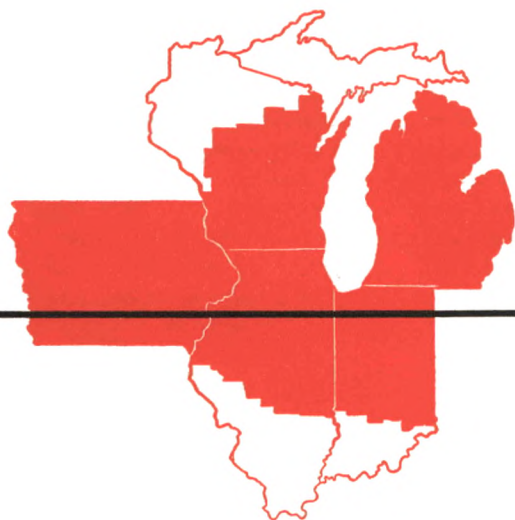


A review by the **Federal Reserve Bank of Chicago**

Business Conditions

1953 January



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Sixty million jobs—plus

Labor markets are tight. Michigan manufacturing centers moved from surplus to shortage in the past year.

AS 1952 DREW TO A CLOSE, over 65 million Americans were at civilian jobs and in the armed services. Unemployment was only a little over 1.4 million—far below the average of recent years. Anyone who was unsuccessful in his search for work was either very discriminating or was reluctant to leave one of the rare areas of labor surplus for greener pastures.

In Midwestern manufacturing centers, personnel managers were being forced to lower their standards and increase advertising outlays in an attempt to fill requisitions. During November, 55 per cent of the purchasing agents of Chicago reported that their firms would have hired additional employees if they had been available.

Detroit, Flint, and other automobile cities which had been allotted preferential treatment on defense contracts in early 1952 because of "allocation unemployment" were having trouble finding enough workers to staff newly-completed defense plants. The completion of new aircraft factories in Battle Creek resulted in the classification of this city as one of four areas in the country with a labor shortage. A general pickup in metalworking plants also has been important in the Milwaukee area and in South Bend. For many defense producers, labor requirements were expected to show a further rise.

Behind the men behind the guns

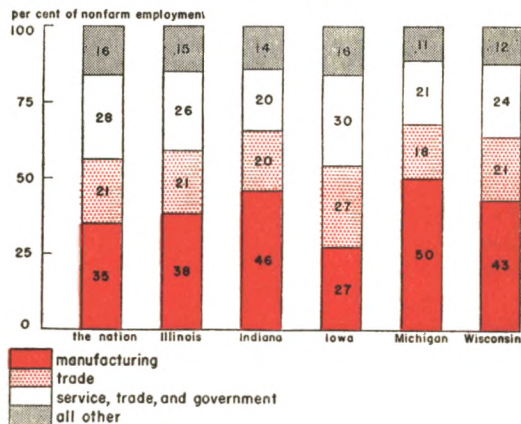
There are several reasons for the tightness in the labor market, but the dominating cause is the defense program. About 3.6 million men and women are now in uniform and perhaps twice that many are working at civilian jobs which contribute to armed preparedness.

Some types of military production, particularly soft goods, are at or past contemplated

peaks. But other vital programs, such as the all-important aircraft build-up, have a long way to go. Production of airframes, jet engines, and electronic equipment requires a relatively large labor input. It may be expected that direct and indirect civilian defense employment will remain at or above present levels for months to come.

The armed forces have stabilized, for the time being, at slightly over 3.6 million. Plans still call for a further rise to 3.7 million, and monthly draft quotas were raised from 30,000 to 50,000 in October in an attempt to meet this goal and maintain rotation schedules. Some states are having difficulty in meeting their requirements under the new quotas. Deferment policies are being re-examined, but there is a general reluctance to expand the pool of potential draftees. In order to avoid additional calls, Defense Department officials are attempt-

Manufacturing dominates District employment picture



ing to push further the program of eliminating unessential noncombatant jobs, and substituting women for men.

The untapped reservoir

In the past two years about 2 million additional workers have been employed. At least one-half of these were obtained by whittling down the number of unemployed; the remainder entered or re-entered the labor force during the period.

The potential civilian man power supply increased by about 1 million per year in the early postwar years. In 1951, however, it declined slightly for the first time since 1944. This was because of the smaller number of persons reaching working age and the increase in the armed forces. In 1952, there may have been an increase of about one-half million.

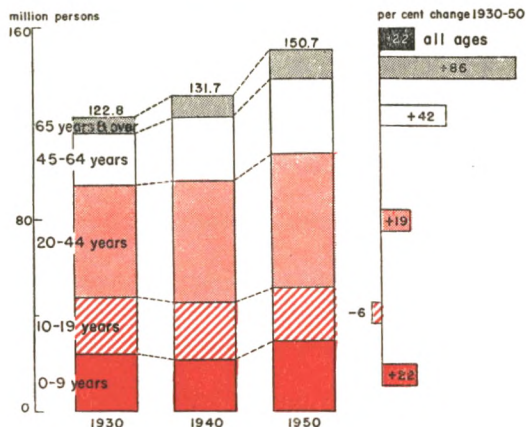
Nevertheless, the nation's man power resources for use in an emergency remain very large. If need should arise, 4.4 million men beyond the age of 45 could be called upon to "help out." A much larger reserve pool exists in the 38 million women not now employed. In addition, hours of existing workers could be lengthened. The average working week in manufacturing today is only 41 hours, compared with 45 in 1943.

Fewer young workers

Draft boards and personnel departments of firms in white collar lines which depend heavily upon recruitment of recent high school graduates face slim pickings. Less than 2.5 million boys and girls per year are now reaching the age of 18—about 17 per cent less than was the case a decade ago. Several years must elapse before the higher birth rate of the early 1940's appreciably affects the available number of young workers.

