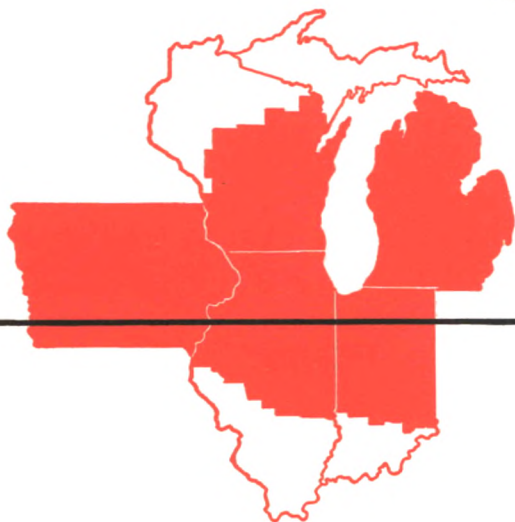


A review by the **Federal Reserve Bank of Chicago**

Business Conditions

1954 May



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THE Trend OF BUSINESS

Spring has yet to bring forth any clear signals of a halt in the downdrift of business. There are some suggestions that the rate of decline is slowing, but movements in a good many of the more popular indicators of activity have been blurred by a welter of seasonal influences.

Unemployment, for instance, has risen only moderately since the sharp increases in January and February. Yet this development looks less favorable when compared with the substantial seasonal declines which ordinarily occur in March and April. On the average for the past six years unemployment has declined 240,000 and 280,000, respectively, in these months.

In another sector, seasonal influences have alternately exaggerated and concealed a lagging trend. Department store sales, after running

11 per cent under year-ago figures in March, jumped ahead in early April. These fluctuations stemmed largely from the fact that the Easter buying season came two weeks later this year. Allowing for Easter, department store sales this year to date have been about 4 per cent below 1953 levels.

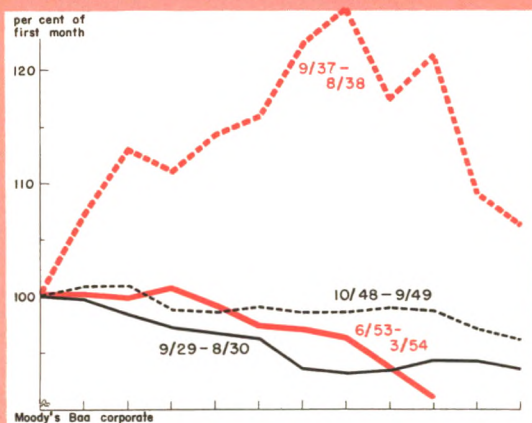
Generally speaking, in most areas of the economy which experience a spring resurgence of activity, the pickup this year is smaller than usual; and in those lines for which spring is the slow season, the letdown this year is greater than last.

Interest rates decline

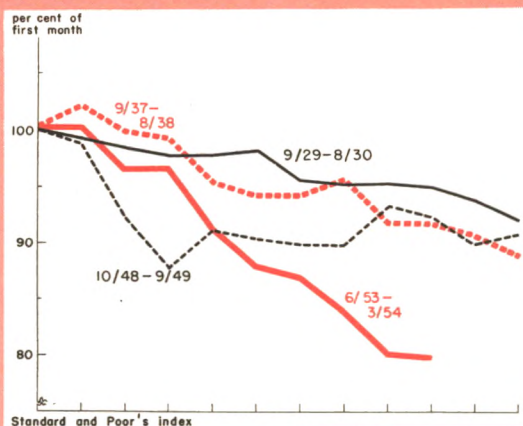
The slower pace of business is being reflected in the credit markets. Net private borrowing demands are smaller, and with inflows

Interest rates: down more than in previous recessions for

medium-grade corporate bonds . . .



high-grade municipal securities . . .



Note: Monthly averages of daily market yields, expressed as a per cent of the average for the peak month in business activity.

of savings remaining high, financial institutions have more funds at their disposal to accommodate demands.

The lending ability of institutions has been further heightened by actions of the monetary authorities. Since June 1953, the Federal Reserve, in moves to adapt monetary policy to the changing pace of the economy, has made reserves abundantly available to the banking system. As these funds percolated through the financial system, eased credit conditions developed in most sectors of the market. Indicative of this, interest rates began declining substantially after the middle of last year and have continued to move downward through the early part of 1954.

Particularly for longer-term securities, the reduction in market yields has proceeded more rapidly than in any of the three previous periods of business downturn. Such rate changes, themselves a result of eased conditions, have brought sufficient market price increases in outstanding issues to erase most of the "book losses" in investor portfolios. As a result lenders feel freer to make shifts in their holdings of loans and securities. In this environment prospective users of credit are finding

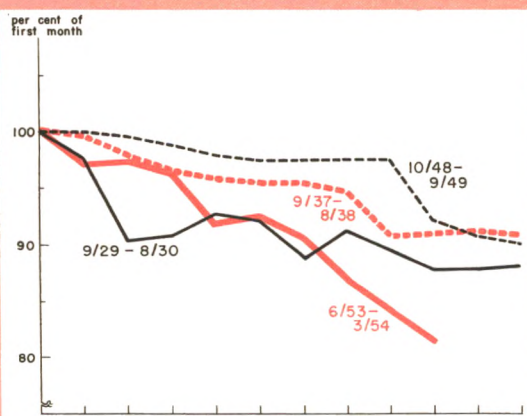
borrowing costs lower and some terms easing, an incentive to both borrowing of new funds and refinancing of outstanding forms of indebtedness.

The most persistent borrowers of new funds in the long-term capital market have been state and local governments. Faced with pressing construction needs, they have floated new security issues in unreduced volume. Such offerings ran at a 400 million-a-month pace during the first two months of the year.

