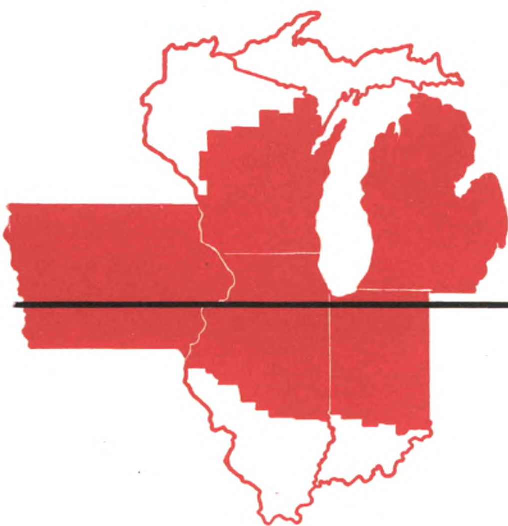
A review by the **Federal Reserve Bank of Chicago**

Business Conditions



1955 December

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THE Trend OF BUSINESS

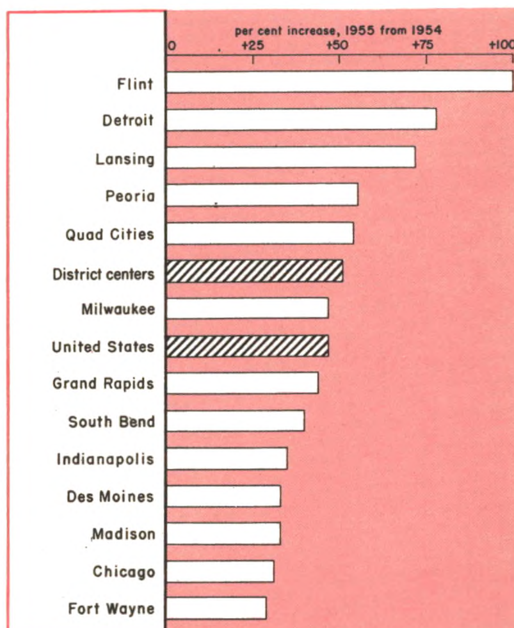
Bullish signs in the business outlook have continued to multiply through the fall. Industrial production has shown further gradual improvement since midsummer and is now 16 per cent above the 1954 low. Despite this spectacular gain, inventories have continued to increase only moderately, indicating that virtually all of the higher output is being passed on in larger final sales. Manufacturers' new orders exceeded 28 billion dollars in both August and September for the first time on record, and order backlogs have climbed nearly 5 billion dollars, or 10 per cent, in the last five months.

The recently completed McGraw-Hill survey of business intentions has bolstered the expectation that capital expenditures would show a further substantial rise in the coming year. According to this survey, manufacturers plan to increase outlays for new plant and equipment next year by a whopping 30 per cent. Firms in several industries, including steel, nonferrous metals and automobiles, anticipate boosts of more than 50 per cent. Total outlays of all businesses are expected to rise less than the manufacturing segment, due principally to a 10 per cent reduction planned in the capital expenditures of public utility and 15 per cent for mining firms. Nevertheless, total business outlays are expected to be up a substantial 13 per cent.

In the current setting, the outlook for Christmas trade appears rosy indeed. Consumers are better off financially than ever before and are still in a mood to buy. Total civilian employment is three million larger than a year ago. One million of the addition came from the ranks of the unemployed and the military and two million entered or re-entered the labor force over the past year. Fatter paychecks reflect widespread increases in wage rates in recent months, and workers in many industries are drawing substantial amounts of overtime pay. Average weekly earnings in manufacturing in October amounted to $78.69, up 9 per cent from a year ago. Total personal income has risen by a 20 billion dollar annual rate, or 7 per cent, over the same period.

Retail sales have been strong during the fall. Total volume in September and October was up 10 per cent from the same months of 1954 and at the highest rate this year on a