The "potential" labor force is sometimes defined as the population 14 years and older. This basis for calculation has become increasingly unrealistic, more so in the Seventh District states than in certain other sections of the nation, be-

Population ages, 1930-50



cause a larger proportion of children are completing high school. However, excellent job opportunities are bringing many of these students into the labor market on a part-time basis. Presently one-fourth of the nation's high school students, one-third of those in Chicago, have some type of job.

"Youth" has become a scarce commodity in the labor market. As a result, newly hired youngsters can demand and receive wages much closer to those paid to older and more experienced workers than was true in the past. Complaints of employers concerning the "attitude" of the younger generation reflect this strong competition for young workers.

Women replace men

The squeeze on the labor market has been lessened in recent years by the larger number of women jobholders—particularly married and older women. Prior to World War II women constituted about one-fourth of the total civilian labor force. At present this proportion is one-third, only slightly below the wartime peak.

Married women accounted for about one-third of all female workers in 1940, compared to one-half of the current total. Many married women and women over 45 who were induced

to enter the labor force during the stringent 1941-45 period have continued to work. Others have since taken jobs as a result of changing social customs, a desire to supplement family budgets, and, of course, the ready availability of suitable positions.

Although women workers constitute almost as large a portion of the labor force as during World War II, the same is not true of older men. Despite frequent references to the plight of retired workers who are forced to seek employment in order to supplement inflation-ravaged pensions, the older men are not meeting labor market deficits under current conditions.

In 1945, 51 per cent of men 65 years and older were employed; in 1952 only 42 per cent of this age group had jobs. Pensions, liquid asset holdings, a high rate of home ownership, and other factors such as the reluctance of many firms to hire men over 55 are serving to keep the majority of these persons at home.

From farms to factories

As the composition of the working population has changed over the past dozen years, there has been an even more striking change in the proportions of workers earning their living in the various activities. During the Forties the relative number of workers in agriculture, domestic service, and those self-employed declined significantly while the proportion in manufacturing, trades and services, construction, and government rose.

Many persons formerly employed in domestic service have been attracted by high factory wages. City jobs have also absorbed numerous agricultural workers. Farm owners have responded by purchasing additional equipment and adopting better techniques. Currently the nation's farms are turning out 40 per cent more produce than in the typical year prior to World War II, despite the fact that 15 per cent fewer workers are engaged in raising crops and livestock.

The rise in manufacturing employment in the

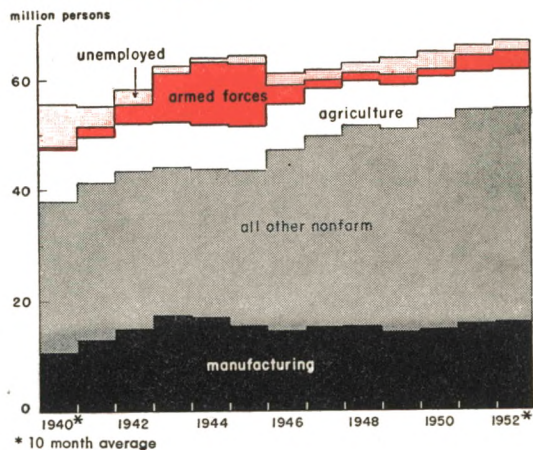
past 12 years has been concentrated in the durable goods category. This group includes military equipment and machinery as well as automobiles and many types of homefurnishings.

Complex industrial developments and the changing character of modern warfare necessitate that large numbers of workers be highly trained—both for research and operational needs. Unfortunately, apprenticeships have not had sufficient appeal for young men who can easily obtain unskilled or semiskilled work at a higher starting wage. At the same time colleges report a drop off compared with earlier postwar years in the number of students in engineering and in the physical and biological sciences.

Men and machines

If there is no step-up in military operations during 1953, the labor market tightness in many lines will tend to be corrected. Output per man-hour has increased rapidly during 1952 and a further rise is likely for next year. But technological progress in modern America assures that the existing level of output of goods and services can be maintained with a gradual decline in the number of man-hours expended.

Nonfarm employment shows steady rise



Old man weather

His actions are partially predictable and may possibly be modified by the rain makers, but to Corn Belt farmers and range cattlemen he still reigns supreme.

MIDWEST FARMERS HAD A GOOD FALL SEASON. The weather favored an early harvest. Their crops were mature and dry and the yields were abundant. Corn—the king of Midwest agriculture—would store well.

What a contrast to the preceding year. Plodding through their muddy cornfields in the fall of 1951, farmers saw much wet, immature corn—corn that would spoil if picked and cribbed. Corn that could only be utilized by early feeding. But feeder cattle prices were sky-high. Old man weather had dealt Midwest farmers a thorny problem indeed.

But he had favored the nation's extensive grazing areas—the semiarid Great Plains and the many hilly, stony, and mountainous regions. With abundant rainfall their vegetation flourished. Modern helicopter and jeep-borne cowboys watched their thriving cattle grow fat and visualized still larger herds to graze on the uneaten grass. They would raise more cattle!

Midwest farmers meanwhile were clamoring for feeder cattle. They needed them to salvage their corn crop. Bidding against one another—and competing with the uneaten grass—prices were driven to an all-time high. Forty cents a pound for choice feeder calves was not uncommon. There were occasional transactions as high as 50 cents—\$150 to \$200 for striping 400 pound calves. Heavier feeders, of course, sold cheaper, as usual, reflecting their less efficient gains and the greater risk in owning them. But they were priced close to the slaughter cattle level.

Reflecting the excellent grazing conditions, most feeder cattle were in good condition—carried more than the usual amount of flesh. Thus, they attracted slaughterers as well as

feeder buyers—still more competition for Corn Belt farmers as they scrambled to fill their feed lots.

