market and stock prices have been relatively stable for some months. Moreover, the delays involved in registration and prohibitions against questionable ballyhoo concerning stock offerings militate against a return to stock financing on the scale of the late 20's.

As a result, more interest is being evidenced in debentures and preferred stock which are convertible into common at a price somewhat higher than the current market. If the common stock rises sufficiently conversion becomes profitable. For several years the American Telephone and Telegraph Corporation has been showing the way to important amounts of in-

### Retail credit survey available

Retail credit practices vary widely in District centers. This is revealed by a recent survey of 2,400 stores in 350 Midwest cities.

Variations are especially apparent in the small cities where aggressive credit dealers or chains following certain practices may dominate the picture, but differences exist in large centers as well.

In the case of department stores, for example, 61 per cent of the sales of Chicago stores were for cash—well above the District average of 56 per cent. For Indianapolis this proportion was only 44 per cent. In general, cash business is relatively large in the smaller cities such as Joliet and Battle Creek in which the ratio was over 65 per cent.

There is also considerable variation in the proportion of credit sales made on the instalment plan by department stores. In most cities charge account sales exceed instalment sales threefold, but in some smaller cities instalment sales actually exceed charge

account business.

These differences in commercial practices, in some cases, may be explained by the varying importance of large chains which commonly emphasize instalment selling. In other cities explanation traces to traditional local practices or the composition of the labor force and income stability.

In the case of auto dealers, cash sales in the large cities ranged between 43 per cent for Indianapolis and 61 per cent for Milwaukee. For many smaller cities the ratio of cash sales is much lower—in some cases less than 30 per cent. Such differences often result from the local banking practices.

The 1951 sales of stores included in the study approximated their record 1950 volume. Total credit sales showed little change although charge account business increased.

*Copies of the recently tabulated survey of sales, inventories, and receivables of Seventh District merchants are now available upon request to the Research Department, Federal Reserve Bank of Chicago.*

direct equity financing through its convertible debentures. Another mammoth flotation of these securities aggregating 500 million dollars is now underway. In July, Dow Chemical announced a 100 million dollar issue of this type.

There are a number of advantages in the use of convertible issues in corporate equity financing. First, these securities are often easier to sell than new common because the exact status of the market at a particular time is of secondary importance; conversion rights will retain some value even if the price of the common declines during the flotation. Second, there is no need for the immediate dilution of the value of existing stockholders' interests which occurs when new stock is sold to the public "below the market." Furthermore, many institutions which are prevented from buying common stocks outright are attracted to preferred or bonds which are "sweetened" by the conversion privilege.

### Bonds are still the mainstay

Despite the greater publicity given to stock issues, the volume of debt financing continues to be far more important. In the past four years over 21 billion dollars of bonds and notes of American corporations have been sold.

Provisions of the excess profits tax law furnish a strong incentive for bond financing. In many instances, the larger capital base which results means that new issues are not only costless on an after tax basis, but may actually be profitable to corporations in the highest tax brackets. Twelve per cent may be earned on new capital before the additional income is subject to EPT. This provision in the tax law applies to common stock as well as bank loans and bonds, but dividends, of course, are not deductible as an expense as are interest payments.

In the Midwest, a variety of firms in the steel, chemical, coal, and office machinery industries have tapped the bond markets in recent months. Most important among the District firms doing security financing, however, have been the utili-

ties, many of which have announced large debt issues in connection with expansion programs extending over the next two to three years. A partial listing of these issues follows. They are all first mortgage bonds due in about 30 years:

	Million dollars	Coupon
Commonwealth Edison Co. Public Service Co.	40	3-1/4
of Indiana . . . . .	25	3-3/8
Illinois Bell Tele- phone Co. . . . .	25	3-1/8
Consumers Power Co. . . . .	25	3-1/4
Wisconsin Electric Power Co. . . . .	12.5	3-1/4

### Bond market strong

Despite some sluggishness and markdowns in the market for new bond issues in the late spring, indexes of bond yields showed little upward pressure. During May and June, Moody's average corporates remained at a fairly stable yield of about 3.16 per cent. This rate, although well above the low point of 2.85 recorded before the pegs were pulled on Government bonds in March 1951, was below the 3.27 high which was set earlier in 1952.

An impressive volume of funds are seeking investment in corporate bonds at the present time. Assets of life insurance companies, the purchasers of the bulk of new corporates, are increasing at a rate of around 4.5 billion dollars per year. Additional funds are provided through payoffs and liquidations of existing holdings.