New car registrations up sharply in District centers in third quarter



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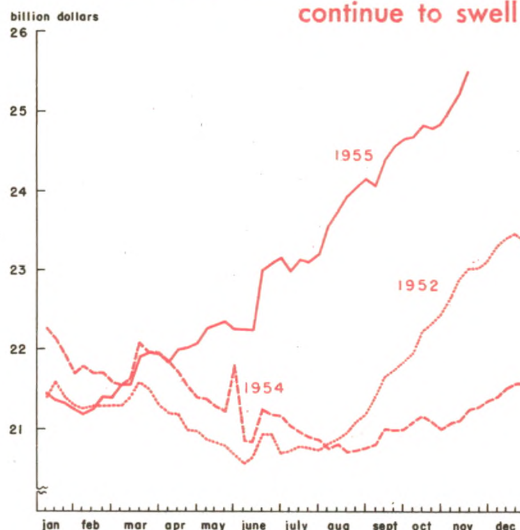
seasonally adjusted basis. Automobile dealers far outdistanced all competitors in the year-to-year gains, but total sales of all retail outlets other than the automotive group were up 7 per cent from the 1954 fall volume. Furniture and appliance stores have made a vigorous showing recently, with sales volume running 10 per cent above that of a year ago. General merchandise outlets, including department stores, have also done consistently better than a year ago. Among major District centers, big store gains over a year ago in the four weeks ended November 12 ranged from 16 per cent in Detroit to 7 per cent in Chicago and Indianapolis.

Peak rates of automobile output seem assured for some months to come. Cleanups of 1955 models appear to have been unusually successful this year, and first reports from manufacturers indicate a continued record sales volume for this time of year in the new 1956 lines. The exceptional strength of sales toward the end of the 1955 model run is evidenced in all District metropolitan centers. New car registrations in the 23 largest centers during the third quarter totaled 51 per cent more than in the same months of last year, as compared with a gain of 25 per cent in the first half.

Manufacturers are scheduling output in November and December at about 750,000 units, up from 470,000 in September and 520,000 in October. If reached, this would rival the peak rate of output achieved last spring—an all-time record. Considerable overtime is being planned to accomplish this objective. Ford Motor Company recently announced a 53-hour week in most of its assembly plants for the rest of this year.

Business inventories continued to show only modest expansion through September, and the high rate of sales since then suggests that the accumulation of stocks has not accelerated appreciably. Virtually all of the increase in recent months has been at the manufacturing level. Even so, manufacturers' stocks have climbed only 4 per cent since the 1954 low, while sales are up 18 per cent and new orders about 30 per cent.

Business loans at leading city banks continue to swell



Data exclude CCC certificates and loans reclassified on October 5, 1955.

At retail, the ratio of inventories to sales has declined somewhat since midsummer, mostly due to the reduction in automobile dealers' stocks, and is now at the lowest point in many years. Auto dealers' stocks, of course, are now being replenished rapidly with 1956 models. Many business firms clearly would like to expand inventories considerably further but have been prevented from doing so to date by the excellent level of sales. Thus, further rebuilding is in prospect for the months ahead. Meanwhile, lead times on deliveries have lengthened. The Chicago Purchasing Agents Association reports that 54 per cent of its members now place orders 60 or more days in advance of delivery, as compared with 26 per cent last March.

Business loans at weekly reporting banks continue to expand rapidly, and bankers report a vigorous demand for additional funds despite the rise in the prime rate posted in October—the second in three months. Such loans have risen 3.6 billion dollars so far this year and 2.0 billion since June 29, in sharp contrast to the declines experienced in 1954 and more modest gains in 1953. The biggest increases in

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borrowings since midyear have been by food, liquor and tobacco manufacturers, commodity dealers and trade firms—all seasonal borrowers. The major groups accounting for the difference in loan trends in this period as compared with last year, however, have been metals and metal products manufacturers, public utilities and transportation firms, and sales finance companies—all of whom have reduced borrowings far less since midyear than in the corresponding 1954 period.

The stock market in recent weeks has recovered much of the ground lost in late September. In part, this reflects the flurry of announcements of year-end dividend extras and stock splits. More important, however, investor confidence appears to have been bolstered by the generally optimistic business news, including the highly favorable course of corporate profits. According to the First National City Bank of New York, after-tax earnings of 516 leading manufacturing corporations in the third quarter were 37 per cent higher than in the same period of 1954.

Haga el favor de despachar . . .

Whether in Spanish, Portuguese or English, the sound of "please ship . . . ," coming from a Latin American importer, has taken on a familiar and pleasant ring to the ears of U.S. exporters. The 3.2 billion dollars in merchandise shipped to the twenty republics to our south in 1954 represented more than one-fourth of total U.S. commercial shipments abroad. In the 1936-38 period, the 600 million in merchandise Latin America purchased here annually accounted for only 16 per cent—one-sixth—of U.S. exports.

These gains have exceeded the increases in exports of other nations to Latin America. Today, the United States supplies Latin America with one-half of its imports, while in the immediate prewar years our southern neighbors obtained only one-third of their foreign purchases from us.

