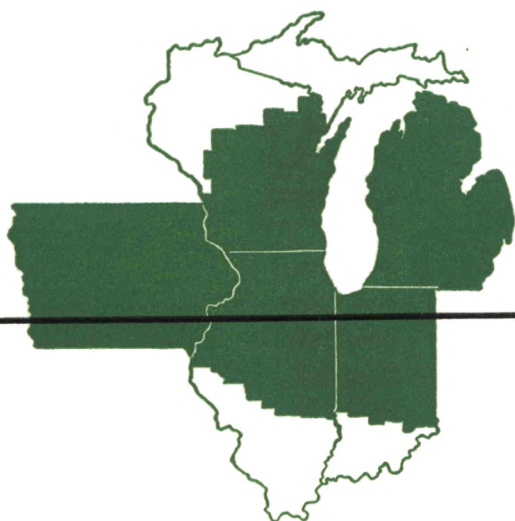


A review by the **Federal Reserve Bank of Chicago**

Business Conditions

1953 June



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THE Trend OF BUSINESS

A RECORD LEVEL OF BUSINESS ACTIVITY continues to be the watchword, as most business measures cling to new highs. Among Midwest industries, the chief exception has been the slackening in output of television sets and major household appliances, reflecting a substantial growth of inventories in these lines from the low point reached last summer. Few economic reverberations have appeared in the wake of last month's peace overtures, as final agreement continues to elude the negotiators at Panmunjon.

At the same time, it must be noted that the new business records of each passing month have been set by steadily slimmer margins. With industrial production 25 per cent above the low of last July, a number of lines appear to be crowding short-term limits in the form of plant capacity, work force, materials supplies, and, in some cases, product demand.

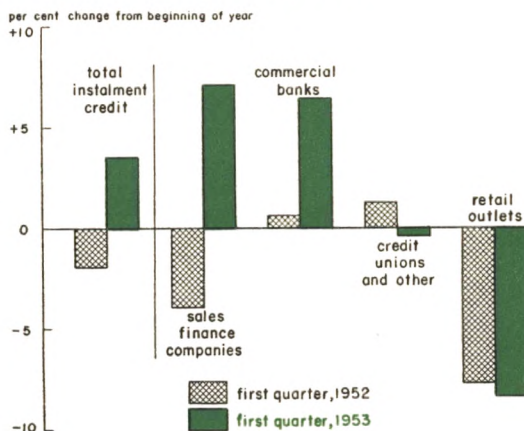
Strong demand for credit

That these limits have been stretched as far as they have is due in part to the continuing credit expansion of recent months. Consumers have relied in increasing degree upon credit in the purchase of durable goods. Businesses have been active in seeking funds to finance new plant and equipment and in borrowing to finance a build-up in inventories and trade receivables as well. Production, demand, and prices have been bolstered as a result.

In good part, this vigorous demand for funds has been met out of the vast flow of savings. But the competition for capital and credit, pressing against the financial markets, produced a flurry of increases in the cost of funds during the months of April and May. The nation's

prime borrower—the United States Treasury—found it necessary to offer a 3¼% coupon in its recent flotation of a billion-plus in 30-year bonds. At the short end, the May 7 issue of 90-day Treasury bills sold at an average yield of 2.35 per cent, 12 points above the 1952 high. In the mortgage field, increases were authorized from 4% to 4½% in the rate on mortgages insured by the Veterans Administration, and from 4¾% to 5% in the rate charged on mortgages insured by the FHA. Corporate borrowers also found that money came higher, a reflection of the fact that lenders were increasingly hard put to find enough free funds to meet demands. Banks, their reserve positions tight, raised the rate charged prime corporate borrowers on short-term loans from 3% to 3¼% in mid-April. By early May, top-grade

Sales finance companies lead in first-quarter consumer instalment credit expansion



corporate bonds in Moody's series were selling to yield 3.35 per cent, in contrast to a 2.99 year-end level.

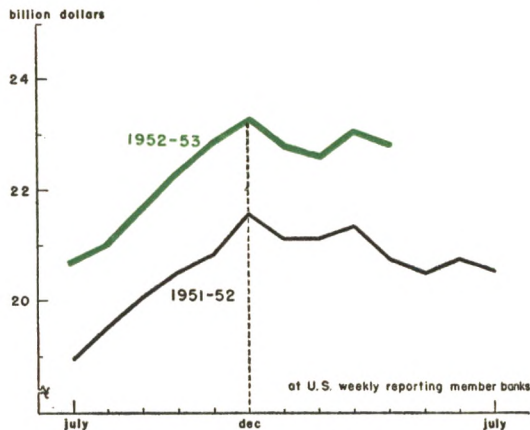
Some of these rate changes, of course, were simply formalizations of shadings in borrowers' costs and credit availability which had developed over a number of months. The exact impact of the tighter credit conditions this spring is impossible to measure. This much, however, can be said: if the net volume of credit demands denied or postponed has been substantial, then the nation has been spared an appreciable resurgence of inflationary pressure. At recent levels, production has had little room to increase to match a further ballooning of credit-based demand. Even with "tighter money," the magnitude of capital and credit extensions obtained by major types of private borrowers has been large indeed.

The rise in consumer instalment credit, uninterrupted since March 1952, shows no signs of abating. During the first quarter of 1953, 650 million dollars were added to the 18.6 billion outstanding at the beginning of the year. This contrasts with a drop of 290 million in the first three months of 1952. All of the net increase was accounted for by a rise in automobile paper, which jumped 300 million in March alone. Other consumer goods paper was paid off more or less in line with the usual post-Christmas trend, while instalment cash loans bulged during March as individuals sought assistance in meeting the demands of the tax collector.