The results are well-known. Western cattlemen enjoyed Cadillac incomes from their cattle sales even though they held back enough animals to make a record expansion in their herds. Gross income of commercial family operated cattle ranches in 1951 showed about a 50 per cent increase over the preceding year. Northern Plains wheat and cattle ranches chalked up similar gains. The only type of unit to show a more spectacular increase was sheep ranches.

Much credit used

Corn Belt farmers, in their struggle to salvage a corn crop, borrowed heavily from banks, production credit associations, and other lenders to finance feeder cattle purchases. Member bank loans to western Iowa farmers, for example, increased 78 per cent in the last half of 1951 and at year end were 48 per cent above year-earlier outstandings. Banks in important Illinois cattle feeding areas had a similar experience.

After the corn crop was fed the cattle were sold for slaughter. They were bigger and fatter, but the price was down. Many Corn Belt farmers grossed from their fattened cattle little more than they had paid for their feeders. Their corn crop, in effect, was “given” to the producer of the feeder cattle because old man weather had determined that there would be uneaten grass on the range and “soft” corn in the Midwest.

But what about 1952! Ah, that is another year, and a different story. The weather

changed! While Midwest farmers watched bountiful crops grow to maturity and complacently started harvesting and storing them, the rains were absent from important grazing areas. The grass was dry and short, what there was of it. And the winter wheat fields provided little fall grazing. Pasture lands which had been leased last spring at record high rentals produced more disappointment than grass. Reflecting the record 1951 herd expansion, cattle numbers were pressing on the feed ceiling. In many areas there were too many cattle for the limited feed available.

The usual midsummer contracting for fall shipment to feed lots was exceedingly dull. Corn Belt farmers, having fared badly the previous year, were shying away from feeder cattle sales much as a skittish horse side-steps prairie dog holes.

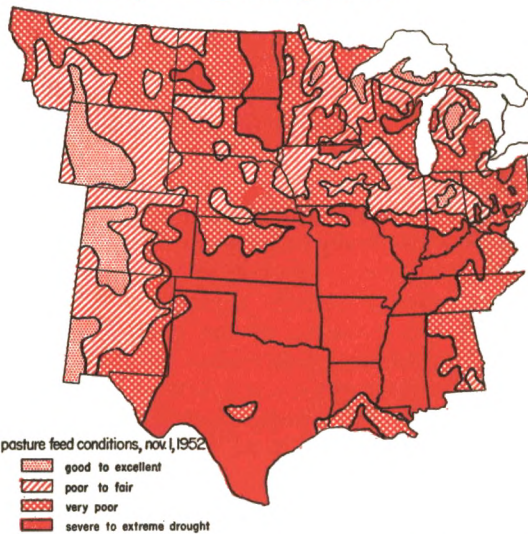
Through the summer and into the fall, the Western cattlemen kept whistling a merry tune although adding an occasional wrinkle of concern to their Stetson-shielded brows. "It would rain again," they reassured themselves. And if they could just hold on a while, the corn farmers would be after their cattle. What other use for the bumper corn crop?

They hung on. The grass grew shorter. They broke out some of their winter feed. They shopped for hay but it was high priced.

Feeder cattle prices continued down. And the corn farmers still were not knocking on their doors. Top calves that would have been bid in actively at 40 cents a year earlier went begging for buyers at 30 cents. Yearling steer prices were off 25 to 30 per cent. Cows that sold at \$250 to \$275 a head in 1951 stood waiting for buyers at \$125 in 1952.

But the producers of feeder stock had to start selling, or buy expensive feed. Most of them increased marketings over a year earlier. Some had no choice. Credit for \$40 hay to be fed to \$15 cows was available, but not to everyone. Furthermore, even though credit was available, was borrowing for this purpose good business for the rancher?

Drought forced increased sale of cattle from grazing areas



Receipts of grass cattle at the big Kansas City market from July 1 to November 15 zoomed to 808,000 head, nearly double the 425,000 received in the corresponding 1951 period. Many of these animals were sold for slaughter. Corn Belt farmers, nevertheless, purchased a larger number than in the preceding year. But they shopped casually. There was no scrambling for cattle to feed "soft" corn. And they weren't competing with uneaten grass on the prairies and hillsides of the range areas.

The average cost of the 200,000 feeder steers purchased at Kansas City was \$23.69 a hundredweight. This compared with \$31.99 for the 126,000 purchased there in 1951. The 68,000 feeder calves moved at an average of \$25.33 re the \$35.03 average for the 37,000 available at this market in the wet corn season.

The Cadillac incomes of the range cattlemen shriveled with the drying of the grass. The corn farmers had moved to the top rail of the cattle pens. They could sell their corn, store it at a guaranteed price, or feed it. They were in no hurry to make up their minds. They

would feed only if cattle were available at "reasonable" prices. They waited. They got the cattle, even more of them than in 1951. The seat on the top rail was comfortable. The temptation to relax was very great. But the cattle are still in their feed lots. Even though purchased at much lower prices than in 1951, the final accounting would not be made until the feeding period was completed and the fattened animals sold for slaughter. With a larger number of cattle on feed than a year ago, slaughter cattle prices might decline. They could still get squeezed. But they felt much more at ease than last year when old man weather dealt them a "soft" corn crop. The shoe really pinched then. But now these uncomfortable boots had been passed along to the producer of feeder cattle.

The market for beef, after all, is measured largely in terms of consumer income and supplies of other meats. Out of each \$100 consumers have after paying personal taxes, they usually spend \$5 to \$6 for meat. Rising levels of employment and personal income are, therefore, good omens for cattle feeders this year. Although America's appetite for beefsteaks and roasts is not insatiable, bulging paychecks provide a sound underpinning for the increased supply of beef now on its way to market.