While our share of the Latin American market is significantly larger than in the 1936-38 period, it is well below the peak level reached in 1947. That year, U.S. producers supplied Latin America with 2 out of every 3 dollars of merchandise it purchased abroad.

By the end of 1947, however, the large dollar reserves that had been built up during the War were substantially depleted. Furthermore, European producers, having made substantial strides toward restoring factories ravished by war, were again in a position to offer stiff competition for the growing Latin American markets. West Germany in particular sought to regain its prewar position in the twenty nations south of the Rio Grande. As a result, the U.S. share of exports to the area declined about one-half by 1949. Since then, United States exporters have held their ground and have continued to sell the twenty Latin American Republics between 50 and 52 per cent of their purchases abroad.

For individual countries, of course, this figure varies considerably. It ranges from over 70 per cent in Mexico to about 15 per cent in Argentina. In general, the relative importance of U. S. trade is the greatest in those nations located closest to us.

Our ability to maintain a substantially larger portion of the Latin American market has been due in part to the increased dollars made available through expanding U.S. purchases from and investment in the republics to our south. United States purchases from Latin America have increased in each postwar year except

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1949 and are now six times the 1936-38 average level.

The rise in U.S. imports from our southern neighbors has been concentrated in two commodities—oil and coffee. Over the 1936-38 to 1954 period, oil imports from Latin America soared from 30 to 470 million dollars; in quantity, the increase was fourfold. An 800 per cent surge in coffee prices swelled U.S. imports from 140 million to 1,400 million dollars. Copper purchases also showed a large gain, rising from a mere 30 million per year in prewar days to 210 million last year. Whereas these three commodities made up 37 per cent of Latin American exports to the United States before World War II, at present they represent 62 per cent of their dollar earnings from the sale of merchandise.

Midwest specialties

Latin America, as is the case with Canada,[1] concentrates a large share of its purchases from the U.S. in products manufactured in the Midwest. Last year, for example, shipments of industrial, farm and electrical machinery south of the border totaled 800 million dollars, while sales of automotive products surpassed the 400 million dollar mark. Together, firms in these industries received two-fifths of the 3.2 billion dollars spent in the U.S. by Latin American nations.

Latin America is also a good customer of the metal and metal products manufacturers and the pharmaceutical houses, both of which are indentified to a large extent with the Midwest. Metals demand in 1954 was the lowest since Korea, but purchases still reached 270 million dollars. The 120 million of medicinals and drugs bought by Latin America represented about 6 per cent of total U.S. output of pharmaceuticals.

In each of these products, the twenty republics to the south accounted for a large share of total United States exports. As the table indicates, about a fourth of our total sales abroad were to Latin America; exports by commodity class ranged up to 49 per cent in the case of pharmaceuticals.

[1]For a discussion of Canadian imports from the United States, see "Exports headed north" in the October 1955 issue of *Business Conditions.*

A dollar cast upon the waters

United States exports to Latin America have fluctuated sharply in the postwar period, mainly as a result of fluctuations in the dollars available for the purchase of our goods (see chart). Their purchases of U.S. goods reached a peak of 3.8 billion dollars in 1947, rapidly drawing down dollar balances built up during the War. In 1948, the increased supply of European products and the limited dollar reserves combined to reduce U.S. exports to Latin America by 700 million dollars in the face of a 200 million rise in their total imports.

The following year an 800 million fall-off in Latin American purchases abroad and deliberate restrictions against U.S. products, imposed by some countries, notably Brazil, to conserve their dwindling dollar balances, brought an additional drop of 400 million dollars. Although this trend continued through the first half of 1950, improved financial positions and a wave of scare buying following the outbreak of the Korean war boosted U.S. export totals in the final months of 1950, through 1951 and well into the first half of 1952. Shipments to Latin America rose to 3.6 billion in 1951 from 2.6 billion the previous year and advanced slightly further during the January-June 1952 period.

Latin America buys many products important in Midwest output

	Exports to Latin America, 1954 (million dollars)	Per cent of U. S. exports
Industrial machinery.....	450	31
Automotive products.....	410	40
Metals and metal products	270	31
Electrical machinery.....	200	34
Farm equipment........	140	35
Pharmaceuticals	120	49
Other products.........	1,600	19
Total	3,190	26

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The day of reckoning, however, was bound to come. The continuing drain on the dollar reserves of a number of Latin American republics forced a considerable tightening of their controls on dollar imports. Moreover, bulging inventories and a leveling off of prices combined with a slowdown in export sales of the countries in Latin America to lower their purchases abroad. As a result, in the final half of 1952 imports from the U.S. declined to an annual rate of 3.0 billion dollars and fell further in early 1953. Since then, United States sales to Latin America have inched up slowly.