Preliminary indications are that the increase in automobile sale paper is extending through late spring. Pressures for continued rapid growth will be strong, if the projected production of Detroit manufacturers over the coming months materializes. (A more detailed discussion of the relationships between credit and car sales appeared in "Financing the Family Car," *Business Conditions*, May 1953.)

Bank loans to business at the nation's leading banks have shown little of their usual seasonal decline since year-end. The drop in

Business loans stay high, show less than usual seasonal decline

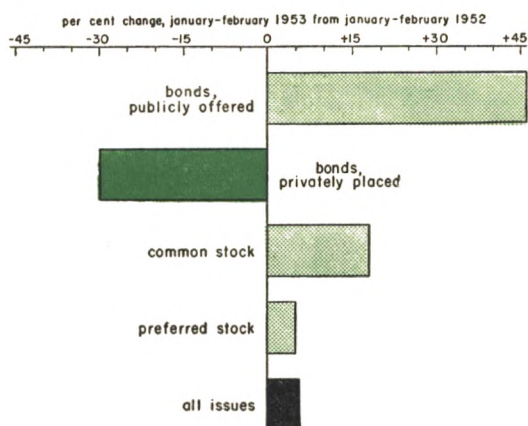


the first four months of 1953 was but 1 per cent, less than the 4 per cent decline of a year ago which itself was smaller than the historical pattern.

Borrowing to finance the increasing concentration of corporate tax payments on March and June 15 has played a part in holding up first-half loan totals. This year, however, a more important influence is the slowness with which many heavy seasonal borrowers have paid down their advances of last fall. At the end of April, net loan repayments by food, liquor, and tobacco processors were running one-third under last year's figures. Delays in the movement of fall and winter production into distributors' hands have been an important contributing factor. Sales finance companies, pressed by the rising demand for consumer credit, have not reduced their loans from large banks at all this spring. And in the case of trade firms, substantial new borrowing has appeared in place of the usual seasonal pay-offs of a year ago.

Some nonseasonal borrowers, such as textile, apparel, and leather concerns and public utilities, have also been adding to their loans much more than in the early months of last year. The chief exceptions are the metals and metal prod-

In new corporate security issues, biggest changes from year ago in bond placements



SOURCE: Securities and Exchange Commission

ucts industries. These firms are still substantial borrowers, but their 320 million loan increase between December and April was a far cry from the billion dollar rise of a year ago, when defense-purpose borrowing was of consequence.

New corporate security issues during the early months of 1953 appeared to be running about 5 per cent above year-ago volume, with the calendar of forthcoming offerings said to be the largest on record. Bonds continued to account for between three-fourths and four-fifths of total flotations. The volume of new bonds reaching the open market, however, was substantially higher than in the same period last year, as a significantly smaller proportion of issues was privately placed.

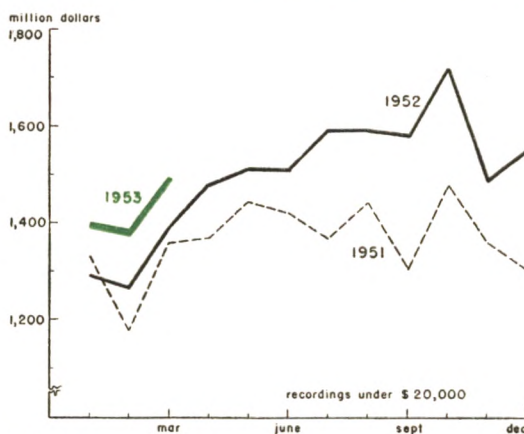
High new issue totals were recorded despite the fact that manufacturing corporations cut their securities offerings to less than half the comparable 1952 figure. The chief offset to this reduction came from the public utilities sector. During the early months of 1953, utilities issues were being offered in a volume double that of early 1952. Expenditures on new plant and equipment by utilities companies are continu-

ing a steady postwar rise and constitute an increasingly important demand for investors' funds.

Residential mortgage recordings, spurred by high construction levels during the mild winter, are also running at new record levels. The first-quarter total of recordings under \$20,000 was 4.4 billion, 12 per cent above the 1952 mark. Over one-half of this total was placed with savings and loan associations, the largest originators of mortgage loans.

As a result of the spring's activity, mortgage debt outstanding on urban one-to-four family properties is now over the 60 billion dollar mark. The level will rise further in the near future, despite a swelling flow of repayments. Starts of new nonfarm dwelling units are continuing at close to a 1.2 million annual rate. The recent increase in rates on mortgages insured by Federal agencies will increase the attractiveness of financing of both these new homes and the substantial volume of older homes changing hands. Consequently, mortgages may be a more rather than less effective competitor for investible funds in the months ahead.

Value of nonfarm mortgage recordings continues to top year-ago level



SOURCE: Home Loan Bank Board

Green light for auto output

*Flood of new cars to ebb in coming months;
tight labor markets to ease.*

FOR THE FIRST TIME in more than a dozen years the automotive industry faces a highly competitive market. Barring serious labor trouble or an unexpected revival of material restrictions, passenger car output in 1953 will be determined by sales volume rather than ability to produce. This spring the pressure of 150,000 new cars per week brought unseasonal declines in used car prices, shorter dealer margins, and anxious glances ahead by industry market analysts.

Business forecasters who, rightly or wrongly, look for lowered automobile output to signal the approach of a general letdown find impressive handwriting on the wall. Continuation of output at the May rate would mean over seven million new cars this year. Only the most brazen optimists expect that the market can absorb more than six million in domestic and foreign sales and larger dealer holdings.