This is not to say that beef prices will not decline somewhat. They probably will ease down a bit more, especially at the retail level as supply is stepped up. As for cattle prices, the better grades of slaughter stock appear to be in the more vulnerable position. But with high-level employment, an active domestic demand, and expanding supply, big price changes are not in the cards.

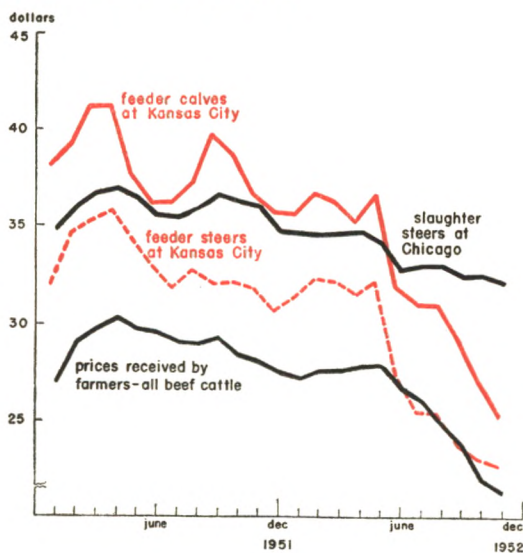
Similarly, windfall profits for Corn Belt feeders are not in the picture. Feed costs are high. The 1952-53 feeding season will likely be recorded as one in which reasonable profits were made by efficient feeders even though slaughter cattle prices trended downward.

Quite obscure at the moment is the effect of drought in grazing regions on the rapid expansion of herds.

In some areas this, no doubt, was brought to a screeching halt, at least until old man weather smiles on them again. Basic breeding herds, however, have been well maintained and the over-all number of cattle on farms and ranches remains above a year ago and at a record high.

The mettle of cattle growers and feeders has been tested again the past two years by the tempestuous smiles and frowns of that irascible old devil, weather. Although science continues to chip away at his thus far impenetrable shell, the independent old fellow continues to foil both those who attempt to forecast his behavior and the "rain makers" who attempt to modify it. Thus, regardless of how he deals out his product—in accordance with passing whims or carefully laid long-term plans—the result may continue to be "bonanza or bust" to individual farmers depending upon whether they happen to bask in the good fortune of his smiles or struggle in the adversity of his frowns.

Cattle prices declined gradually for a year, then feeders broke sharply



THE Trend OF BUSINESS

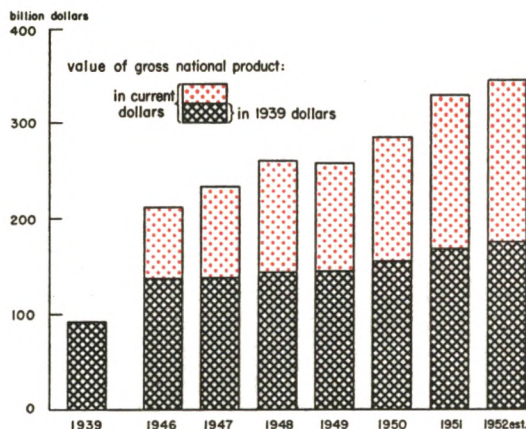
IN THE FINAL QUARTER OF 1952, most over-all measures of activity were at record highs. Physical output and personal income exceeded previous periods by a fair margin; business profits showed substantial gains and unemployment declined to negligible proportions. Now at the beginning of 1953, the belief is widespread that existing momentum assures an excellent, perhaps rising, general level of business activity for several months to come.

Although there has been a trend recently toward viewing 1953 as a good year throughout, many turn-of-the-year forecasts hold that a downward trend will be evident before the close of 1953. Developments in the vital areas discussed below will go far toward determining the over-all course of events during the year.

National security outlays have been running at about the present annual rate of 50 billion dollars since the first quarter of 1952. Thus, the fall boom owed very little to additional impetus from the defense program. Official pronouncements, however, still point to a further rise in the rate of total military expenditures. Truck and tank output is scheduled to be reduced later this year, but the more important aircraft program appears to be behind schedule.

Plant and equipment expenditures of business in 1953 will approximate the 1952 record of about 27 billion dollars, according to recent private and Government surveys. These outlays may be heavier in the first half of the year than in the second, however. Should a decline occur in this sector, it may be completely offset by the rise in other types of private and public construction which has been projected for 1953.

Total output of goods and services in 1952 set new records in both dollar and physical terms



Business inventory building has helped boost activity to recent high levels, but stocking in most lines appears to have been moderate and in line with sales. An end to the net gain, however, would remove an element of strength from the business picture. Moreover, holdings in most lines are sufficient to permit another period of reduced orders should sales decline.

Consumer spending accounts for two-thirds of total sales and therefore is always the final key to general business expectations. Although durable goods account for only about 15 per cent of total consumption spending, attention is often focused on this segment because of the postponability of large purchases. Despite heavy buying in the past seven years, industry leaders expect to sell up to 20 per cent more automobiles and television sets in 1953

than in 1952. A favorable outlook for appliances is bolstered by the expectation that new housing starts will about equal the 1952 total.

Private debt has doubled in the past seven years, but still remains smaller than in prewar decades relative to the current flow of income. Outstanding borrowings and service charges probably can be carried without difficulty if income remains high. Nevertheless, like the inventory situation, debt would become more of a problem if other activity props sag. In addition, a substantial reduction in the rate of private debt growth would remove or moderate one of the potent expansive elements which has characterized the postwar economy.

The fall credit rise

The strengths and weaknesses of the longer-term business outlook cannot be viewed in isolation from dynamic factors now at work in the economy. The very vigor of the recent business upturn has caused concern over its further generative potentialities and duration. Under present conditions, the possibility of a temporary resumption of price inflation cannot be ruled out.