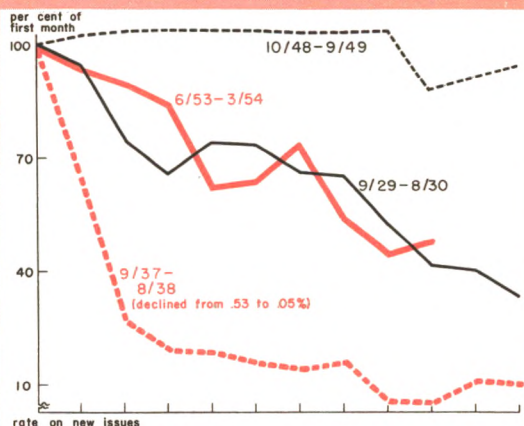
Corporations, on the other hand, are tapping the long-term market for new funds in smaller volume than last year. The drop in new offerings is most substantial among manufacturing concerns and financing institutions. Public utilities, in contrast, are planning borrowing programs which will raise about as much money this year as their 3 billion 1953 total.

In the shorter-term area, the commercial paper market has experienced a considerable pickup in activity. Top-drawer businesses have been selling their own notes, both privately and in the open market, in place of borrowing from banks. The purpose: to take advantage of the more than 1 per cent differential between the commercial paper rate and the 3 per cent bank

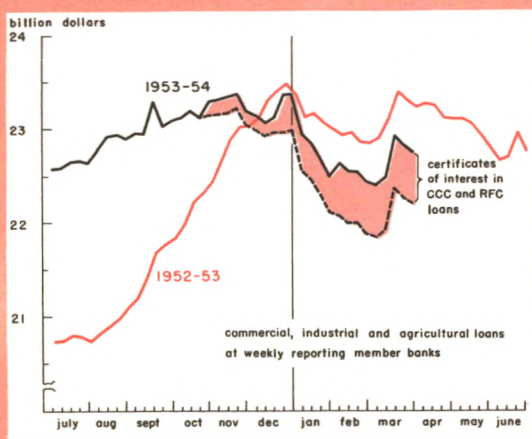
long-term Governments . . .



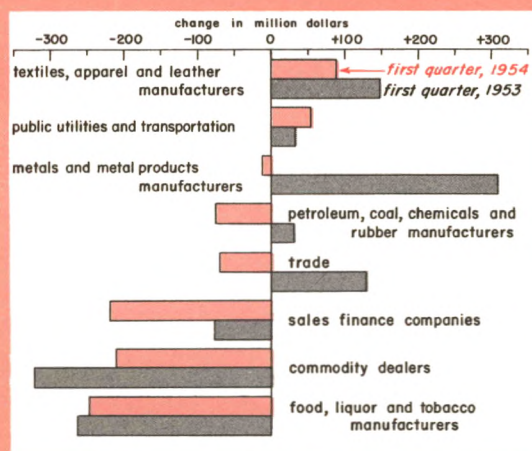
and short-term Governments, except 1937-38



Business loans have slipped below year-ago levels since November—but bank investment in CCC and RFC certificates has cushioned the decline.



Most major industries are paying back bank credit this spring. Biggest change from year-ago demands are in metals, trade and sales finance concerns.



First-quarter change in commercial loans, by industry, at leading banks

loan rate. Sales finance companies have been particularly active on this score.

Less business borrowing

Business loan totals at leading banks reflect the reduced borrower reliance on bank credit. After touching a fall peak of 23.4 billion on December 30, commercial, industrial and agricultural loans at weekly reporting member banks slid off 666 million through April 7. During the same season last year, the net drop was only 93 million.

Loans in March underwent a sharp but temporary rise as firms turned to banks for cash to make tax payments. A more persistent influence buoying loan totals, however, was bank investment in Commodity Credit Corporation and Reconstruction Finance Corporation certificates of interest. Both these Governmental agencies have established "pools" of loans against which they have sold certificates of interest. Through April 7, the nation's leading banks acquired about 600 million of these certificates, one-third of these after the first of the year. Without such acquisitions, the business loan figure in early April would have stood more than a billion dollars below the level of a year ago.

The drop since year-end in the total of private business loans at leading banks was in part a repetition of the usual seasonal pattern. Food, liquor and tobacco processors and commodity dealers, the major seasonal borrowers among American businesses, have paid back 360 million of the loans obtained last fall. For these concerns, however, the reduction was some 200 million smaller than in the first quarter of last year. Partly this was a result of their smaller loan demands to purchase agricultural products last fall, but partly also it reflected a slower liquidation of inventories of crops and processed products.

Among nonseasonal borrowers, metals and metal products producers exhibited the sharpest change in loan demand between this year and last. In the first quarter of 1953, such concerns borrowed 310 million in additional funds from leading banks; in 1954 the com-

parable figure was a 10 million net paydown. Other basic producers such as oil, coal, chemical and rubber firms also were making net repayments of bank lines whereas last year they were adding to borrowings. To some extent, these reversals in net credit needs are related to completion of plant expansion programs and refinancings of bank debt with marketable securities. More importantly, businesses are generating more funds internally than ever before, through retained earnings, depreciation allowances and liquidation of inventories.

Some of these same influences can be traced in the borrowing patterns of firms operating at the wholesale and retail level. A shift in inventory position apparently lies behind the moderate reduction of loans by wholesale and retail establishments since the beginning of 1954. Refinancings of bank debt into other forms have played a role in the decline of bank borrowings of sales finance companies. The latter concerns have cut their bank lines by over 200 million since the first of the year. This decline has been shaped by more than simply the availability of cheaper credit elsewhere, however; finance companies find themselves with a reduced need for funds because of the decline in instalment demands of consumers.