The return to seasonal markets

In prewar years about 55 per cent of each year's automobiles were produced in the first half. As a result, car output declined 20 per cent from the first to second half of the average year. This pattern has been obscured heretofore in the postwar period as a result of unsatisfied demand and output restrictions.

If the 3.4 million car output anticipated by *Ward's Automotive Reports* is realized in the first half of 1953, some decline doubtless is in prospect for the following months. A spokesman for the Ford Motor Company has estimated that the industry can dispose of 5.5 to 5.7 million units for the year as a whole. This would mean a decline of 40 per cent from the second quarter rate of output. Such a development would be accompanied by sharply reduced automobile employment.

Most of the impact of a reduction in the rate of auto output would be felt in the Midwest. Michigan, Indiana, Ohio, Wisconsin, and Illinois account for about 80 per cent of all industry employment. Despite some decline over the years, Michigan alone still averages 55-60 per cent of the total.

The effect of the expected decline in automobile output will be softened to the extent that the current situation is one of "over-employment." Manufacturers report that a major block to larger production in recent months has been their inability to hire an adequate labor force.

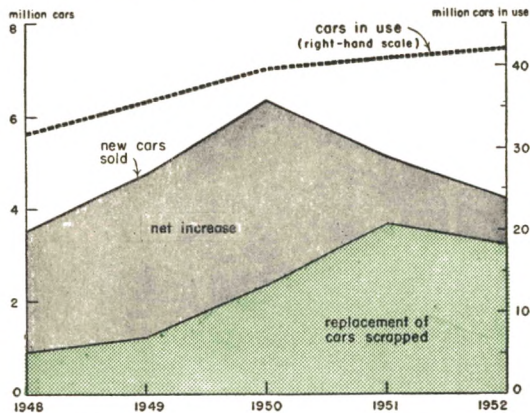
A drop in new car demand will not be welcome, but there will be some compensating benefits. Profit positions will be protected, in part, by elimination of high cost operations requiring the use of marginal workers, double shifts, and overtime. In addition, premiums now being paid for steel and other components would disappear.

Some months ago the prospect of a sizable decline in auto output in the second half would have been regarded with equanimity. The expected rise in employment and production in the numerous defense plants built and equipped by the automobile industry could be counted upon to take up the slack. Now, however, many of these orders are being cancelled or scaled down as a result of the Defense Department's move to economize on aircraft procurement. "Secondary" contractors of the Midwest will be affected more than proportionately by cutbacks.

Automobiles and jobs

At the present time, about 950,000 workers—approximately 5 per cent of all manufacturing employment—are engaged in producing

Slower growth in number of cars in use



SOURCE: R. L. Polk & Company

motor vehicles and parts. Several hundred thousand additional persons are making the materials used by these plants. In recent years almost 20 per cent of the nation's steel output has gone to the auto industry, as well as a substantial portion of all plate glass, copper, upholstery fabric, and rubber products. Altogether, motor vehicle production may account for 10 per cent of total industrial output.

If the auto industry is important to the nation as a whole, it is vital to several Midwest cities. Michigan centers with the largest motor vehicle employment are listed below, along with the proportion to total wage and salary workers in these localities as of March 15.

	Auto employment	Per cent of total
Detroit-Pontiac	426,000	31
Flint	50,500	45
Lansing	26,200	35

Obviously, many of the workers not employed in automotive plants are engaged in supplying the needs of those who are. Each of these cities, along with South Bend, Indiana, and Kenosha, Wisconsin, can be characterized

as "automobile towns." Their fortunes rise and fall with the demand for new cars.

The importance of a slowdown in automobile output to Michigan cities was exemplified in late 1951 and early 1952 when allocations sharply reduced allowable car output. Unemployment in Detroit alone was estimated at 121,000 in late 1951. In recent months it has touched a rock bottom of 20,000. In part, the tightened labor market has sprung from increased defense work, but the gain in civilian automobile production—up 51 per cent in the first four months of 1953 over the previous year—has been primarily responsible.

The great steel strike of last summer brought the automobile industry to a sharply slower pace as inventories were used up. Total employment skidded in July and August and did not regain the pre-strike level until mid-September.

Swings in industry employment are noticed earlier in Michigan and neighboring states because this region produces a large volume of parts and subassemblies which are shipped elsewhere for inclusion in finished vehicles. Most of the shift in the location of the industry away from District centers has resulted from the trend toward placing assembly plants closer to consumer markets.

Dealer stocks rising

New car stocks have been building up fairly rapidly in recent months. Despite production problems and good sales, *Automotive News* estimates that dealer inventories on hand or in transit rose by 205,000 to 580,000 in the first four months of 1953. Most of the rise in total retail inventories in that period was traceable to this factor. Averaging holding per dealer was 12.8 on May 1—a new postwar high—more than ample in some instances. Nevertheless, some major producers would like to see their dealers' holdings at a considerably higher level.

Larger dealer inventories, with more cars on the way, are in themselves a powerful stimulant to greater selling effort. One method is to

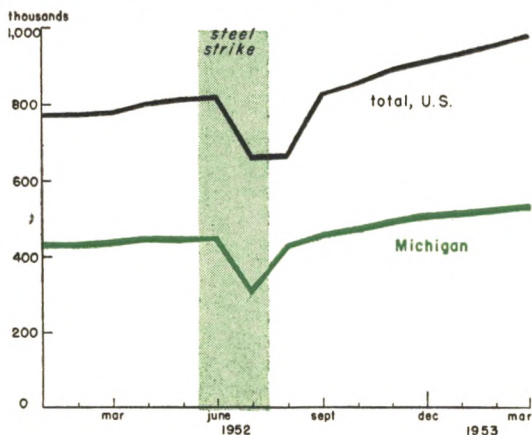
grant more liberal allowances for trade-ins. During the postwar period, dealers handling the more popular models have been in a pleasant position. Profits have been possible on both new and used cars. In the 1930's, it was estimated that most dealers merely broke even on car sales and depended upon sales of services and parts for their profits.