In the fourth quarter, the stepped-up tempo of physical activity brought with it a sharp rise in credit extension. During November a larger-than-usual expansion in business loans took place and a significant share of the total was accounted for by industries which had not been borrowing heavily up to that time. In earlier months the increase in total business borrowing was probably less than might have been expected seasonally.

Part of the increase in business loans resulted from larger credit extensions to finance companies. Total consumer credit outstanding jumped 650 million dollars during October to a record 22.3 billion dollars. There is evidence that a further rise occurred in the following weeks.

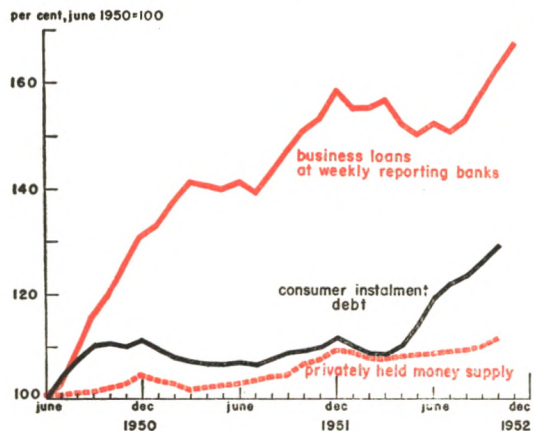
Private loan demand plus increased Government borrowings in recent months resulted

in an extremely tight money market late in 1952. Bill rates in December topped 2.2 per cent, the highest in 19 years. In order to augment reserve balances, member banks borrowed heavily from the Federal Reserve Banks this fall. Such indebtedness ran well above a billion dollars in the first half of December, more than double the total outstandings a year earlier.

The privately held money supply increased by 1.1 billion dollars in the month of November partly because of the loan rise. The total amount of money in the hands of the public at the end of November exceeded 190 billion dollars and was 10 per cent more than in March 1951 when the gradual fall in the wholesale price level began.

Inflationary pressures have been dormant, not dead. While expanding credit has been adding to buying power, price controls have been dropped from a growing list of goods and the wage stabilization program has been subjected to increasing strain. Bank loans ordinarily begin a seasonal decline in January. Many observers will closely follow this trend as important due to business developments in early 1953.

Sharp credit upturn in late 1952 continues post-Korea trend



TV tonics

Fall spurt largely traceable to heavier buying in existing television areas. New stations to bolster sales in '53.

IN THE FINAL MONTHS OF 1952, sales and production of television receivers reached a level rivaling previous peaks. Set output bounded from the year's low of 200,000 in July to over 750,000 in September. Production was maintained at about this rate during the fourth quarter.

The end of the ban on new station construction is only one of the factors leading to the fall boost in set output. In fact, most of the increased sales came in existing TV areas. In these cities the seasonal impetus to sales toward the end of summer has been well established. The recent gain, however, was more than seasonal. Consumers were lured to the purchase of their first or second TV set by larger screens, easier credit terms, and lower prices. In addition, many dealers were rebuilding stocks which had fallen to meager levels relative to sales.

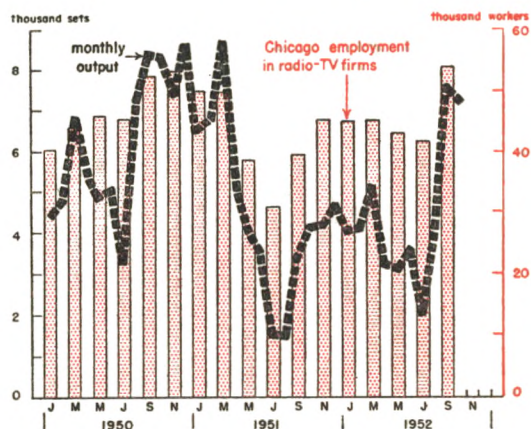
Good prospects for 1953

Television producers are optimistic concerning 1953 business. One industry spokesman has forecasted set output at 7.2 million units—about 20 per cent above 1952 and close to the 7.5 million record set in 1950. Other firms are more modest in their expectations, looking to total production of something over 6 million sets.

Almost 100 new stations are slated to begin operations this year in contrast to the mere handful that went on the air for the first time in 1952. Altogether, the new markets are expected to absorb about 2 million sets during 1953—perhaps one of every three or four produced. Obviously, demand in older TV areas will have to remain high to justify current optimism.

Seventh District department stores kept tele-

Employment in electronic firms follows TV set output



vision inventories 20 per cent or more below the same months of the previous year through the fall of 1952. All experienced dealers will be careful to avoid earlier encounters with mounting stocks at a time of lagging demand. Moreover, they are unlikely to be egged on by fears of shortages.

An indication that commercial color TV was imminent could seriously dampen sales to customers fearful of acquiring obsolescent merchandise. Such a development is unlikely in 1953, however, because of NPA pronouncements concerning the use of scarce materials and engineering talent together with continued uncertainty concerning color systems now under consideration.

The most important item on the credit side of the TV balance sheet is the vast potential market which still exists. Although 20 million

TV sets had been installed by the end of 1952, the number in service was expected to be doubled within a few years. Continued program improvement and extensions of the coaxial cable network to new areas are attracting additional first purchasers. Moreover, the two-set family is becoming increasingly common. Set owners have found that the set trade-in value of a small screen receiver is negligible and that family arguments over choice of programs are avoided by keeping the old set in service.

Employment at peak

In its short life span the TV set production industry has had some violent ups and downs. At the end of 1950 growing demand for television plus scarcity fears had brought production to a 10 million yearly rate. Material allocations threatened the industry momentarily in early 1951, but fast footwork in providing substitutes kept production at high levels.

In April of 1951 heavy inventories at both the manufacturing and trade levels together with a drastic fall in demand dictated sharp cutbacks of production schedules. Set output fell to less than 150,000 in July and August—a decline of 83 per cent from the March rate.

