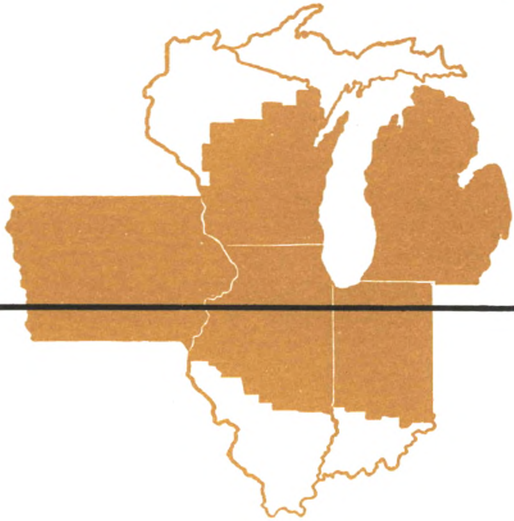
A review by the **Federal Reserve Bank of Chicago**

Business Conditions



1954 September

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THE Trend OF BUSINESS

In fall and spring, business activity turns up seasonally from the sluggish summer and winter months. September and March experience is watched closely for indications of the tone for the months ahead. Developments this month, therefore, are likely to have a more than usual impact upon continuance of public confidence in good times.

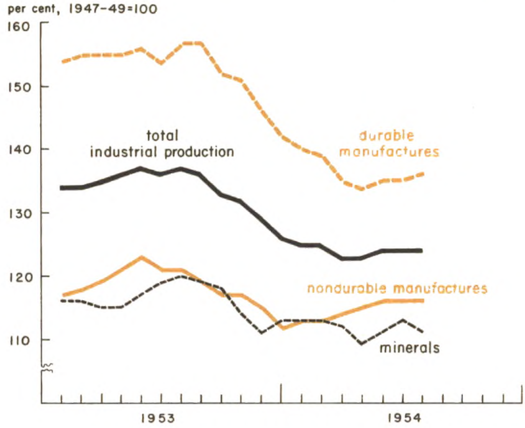
July and August continued the general stability which has characterized the economy since the sharp declines of the second half of 1953. Those who hoped that summer would bring advance confirmation of a new upswing were disappointed. Manufacturers continued to place orders cautiously, and inventories in some lines seemed to call for further downward adjustment. Steel output lingered at about 62 per cent of capacity in August, and the industry experts were inclined to again push ahead another month the time for a revival of ordering. In July, seasonally adjusted employment which had declined almost continuously for the past year reached its lowest point since mid-1952. Reductions in recent months, however, have been much smaller than last fall. Moreover, the July decline in large part was caused by strikes in the lumber and rubber industries.

If recent developments have failed to establish a case for vigorous resurgence in the near future, there was ample evidence that optimism concerning the ability of the economy to avoid a sharp general contraction of magnitude was justified. Tax cuts, easier money and other Government moves have been important, but stability may well owe more to the refusal of businessmen and consumers to retrench in the face of uncertainty. As in 1946 and 1949, the willingness of the consumer to spend his income freely has provided strong support.

In the early months of 1954, total retail sales continued at the somewhat depressed levels of the latter part of 1953. In April, and again in June and July, results about matched those recorded last year. Many merchants, particularly those specializing in soft goods, now anticipate little difficulty in beating last year's figures in the fall. Sales in the similar period in 1953 had suffered noticeably from warm weather.

Over-all stability in recent months does not mean that adjustments in particular lines have been completed. Rather, further declines in some sectors have been balanced by improvements elsewhere. Output of capital equipment, automobiles, farm machinery and appliances, for example, was being reduced in early summer. Meanwhile, TV and furniture output improved as inventory gluts were eliminated. Electric power and construction continued to

Production level after 1953 drop



boom, setting all-time records. Coal mining, steel production and carloadings remained at depressed levels while most soft goods producers held to the schedules of last spring, not far from last year's highs.

Predictions that competitive conditions during 1954 would resemble prewar experience are being realized. Basic reasons for this situation are simple. First, aggregate demand is significantly below the level which business demonstrated it could meet last year. Second, physical capacity has increased further in 1954. And third, business efficiency has reached a new high. Materials are flowing readily, the quality of work force has improved and the breaking-in period for many new facilities has passed. Cost cutting, moreover, has been spurred by slimmer profits and the expiration of the excess profits tax.

Sharper competition, of course, has caused individual hardships. Profit margins have been shaved, business failures have risen and the problems of finding and holding a job have increased. In general, these developments have benefited buyers at the expense of sellers.

A trend toward lower prices of finished goods may be reversing a long upswing. Raw material prices have long since relinquished the gains of the early post-Korean period. Processed goods, however, have tended to rise further or hold steady. Published indexes of prices continue to be highly stable, but there is evidence that price concessions have become more common.

In some cases, price reductions are indirect. That is, list prices remain unchanged, but buyers are favored through freight absorption, better grades at the same price or other similar benefits. In industries such as chemicals and building materials, which have greatly expanded capacity to produce standardized products, price shaving has been reported, but instances are spotty and regional in nature. Bids on some new construction are coming through at substantially lower levels than last year although construction cost indexes have not declined.

At the retail counter, TV sets and appliances have been reduced, and makers of other items have claimed that quality in various price brackets has improved. Mail order houses have indicated that fall catalogs contain numerous price reductions. Studebaker intends to cut the factory list of 1955 models by about $100. Meanwhile, 1954 cars which remained in large supply at the end of July are often available at "bargain prices."