Auto loans slacken

Total consumer credit, after climbing to an all-time peak in December, dropped more rapidly in the first two months of 1954 than in any other postwar year. Over half of the 1.4 billion decline was in non-instalment credit, representing a somewhat larger than usual retirement of charge account balances built up during the Christmas season. The 650 million drop in instalment credit centered in contracts for the purchase of consumer durables. This was the first reduction in such outstandings since March 1952. It stemmed primarily from lower extensions and higher repayments of automobile credit.

Although used car sales were running close to last year in terms of number, credit require-

ments were reduced because of price declines ranging up to 25 per cent. In the new car market, list prices were little changed, but the number sold was about 10 per cent below a year ago. Moreover, in the average car sale, an increased proportion of the total price was being covered by cash and trade-in allowance. The combined effect of these influences caused a 4 per cent drop in the total of automobile paper outstanding during the first two months of this year.

Active demand for mortgages

Mortgage lending on residential properties has thus far held closer to 1953 levels than has any other major type of private credit extension. In the first two months of 1954 mortgage recordings on nonfarm properties selling for \$20,000 or less matched last year's record pace.

With new housing starts running throughout the winter at a more than one million seasonally adjusted annual rate, mortgage originations from new home purchases are continuing high. In the market for existing homes, however, some softening in prices is paring the dollar volume of mortgage credit. Another dampening influence on the growth of total outstandings is the swelling volume of repayments on the almost 50 billion addition to residential mortgage indebtedness since the end of World War II.

Declining rates of return on other investments have given some impetus to real estate lending. As market yields on corporate and Government securities have declined, the prevailing fixed rates on FHA- and VA-insured mortgages have become increasingly attractive to investors. One indication of this is the fact that private marketings of mortgages at a discount, the rule a year ago, have now become an exception. Somewhat lower rates and longer terms than were customary six to eight months ago are now generally available to qualified borrowers. Mortgage money for new homes is easily obtainable in most urban centers. This easier credit situation will be a sustaining force for residential construction in the months ahead.

Agriculture provides diminishing share of the nation's income, now about 6 per cent of the total

Agriculture is a declining industry." Considerable reaction and some resentment greeted this statement by a prominent agricultural economist a few years ago. In terms of production efficiency or volume of output, the statement is untrue; but in terms of agriculture as a share of the total economy, and this is the context in which the idea was presented, the statement is correct.

The share or shares

The importance of agriculture to the economy is measured in a number of ways. It may be measured by the proportion of the population or of the work force that it supports. In an economic sense, however, the importance of an industry can best be measured by its contribution to the total income produced.

	Agriculture's share		
	1929	1941	1953*
	(per cent of total)		
Population	25.1	22.7	15.5
Employment	22.0	18.1	10.5
National income	8.9	8.3	5.5
Personal income	9.8	9.7	6.0

* Estimated

SOURCE: U.S. Departments of Agriculture and Commerce

The three years in the table were chosen for several reasons. They are years of relatively full employment, separated by equal time intervals. And in each of the three years the prices of farm commodities had about the same relationship to prices of other goods and services. The striking difference between the four measures calls for an explanation.

What is a farm? Or a farmer?

The Bureau of the Census defines a farm as a place of three or more acres on which the

value of agricultural *production* (exclusive of home gardens) is 150 dollars or more per year. The agricultural products can be either for home use or for sale. Places of less than three acres are counted as farms if the value of *sales* of agricultural products amounts to 150 dollars or more.

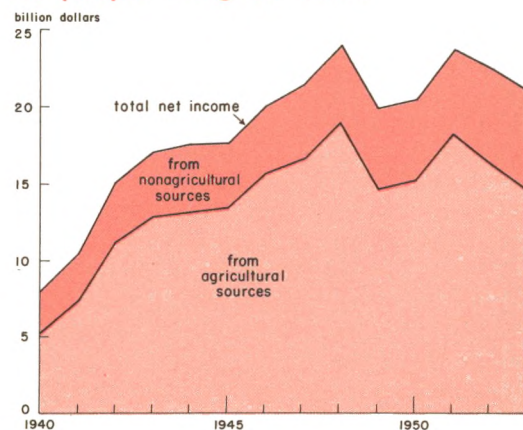
Obviously, this definition includes many tracts of land that are not customarily thought of as commercial farms. For example, it includes a large number of plots that are primarily residences, as well as many part-time farms for which the farming operation is a minor part of the economic activity of the family. In 1949 these noncommercial "farms" comprised almost one-third of all farms counted by the Census. This is part of the explanation for the fact that whereas 15 per

Economic class of farm	Percentage of all farms, 1949
Commercial	69
Part-time	12
Residential	19

cent of our population lives on farms only 5½ per cent of the national income originates in agriculture.

A "farm worker" is defined as one who does

Nonagricultural sources have provided a growing portion of income for people living on farms



any work on a farm for pay or profit during the week the survey is taken or who worked on the farm without pay for 15 hours or more during that week, provided that the number of hours worked on the farm is greater than the hours worked in some other industry. This definition includes many people on part-time and residential farms. Thus, an important part of agriculture really is a halfway house, or transition stage, between farm and nonfarm activity. In this respect it may be noted that the large number of part-time and "under-employed" workers in agriculture, in combination with the limited amount of land and equipment with which many of them work, results in a much smaller *average* value of products produced per man than in most other industries.