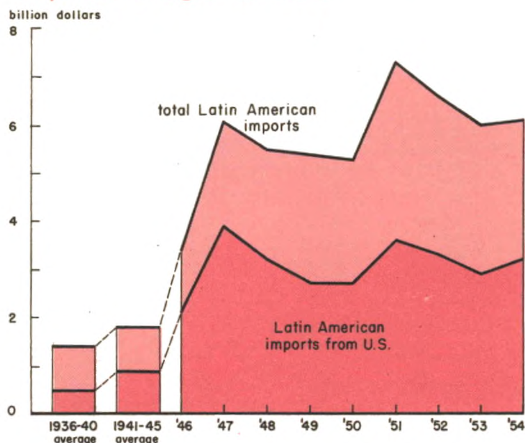
Variation by country

The pattern, naturally, differs from country to country (see chart). The experience of each nation is intimately tied in with its internal policies as well as its own export situation.

Last year, five countries—Mexico, Venezuela, Brazil, Cuba and Colombia—accounted for 75 per cent of U.S. exports to Latin America. The next three countries in order of importance—Argentina, Panama and Peru—together absorbed an additional 10 per cent of shipments to our southern neighbors.

Venezuela and *Colombia* have, in the postwar period, taken an increasingly large share of U.S. sales to Latin America. Exports to these countries have shown the greatest and most consistent gains over the past decade.

One-half of Latin American imports bought in U.S.



Venezuela in 1946 purchased only 200 million of U.S. merchandise, one-tenth of our sales to Latin America. Now, annual shipments to this country, rich in oil and iron ore, total over 500 million, fully one-sixth of exports to the 20 republics combined.

The persistent rise in U.S. oil imports from Venezuela has paved the way for their increased purchases here. The petroleum fields in Venezuela have "pumped a steadily rising flow of dollars" from the United States. At present, three-fourths of U.S. imports from there are made up of oil and oil products.

About 17 per cent of the dollars Venezuela spends in the U.S. goes for industrial machinery with an added 10 per cent for purchases of electrical and farm equipment. This typifies the increased industrialization that is taking place in many of the Latin American countries. The most significant feature of our exports to Venezuela, however, is that they account for almost one-third of U.S. passenger car sales south of the Rio Grande, a reflection of the doubling in Venezuelan real national income over the past decade.

Coffee has been the key to the Colombian prosperity. The rate of growth in national output in the last five years has exceeded that of any other Latin American nation. The second largest coffee producer, Colombia reaped a rich harvest when coffee prices doubled in 1949-50. Although the quantity of U.S. imports from Colombia dropped by 14 per cent in 1950, the value rose by 30 per cent. The drop in coffee prices in 1955, combined with a slide-off in volume of U.S. coffee imports, drew down U.S. purchases from Colombia by 30 per cent. This decline has been reflected in only a slight decrease in Colombian purchases in the United States thus far.

Machinery also bulks large in Colombian imports. Machinery and automotive products make up 55 per cent of its purchases in the U.S. In addition, one-tenth of its imports from this country are composed of metals and metal products.

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Latin America accounts for over a fourth of total U.S. exports

Mexico continues to hold its position as the United States' largest Latin American customer. In fact, Mexico ranks third in importance in U.S. export trade, trailing only Canada and the United Kingdom.

In the early postwar period, Mexico made rapid strides toward industrialization but has been plagued by inflation. Both in 1948 and 1949, the Mexican peso was devalued in order to cut down on imports. These devaluations, together with a shift away from the purchase of capital goods, reduced U.S. sales to Mexico in each of those years.

Machinery again leads the field of U.S. exports. For Mexico, the amount spent on industrial and electrical equipment and farm machinery in 1954 represented 26 per cent of its purchases in this country. The other major commodities are auto products, 13 per cent; chemicals, 12 per cent; metals, 9 per cent; and a rising amount of petroleum products that now account for 8 per cent of Mexico's purchases in the U.S.