Plant and equipment expenditures are slipping below earlier estimates. The most recent SEC survey of business capital spending plans indicated moderate downward revisions of earlier plans. In previous postwar years actual outlays usually exceeded "preliminary" estimates. It is apparent that some industries overestimated the strength of demand and profits in 1954. As a result, expansion is less necessary and financing from internal sources more difficult. Reductions from original estimates were most noticeable in the chemical, petroleum, rubber and mining industries.

The trend toward consolidation has become increasingly evident as more business firms are turning to mergers to increase profit potentials. Examples in the automotive and textile fields have received considerable publicity, but there are many cases of mergers between firms turning out noncompeting products.

Improved efficiency revealed by employment data

During the year ending in July 1954 . . .

*manufacturing production worker employment declined from 13.9 to 12.3 million, a drop of **11.6 per cent,***

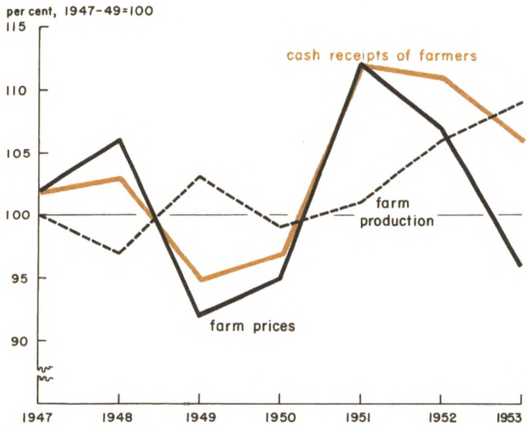
*meanwhile, the average work week fell from 40.3 to 39.4 hours or **2.2 per cent,***

*as a result, the number of production hours was lowered by **13.6 per cent,***

*but total factory output declined only **9.2 per cent,***

*therefore, output per man-hour **rose** by about **5 per cent.***

Farm income drop expected this year would continue trend begun in 1951



The reasons include attempts to cut costs through elimination of duplicating jobs, the fuller use of facilities and diversification.

Union demands are meeting stiffer opposition from management. Strikes in the rubber, lumber and airline industries highlight some increase in labor difficulties. Unions in other lines have avoided work stoppages by presenting less ambitious requests than in recent years. A dramatic development was the agreement of Studebaker workers to take wage cuts to place their employer in a better cost position.

Output per man-hour has gained noticeably as job opportunities declined. Wage and salary employment in July was 1.9 million or 3.8 per cent below last year. The decline in over-all output was somewhat smaller. Thus, the output of goods and services per worker has increased. Higher productivity in manufacturing is fairly evident. Factory output was 9.2 per cent less in July than a year ago, but production worker employment was down 11.7 per cent and the average work week at 39.4 hours was one hour shorter. Moreover, between January and July when seasonally adjusted output was virtually constant adjusted production worker employment declined by about 650,000.

Farm income continues to slide as hog production is boosted and wheat and cotton are cut back. Except for the influence of Government support programs, the farmer operates in a competitive market in the classical sense. There are no "list prices," and market quotations reflect day-to-day shifts in supply and demand. As a result, farm income benefited immediately from the price gains after Korea. Since early 1951, however, receipts of farmers have been heading downward.

Total cash receipts this year will be down 3 to 5 per cent from 1953 according to various estimates, and the second-half comparison with last year probably will be less favorable than the first half. Second-half receipts, it should be noted, account for about 60 per cent of the year's total.

Currently, heavier marketings of hogs and cattle are causing downward price adjustments. Livestock prices are not directly affected by support programs. Among the basic crops, receipts from wheat and cotton will also be appreciably lower because of reduced acreage and large stocks accumulated from previous years.

The downtrend in income has restricted farmer buying of machinery and equipment and this situation is likely to continue into 1955. Furthermore, farmers may become increasingly reluctant to draw upon their liquid asset holdings. The farm sector must be included in any list of industries which continue weak in the face of over-all stability.

THE FARM PROGRAM

Farm price supports, a corner turned

As the 83rd Congress headed into the closing days of its second session, a long struggle over farm price support policy was brought to a head. Many issues were at stake, but the major one, stated broadly, was whether the time had come in the postwar world to lessen the rule of legislative mandate in determining agricultural prices and to begin the turn toward greater dependence on supply and demand conditions surrounding each agricultural commodity. In the Act which finally emerged, a short step was taken in the direction of allowing market prices to play a greater role. But to say that the step was unimportant would be an error. Its meager dimension is overshadowed by the significance of the direction in which it was taken.

Congress had faced this same issue on several other occasions since the end of World War II and, although always registering an intent to move eventually in the direction of less Government and more supply-demand forces in the pricing of agricultural commodities, it on each occasion decided to postpone the date when the move would be effected.

This time, however, the combined effects of rapidly accumulating stocks of commodities of which burdensome surpluses had already been piled up, the desire to reduce Government spending and taxes, a growing awareness on the part of farmers that rigid and comprehensive production and marketing controls would have to be accepted, and growing opposition to "high" food prices tipped the legislative balance mildly in the direction of lower price supports.

Shaping long-run policy

The recent action takes on its full significance only when it is viewed in its longer-term setting. Although Government aids to agriculture, as to other segments of the economy, have a long history, it was not until the latter half of the 1930's that serious consideration was given to *permanent* Government price support programs. Until that time, such programs as had been inaugurated were viewed as emergency measures. Support was provided at relatively low levels and on a temporary basis. Not until 1942, when price supports were used to provide incentives to farmers to engage in all-out production to meet wartime needs, were supports raised as high as 90 per cent of parity. To give farmers a period in which they could adjust from wartime to peacetime demands, support was extended at this level for a period of two years after the end of hostilities. However, during the War and for several years thereafter, the price support program was largely inoperative because other forces held prices above support levels.