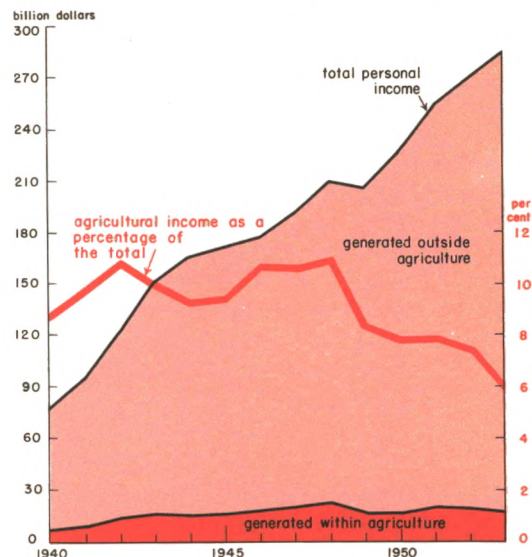
Farm income or income of farmers?

"National income" originating in agriculture is the net value added to production by farming activity, *valued at going prices*. It is equal to the excess of the market value of agriculture's products and the subsidies it receives over the sum of the following costs: purchases of goods and services from other enterprises, depreciation charges, and taxes on farm property. In 1953 it accounted for 5.5 per cent of the national total. This, however, is not a measure of the income of people living on farms.

In 1952 more than one-fourth of the net income of people living on farms was derived from nonagricultural sources. In the past decade this proportion has shown some tendency to increase as earnings from off-the-farm jobs have become more important. The *total* net income of farm operators and workers residing on farms amounted to about 7 per cent of the national income in 1953.

Just as the farm population receives part of its income from nonagricultural sources, so also does the nonfarm population receive part of the income which originates in agriculture. Personal income from agriculture—as an industry—includes the net income of farm operators, wages paid farm workers and net rent and interest payments on farm land and loans. This probably is the best measure of the role

Agriculture produces a declining proportion of total personal income



of agriculture in national economy. Six per cent of the nation's personal income in 1953 originated in agriculture.

Agriculture and economic growth

Agriculture's diminishing share of the nation's business reflects the fact that for many years other industries have expanded faster than farming. Although the desirability of this trend has been questioned on occasion, back-to-the-farm movements have never received wide support except in periods of depression when urban jobs were scarce. Actually, a declining share for agriculture is consistent with and even necessary for the achievement of rising levels of living for the nation as a whole.

Virtually without interruption since the "work or starve" order of Captain John Smith in Jamestown colony three and a half centuries ago, farmers have been learning to accomplish their tasks more effectively and with less physical effort. After the Revolutionary War this process was accelerated as science and agriculture joined hands. In the new nation 95 per cent of all gainfully employed persons

earned their living in agriculture. Manufactured goods, such as there were, came almost entirely from England and the Continent.

As our economy grew and developed, non-agricultural production became a progressively larger part of the whole. Although people's desire for any one commodity is limited, their desire for commodities in general is not. Therefore economic progress in the United States involved the provision not only of larger quantities of a certain group of commodities, but also—and more importantly—of an ever-widening *variety* of goods and services. By 1910 the farm population had fallen to one-third of the total. Last year it constituted only 15½ per cent, and farm employment was an even smaller proportion.

Today a farm worker in America produces enough to feed 25 people. In countries with underdeveloped economies, and even in most other industrialized nations, farm productivity is very much lower. In most areas of the world the mass of mankind is concerned primarily with the problem of getting enough to eat. Americans, however, take the full meal for granted. They are interested in different kinds

of food and especially in the nonfood products and services that make up the vaunted American standard of living.

More effective methods of agricultural production have released manpower and savings for the construction of buildings, machines and equipment which make up a modern industrial society. This process has also facilitated the flow of implements, power units and fertilizer from industry back to agriculture, thereby further boosting farmers' productivity.

It is because of these developments that farm income and farm production occupy an ever smaller place in the aggregates. While agriculture may still be called the most "essential" industry, it is quite apparent that manufacturing and trade are the areas of greatest growth potential.

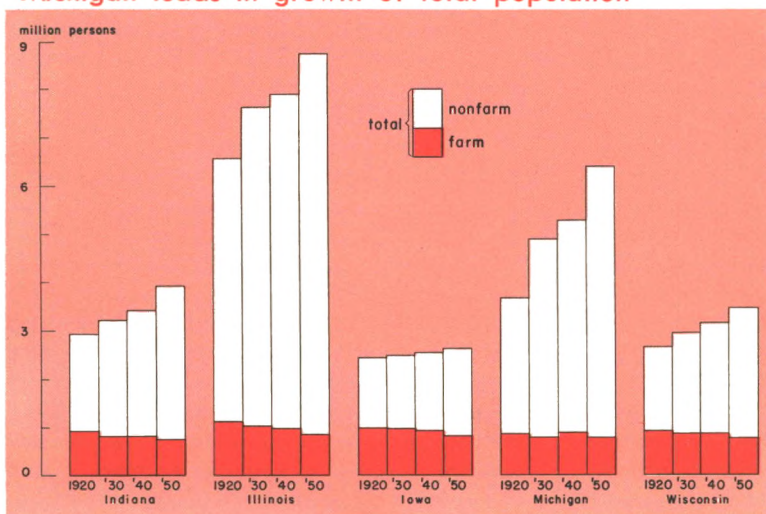
Shift of labor difficult

The transformation of food surpluses into capital available for industrial and commercial uses and the shift of labor from farm to non-farm occupations are not accomplished without friction and difficulties. Food surpluses mean low farm prices, and low prices can mean low

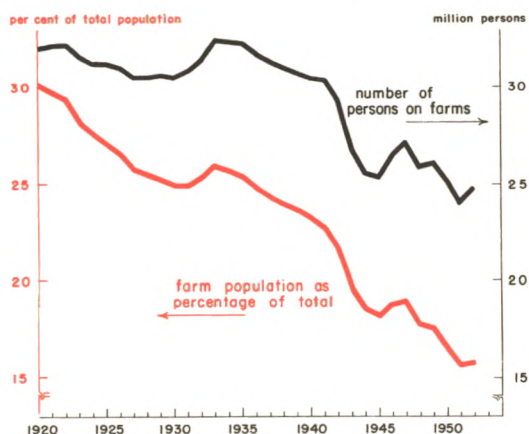
farm incomes. Low incomes tend to push workers out of agriculture, just as high industrial wages and ample employment opportunities tend to pull them out.