Chicago has a special stake in television production. Such well-known firms as Ad-

miral, Hallicrafter, Motorola, Raytheon, and Zenith are all important Chicago area employers. Most of these firms produce a variety of products, but changes in the level of TV set output have been especially important in causing employment fluctuations.

In September, according to the Illinois Bureau of Employment Security, 70 Chicago area firms which produce television and radio sets or parts employed about 54,000 persons. This total, the highest on record, indicated a 22 per cent jump from the July number. Employment continued at a very high level through the remainder of 1952.

During the months between March 1951 and last September, employment was bolstered in Chicago radio-TV firms by a large volume of defense orders. Currently, about 40 per cent of their employees are engaged in "essential" work—primarily finished military goods.

New stations widen market

From July 1 through early December the Federal Communications Commission granted permits for 127 new stations out of a backlog of 900. Only 108 stations had been on the air prior to the four year freeze which came to an end in 1952.

Prior to the ban, 16 stations had been operating in the Seventh District (see table). Peoria was scheduled to join this group on Christmas Day. Thus far, 14 additional broadcasting companies have announced intentions to begin operations during 1953 in important District centers including Flint, South Bend, Rockford, Green Bay, and Sioux City.

Although the FCC has proceeded carefully

Set installations up one-third in a year

Viewing Area	November 1, 1951	November 1, 1952	Gain
Chicago	1,020,000	1,290,000	+ 26%
Detroit	560,000	753,000	+ 34%
Milwaukee	280,000	375,000	+ 34%
Indianapolis-Bloomington	187,600	328,000	+ 75%
Grand Rapids-Kalamazoo	134,800	188,000	+ 39%
Davenport-Rock Island	74,000	156,000	+111%
Lansing	67,000	106,000	+ 58%
Ames-Des Moines	66,000	98,400	+ 49%
Total in Seventh District	2,389,400	3,294,400	+ 38%
Nation	14,545,900	19,000,000	+ 31%

Source: National Broadcasting Co.

in granting permits to new stations, the real impediment to speedy nation-wide TV service is the production and installation of transmission equipment. Even if the necessary equipment were itself in ample supply, the successful installation of telecasting facilities is a slow and painstaking process.

Retailing bonanza

In cities such as Chicago, Detroit, and Milwaukee, TV installations now have reached a considerable degree of saturation. The process was gradual, however, slowed at first by availability of materials and the spread of customer acceptance of a new product. Department stores and furniture and appliance dealers in new TV areas face quite a different situation—a market which has been pre-sold.

In Portland, Oregon, where the first Ultra High Frequency station was installed in October, sales of TV sets have been so brisk that one-third of the potential market was expected to be supplied by the end of the year. Merchants in other cities have made dealer arrangements with manufacturers and have begun to stockpile sets months before local stations were scheduled to go on the air.

Television dealers in new centers will be able to plan inventories more successfully than did their counterparts in existing TV centers a few years ago. First, since established set producers have the facilities and materials needed to turn out all of the sets that the national market is likely to be able to absorb, there need be fewer difficulties with “off-brands.” Secondly, the technology of the industry appears to have been temporarily stabilized to a considerable degree. No major changes in screen size or picture quality are likely to occur in the near future short of the introduction of color. Production is now heavily concentrated in the 21 and 27 inch picture tubes, about the optimum size for the average home. In short, inventory problems of TV dealers from now on will bear a closer similarity to the hazards inherent in the handling of any consumer durable goods.

The 100 billion dollar backlog

Growing demand for state and local government facilities to boost spending throughout the decade.

STATE AND LOCAL GOVERNMENT ACTIVITIES, which last year consumed more than 23 billion dollars worth of goods and services, promise to be among the steadiest sources of demand during the rest of the 1950's. The heaviest pressure for continued high levels of spending comes from the backlog of needs for new public facilities frequently estimated to total more than 100 billion dollars. Operating and maintaining these new facilities plus existing ones would add billions more to spending by non-Federal governments in the years immediately ahead.

While Federal nondefense spending has increased little during the postwar period and is currently less than one-fourth above the 1946 level, state-local spending is now nearly two and one-half times its 1946 rate. The steady upward trend of the last seven years is likely to continue unabated in the years ahead.

State-local standards

Over the past 25 years, the goods and services supplied by private producers and by the Federal Government have been developed vastly in quality, quantity, and variety. By and large, however, state and local governments have lagged behind. This has been most apparent in three of the four major state-local activities dollar-wise—highways, schools, and mental hospitals—as the recent volume of popular criticism of the inadequacies of the highway system and the condition of the mental hospitals and the school plant testifies.

For instance, the comfort, convenience, and

flexibility built into the motorcar in the past 25 years have been phenomenally successful in competing for the consumer dollar. Consumers spent almost four times as much for automobiles last year as they did in 1929, while most other expenditures increased 200 per cent or less. But the public roads over which the motorist operates his car have not been extended and improved enough to eliminate the congestion and hazardous conditions that seriously limit the full enjoyment of today's better automobile.

Such lack of improvement in state and local government services frequently prevents full enjoyment of the improved products of private industry. Not many people can have spacious lawns or air conditioned homes in a community with an uncertain or inadequate water supply. Frequent airline arrivals and departures lose much of their convenience if passengers must wait half an hour for an unloading gate at overcrowded municipal airports.

Sources of the difficulty

The reasons for the disparity between the standards of state-local services and those prevailing elsewhere in the economy are in part the war imposed lag in construction of new public facilities and the limited financial resources of local governments. State-local construction activity was at a low level during much of the Thirties, except for highways and airports, and even in these areas the provision of additional facilities lagged behind the increase in motor vehicle and air travel. During the war, state-local construction fell far below even the depressed levels of the middle Thirties. In 1944 highway construction outlays, for example, were less than one-fourth of those in the better prewar years.