Exports to *Cuba* have been somewhat erratic in the postwar period because of fluctuations in sugar prices and hence export receipts. As with most other countries, exports to the United States play a big role in their purchases here. Cuba concentrates over 60 per cent of its

—continued on page 14

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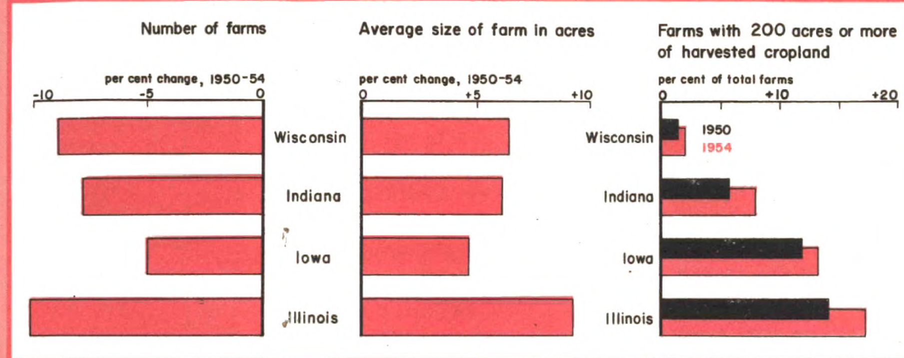
Agriculture

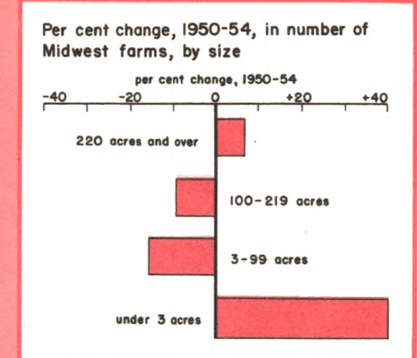
The countryside continues to change. Persistent economic forces, ever at work in a progressing society, are affecting agriculture as well as other industries. With better tools and a greater knowledge of their plants, animals and soil, farmers accomplish much more than formerly in each hour of work. And this means that they must have a bigger business if they and their new machines are to be fully employed.

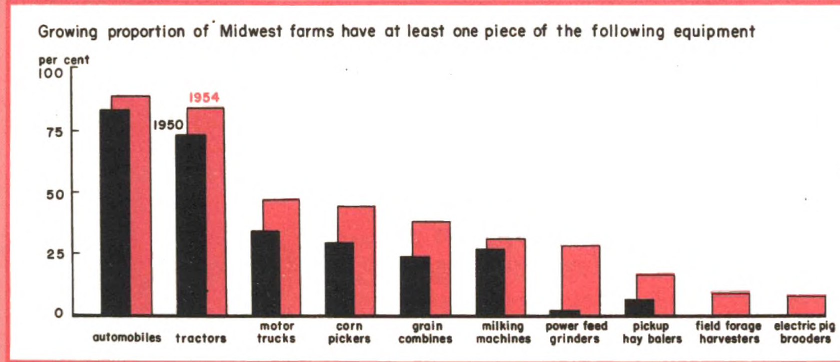
Preliminary census reports for four Midwest states serve to highlight some of the adjustments taking place. The number of farms is declining and the average size is increasing. The increase in average size reflects the larger number of farms 220 acres and over. The number of small and medium-sized farms has declined, but the number of tiny units, reflecting the trend to suburban living, shows an increase. The move to better utilize improved machinery is evident also in the increase in number of farms having 200 acres or more of *cropland*.

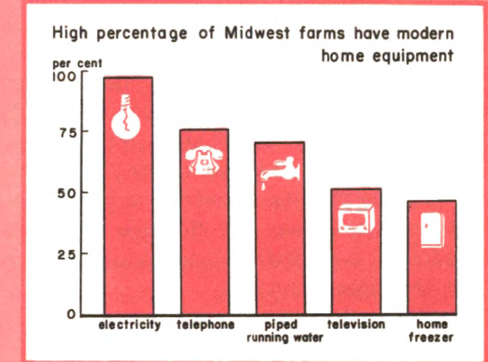
Labor-saving farm equipment and good employment opportunities within driving distance have enabled many farmers to supplement their income by work off the farm. The proportion of *farm operators* with off-farm jobs has increased in each state. The accompanying chart does not include the other members of the farm families for which this trend probably is even more pronounced. Progress is evidenced also in the acquisition of the many facilities and gadgets which contribute to comfortable living whether it be on the farm or in town.