The "pull," however, is much more effective than the "push." That is, the labor shift from farm to nonfarm jobs is most facile during prosperity when jobs are plentiful. This despite the fact that farming is most profitable in these same periods. In periods of severe industrial unemployment, when farm incomes are low-

People on farms declining in all District states; Michigan leads in growth of total population



Downtrend in farm population interrupted only by depression and the return of servicemen



est, labor may shift back to the farm. For example, the farm population, even as a percentage of the total, increased between 1930 and 1933, temporarily reversing a long-term decline.

Much of the labor shift, of course, consists of the movement of young folks. In fact, an important element in the shift has been the migration of young women. As a result, the ratio of women to men is definitely higher in cities than in rural areas.

Of course, to a limited extent the problem of transferring farm labor to industry has been eased by locating industrial plants in smaller centers. This trend was especially noticeable in the war and postwar years when the labor market was tightest. These plants generally were located on the fringe of previously existing industrial areas. This helps to account for the importance of part-time farming in some areas and, hence, for the increasing importance of nonagricultural income to farmers.

Labor, capital, technology

Despite many retarding influences over the years, labor has moved from farm to nonfarm activity, and the number of farm workers has declined not only as a percentage of the total labor force, but also in absolute numbers since

World War I. This is a notable achievement, especially in view of the fact that the birth rate is higher on farms than in cities and towns. Because a smaller number of farms encompass the same amount of land, the average size of farm has risen. New machinery and methods have enabled a farm worker to handle more land. And the larger size of farm permits the economical use of still more technological innovations.

The stock of farm capital (in constant dollars) has continually increased. But like farm

Type of farm capital	Percentage of 1930 amounts	
	1910	1952
Service buildings	81	113
Machinery	47	224
Power	24	161
All types	57	147

labor, capital too has decreased as a proportion of the total in our whole economy.

If both farm labor and farm capital are becoming a smaller and smaller proportion of the totals for the whole economy, then it must be expected that the value of agricultural production would follow the same pattern. This is in itself not a bad thing. "Economic progress involves the provision not only of larger quantities of a certain group of commodities, but also—and more importantly—of an ever-widening *variety* of goods and services."

LABOR

Unemployment boosted by both population gains and drop in employment

In March of 1954, sixty million Americans were at work. Although this total was the largest ever recorded for the month except for 1953 and 1951, it represented a drop of 1.4 million from the previous year. Moreover, the number of people of working age rose 1.3 million during the period. As a result, the pro-

portion of the population at work declined.

The increase in people of working age coupled with the decline in employment suggests a rise of about 2.8 million in unemployment. Actually the number of jobless was estimated to have risen only 2.1 million. The difference represents an increase in the number of people who were neither working nor looking for work.

Factory layoffs swell jobless totals

The drop in manufacturing employment over the past year about equaled the decline for the total. The number of workers in mining, construction and transportation were also lower, but gains in finance, service and Government offset these reductions.

The fact that additions to the number of jobless have come largely from the ranks of factory workers has affected the age breakdown of those employed. Information on the age distribution of the working force in February indicates that there were about 550,000 fewer workers in the 20-24 age bracket than a year earlier. A large portion of this drop is traceable to the fact that the number of people of this age has been shrinking as a result of the low birth rates in the early depression years. But this is only part of the story. Jobs held by such persons have also declined because low seniority workers in manufacturing are usually laid off first. Increased placement difficulties for inexperienced workers may also be a factor.

Older people also have been affected more than proportionately by the decline in employment. About 9 per cent fewer persons 65 and over were working in February despite a rise of 4 per cent in the

total number of people in this age bracket.

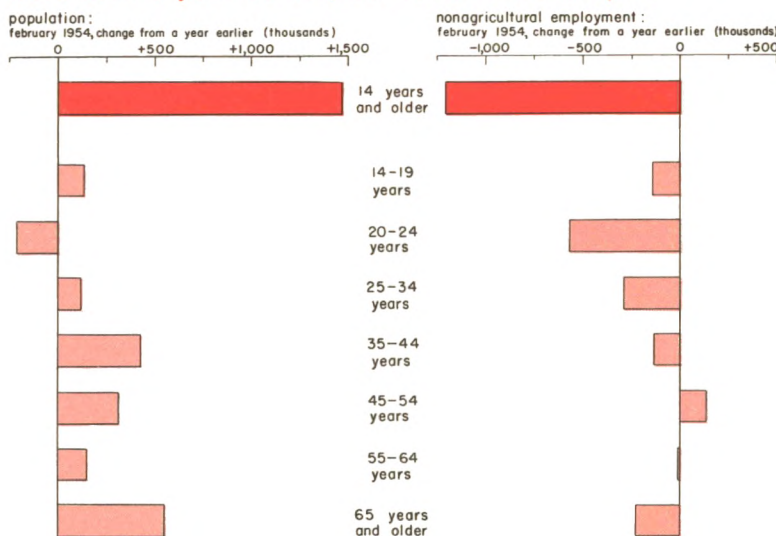
There was relatively less change in the number of workers in the 25 to 64 group which makes up the bulk of the labor force. Within this category, employment in the 25-44 age group was off slightly, while in the 45 and over group there was a small increase. Moreover, in the case of individuals aged 45 to 54, the rise in employment kept pace with the increase in population. All of the pickup in this age group, however, was accounted for by a rise in the number of women working.