Construction activity fell below replacement requirements and the needs of a growing population which has been rapidly shifting from rural to urban areas and within metropolitan areas from the core cities to the suburbs. In the last 60 years, the proportion of the popu-

lation living in urban areas has increased from a third to nearly two-thirds—from 22 million to 96 million. By far the largest single-decade shift occurred from 1940 to 1950.

The postwar efforts to make up the deficiencies resulted in state-local capital spending at more than double the dollar rates of the late Twenties. The effects of these heavy expenditures were more than offset by two factors: the inflation in costs and the expanding basic demand for public facilities due to large increases in school enrollments, motor vehicle travel, and urbanization.

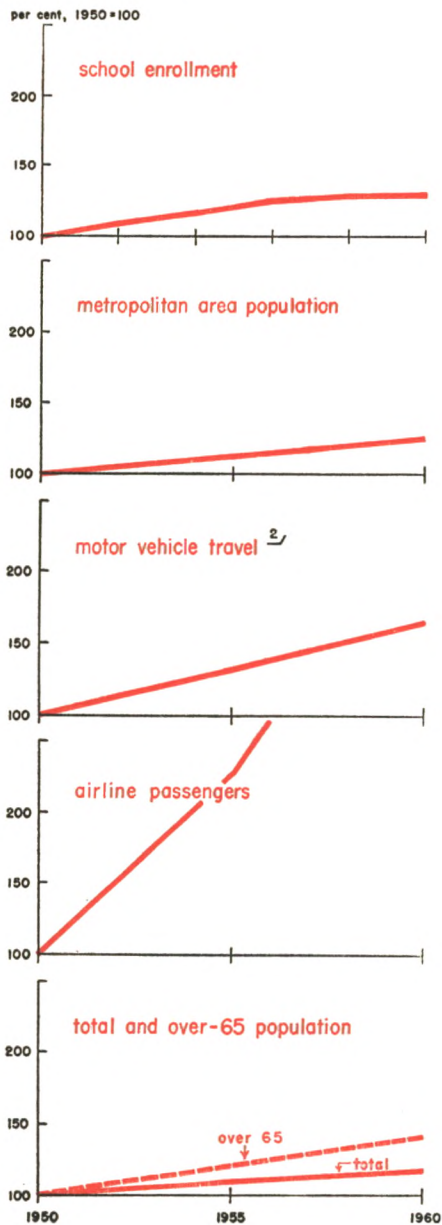
Nature of the backlog

The 100 billion dollar backlog of state-local construction needs during the 1950's includes two distinct elements: raising standards by eliminating the accumulated deficiencies and at the same time providing the facilities that will be required by normal obsolescence and continued growth of the country during the next eight years, especially the continued shift from the country to the cities and from the larger cities to their suburbs. Meeting the needs which existed at the beginning of the decade accounts for about 70 per cent of the 100 billion dollar estimate. Public construction needs, both the current ones and those which will develop during the period, are dominated by the estimated requirements for four types of activities—roads, schools, hospitals, and water and sewer systems—to the extent of more than 90 per cent of the total. Highway needs alone make up two-thirds of the total.

To cite these estimates of needs is not to say that all of them are of the same degree of urgency or that all of them will be met in the next 10 years. To begin with, the anticipated growth may not occur. As the chart indicates, present expectations are that school enrollment, metropolitan area population, and the over-65 population will increase by a fourth or more, motor vehicle travel by about two-thirds, and airport usage by as much as 300 per cent from 1950 to 1960.

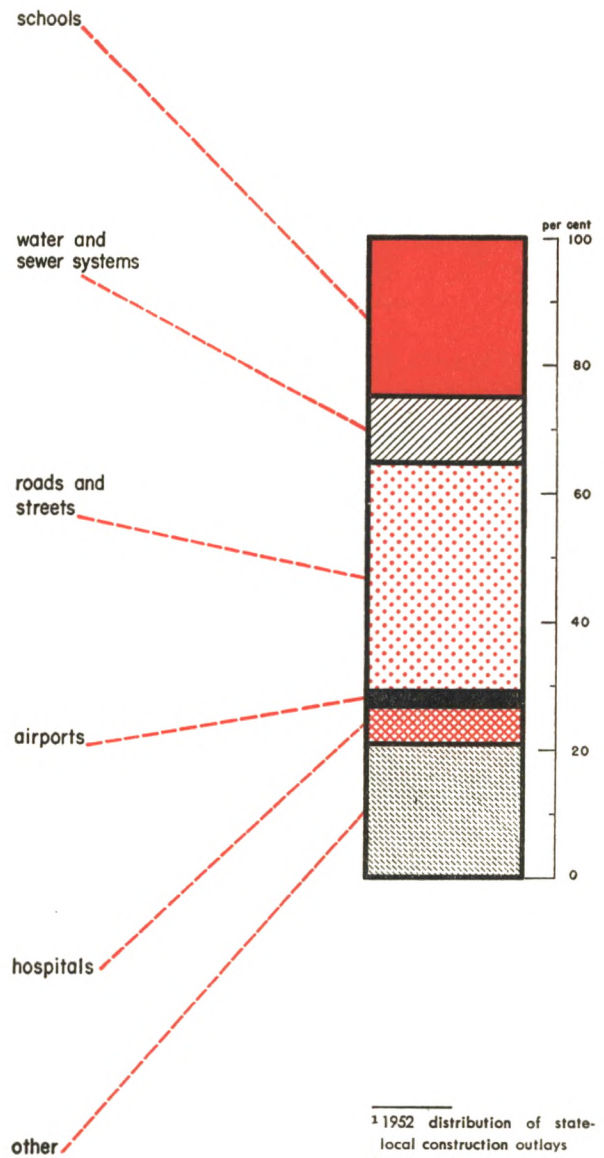
Basic demand for public facilities to rise during 50's

To maintain current standard, increases in . . .



will require greater outlays for . . .

which now account for most of state and local construction:¹



¹ 1952 distribution of state-local construction outlays
² vehicle miles travelled

Moreover, many of the needs created by normal obsolescence can remain unmet for some time with only minor inconvenience, if financial conditions so dictate. Even more important, any comprehensive listing of "needs" tends to include much that is *desired* rather than *required*, and this list is no exception.