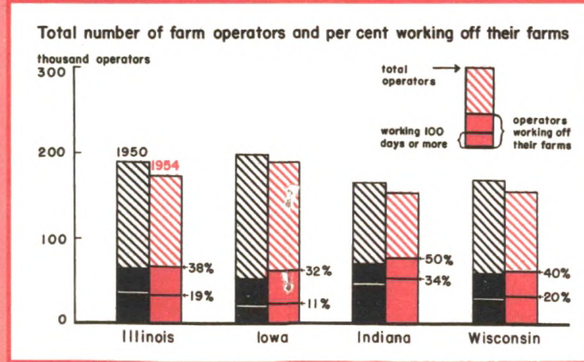
The trend toward specialization is evident also in the census reports, both as it applies to areas and to individual farms. The proportion of *general farms*—having less than one-half of their sales in any one type of commodity—has declined in each state. The proportion of farms receiving most of their income from sales of crops increased sharply. Markets for grains, including "sales" under price support programs, have been quite attractive, and soybeans have become a more important Midwest crop. The proportion of *dairy farms* declined in Illinois and Indiana, and the number of milk cows on farms declined in each state except Wisconsin, where it increased materially. Fewer, larger, more specialized and better-equipped farms, manned by even fewer workers are clearly indicated in recent Midwest trends. These changes have been taking place for many years and there is no evidence in the 1954 Census reports that they have "run their course."

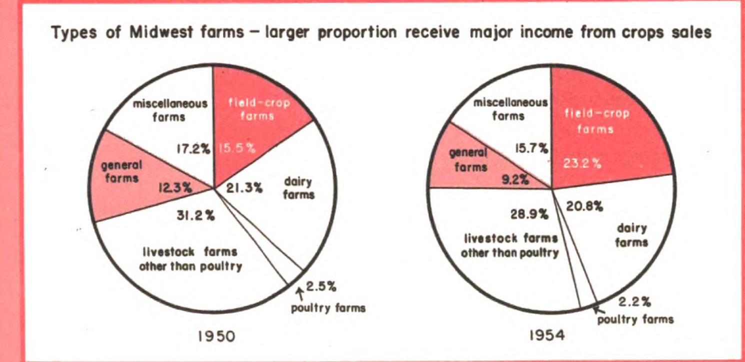












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Changing fashions in department store credit

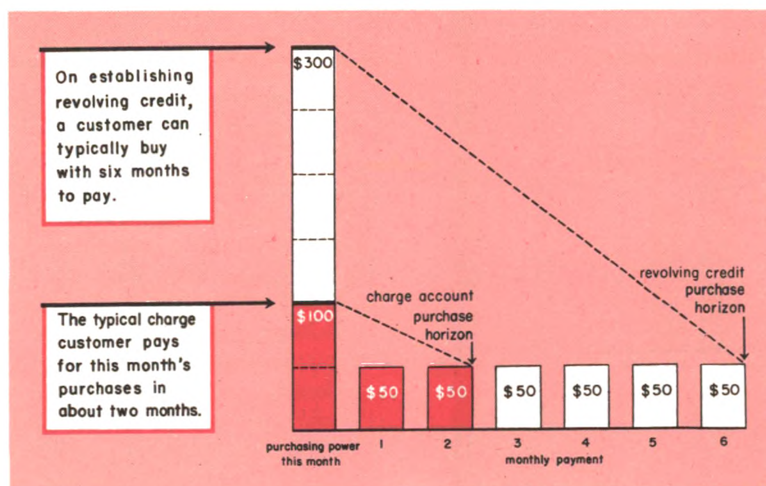
Credit is a persuasive salesman. In a rich economy where a tremendous range of goods and services continuously assaults the consumer's attention—and pocketbook—merchandisers miss few opportunities to break down consumer resistance. One of the toughest barriers to overcome is the limitation imposed by the amount of ready cash in the hands of consumers. Sellers for cash must provoke buying when consumers have funds; sellers for credit, on the other hand, can tempt their clientele at any time.

The power of the credit technique bears particularly on sales of big-ticket items. As early as the 1920's, department stores offered hard goods on the instalment plan. Since that time, instalment sales of refrigerators, ranges, furniture and similar merchandise have expanded into a permanent and significant part of the department store sales pattern. More recently the growth of revolving credit plans has furnished more and more customers with the opportunity to buy apparel and other soft goods items on deferred payments.