Overtime off sharply

The number of people working between 40 and 48 hours dropped by more than 20 per cent in the 12-month period. Moreover, a year ago there were 6.3 million jobs offering six days of work per week. The current figure is well below 5 million.

As those working over 40 hours declined, there was an increase of 1.1 million in the number of people working 30 to 40 hours a week. Undoubtedly most of the increase in this category reflects a shortening of the work week for manufacturing jobs which a year

In most age groups, more people were available for work than a year earlier, but fewer were on jobs



earlier had been on an "overtime" basis. Moreover, many of these jobs have been cut well below 40 hours.

Persons working over 48 hours in nonfarm jobs number about 7.5 million. The size of this group has also declined but more moderately than the 40-48 hour category. Professional people and the self employed account for a large portion of this group.

Turnaround in farm employment

Agricultural employment, which averages about 10 per cent of the total, had been running a half million or more below the corresponding months a year earlier from October 1953 through January of this year. Since then this situation has changed. In February and March farm jobs were about as numerous as in the same months of 1953. Nonagricultural employment, meanwhile, continued to show declines below year-ago levels through March.

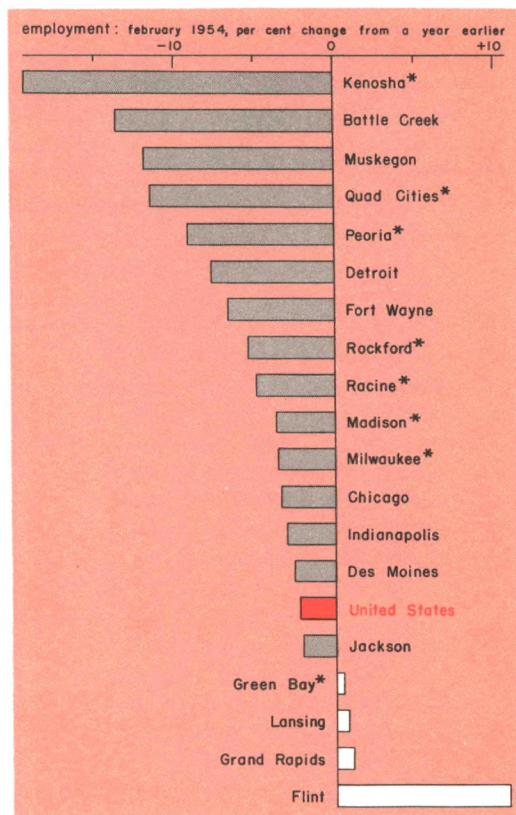
	Agricultural employment	Non- agricultural employment	Total employment
Change from a year earlier (millions)			
October 1952	-0.6	+0.5	-0.1
November 1952	-0.6	-0.1	-0.7
December 1952	-0.7	-0.4	-1.1
January 1953	-0.5	-0.5	-1.0
February 1953	*	-1.1	-1.1
March 1953	*	-1.3	-1.3

*Less than 50,000

The relative strength in agricultural employment, however, is not entirely an optimistic note. This development may merely reflect a return of workers to rural areas now that job opportunities in metropolitan centers have become more limited. Evidence to support this possibility is offered by reports of out-migration from a number of Midwest urban areas. While such a movement may partially ameliorate the unemployment situation in industrial centers, it does not detract from the current under-utilization of the nation's labor resources.

In nonagricultural employment the biggest decline was a drop of over 7 per cent in manu-

Most District areas show a bigger drop in nonfarm employment than the nation



*Comparison for January

facturing. Moreover, for production workers the drop was 9 per cent. Unskilled and semi-skilled workers have been affected most.

District employment off more

Labor market reports for January and February show that in 14 of the 20 major District areas nonfarm employment has fallen relatively more since the beginning of last year than in the nation. The largest declines have been in Kenosha, Battle Creek, Muskegon and the Quad Cities area. These centers have been affected by lowered demand for automobiles, farm equipment and industrial machinery and

a tapering off in defense work. The only major District city which has experienced a sharp drop in employment so far is Detroit.

Most large cities in this area are more or less diversified. In these cases employment declines are nearer to the U. S. average. For all reporting District areas combined the drop was around 4 per cent, compared with a nationwide decline of a little more than 2 per cent.

Smaller communities not shown on the chart also reported widely divergent employment trends. Janesville, Manitowoc and the Neenah-Menasha area in Wisconsin and Saginaw, Michigan, had employment gains over a year ago ranging from 2½ to more than 15 per cent. On the other hand, declines of 7 to 10 per cent were registered in Beloit and Oshkosh, Wisconsin, and Port Huron in Michigan.

In some localities employment opportunities have become more limited for unskilled and inexperienced workers. Cutbacks in overtime also have followed the national pattern.

Withdrawals of women from the labor market, together with out-migration of jobless workers, have dampened the rise in unemployment in some areas, such as Peoria and the Quad Cities. Some of these people were seasonal workers and commuters from nearby rural areas. Others had moved into the area during the prior year or more and were vulnerable to layoffs because of low seniority. In a few areas such as Madison and Green Bay net in-migration of job seekers is reported.

Job declines still limited

The job shrinkage thus far has been concentrated in the younger and older groups of workers—those under 25 and over 65. Persons in these age brackets have accounted for almost 80 per cent of the drop in employment although they comprise only one-fifth of the labor force. In addition, virtually all of the decline has been reported in manufacturing lines. Should further contraction in job opportunities occur, other groups, of course, would be affected.

Insofar as population growth continues to add to the number of people of working age, bringing employment back to previous levels

would not wipe out increases in the number of job seekers. The maintenance of relatively full employment over any considerable period of time will necessarily require advances in the number of people at work.