It was in this setting that Congress and farm leaders tackled the problem of long-run postwar farm policy and came up with the Agricultural Act of 1948. Embodied in this Act were both short-run and long-run features. The former were largely an extension of the wartime program; the latter provided for lower level supports beginning in 1950 with the objective of bringing support prices more in line with "free" market prices. The long-run features of the Act, however, were never allowed to go into effect. The Agricultural Act of 1949, similar to its 1948 predecessor, extended for another year the wartime level of support for a number of commodities and again scheduled lower level supports to become effective in later years. Similar actions on other occasions have perpetuated the wartime support levels for certain crops through the 1954 crop year but always with provision for lower support at a later time.

The 1954 Act

At this juncture the 83rd Congress took up the problem. The Act which it finally hammered out is similar to preceding postwar legislation in that it provides for a higher level of price support in 1955 than in subsequent years. This has led some observers to suggest that struggles over farm price support are likely to be annual events for the foreseeable future.

The outstanding feature of the 1954 Act is that it provides for small *reductions* in support levels for several crops *next* year. This is heralded by its proponents as a positive indication that the stage is now set for the gradual introduction of a substantial degree of flexibility into the year-to-year levels at which prices of farm commodities are supported. Whether the long-run features of the 1954 Act will succumb to a succession of postponements, as has happened so regularly in the past, will be determined in future sessions of Congress.

Among the many commodities produced and sold by American farmers a few have acquired special status. These have been labeled "basics," and include wheat, cotton, corn, tobacco, rice and peanuts. Support for these commodities, except tobacco which stands aloof even from its distinguished company, is to be provided within the range of 82½ to 90 per cent of parity for 1955 crops, the level within this range being determined by their supply in relation to "normal supply" as defined for each of the commodities. For tobacco, the level may remain at 90 per cent indefinitely if its producers continue to approve marketing controls. Beginning in 1956, support of wheat, cotton, corn, rice and peanuts is to be provided within the range of 75 to 90 per cent of parity, again depending upon supply.

Stocks that don't count

To minimize the effects of stocks on the determination of support level, the Congress provided that as much as 2.5 billion dollars of commodities acquired by the Commodity Credit Corporation from the 1954 and preceding years' harvests should be "set-aside." The set-aside commodities are to be ignored when totaling supplies for use in determining the level of support for 1955 and subsequent years, although they are included as part of total supplies in calculating acreage allotments. Furthermore, such stocks may *not* be released to usual markets unless prices have risen to 105 per cent of parity. Their disposition is limited largely to barter for strategic imports and donation or sale for school lunches, research uses and foreign and domestic relief.

The Secretary of Agriculture is permitted some freedom of action in determining the makeup of the set-aside. The law requires, however, that he include 400 to 500 million bushels of wheat and 3 to 4 million bales of cotton. This is expected to result in support prices at 90 per cent of parity for cotton and at the minimum of 82½ per cent of parity for wheat for the 1955 crops. Support of corn, rice and peanuts probably will fall between 85

Prices received by farmers have continued to decline relative to prices of things they buy

Index (1910-14 = 100)	July 1951	July 1952	July 1953	July 1954
Prices received	294	295	260	247
Prices paid	282	286	278	280
Parity ratio	104	103	94	88

and 90 per cent. The levels finally determined will depend somewhat on this year's harvest, exports and other factors affecting supply.

Price support is *required* for a few commodities in addition to the basics. For milk and milk products the required range is 75 to 90 per cent of parity with the specific level within this range determined by the Secretary of Agriculture. These commodities are supported currently at the minimum level and apparently will remain at that figure. A concerted effort by certain dairy interests to raise the minimum figure was turned down by Congress.

Also included in this group are tung nuts and honey, with support required at 60 to 90 per cent of parity, and wool (including mohair). Price support for wool, beginning April 1, 1955, and continuing for four years, is required at a level, up to 110 per cent of parity, which will encourage the production of approximately 300 million pounds a year. This is 30 per cent above 1954 production. If a 300 million pound output is reached, support then must be at a level between 60 and 90 per cent of parity deemed necessary to further boost production to 360 million pounds. The support price is to be provided through direct payments to wool producers. This method of supporting wool is a sharp departure from the practice of supporting prices of commodities currently in use. It is designed to minimize the interference of support prices with international trade. Tariff revenues collected on wool and woolen materials are earmarked for this purpose. The payments are to make up the difference between the announced price goal and the market price for wool.

Other commodities may be supported at the discretion of the Secretary and at levels which he deems appropriate. A number of programs and techniques are available through which limited support may be provided. But they are specifically required and spelled out in great detail only for the few commodities discussed above.

Other features

Among the many additional features of the recent legislation is the establishment of a commercial wheat area. Producers outside this area will not be subject to marketing penalties for wheat produced in excess of allotted acreage, but support will be provided at only 75 per cent of the support level in the commercial area. This is similar to the present program for corn.

Marketing quotas were eliminated as a device for obtaining production control on corn. Hence the program will continue much the same as in the current year except that the support level can be below 90 per cent of parity.