Any dealer can enjoy a sales upsurge based upon larger trade-in allowances than those generally available. On the average two or more used cars must be disposed of to complete the chain started by a new car sale. Apparent prosperity of some dealers may be unmasked by a growing stock of used cars. One large finance company has announced its intention to refuse to floor plan additional new cars for dealers who are accumulating too many older models.

Limitations of the "hard sell"

The return to "normal markets" and plentiful supplies is sometimes light-heartedly dismissed as merely requiring a revival of hard selling, more advertising, salesmen's contests, and the conversion of fledgling "order takers" to rough-and-ready merchandisers. Unfortu-

Auto employment has responded to changes in steel supplies



nately, such an approach oversimplifies the problem facing the automotive industry.

There are now over 42 million cars on the road, compared with 29 million in 1941. This means one car for every 3.8 persons as against a prewar ratio of 4.9.

Credit to customers and dealers, the lifeblood of the industry, is running thinner. Lenders are being forced to ration new credit extensions as a result of shortages of funds and some deterioration of the average risk.

The current annual output rate of 7.5 million passenger cars is a huge number by past standards. Before 1949 the industry had topped 4 million units only once—in 1929.

Stiffer competition may stimulate sales to some extent by slicing the fat from dealers' margins, trimming unwanted frills and equipment, or lowering manufacturers' prices. But the effect on total output will be limited. It was not flabby selling methods that allowed auto output to be halved between 1937 and 1938 or reduced assemblies to the 1.1 million trickle of 1932.

Vigorous merchandising methods, moreover, can be expected to draw blood. In the years just prior to World War II, one of every four car dealers annually turned in his franchise. During that period grand old names gradually disappeared from the ranks of the manufacturers.

Longer-run estimates of the passenger car market point to annual demand for about 4.5 million units (3.5 million replacement plus potential growth)—assuming fairly prosperous business conditions. Although capacity is ample to produce a much larger number, 4.5 million cars would represent fairly good business for the communities involved. The real danger to automobile output and employment is not market saturation, but rather the effect of a general business downturn which could reduce the market for cars to a fraction of the current level.

Farm price support

Present program to continue this year at least.

PRICE SUPPORT LOANS AND INVENTORIES of the Commodity Credit Corporation are mounting rapidly. At the end of March they totaled 3 billion dollars—77 per cent above the year-ago amount. Agriculture Secretary Benson has expressed fears that before the end of next year the entire 6¾ billion borrowing authority of the CCC will have been exhausted.

The value of price support extended on 1952 crops is now about 2½ times the amount committed at this time last year for support of 1951 crops. This is occurring in a period of full employment and strong domestic demand for farm products. The result has been a widespread discussion of farm programs, often suggesting that important changes are imminent.

This largely overlooks several important facts: (1) the present law extends current support levels through 1954, (2) the administration has pledged to administer the present law faithfully, and (3) there has been much support in Congress for the present program.

In a speech at Purdue University last month Secretary Benson said: "I'm not urging that we scrap our farm programs. There is absolutely no question of that. These programs have been built up by farmers and farm organizations, by Congress, and by the people. But . . . we need to fix the programs that are not doing the job for which they are intended."

Just what form the fixing will take is a matter of conjecture. In any case, it is unlikely that the present law will be changed substantially before the 1954 crop year. Meanwhile, we probably will see a more widespread use of certain parts of the program (acreage allotments, marketing quotas, etc.) that haven't been in the public eye for quite a while. It may be appropriate, therefore, to review the major features of the present structure.

Most people think of parity prices as *fair* prices. What is a fair price? One old-timer sagely observed that it is "20 per cent more than you can get." However, there is some reasoning behind the parity idea.

Parity prices

It is generally agreed that agriculture was left out of the prosperity that characterized the 1920's, and during the Great Depression of the early 1930's agriculture was severely depressed. Obviously, farmers were poor because farm product prices were "low." Some congressmen asked themselves if these prices could be raised and, if so, how high should they be.

From 1910 to 1914 there was a period of peace during which farmers were comparatively prosperous. Consequently, the level of agricultural prices between 1910 and 1914 was chosen by Congress as a goal for price-raising efforts.

This reasoning was upset by a very disquieting statistic: in 1930 (not a good year for agriculture) prices *received* by farmers were 25 per cent higher than the average from 1910-14. Further research disclosed the source of the difficulty: prices *paid* by farmers were 50 per cent higher. Hence, a bushel or hundred pounds of farm produce had a much lower purchasing power in 1930 than was the case in 1910-14.

The following pricing goal seemed obvious: at all times keep the prices *received* by farmers in the same relationship to prices *paid* by farmers as existed in 1910-14. So a formula was devised to turn out such "parity" prices for each commodity. As changes occurred in prices paid by farmers, parity prices changed. But at all times they gave each commodity the same purchasing power as it had in the so-called base period (1910-14).

As time passed, this pricing objective was

subject to more and more criticism. Parity prices for *different commodities* always stood in the same relationship to each other as existed in 1910-14. But since then there have been changes in cost of production and consumer demand for different farm products.