"DEMON" DEBT

Although debt has grown enormously in recent decades, it has not outdistanced production

Last year the American economy passed the 900 billion mark in indebtedness. In comparison with the amount of debt a generation or even 15 years ago, today's figures are so huge that at first glance it looks as if the nation is afloat in a sea of debt. Actually, the physical output of the economy and its productive capacity have about kept pace with the growth in indebtedness since the end of World War I.

Savings and debt

The amount of debt is closely related to the dimensions of the economy and to the tempo of economic activity, for debt performs vital economic functions. For one thing, it is the major device for transferring investible funds from savers who are seeking safe and profitable outlets for their savings to individuals and firms who will use them—use them to finance the production and sale of more and new kinds of products and services. Debt is involved when savers lend money directly to investors or buy their promises to repay borrowed money—usually in the form of bonds or mortgages. Debt is also involved when savers deposit their savings with banks, savings and loan associations and insurance companies, which in turn lend such funds for construction, equipment purchases and for business working capital.

Another way in which savings may be put to work is through the purchase of stock in business concerns, which makes savers part owners of the business. Though ownership of

equity shares is often more profitable than investing via forms of debt, it is generally riskier, and to most savers the safety and ready availability of their assets is the overriding concern. Thus the great bulk of individual savings flows into financial institutions and debt securities and only a small portion into equities.

A second economic function of debt is to afford a means of creating the entirely new funds that may be needed by an expanding economy, above and beyond those accumulated by savers on their own hook. Such "money creation" is done by the banking system as a whole, when banks use their excess reserves to make additional loans or to buy additional Government or municipal securities, mortgages, corporate bonds or other debt instruments. This creates more checkbook money—bank deposits—and spreads it throughout the banking system.

Debt and output growth compared

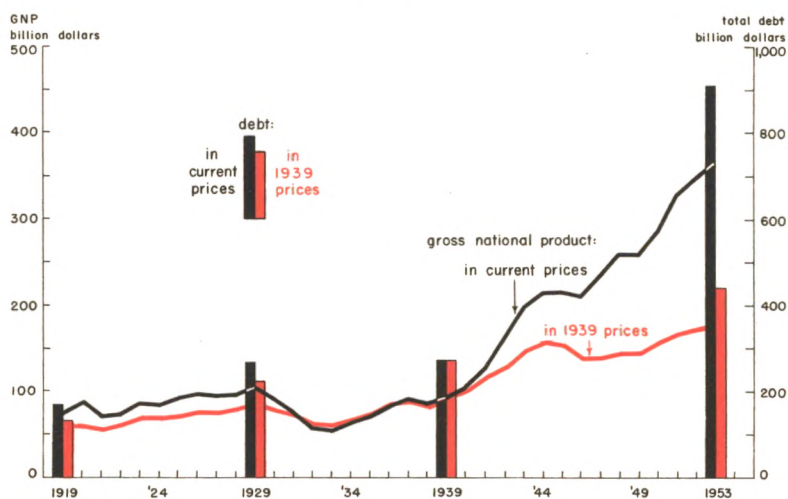
When World War I was over, consumers, farms and businesses and the Federal, state and local governments owed debts totaling about 130 billion dollars, and financial institutions—banks, savings and loan associations and life insurance companies—had obligations to their depositors, shareholders and policyholders totaling 40 billion. Today, the total has soared to above 910 billion dollars, over five times the 1919 figure. During the same 35 years, the value of the country's output of goods and services increased about as rapidly, from between 75 and 80 billion dollars in 1919 to 367 billion last year. If we adjust for the higher price levels prevailing now, both debt and output

are about three times the 1919 levels. And since there has been a 50 per cent increase in the population since 1919, the increase in debt and output per head (corrected for price changes) is smaller—about twice the 1919 levels.

The intervening 34 years have not, however, seen a side-by-side steady advance of output and debt, for the country has experienced boom, depression, total war and then boom and cold war in succession. In the 1920's output rose substantially in both dollars and real terms—about a third—but debt rose considerably more rapidly than either national output or the nation's wealth. The rise in consumer and business debts paced the expansion, especially debt incurred to buy real estate and securities. Since a big factor in the boom of the late Twenties was the repetitive transfer of real estate and securities, which added very little to either output or wealth, much of this debt was on an extremely unstable basis, as the ensuing financial debacle of 1930-1933 proved.

During the Thirties, there were big changes debtwise. Government borrowing increased rapidly due to deficit financing, and deposit liabilities of the banking system also increased

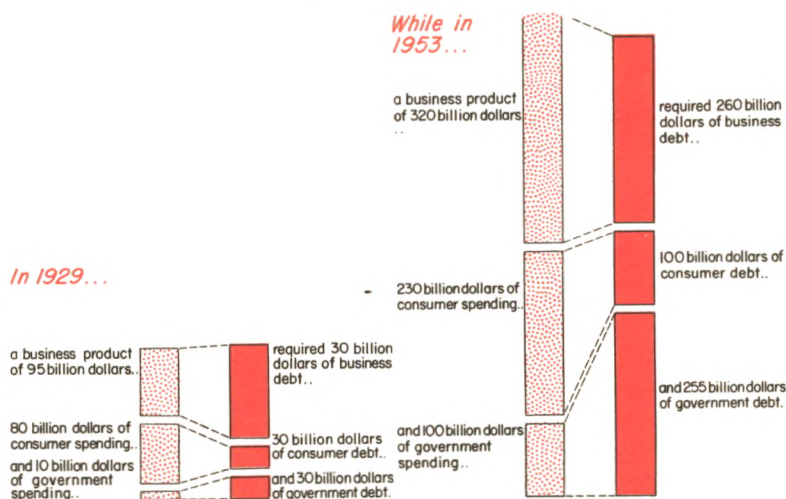
Nation's total debt and output have grown at about the same pace