Until the development of revolving credit, soft goods have typically been sold either for cash or on charge; and, in many instances, a charge sale is essentially a cash sale. Some charge plate holders prefer this mode of payment simply for its conveniences—elimination of the necessity to carry large sums of cash, greater ease in making returns and adjustments, systematic monthly payment of a consolidated bill and the record of payment afforded by a canceled check. To others it may permit a purchase that might otherwise be deferred for a month or two; but, even so, as long as credit is available only as short-term charge credit or instalment credit for individual hard goods purchases, its effect is to limit the purchase horizon of soft goods customers of department stores. In particular, the soft goods customer has lacked the ability to buy a variety of small items now—say a complete outfit—and spread payment over many months ahead.

Aggressive merchandisers first approached the problem of lengthening the soft goods purchase horizon by the sale of coupon books. The

The revolving credit customer's purchase horizon is about triple that of the charge account customer



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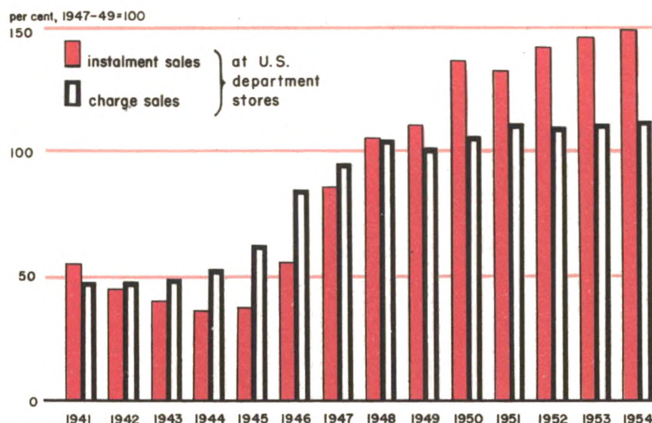
coupons could be used as cash to buy anything in the store, but typically payment for the book took place in six monthly instalments. Such books, however, have not completely met the problem. For one thing, they do not carry the prestige of a regular charge account and, for another, once the original book is used, the customer is free to transfer his purchases to other stores.

During the depression, some department stores fell into a habit that in practice amounted to serial payment of charge accounts. Happy to deal with their "good but slow" charge customers, they freely granted them the privilege of paying on a 30-60-90 day basis with neither formal contract nor carrying charge. In the prosperous years during and since the War, many customers have consequently felt free to pay off charge accounts in several instalments. In 1954, for example, the ratio of monthly collections to department store charge account balances was slightly less than one-half.

Although both coupon books and three-month terms are still part of the credit schemes at some stores, a new method of extending credit has been devised in recent years to expand credit sales of soft goods. Known by various names but commonly dubbed "revolving credit," the plan consists in essence of setting up a customer as a sound credit risk and assigning him a credit limit. The customer then has the privilege of being perennially in debt to the store up to that amount. Monthly payments are required, but once the customer has cleared part of his quota through repayments, he can immediately rebuild his debt back to the maximum. Charges for the credit service are based on the unpaid balance at the end of each month—usually 1 per cent, but occasionally as much as 1½ per cent.

Revolving credit plans have grown rapidly in the last five years, especially in large department stores. The National Retail Dry Goods Association reports that 42 per cent of stores with annual credit sales over 20 million dollars offered a revolving credit plan in 1950; at the beginning of 1955, 65 per cent did so. On the other hand, it has only been since 1952 that stores with a smaller credit volume have become greatly interested in the plan. Between that year and 1954 the proportion of department stores with credit sales between 2 million and 5 million dollars offering revolving credit plans rose from 24 to 44 per cent.

Instalment sales, including revolving credit, have risen more than charge sales



It is generally agreed that the percentage of total department store credit extended under revolving credit schemes has increased along with the number of stores offering such plans. Unfortunately, stores have, with only a few exceptions, merged their revolving credit sales with their other accounts. Consequently, separate reporting has not been possible, and revolving credit sales are included under instalment sales in Federal Reserve statistics.

It can be seen that revolving credit, as developed in department stores, combines the time payment feature that makes instalment sale so effective in the promotion of household goods with the emphasis on soft goods that characterizes the privilege of charging. At the same time it encourages customers to satisfy substantial immediate requirements for soft goods even

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when they need a number of months to pay off the entire bill.

How revolving credit has grown

Revolving credit has entered the credit picture in two ways. In many stores it has been introduced alongside of regular charge and instalment account facilities already offered. This has been the case in most of the big State Street stores in Chicago and the leading Detroit department store, Hudsons. On the other hand, the giant mail order chain, Sears, Roebuck and Company, has established revolving credit in more than 250 of its 700-odd stores despite a general policy of not offering charge accounts to its customers. Montgomery Ward is also experimenting with revolving credit in its retail outlets.