Furthermore, to meet the over-all construction goals, the pace of state and local construction activity would have to be greatly accelerated—from the current rate of between 5 and 6 billion dollars a year to about 12 billion annually in the remaining seven years of the decade. Highway construction activity, in particular, would have to be increased to and maintained at more than three times its current levels.

Pressures vs. resources

Despite these qualifications, pressure to narrow the gap between standards consumers associate with private producers and the scope and quality of services they receive from state and local governments probably will be continuously applied in the next few years. However, existing methods of state and local finance are not apt to prove flexible enough to supply the resources needed for this vast expansion.

The small size of most local government tax bases is one serious limitation. The economy of a particular area may provide tax bases—sales, income, or property—large enough to support a much improved level of local government services. However, the geographic boundaries of few local government units encompass a whole economic area. In practice, most units cannot tax these bases heavily—particularly income and sales—without causing taxpayers to take the relatively easy steps required to avoid paying the higher taxes. That is, they can move their homes or businesses or legally shift taxable transactions to low-tax or tax-free sections of the same area.

Although there are some areas in which state-local tax burdens are relatively light and borrowing has not been used on a large scale,

notably the bigger centers in the Midwest, many state and local governments today are straining conventional methods of finance merely to maintain current standards of service. Generally speaking, more intensive use of existing tax sources directly or as a pledge for debt service holds forth little promise of really serious inroads into the backlog of needs.

New methods are developing which will help in certain areas. The levying of special charges for the use of facilities of a quasi-commercial nature has been growing. Charges for sewerage service, fees for the use of airports and other publicly-owned terminals, and toll financing of roads are the outstanding examples. Toll road experience, in particular, indicates how much users are actually willing to pay under a pricing system for superior facilities, since typical toll charges are equivalent to tripling the usual gasoline tax rate.

Another fiscal resource to support improved state-local facilities could come from possible reductions in Federal tax rates as the burden of defense spending eases. State and local governments should find it easier to increase their own tax rates particularly if Federal taxes on the same bases were cut, for example on gasoline, tobacco, or liquor. In a period of recession and declining over-all demand, moreover, the improvement of the state-local capital plant might be among the most acceptable and productive ways in which Federal spending through the grant-in-aid device would be used to offset declines in private spending.

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Country banks buy Governments

SINCE JUNE, country banks in the Chicago Federal Reserve District have been acquiring U. S. Government securities at a lively pace. In fact, their purchases of Governments from January through October 1952 accounted for fully half of the 600 million dollar net increase in Governments held by all U. S. member banks. This is the sharpest growth in Government holdings of these banks since the days of World War II.

Rural banks in Michigan and Iowa have led the parade of District purchases. Substantial net additions to holdings, however, have been reported in the outlying areas of every District state. A similar investment policy has been followed by many smaller urban and rural banks in the Great Plains and Far West areas during these months.

This is in sharp contrast to the record of larger city banks whose purchases of Governments were constrained by tight reserve positions and active loan demand. For example, the rate of increase in Government holdings of large District city banks during the first 10 months of 1952 was but half as great as in the country banks. This gap was narrowed in November only because large city banks bought substantial amounts of Treasury Tax Anticipation Bills for resale.

The sharp rise in net purchases by country banks does not represent an attempt to buttress previously slim Government portfolios. Even before the 1952 bulge in buying, they had more than half their total earning assets invested in Governments. As the year progressed, these banks have simply found themselves able to invest profitably in a Government securities market which has been conditioned by the tight position of larger banks.

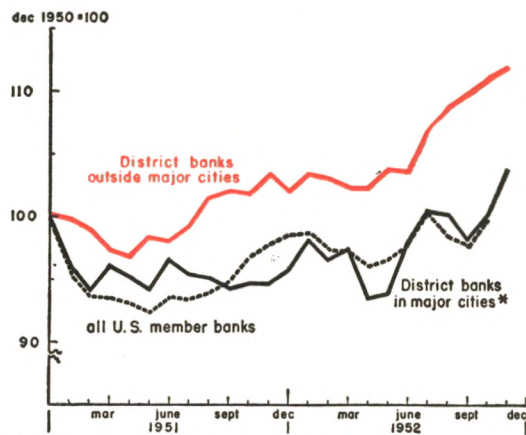
Country banks have had an unusually large volume of funds available to make Government purchases. The inflow of deposits into Midwest agricultural and smaller urban areas

this fall was the largest since 1947, and greater than in most other parts of the country. On the other hand, a spotty slackening of loan demand and a significant tightening in lending policies narrowed the chief competing outlet for their funds.

At the same time, there has been an increased market supply of relatively high-yield Government securities, particularly in the intermediate maturity range. The 2½ per cent six-year bond offered last July 1 and the newly eligible 2¼ per cent bonds of 1959-62 are issues in point. Smaller banks have poured a sizable portion of their investible funds into this section of the market. In the Midwest, country bank holdings of Governments with 5 to 10 year maturities rose 70 per cent during the first three quarters of 1952.

This shift in the emphasis of their lending-investing programs has given District country banks an increase in the size, a lengthening in maturity, and an addition to the yield of their Government portfolios.

Government holdings rise most in District country banks



* Chicago, Des Moines, Detroit, Indianapolis, and Milwaukee