after 1934 due mainly to a huge inflow of gold. Private debt, along with private output and prices, was at a depressed level due in a considerable degree to the liquidation following 1929. Even by 1939, with total debt at its interwar peak, consumer and business indebtedness was about 20 per cent under the 1929 level. Meanwhile, gross private output was about 15 per cent below its 1929 peak. Since prices were lower, at the end of that depressed decade, the declines from 1929 in real terms were nothing like this: private debt was only slightly lower and private output very slightly higher. In short, there was a lot more debt in the economy at the end of the Thirties relative to the nation's output, but the private sector had not stimulated this growth. Rather it originated in conditions external to the normal functioning of the economic mechanism—an increase in the Treasury's buying price for gold in 1934 and the Federal Government's deficits.

In the nearly 15 years of war and postwar boom since 1939, debt has grown less rapidly than output. During the war, consumer and business debts rose slowly, but the Federal debt soared because of huge wartime deficits, and bank deposits rose rapidly as well. During most of the postwar years, the Federal debt either declined or remained stable, but consumer, business and state and local government debt rose steadily, and large inflows of savings swelled financial institutions' obligations to savers. Last year, however, a substantial Federal deficit and the extremely high level of business activity in the first part of the year gave a big fillip to all types of debt. Now output is about four times as high as in 1939 and

Business output has risen at a faster rate than business debt since 1929



debt is somewhat over three times as high.

Actually, the most meaningful standard against which debt growth may be measured is the need for funds with which to finance the activities of the major classes of borrowers—businesses, consumers and governments. Business needs for funds depend on the volume of new plant and equipment they are building or buying, the level of inventories they are carrying and a variety of miscellaneous working capital requirements. Such needs are roughly proportional to the level of output and sales, and to this extent business output is as good a guide to relative growth as any other. Whether these needed funds are supplied by borrowing or from increased owners' equities (either issues of new stock or reinvestment of retained earnings) depends on the institutional framework of the economy and general business conditions. In any event, business gross product—business sales plus changes in inventories—is now over three times as high as in 1929, while business debts are less than twice as high.

Consumers' use of credit is closely related to their income and spending. Consumer debt now stands at about two and a third times the

1929 level, while consumer expenditures have doubled. Government debt, largely due to depression and World War II Federal deficits, is eight and a half times the 1929 figure; expenditures by government bodies last year were ten times as great as then.

Institutional framework varies

There have been a number of changes in our institutions which would tend to encourage more, rather than less, debt at a given level of business activity. Debt as a means of transferring savings is relatively more attractive to both savers and investors than in earlier periods: to savers, because the financial institutions which are the principal intermediaries in the transfer process are stronger, safer and better managed and because of Government guarantees and insurance of a variety of types of loans and deposits; to businesses, because debt offers tax advantages in a period of high tax rates and because interest costs have been at historically low levels for many years. Moreover, consumer credit is a more developed institution, and the nearly universal amortizing of home mortgages makes them more attractive debt instruments. Also, governments have a bigger role in the economy today than in 1929 or 1939, and governments are nearly always large debtors.

There are some offsetting factors, however. With the recent high level of consumer incomes and savings, substantial retained corporate earnings and depreciation charges and advanced levels of government tax receipts, nearly all individuals and institutions have been better able to pay for their purchases out of current incomes and past savings than at any time in the past. This, of course, is the result of many years of inflation and prosperity. Then too, although the widespread use of the principle of amortizing debt makes debt more attractive, it also means that large repayments of debt are taking place constantly, thus reducing the net increments to the total stock of debt. Also important is one heritage of 1929-1933: so many lenders and borrowers were burned by the widespread practice of borrowing to finance

speculative transfers of real estate and securities that both seem reluctant to increase debt for nonproductive purposes. Moreover, regulations now on the books or utilized in the postwar period permit direct control of the proportion of credit going into these transactions.

Another reason for the relatively more moderate use of private debt today than in earlier periods relates to the sequence of events of the war and postwar periods. The enormous spending and borrowing of the Federal Government during World War II boosted the active money supply—currency plus private demand deposits—from 65 billion dollars at the end of 1939 to 150 billion at the end of 1945. In most of the eight years since then the active money supply has continued to increase, but in the main the increases have been moderate ones, with the notable exception of the immediate post-Korea period. What has happened is that the economy has “grown up” to the bigger money supply, in part by price inflation, but also because of a substantial increase in the nation’s real output in the postwar period. Evidently the economy has not needed to go into debt more heavily to create new money, but has been using the money supply more fully.

All told, it means that with our 900-odd billion dollars of debt, we are in a better relative position debtwise than at many times in the past, although this of course may not be true for individual consumers or businesses. Also, the greater powers and longer experience of the Federal Reserve System, which can influence the creation of new debts and the transfer of old ones, will contribute to our goal of growth without inflation or depression.

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Trends in selected District centers

The trend of business in individual areas may be quite different from that for the nation or other areas. The most striking changes ordinarily occur in the smaller communities which reflect developments in a few major industries.

Flint, for example, is the only Midwest auto center where activity is above year-ago levels as measured by all four of the indicators charted

below. Racine, on the other hand, shows debits and employment below a year ago. Here the seasonal rise in farm machinery was more than offset by cutbacks in other lines.

The larger and more diversified centers usually show more similarity to each other and to the nation. Detroit, however, presents less favorable comparisons with a year ago than does Chicago.

Broad measures, like employment and debits, fluctuate less than the more selective measures—new cars and houses, for example. All indicators are plotted so that an equal vertical distance represents an equal per cent change.