The Agricultural Act of 1949 provided a *modernized* parity formula that reflects changing conditions. That is, as time goes on, parity prices for different commodities change with respect to each other. However, the new formula still maintains the 1910-14 relationship between the *general level* of all prices received and paid by farmers.

Actually, the 1949 Act established a dual parity system, giving cotton, corn, wheat, rice, tobacco, and peanuts the privilege of using (for six years) either the old or the modernized formula, whichever gives the higher parity price. For other commodities, *transitional* parity prices were set up to cushion the drop where the modernized formula produced a much lower price than the old formula.

What per cent of parity?

The present law does not specify that any

commodity shall be supported at 100 per cent of parity.

Through the 1954 crop year, corn, wheat, cotton, rice, tobacco, and peanuts must be supported at 90 per cent of parity unless supplies become too large and producers reject production controls. After 1954, these commodities are to be supported between 75 and 90 per cent of parity, depending on the size of the supplies, provided producers have not rejected controls.

Price support within designated ranges is now required for the following commodities: milk and milk products, 75 to 90 per cent of parity; tung nuts, honey, and wool, 60 to 90 per cent. The Secretary of Agriculture decides where within these ranges the price shall be supported. Other commodities may be supported at the discretion of the Secretary.

Methods of support

Prices can be raised either by restricting free market supply or by expanding demand. The existing law provides for three general methods of limiting supply: (1) Commodity Credit Corporation (CCC) operations and production and marketing controls; (2) marketing agreements and federal orders; and (3) tariffs, embargoes, and import quotas. On the demand side the law provides for subsidies using funds derived from tariff revenues, appropriations for the school lunch program, and other funds.

For storable commodities (like corn) CCC makes nonrecourse loans. That is, the farmer stores his produce and pledges it as security for a loan.

Parity situation, April 15, for selected commodities

Commodity	Applicable parity formula	Effective parity price (dollars)	Announced level of support (per cent of parity)	Price received by farmers (per cent of parity)
Corn	old	1.77 bu.	90	82
Wheat	old	2.44 bu.	90	85
Milk	modernized	4.69 cwt.	90	94
Butterfat	modernized	.74 lb.	90	89
Potatoes	modernized	1.64 bu.	none	82
Beef cattle	modernized	21.00 cwt.	none	82
Hogs	modernized	20.30 cwt.	none	102
Chickens	modernized	.31 lb.	none	89
Eggs	transitional	.47 doz.	none	110
Turkeys	modernized	.38 lb.	none	87
Oats	modernized	.88 bu.	85	86
Soybeans	modernized	2.78 bu.	90	101

If he wants to repossess his produce, he pays off the loan. Otherwise, CCC has no recourse but to take possession of the produce. Perishable products (like butter) are supported by outright purchase by CCC.

Historically, the price support investment by CCC has been much larger than its realized losses from the program. From October 1933 through March 1953, CCC lost about one billion dollars—a small fraction of its total investment—through price support operations. But wars have conveniently bailed out CCC in the past, and it is not certain that this will happen again. Because there is a limit to the amount of commodities that CCC can accumulate, the law requires production controls—marketing quotas and acreage allotments—under certain conditions.

Marketing quotas are effected as follows: the quantity of a given commodity that will assure adequate supplies—the national marketing quota—is determined. This quantity usually is translated into equivalent terms of acreage. The national acreage is allotted among states, counties, and, finally, among individual farms. The marketing quota for an individual farm is the quantity produced on the acreage allotment. When quotas go into effect, the marketing of “excess” production is penalized.

Marketing quotas cannot be imposed until *current supply* reaches a specified percentage of what the law defines as the *normal supply* for the commodity in question. “Current supply” for any crop year is defined to be production plus carry-over into that year. “Normal

supply” is defined separately for each crop.

The Secretary must proclaim marketing quotas when the “current supply” of a field crop exceeds the “normal supply” by the specified percentage. However, the quotas do not go into effect unless they have been approved by two-thirds of the producers voting in a referendum. If quotas are rejected for corn, cotton, wheat, rice, or peanuts, the support level automatically drops to 50 per cent of parity and is provided only to those producers who comply with acreage allotments.

Other support methods

Another method of limiting supplies is marketing agreements. The law authorizes them for milk, certain fruits and vegetables, soybeans, hops, honey bees, and naval stores. Milk marketing agreements deal largely with the pricing of milk to producers. Fruit and vegetable agreements emphasize the regulation of quantities and grades marketed.

Tariffs, embargoes, and import quotas constitute still another method of restricting supplies. Import quotas are important in the support of sugar prices. A number of supported dairy products are now protected by embargoes against imports.

On the demand side, methods of support include subsidies for domestic consumption and exports. Section 32 of the Agricultural Adjustment Act appropriates 30 per cent of the gross receipts from customs duties for programs to encourage the domestic consumption and export of agricultural products. The present law provides that these funds be devoted to perishable agricultural commodities whose support is at the discretion of the Secretary.

The National School Lunch Act authorizes the USDA to provide assistance in the form of funds and food to states and territories for use in school lunches. Other support measures include the International Wheat Agreement and purchases under Mutual Security requisition.

Together, these various measures comprise the present price support program.

CCC price support investment, March 31

Commodity	Investment (thousand dollars)
Wheat	1,126,211
Corn	819,062
Cotton	321,742
Tobacco, rice, and peanuts.....	251,549
Butterfat and milk.....	100,757
Wool, honey, and tung oil.....	68,257
All other commodities.....	378,065

More trade! But how?