To further strengthen the Department's efforts to boost exports of agricultural commodities, the agricultural attaches of our foreign embassies are placed under the supervision of the Secretary of Agriculture. The Congress had previously passed the Agricultural Trade Development and Assistance Act of 1954 which is designed to increase the export of surplus agricultural commodities outside usual market channels to friendly nations.

Modern parity

An important feature of postwar agricultural legislation has been the provision of a "modernized" procedure for calculating parity prices for the individual commodities. The parity price of a number of important commodities has been calculated for many years using 1910-14 average prices as the base. This had the effect of freezing the price of corn, for example, relative to prices of other commodities. Hence, important changes in production, cost or demand conditions which have occurred over the years were not reflected in parity prices. This was especially noticeable as between the grain crops, production of which has been mechanized within this period, and the livestock items for which mechanization has made much less progress. Thus, the 1948 Act provided that the parity prices of individual commodities be adjusted one to another in accordance with their average relationship over the most recent 10-year period. This provision has been carried along in subsequent acts but has not been allowed to go into effect for those "basic" commodities for which it would reduce parity prices.

The 1954 Act provides that modernized parity be extended to these few remaining commodities beginning with the 1956 crops but limits the amount of reduction which may be made in any one year to 5 per cent of the parity price. The full effect would be to reduce the parity price of cotton by about 2 cents a pound; wheat, about 40 cents a bushel; corn, about 22

Market prices of some major farm commodities are well below "parity"

Commodity	U.S. average market price July 1954	Parity price as of July 1954	Market price as a percentage of parity price
Corn (bu.)	$ 1.50	$ 1.82	82
Wheat (bu.)	2.00	2.50	80
Soybeans (bu.)	3.47	2.80	124
Hogs (cwt.)	21.20	20.60	103
Beef cattle (cwt.)	15.80	21.00	75
Eggs (doz.)	.34	.46	74
All milk (cwt.)	3.69	4.70	79

cents a bushel; and peanuts, about 3 cents a pound. Thus, Congress has provided for a downward adjustment in the parity price for these commodities which would allow further gradual reductions in the authorized support level beginning in 1956.

Controversy ahead

That Congress does not deem its recent action to be final is indicated by its instruction to the Secretary to make detailed studies of various methods of production control and price support for dairy products and of various two-price systems which could be applied to rice. Two-price proposals have also been made for wheat and may be expected to come up for further study and Congressional consideration in future sessions.

HOME BUILDING

Housing market: easy terms boost sales

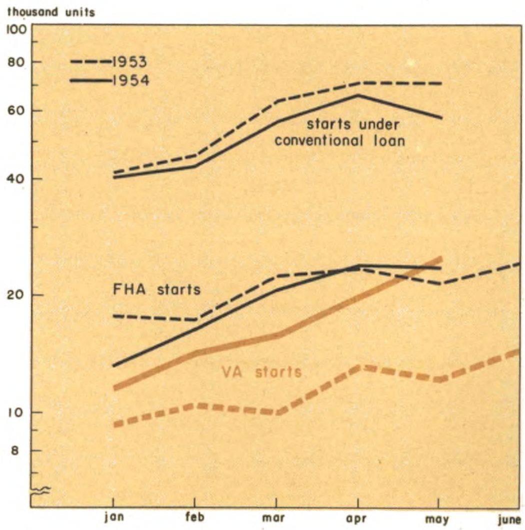
Unexpectedly holding at last year's high level, residential construction provided a major prop to business throughout the spring (see pp. 8-11 in the August issue of *Business Conditions*). Since then home-building activity has picked up even further. Privately financed housing starts, which ran about equal with those of early 1953 in the first five months of the year, showed strong year-to-year gains of 13 per cent in both June and July. At the current rate, total starts for the year will approach 1.2 million, less than in 1950 but significantly more than in the years since then.

Much of the new strength in home building has come from projects catering to the veterans' market. Down payments have been reduced and loan maturities lengthened as funds for investment in VA-guaranteed mortgages have become more readily available this year. As a result, many builders have boosted project construction of houses intended for sale after completion, and prospective buyers have been attracted in large numbers by the easier terms.

Despite the upsurge in speculative building in recent months, the tone of the market continues strong in most communities. A recent survey of major Midwest centers revealed that houses were selling readily, and none of the builders contacted held appreciable inventories of completed unsold houses. In fact, many firms reported that they were sold ahead well into the fall, and virtually all were optimistic regarding future prospects. Easier credit terms, particularly for VA loans, were frequently cited as the major cause of the strength in demand.

Now, the new Housing Act has significantly liberalized minimum mortgage terms required by the FHA on both new construction and used houses. Loan maturities have been lengthened to 30 years, as for VA mortgages, and down payment requirements have been sharply reduced for all but the lowest-priced houses ($7,000 or less). If lending institutions generally go along with the new FHA terms, as they have in the past, the additional stimulus provided the housing market would appear to

VA-financed housing starts gain sharply from last year



be substantial. This is the first time in the postwar period that mortgage loans would become available to the nonveteran market—still the major source of new housing demand—on such easy terms.