The insurance companies apparently have stopped liquidating Governments in important amounts and that source of funds for business is largely at an end. On the other hand, some companies have withdrawn temporarily from the real estate mortgage market and are interested in diversifying investments through purchase of a variety of corporates.

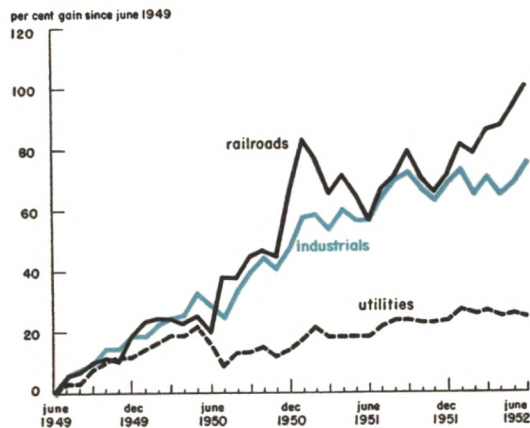
Noninsured pension funds are growing at a rate of over 1 billion dollars per year. Although a substantial portion of pension fund money is going into common stocks and Governments, some corporate bonds are purchased. Moreover, since pension funds made important purchases of Governments from life insurance companies last year, additional money was made available to the private bond market indirectly.

It is probable that a large volume of new corporates can be absorbed during the second half of this year without important upward pressure on yields. In fact, prices may move higher if the Treasury does not attempt to tap the long-term market later this year.

### Smaller flotations in '53?

Since industry is moving over the hump in the post-Korean expansion of capacity and inventories, it is probable that 1952 will prove to be the peak year for corporate financing for some time to come. Capital spending is likely to decline substantially next year and this use of funds has been the most important reason for large new issues. In addition, it is probable that total business inventories will rise only seasonally through the rest of this year. With

### *Railroad stocks lead three year bull market*



corporate assets growing at a more moderate rate it is apparent that the most pressing needs for additional capital issues will decline.

Changes in the tax law also could work toward reducing requirements next year to a greater extent than is indicated by an analysis based on the existing law. For example, the acceleration of corporation tax payments may be altered so as to smooth out collections and thus ease working capital problems. It is also possible that the premium on debt expansion under the present EPT will be modified.

In certain industries high-level capital outlays are in prospect for some years to come. The electric utilities will continue to offer new securities in large volume; growing capacity has just managed to keep production of power ahead of demand throughout the past seven years. The expansion of natural gas pipelines as well as the development of new oil and ore reserves also will require sizable amounts of funds. Further demands on the capital market will result from plans for shopping centers, housing developments, and office buildings.

Whatever the aggregate volume of new corporate issues in store for the period ahead, over-all financial planning will be influenced by memories of the difficulties caused by excessive fixed charges and inconvenient debt maturities in previous downswings. Business firms, generally, weathered the earlier postwar years without serious deterioration of their financial position. Large earnings retentions before the reimposition of the excess profits taxes assured that total equity capital sources would keep step with demand.

Now it appears that the main impact of the secondary postwar boom has been absorbed without important deterioration of financial health. Nevertheless, many corporate managements are following the cautious road leading toward a "cleaner" balance sheet in order to prepare for future developments. Many firms not undergoing rapid expansion will continue to sell securities for the purpose of improving liquidity and stiffening capital structures.

# Farm assets<sup>1</sup>

THE FINANCIAL POSITION OF AGRICULTURE CONTINUES exceptionally strong. Reflecting a near record net income last year, farmers made important additions to their stocks of farm machinery and motor vehicles, household furnishings and equipment, deposits and currency, and to the number of livestock on farms. In addition to the increase in physical quantity of these assets, prices were at a higher level than in 1950 with the result that the total value of farm assets stood at a record high on January 1, 1952.

	Billion dollars	Per cent change from 1951
Real estate . . . . .	94.6	+ 9
Livestock, machinery, etc. . . . .	51.5	+12
Financial assets . . .	22.9	+ 5
Total assets . . . .	169.0	+ 9
Mortgage debt . . .	6.3	+ 8
Other debt . . . . .	7.9	+12
Owners' equities ..	154.8	+ 9
Total claims . . .	169.0	+ 9

Not all of the advance in farm asset values represented an increase in net worth. Farm debts also rose. The 8 per cent advance in farm mortgage debt, for example, brought its total to about the prewar level. Non-real estate debt increased even more rapidly and totaled more than two and one-half times the prewar amount.