As foreign aid is reduced, the United States must either buy more abroad or face a drop in its export sales.

IN RECENT MONTHS, supporters of freer trade have been rallying their forces under the banner of *trade, not aid*. During the postwar period, dollar deficits of foreign nations were solved largely by U. S. economic assistance programs. Now, however, many feel that the time is ripe to re-examine the nation's foreign economic policy and modify it in the light of changing world conditions. The proponents of increased U. S. imports believe that our economic and political interests can best be served by adopting a policy to promote, rather than restrain, the international flow of goods.

Foreign aid finances deficit

From 1946 through mid-1952, foreign nations accumulated about a 34 billion dollar deficit on total international transactions of 113 billion and exclusive of military goods sent or purchased by the U. S. for the use of other countries. Over 30 billion or 90 per cent was covered by U. S. foreign economic aid in the form of loans and grants. In the last two years the annual shortage of dollars has been reduced, partly, however, as a result of such temporary factors as import restrictions and quotas. It seems likely, therefore, that balance of payments difficulties will continue to plague a number of foreign countries, particularly if military aid and expenditures abroad for goods and services are cut down.

As U. S. foreign aid programs are reduced, the resulting "dollar gap" could be closed by any combination of three possible courses: more exports by the U. S., more imports to the U. S., or an increase in the rate of U. S. investment abroad. The latter alternative seems least likely to be a material factor in meeting the current situation and, of course, in the long

run must depend on the prognosis of an increase in trade.

Either of the remaining alternatives—a decrease in U. S. exports or an increase in imports would have some depressive effect on general business activity. But the impact would be concentrated on limited segments of our economy. If trade barriers were lowered, the protected industries would find themselves confronted by more intensive foreign competition and limited prospects for expansion, if not outright contraction.

On the other hand, a shrinkage of exports would cause production cutbacks and reduced employment in the exporting manufacturing industries and would have far-reaching effects on several important agricultural commodities. The importance of foreign markets to Midwest industry and agriculture was discussed in the May issue of *Business Conditions*.

A decline in export sales would hit our most efficient industries—those in which U. S. production advantages are the greatest. Domestic products that compete with imports generally are those in which we have least relative advantage. This, judged alone, although difficult to evaluate quantitatively, should throw the balance in favor of measures designed to maintain the present level of exports.

An easy choice

But go one step further, say the "trade, not aiders," and the choice will be much clearer. A third group—the consuming public—is also directly affected by a nation's trade policy. International trade is based on the same principle as trade between individuals or between regions within a country. Both parties to an exchange gain by having each specialize in the

production of the goods which he produces most efficiently in relation to the other producer.

More trade among nations means that benefits can be realized from specialized natural endowments—climate, resources, soil, and the like and special talents and skills that may be found in certain areas or regions. Consumers and producers would be able to buy at lower prices than would prevail with restricted trade. Moreover, the general level of real income in all trading countries—the amount of goods and services available in the market place—would be increased. Thus, the supporters of increased imports argue that in order to maximize the general economic welfare of the U. S., we should adopt policies that promote, rather than restrain, trade.

To moderate severe shocks

A number of recommendations and suggestions have been offered to facilitate adjustments in import-competing industries. Among the recommendations made in cases where sharp reductions would cause great hardship are (1) a gradually lowering tariff, (2) temporary industry subsidies, (3) preference in defense contracts, and (4) government assistance to both industry and labor to adapt to the production of new, more profitable lines. Free traders point to the fact that throughout its history, U. S. industry has had to readjust to changing conditions. The continued introduction and acceptance of new products and cheaper processes have been a major factor contributing to our industrial strength.

Our trade policy has been liberalized considerably since the Reciprocal Trade Agreements program was instituted in 1934. Since then, the average level of duties on dutiable imports has been reduced from 25.8 to 12.5 per cent. Thus, the rates of the Smoot-Hawley Tariff of 1930 have been virtually sliced in half. Imports in both 1951 and 1952 totaled about 11 billion dollars, as compared with 2.4 billion in 1939 and only 6 billion as late as 1947. The physical volume of U. S. imports has increased by 60

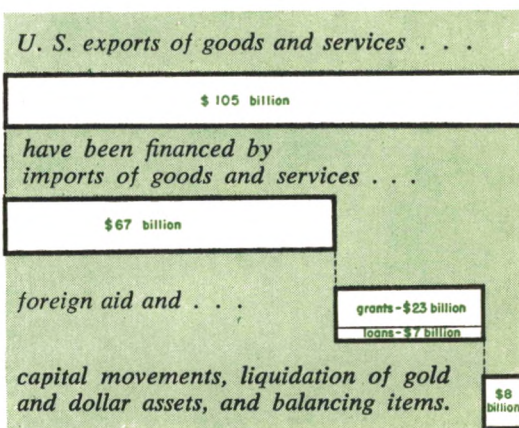
per cent since the immediate prewar period.

Yet, our imports presently are a smaller percentage of national income than they were in 1929. Some tariffs are still as high as 200 to 300 per cent of the value of the product. In addition, trade is hampered by quotas, Buy American provisions, tying clauses in foreign aid laws that require goods financed by loans and grants be purchased in the United States and shipped in U. S. bottoms, and by antiquated customs procedures that serve to confuse and thwart the foreign exporter.