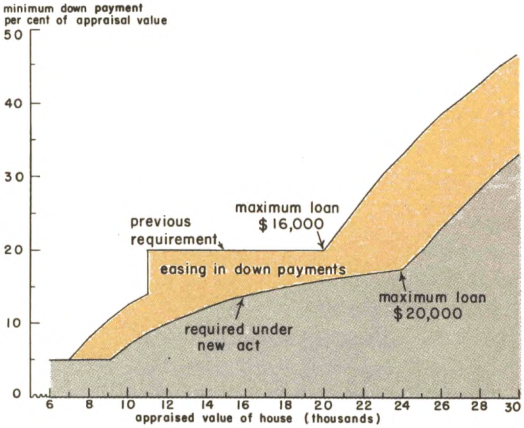
The willingness of lenders to provide mortgage funds at these liberal terms is directly attributable to the VA guarantees and FHA insurance of such loans. The equity position of buyers is much less important than with conventional loans, since lenders are relatively well protected against loss by governmental participation, even if property values fall well below the unpaid loan balances. In addition, the standardization of loans and procedures under the FHA and VA has promoted the development of national mortgage markets—with many institutions lending on properties located far from their home offices — thus adding greatly to the fluidity of mortgage funds. Clearly, governmental policies have played the major role in bringing about the easier credit terms and ready availability of funds so important to the stronger tone of housing markets in recent months.

The VA building boom

The larger volume of housing starts so far this year has been entirely accounted for by units carrying VA financing. Through May, in fact, VA starts were 57 per cent greater than in the same months of 1953, while FHA starts were down 5 per cent and starts financed with conventional loans and by other methods had dropped off 10 per cent. Moreover, the margin of gain has widened as the year progressed. One-fourth larger than last year in January, VA starts were double the 1953 volume in May, and new appraisal requests have continued to come in at more than twice the year-ago rate through July.

This boom in VA-financed houses has been made possible by the greatly increased attractiveness of these mortgages to lending institutions as compared with last summer. Subsequent to the increase in interest rates on VA loans from 4 to 4½ per cent in May 1953, yields on alternative investments dropped sig-

Down payment requirements on FHA loans eased by new housing act



nificantly in the fall and winter. Moreover, a falling off in the demand for borrowed money by businesses and consumers accompanied the decline in rates. Faced with a continuing large inflow of savings and debt repayments, institutions have turned increasingly to mortgages as an outlet for their funds. Life insurance companies, as a prime example, boosted their acquisitions of VA mortgages in the first half to 450 million dollars, two and a half times the reduced volume of early 1953.

Pressed by the competition for mortgages and by the demands of builders, most lenders have eased the terms on VA loans which they will accept. Such loans are now commonly available in Midwest centers at 5 per cent down and 30 years to pay, as compared with the 10 or 15 per cent down payments and 25-year maturities most frequently required at the turn of the year. Loans requiring no down payment have not become generally available in this area, as is reported to be the case in some other sections of the country, except that some builders in Detroit have obtained commitments on these terms in significant volume.

Easier terms for nonveterans too

Mortgages never have been available to nonveterans at terms comparable in leniency to

Monthly payments lowered by longer loan maturities

Amount of loan	20 years Monthly payment[1]	20 years Gross income needed[2]	25 years Monthly payment[1]	25 years Gross income needed[2]	30 years Monthly payment[1]	30 years Gross income needed[2]
$10,000	$ 79	$355	$ 71	$320	$ 66	$295
12,500	98	440	89	400	83	370
15,000	118	530	106	480	99	445
17,500	137	615	124	560	116	520
20,000	157	705	142	640	132	595

[1]Includes interest and principal on 5 per cent loans plus provision for tax and insurance reserves estimated at 1½ per cent of the total loan.

[2]For illustrative purposes, it is assumed that gross monthly income should be 4½ times the total payment. In practice, this ratio varies widely according to the individual circumstances of borrowers.

These data illustrate the effects of lengthened maturities in reducing the gross income needed by borrowers to qualify for loans.

those guaranteed by the VA. A few buyers have found it possible to cut their needed down payment by obtaining second mortgages from builders or others, but these have involved heavy monthly payments since the second loan maturities generally run from three to five years. For the most part, FHA loans have carried the easiest terms. During most of the postwar period, FHA down payment requirements have been 20 per cent, except on low-priced houses, maturities 20 or 25 years, and maximum loans $14,000 or $16,000. The alternative has been a conventional mortgage, on which lenders have required 25 per cent or more down and no more than 20 years loan maturity.

Under the new Housing Act, however, FHA terms have been relaxed substantially. Minimum down payments have been reduced to 5 per cent on new construction appraised at $9,000 or less and 25 per cent of the excess up to a maximum loan of $20,000—sharply less than was required before in most price classes (see chart). The buyer of a new house appraised at $12,000, for example, would need only $1,200 as compared with $2,400 before; a $15,000 house would require $1,950 as compared with $3,000; and the down payment requirement on a $22,000 house would be reduced from $6,000 to $3,700. Requirements for used houses, based on the appraised value, are only slightly higher.

For all houses appraised at more than $24,250, the minimum down payment requirement has been reduced by $4,000 because of the higher FHA loan limit. This is not as significant as it seems, however, since larger loans were typically available on a conventional basis than under the old FHA terms for these higher-priced houses.

In addition to the lowering of down payments, FHA maximum loan maturities have been extended to 30 years for new and probably all postwar used houses. This compares with 20 years for used houses and 25 years for most new construction under the old law. That this can make a significant difference in the size of the monthly loan payment is shown in the accompanying table. Since FHA credit standards require that a borrower's gross monthly income cover his total payment by several times—generally four to five, depending on individual circumstances — the longer maturities also would increase the proportion of acceptable applicants for a loan of any given size.