Owners' equities, nevertheless, reached an all-time high of 155 billion and account for over 90 per cent of the total value of farm assets. It is clear, therefore, that agriculture generally is only lightly encumbered with debt.

Farmers' holdings of deposits and currency advanced about 800 million and farmers' equi-

ties in cooperative associations increased about 200 million. Their holdings of savings bonds, on the other hand, were about the same on January 1 as a year earlier. The advance of about 8 billion dollars in value of farm real estate, primarily a price increase, accounted for the major portion of the rise in assets.

## The Midwest

Developments in the Seventh District have differed in some respects from those for the nation. Increases in farm real estate values and farm mortgage debt were moderately less, but non-real estate debt, especially in the important cattle feeding states of Iowa and Illinois, increased much more than the U. S. average. Demand deposits held by District farmers increased relatively much less than in other areas.

District bankers, probably viewing farmers' financial positions largely from the credit standpoint, report that the over-all situation at mid-year had improved from a year earlier in Michigan and Wisconsin. Iowa conditions are different, however. Nearly two-thirds of the member banks in this state report that the financial position of farmers weakened over the past year. Relative to prospects for the remainder of the year, the farmer demand for non-real estate credit continues very active but most bankers expect that outstandings at year-end will be smaller than at the close of 1951. With large harvests in prospect the financial position of farmers probably will improve further during 1952.

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**Business Conditions** is published monthly by the FEDERAL RESERVE BANK OF CHICAGO. Subscriptions are available to the public without charge. For information concerning bulk mailings to banks, business organizations, and educational institutions write: Research Department, Federal Reserve Bank of Chicago, Box 834, Chicago 90, Illinois. Articles may be reprinted provided source is credited.

<sup>1</sup> This article is based largely on "The Balance Sheet of Agriculture, 1952," a study prepared in the Bureau of Agricultural Economics, U.S. Department of Agriculture, and published in the July issue of the Federal Reserve Bulletin. Copies of the full report may be obtained from: the Board of Governors, Federal Reserve System, or the U. S. Department of Agriculture, Washington, D. C., or from the Federal Reserve Bank of Chicago, Chicago Illinois.

# A big harvest

GOOD TO EXCELLENT crop and pasture conditions prevail throughout most of the Midwest, and for the U. S., midyear prospects point to a total crop production second only to the record volume harvested in 1948. Realization of this large volume likely would result in moderate downward pressure on some prices as the harvest progresses and stimulate a broad interest in price support loans, particularly for wheat and corn.

Output will be boosted above last year due to both increased acreage and high yields. Major acreage increases are in winter wheat, oats, soybeans, and potatoes. Near record yields of corn, wheat, and soybeans are indicated. A wheat harvest of over 1.2 billion bushels would be more than ample to meet domestic and export requirements. The soybean crop, three-fifths of which is produced in District states, may be of record size.

## King corn

The Seventh District is primarily a feed and livestock producing area. Corn production in these states, estimated at 1.6 billion bushels, would be up nearly one-fifth from last year. For Iowa, the leading state, a harvest of nearly 650 million bushels would exceed last year by more than one-third.

Nationally the corn crop provides about three-fourths of the feed grain supply and is estimated at nearly 3.4 billion bushels, one-seventh more than in 1951. Although the carry-over from previous crops will be reduced substantially by October 1, realization of a crop of this size would result in a total supply this fall moderately larger than a year ago.

The oat crop, second in importance as a feed grain, is estimated at approximately 1.4 billion bushels, somewhat larger than in 1951. Production in District states, which account for nearly one-half of the total, is up one-

seventh. Smaller carry-over stocks, however, will about offset the larger production. Barley supplies will be reduced sharply and supplies of grain sorghums are expected to be moderately below year-ago levels. The hay crop will be smaller, but generally adequate.

Reflecting the good corn prospects, total feed grain supplies probably will be slightly in excess of a year ago. Feed requirements, furthermore, may not be as heavy as in 1951-52.

Farmers have reported intentions to raise about 9 per cent fewer pigs this year. Over 40 per cent of the feed grain supply normally is used by hogs. Chickens also are currently experiencing some cutback. Dairy cow, horse, mule, and sheep numbers are indicated to show little change. The rising trend in beef cattle shows no evidence of slackening, but only about 10 per cent of the feed grains are used in their production.

Thus, the carry-over of feed grains at the end of the 1952-53 season is likely to show some increase. Nevertheless, further efforts may be made to boost their production to even higher levels in 1953, thereby permitting a further accumulation of stocks or expansion in livestock production.

## *District production changes from 1951 similar to those for the U.S. . . . but more extreme*