Confusion deters trade

It is often charged by the proponents of freer trade that one of the most effective obstacles to the importation of foreign goods, and one that is difficult to measure in quantitative terms, is the overwhelming uncertainty confronting a foreign manufacturer who considers selling in the U. S. market. First, he must try to anticipate the classification of his product by the customs officials. For example, there are 12 different rates on wool and worsted fabrics. Dolls and toys merit 11 different rates on very similar products. Moreover, the valuation pro-

Foreign aid finances large share of U. S. postwar¹ exports



¹fiscal years 1947-1952

cedure is frequently as baffling and confusing. Over three-quarters of a million customs entries are awaiting classification and valuation, and about 80,000 undecided classification cases and a similar number of contested valuations are now on the dockets of the Customs Court.

A move to eliminate some of these difficulties has resulted in the Customs Simplification Bill that has been introduced in Congress. Last year the House passed a similar bill, but it was not acted upon by the Senate. The proposal has received broad support from business leaders throughout the country.

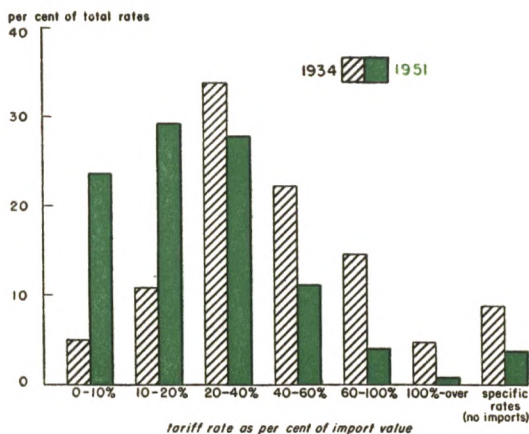
Additional barriers to trade

Probably the greatest uncertainty confronting foreign businessmen who might attempt to develop a U. S. market for their products is the constant fear that some day they will, with little notice, be cut off from access to their U. S. customers. Although duties have been sharply cut, the lower rates have never been enacted into law. If after the tariff concessions have been made the Tariff Commission determines that the influx of a product from foreign sources is causing "serious injury" to a domestic industry, the President has the authority under the "escape-clause" provision to withdraw all or part of the concession. Thus, the foreign exporter may suddenly find himself excluded from the U. S. market. As a result, claim the advocates of more imports, foreign businessmen are discouraged from making the necessary expenditure to establish their products in the U. S.

The same principle applies to agricultural commodities. Under Section 22 of the Agricultural Adjustment Act, the President is authorized to impose fees or quotas on any farm product entering the U. S. "in such quantity . . . as to interfere with any program administered by the Department of Agriculture." Since 1951 this Section supersedes all other trade agreement provisions, old as well as new.

In recent months, the conflict between domestic farm support programs and efforts to promote world trade has been vividly demon-

Over half of tariff rates now under 20 per cent



strated. With the production of agricultural commodities increasing in both the exporting and importing countries, the prices of many farm products in world markets have dropped below U. S. support levels. As a consequence, foreign countries have turned to other, cheaper suppliers for such products. Furthermore, we have set up barriers to the flow of foreign farm products into the U. S. when it interfered with a support program. Thus, the conflict inherent in the objectives of expanding foreign trade and of price maintenance in domestic markets is seen, along with the tendency to resolve such conflicts in favor of the domestic programs.

Tariff reduction limited

The supporters of free trade also point to other obstacles that tend to slow down or diminish the flow of goods into the U. S. Of major importance is the limitation on tariff reductions in our present Reciprocal Trade Agreements Act. The President has the authority to lower the duty on any product by no more than 50 per cent of the 1945 rate. Furthermore, according to a 1951 amendment to the Act, before making a tariff concession the

Average duty rate reduced

Year	Customs receipts as per cent of dutiable imports
1938	39.3
1941	26.8
1947	20.1
1949	13.8
1951	12.5
1952 (9 months)	12.9

President must await a Tariff Commission report fixing the level below which a duty cannot be cut without "causing or threatening serious injury to the domestic industry producing like or directly competitive articles." If he makes a concession beyond this "peril point," the President must explain his action to Congress.

The proponents of freer international movement of goods also attack two other legislative restrictions on trade. One is Section 104 of the Defense Production Act of 1951, sometimes referred to as the "cheese amendment." Under this provision the President is authorized to set up quotas on imports of items such as fats and oils, dairy products, peanuts, and rice if imports of these products reduce or impair domestic production of these commodities below the level that the Secretary of Agriculture thinks is necessary "in view of domestic and international conditions." Under this Section, controls were imposed on cheese imports although the U. S. was then selling more cheese abroad than it purchased from other countries.

The Buy American Act, passed during the depression period, has also come in for a good deal of criticism. This Act provides that all government purchases must be made from U. S. producers, unless the price quoted by domestic manufacturers is more than 25 per cent higher than that of foreign firms. This has led to the anomalous situation of the U. S. Government giving economic aid to foreign countries to finance their import surplus, but yet unable to reduce the need of those countries for aid by

the purchase of less expensive goods from them.

Public policy shaping up

In the next few months, the U. S. will have to make a number of important decisions concerning the future course of its foreign economic policy. President Eisenhower has requested 5.8 billion dollars in foreign aid funds for the 1954 fiscal year, a drop from 6.5 billion the previous year. And Congress may cut these appropriations even further. As a result, the issue of whether to promote the importation of foreign goods or let U. S. exports decline will be hotly debated.

The Administration has requested that the Reciprocal Trade Agreements Act be extended in its present form for a year to permit a thorough study of our foreign economic policy. The bill that Congress is now considering, however, seeks to add restrictive amendments to the extension of the Act. Presidential action in regard to the peril point provision and the escape clause would be mandatory upon recommendation of the Tariff Commission. In addition, it is proposed that a quota be set on oil imports and a sliding-scale duty put on U. S. purchases of lead and zinc. Meanwhile, the advocates of a higher level of trade will be pushing for an immediate liberalization of U. S. foreign trade policy. Although the impending political decisions will determine the direction of international trade policy in the months ahead, their major economic effect will be felt in the years ahead.