Broadened market potential

Clearly, the reductions in minimum FHA terms could significantly expand the potential housing market, if widely adopted by lenders. The relaxation would be of the same general magnitude as that which has occurred for VA loans since the turn of the year. Considering the present competitive situation in the mortgage market, it seems likely that at least some lenders will go along with the new terms immediately and that others will do so in time. Presumably, most of those national lenders who have been making commitments for VA loans on easy terms will have little objection to FHA loans on the new but still somewhat less liberal basis.

Equally important will be the attitude of local lenders. Heretofore, many savings and loan associations have not been active in making FHA loans, preferring to by-pass the one-half per cent insurance charge. They apparently have felt that they could compete with the FHA with conventional mortgages through a combination of nearly as lenient terms, greater speed in processing applications and more flexibility in arranging and renegotiating individual loans. There is some indication that this attitude is changing, since the further relaxation of FHA terms has greatly increased the differential between insured and conventional mortgages.

Banks may or may not subscribe to the new FHA requirements, depending on their individual loan policies. But if savings and loan associations enter the FHA market in volume at close to the new minimums, there should be ample funds available to meet the probable expansion in FHA loan requests. This could be especially important in Midwest centers where savings and loan associations provide a major share of the mortgage money. In May, for example, these institutions accounted for 63 per cent of all mortgage recordings of $20,000 or less in Chicago, 57 per cent in Milwaukee, 52 per cent in Des Moines and 36 per cent in Indianapolis. If more associations in such centers begin making FHA loans in volume, the consequent increase in the proportion of FHA to conventional loans would in itself represent a marked easing in average terms available to prospective home buyers.

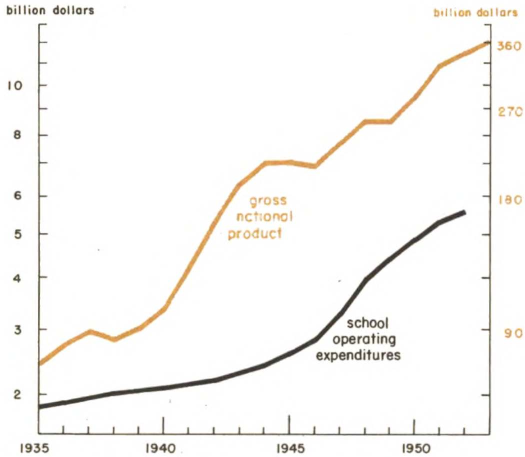
Schools for the modern economy

Americans have worked hard—very hard—to achieve an unparalleled standard of living. But other peoples in other places and in other eras have also worked hard, perhaps a lot harder than we have, to get high standards of living without very much success. Why have we succeeded where others have failed? Any explanation must rest heavily on our traditionally well-trained, responsible and ambitious labor force. For this, the public school system deserves a large measure of credit. From the earliest days, we have devoted an appreciable share of our resources and an even larger share of our civic consciousness to education—beginning with the reservation of public lands for the support of schools in the newly opening western frontier, down through the present.

In education, a society cannot rest on its past achievements. The American economy is a rapidly changing sector of a fast changing world, and the changes require a labor force capable of exploiting new technological opportunities. In our economy, for example, power tools and equipment have largely replaced physical strength and stamina, thus enormously increasing labor force productivity. It seems clear that automatic processes will increasingly replace machine feeders and tenders, with great improvements in productivity again. And these same processes will require more machine designers, builders and repairers.

To exploit fully these possibilities and the

School operating costs, after depression and wartime lag, match recent growth in national product



mounting applications of science to the business of producing goods and services more people must be better prepared to earn a living in a new kind of industrial world, an even more complicated world. So the school system has an enormous job to do—to train people to perform the more highly skilled and more responsible jobs automation will offer and to use the greater leisure it will provide. This is in addition to the other constant tasks of education, such as imparting the knowledge men have accumulated through the ages and developing the good citizenship a democracy needs for survival.

It's hardly news to say that all this costs a lot of money and that school finance is a very troublesome problem today. Millions of home owners for several years now have been feeling the pinch of rising school costs in the real estate taxes they pay to support their schools. What is at the root of their problem? For one thing, an enormous bulge in the school-age population (caused by the high birth rates of the past decade) is crowding over-aged school buildings, and hundreds of thousands of school children in the newer suburban sections, which have grown most rapidly, have been attending schools in shifts reminiscent of war workers in aircraft factories. For another, school teachers' salaries have not been sufficiently high to attract to the profession and to keep actively at work enough teachers. Moreover, the attrition of competitive jobs on the teaching force has been especially strong in the case of the better trained and more aggressive teachers.

The battle of the bulge

Since 1946, grade school enrollments have increased by about 30 per cent. This is a spectacular rise for such a brief span of years, and its impact is visible in the extreme overcrowding of school buildings, especially in the suburbs where enrollments have risen most rapidly. And this is despite billion dollar construction programs in each of the past four years.

The enrollment bulge is the fruit of the turnabout in birth rates brought on by the War. The country's birth rate started declining fairly sharply in the Twenties, and this drop was accentuated by the depression's impact on family formation. Five or six years after a change in birth rates, its effects begin to hit the schools, so in 1931 grade school enrollments started dropping. The drop continued until 1946. Since then the War and postwar baby crops have rolled into the schools, jamming them beyond the most extravagant estimates of their capacity. Before long, the full force of the bulge will hit the high schools, in which enrollments so far have risen only moderately.

This all means that the 10 billion dollar plus backlog of needs for new school facilities requires careful planning and close attention to the trend in birth statistics to decide how fast and how far to expand facilities when enrollments may level off again in a few years. A partial answer may lie in the idea of more flexible school building design and utilization stimulated by postwar expedients.