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Savings bonds *continued from page 16*

the debt ownership among the millions of small savers in the country—the development may mark a return to the original idea. (Over 43 million individuals now own E bonds.)

The timing of this renewed emphasis on E's is fairly auspicious. For after 32 months (beginning May 1950) of continually running in the red, E bonds became a net source of cash for the Treasury in the first quarter of 1953, although they ran a deficit again in April. The improved performance stemmed both from increased sales and decreased redemptions. The pickup in sales began to show up somewhat in the latter months of 1952.

The improvement which took place in E bond sales vs. redemptions in the first quarter, however, appears to reflect a somewhat temporary development. January, February, and March typically produce a seasonal high in savings bond sales each year. This is generally assumed to reflect lump-sum purchases by larger investors of the maximum amount legally permitted to be acquired by any single investor in a year. When the terms of E bonds were revised in mid-1952, this maximum was raised from \$10,000 to \$20,000 per year.

In the early months of 1953, sales of large denomination E bonds showed a gain of more than 20 per cent over the comparable months of 1952, while in the same period sales of the smaller denominations (under \$500) increased by less than 3 per cent. To the extent that this reflects the lift in the maximum, sales through the remainder of the year may not continue at the improved pace.

Headway seems to have been made, however, under the Payroll Savings Plan. The latest estimate indicates that some 7,900,000 individuals are currently buying E bonds in this fashion, an increase of 1½ million over 1951. Current monthly deductions for bond purchases average \$20 per person, which would mean that roughly half of all E bonds now sold are acquired through the payroll deduction device. But these smaller denomination bonds also ex-

perience the greatest attrition—somewhat more than half of them being cashed in within a year of purchase. Sales in this area, therefore, have to be considerably expanded in order to produce a lasting gain for the bond program.

The drain of maturing E's

Another factor, also on the redemption side of the picture, will assume increasing importance in determining the future of E bonds—namely, the redemption of *maturing* issues. From May 1951 when E bonds began to mature through the end of 1952, some 4.9 billion dollars of these bonds reached maturity. Of this total amount, 1.2 billion—less than 25 per cent—were redeemed. The remainder have been held under the optional extended maturity—except for an insignificant amount which were exchanged into Series G bonds. The 25 per cent redemption ratio also continued in the first four months of 1953. As small as this proportion appears, had it not been for the redemption of these matured issues, the E bond program would have shown net sales not only for January, February, and March of this year but for April, as well as the last five months of 1952.

Even if there is no increase in the *rate* at which holders redeem their matured bonds (this rate has remained surprisingly constant), the growing volume of maturities in the months ahead will pose a problem. Of the 36 billion dollars in E bonds currently outstanding, a total of 5.1 billion will mature in 1953, and maturities will reach a peak of 5.6 billion in 1954. Assuming that the 25 per cent redemption ratio continues, an estimated 900 million dollars of these matured bonds will be redeemed from May through December of this year and an additional 1.3 billion in 1954. These amounts may well run in excess of the current edge of sales over unmatured redemptions. For the Treasury to overcome this hurdle, therefore, the recently improved E bond sales will have to expand even more in the months and years ahead.

Operation savings bonds

With the problem of F and G maturities disposed of, the Treasury will now concentrate on more and more E bonds.

ANOTHER PRESCRIPTION for what-ails-savings-bonds was drawn up and administered a month or so ago. Prepared by a new doctor, the prescribed dosage was designed to ease any degenerative effects resulting from the beginning maturity of Series F and G bonds. The medicine was simple and as effective as could be anticipated. It offered holders of F and G bonds maturing in 1953 the opportunity to exchange their holdings into the new 30-year, 3¼ marketables. By May 1, the date the exchange offering closed, some 419 million dollars of the maturing 1.1 billion were exchanged; the remainder will be paid off in cash as they mature.

In a sense, the remedy was more in the nature of surgery than a shot in the arm. Insofar as the bonds are exchanged for other Government securities, the total amount of Treasury borrowing remains, of course, unchanged. Whether the bonds are cashed in or exchanged, however, the over-all *savings bond* program as such will experience a resultant cutback. Should the Treasury continue this policy for F and G's maturing in the years ahead, the size of the cutback will be substantial. Of the 58 billion dollars of savings bonds now outstanding, almost 23 billion—39 per cent—are F's and G's, and well over 2 billion dollars of these issues will mature in each of the next seven years.

The Treasury will continue to sell F and G (now J and K) bonds. But since early 1951, monthly redemptions (all prior to maturity) of both Series F and Series G bonds have exceeded sales. Even the improved terms offered via the J and K series since May 1952 have not increased the monthly sales volume. In 1953 the public cashed in 350 million dollars more of

these bonds than it bought; in 1952, 325 million more. The obvious conclusion is that institutions which, during the war years, acquired the bulk of F and G bonds have now found alternative, more favorable investment opportunities for the use of their funds.

E's to carry the load

As a result of this turn of events, the Treasury recently announced that the promotional activity of the Savings Bond Division will be "concentrated exclusively on the sale of Series E and H savings bonds." Since E bonds are most closely akin to one of the major objectives of the savings bond program—spreading

—continued on page 15

In the first quarter of 1953, E bonds provided funds for the Treasury—after a 3 year steady cash drain