Far more of a complication than the unevenness of the bulge over time is its geographic unevenness. Accompanying the rise in the birth rate has been a massive migration to the suburbs of the big cities, both from smaller towns and from the big cities themselves, particularly on the part of young couples of child-bearing age. Naturally, a major share of the growth in grade school enrollments has been in suburban schools, while in some places city schools still have unused capacity. What makes things worse is that there are many completely new suburbs—communities that seven years ago were farms or golf courses, like Park Forest, Illinois, and Levittown, New York. These places had hardly any school facilities at all to begin with and have been fighting a running battle with the birth rate and their own growth in their efforts to house the school children. Since most real property in a suburban community consists of the homes of its citizens, this is all reflected promptly and painfully in the taxes they pay.

However, the acute phase is coming to an end. The housing shortage—which originated in the high birth rates and stimulated much of the migration to the suburbs, where project builders could provide new homes at moderate prices—is over with in most communities or

How public school money is spent . . . and where it comes from

- During the school year 1953-54, some 70,000 local governments employed 1,100,000 teachers to provide elementary and secondary schooling for 30 million pupils.

- These school programs cost almost 8 billion dollars, of which about a fourth was for new buildings and equipment and the rest for operating the schools, largely paying teachers' salaries.

- Nearly all school authorities raise money for new buildings by borrowing; the much larger current operating expenditures are financed from current revenues, though much short-term borrowing is done for current expenses in advance of tax receipts. The contribution of borrowed funds to school costs is fairly small, less than 20 per cent of the total. Much of the new long-term borrowing is offset by obligations to repay previously incurred long-term debts—nearly 300 million dollars a year at present (not counting almost 100 million dollars of interest payments).

- The really important sources of the schools' current revenues are local property taxes and state aids, derived in most states from the receipts of sales and/or income taxes. These two sources provide all but about 3 per cent of current revenues, about 40 per cent coming from state aids and the rest from local property taxes.

at any rate is not the nationwide phenomenon it was a few years back. Hence, though the migration to the suburbs will no doubt continue, sudden massive movements to entirely new sections are not to be expected. In a few years, even the Levittowns and Park Forests will begin to enjoy the comforts of a modicum of municipal maturity. Moreover, even if birth rates are maintained at higher levels than now seem likely, most communities by now have accustomed themselves to the idea of rising enrollments and are planning accordingly. In this respect, local school authorities are luckier than some other state and local agencies—highway agencies, for example—which seem doomed to pursuit of forever skyrocketing needs for new facilities.

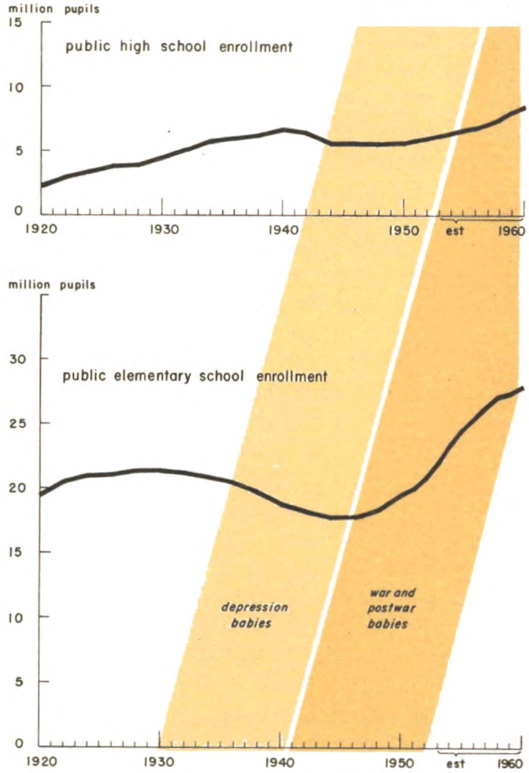
Teachers' salaries

In terms of the nation's resources, teachers' salaries are a much bigger problem for the future than school buildings. Paying teachers takes well over half of most school budgets. Moreover, there is a long way to go to reach adequate levels in salaries, at least if the usual standard of adequacy is used—that is, salaries high enough to attract well-trained and capable young men and women into the teaching profession and to retain them and those already in the field in the face of the blandishments of other careers.

Teachers' salaries have been in the headlines throughout the postwar period. It's been true for a long time that teaching, except in a few big cities, has been poorly paid compared with many other occupations requiring less expensive training and less ability, but the security of teachers' incomes, both in recession and in old age, to some extent offsets the low base pay. However, the growth in old age security —through both private pension plans and Social Security—and a decade and a half of full employment have reduced the appeal of these offsets.

It goes without saying that many thousands of young men and a good number of young women with the background and ability to become fine teachers go into the business world

Profile of the bulges



each year because of the greater financial rewards, both to start with and later on. But this disadvantage applies to many other professional careers as well as teaching and probably always has been true—except perhaps in the 1930's when opportunities in the business world were extremely limited, especially for new entrants. The difference in recent years—besides the spread of security to nonteaching occupations—is that many alternative professional careers have had a boost in status and in pay relative to teaching.

Young college graduates can do better by getting jobs in the lowest professional grades of the Federal civil services, as social workers or psychologists, or in laboratories or research organizations than they can in teaching, except in the school systems of the larger cities. These alternative professional opportunities are usually sought by the most aggressive and ambitious graduates, so grade and high school teachers tend to come only from those with a special interest in teaching that has a limited pecuniary aspect or simply from those who will not or cannot compete for better paying jobs.

So school teaching has become a relatively less attractive career. Elementary schools, for example, need about 60,000 teachers a year just to replace those who retire, die or leave teaching. Yet fewer than 35,000 new graduates go into elementary school teaching annually. And, moreover, there will need to be an overall net growth in the grade school teaching force of 150,000 during the next five years just to accommodate the expected rise in enrollment. To reduce the pupil-teacher ratio would mean an even further increase in the total number of teachers needed, although there probably never has been a time when classes have been small enough in all communities to meet educators' ideals.

An additional factor is the finding of professional surveys that there are many teachers who do not meet even the most minimal standards. About a third of the country's elementary school teachers do not have college degrees, and over a fifth of the new teachers certificated each year have the equivalent of half or less than half of a complete college education. Since school authorities can be expected to hire the best qualified teachers they can get at the going salaries, the salaries in many places are clearly too low to overcome a "good teacher" shortage. And this is despite the fact that school boards have had to raise funds for large increases in salaries, merely to match rising living costs. Also, they have been in the labor market for *additional* teachers to handle the expanded enrollments. Altogether the problem has become much more severe in the past few years.

Moreover, despite all the discussion and all the action of school boards and state legislatures, teachers' earnings are only a little bit ahead of inflation, compared with prewar. Their average earnings have little more than doubled since 1940, which means an increase in purchasing power of about 10 per cent. This compares, for example, with increases approximating 50 per cent for manufacturing and Federal Government employees.

Considering living costs, teachers made small gains during the War which were more than offset by the 1946-48 rise in prices. Between 1948 and 1950 they made up this loss, and since 1950, despite the post-Korea price rise, there has been a real gain of about a tenth.

A large part of the increase in the average since 1946 is due to very big percentage increases in the extremely low salaries paid rural school teachers in most states. Such big raises were not always initiated by local school boards. Often they were the result of much-publicized state laws which specified minimum salaries for teachers which were above those paid in many rural schools; these legislative minimums were almost always accompanied by substantial increases in state tax funds appropriated to local school systems. Though such laws have in some places practically revolutionized rural schools, they have had little effect on the bigger problem of noncompetitive salaries in urban schools. This is basically a question of whether taxpayers are willing to bear large increases in taxes in order to raise the whole schedule of teachers' salaries, not just the minimum. A decision on this fundamental issue will come only gradually and piecemeal, for this is the characteristic American way, but one way or another, it will determine future levels of school expenditures and the nature of public school instruction.

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Loans level, earnings up

Total loans little changed, net profits up 50 per cent—these two seemingly conflicting results stand out in the Seventh District banking picture at midyear. They reflect, respectively, the mixed trend of general business and the easing credit conditions and rising securities prices which have accompanied it.

In the second quarter of 1954, as in the first, the total of loans outstanding at Seventh District member banks remained virtually unchanged. Business loans declined 3 per cent, in contrast to a stable level in the second quarter of 1953. The drop was concentrated in the District's leading cities—Chicago, Des Moines, Detroit, Indianapolis and Milwaukee. Chief causes were seasonal paydowns by food, liquor and tobacco processors and continuing heavy repayments by metals producers.

Production loans to farmers at the District's country banks climbed 6 per cent during the quarter, as farmers turned to bank credit to supplement their own resources during the spring planting season. During this same period last year such farm loans had been reduced slightly on balance.

Mortgage holdings grow

The real estate credit sector gave clear evidence of the continuing boom in housing. Midwest bank holdings of residential mortgages rose about 3 per cent between April and June, with VA-insured loans increasing a little more rapidly than any other kind. A spurt in the popularity of VA mortgages with Chicago banks keynoted this trend. For all District members, holdings of each type of residential mortgage paper at midyear were about one-tenth larger than a year ago.

In the consumer credit area, opposite trends were appearing. Second-quarter increases in almost all types of instalment credit were well below year-ago rates, and modest net declines occurred in the important automobile paper category. Chief exception to this slowing pace was a 9 per cent growth in non-auto retail instalment paper at banks outside the major cities.

Bank income and outgo

Operating earnings of Midwest member banks showed a moderate improvement in the first half of 1954. Leading this advance were banks in the major cities other than Chicago, with a 14 per cent gain over first-half 1953 in interest income from Government securities and an 11 per cent gain in loan income. In more modest dimensions, other District banks followed this pattern of a relatively greater income gain from securities than from loans. At the same time charges and fees, while small in total, were running 15 per cent above last year's levels.

The half-yearly increase in expenses, however, was slightly more rapid than the rise in operating income. All expenses except interest on borrowed money were up, although Chicago banks held their rise in costs to about half the average 11 per cent increase elsewhere. As a result, net current earnings topped year-ago levels by 10 per cent in Chicago, 5 per cent in the other four major cities and a bare 1 per cent in the remaining District centers. By way of comparison, first-half 1954 net current earnings for all the nation's member banks averaged but 1 per cent above the year-ago figure.

In the first six months of 1954, however, the big factor in Midwest bank profit trends was a turnaround in the "below the line," nonoperating accounts. In place of moderate net losses and charge-offs, banks obtained net recoveries on assets equal to more than one-fifth of their net operating earnings. These recoveries were largely premiums on securities sold, obtainable because of the substantial drop in market interest rates. As a result, even with much higher estimates of income tax liability, net profits after taxes were reported averaging about 50 per cent above first-half 1953, in both larger and smaller Midwest centers.