One aspect of revolving credit—namely, the fact that it is continuous credit—has been carried over into some instalment sales systems in the form of a continuous budget account. A continuous budget differs from the conventional instalment contract chiefly in that credit is established only once. On the basis of the original document, new purchases of big items can be made by an "add on" arrangement that saves the customer the trouble of making out forms and re-establishing his credit.

Although it is probably a long way in the future, some observers suggest that all forms of credit ultimately may be combined into one administratively. A revolving credit plan with the proviso that accounts paid in 30 days will not be burdened with any carrying charge preserves the convenience of the charge plate with the savings of cash payment. The possibility of time payment, however, permits the extension of the purchase horizon. It is most probable that six-month terms would be retained on soft goods and longer terms given on hard goods, but both programs could be operated from the same credit files. Any customer, once he had established credit, would know that he could buy any goods in the store on terms. While this development would be a logical evolution of present trends in credit-granting schemes, it is not imminent. Many charge account customers apparently prefer to continue on their present basis which combines convenience with prestige. Whatever its long-term development may be, however, one immediate effect of revolving credit has been to permit department stores to offer credit to more of their customers for a wider variety of purchases than ever before.

Corporate profits soar

The rapid rise in general business activity since mid-1954 is carrying 1955 pre-tax corporate profits to the highest level in history. As usual, corporate earnings are showing much larger changes than many other economic measures. For the year as a whole, profits may exceed 1954 by 25-30 per cent, whereas the rise in over-all activity will be about 7 per cent. Between 1953 and 1954, profits dropped 11 per cent in contrast to a mere 1 per cent decline in the nation's output.

At the start of 1955 there was a common tendency to underestimate the strength of the upturn in progress at that time. The Treasury Department, for example, forecast a decline in tax receipts from corporations in fiscal 1956. In late summer, estimates were revised upward by 2.2 billion dollars or 8 per cent. Since then, sights have been raised another billion or two.

Many of the costs of doing business are fixed or move up very gradually during a period of rising sales. Thus, costs per unit tend to fall

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as output advances. This fact, coupled with the ability of business firms to increase prices in a time of exuberant demand, has more than offset added costs resulting from the substantial wage boosts and rising prices of many raw materials, particularly metals, during the current year.

The tendency for costs to catch up with increased selling prices may put a damper upon further improvement in profits from current record levels in the months ahead. Finished goods prices have risen about 5 per cent since last year, more than the prices of things producers buy. To date, profit gains over last year have shown continued improvement on a quarter-to-quarter basis. The First National City Bank's tabulation of 739 firms showed a 33 per cent rise in the third quarter compared with a 31 per cent boost for the first nine months. Fourth-quarter comparisons will be affected, of course, by the pronounced upturn noted in the final months of 1954.

Biggest gains in hard goods

Despite the large gain in total business profits, there was a wide dispersion between firms within a given industry as well as between industries. The following table shows profit changes before taxes for various industrial and utility categories. Since some industries have shown substantial advances from relatively depressed levels, comparisons are made with 1953 as well as last year.

	First six months	
	1954-55	1953-55
All manufacturing	+30	+1
Food	+8	+5
Textiles	+23	−15
Chemicals	+33	+12
Oil refining	+6	+5
Steel	+73	−3
Machinery, electrical	−3	−31
Machinery, other	+6	−20
Motor vehicles	+76	+33
Railroads	+74	−16
Electric power	+10	+15
Telephone	+23	+37

SOURCE: FTC, ICC, FPC and FCC.

Sales of manufacturing firms during the first six months of 1955 topped last year's first half by only 10 per cent, demonstrating the greater than proportional impact of increased volume upon profits. Sales and profits before taxes barely exceeded the 1953 totals. Mainly because of the ending of the excess profits tax in the interim, after-tax earnings of all manufacturers were 23 per cent higher this year than in 1953 and after-tax margins on sales rose from 4.4 to 5.3 per cent.

The large profit increases for steel, automobiles and railroads are largely responsible for the more than proportional gains in activity noted in the Midwest. Virtually all business categories are reporting substantially larger profits than last year (the electrical machinery group was strongly influenced by the poor showing of Westinghouse), but many of the groups did not regain 1953 levels. Some lines such as railroad equipment and industrial machinery were only beginning to taste the fruits of booming orders in the first half of this year, but profit comparisons will improve for the year as a whole. In short, it is evident that the profit upsurge has been selective and that stiff competition has continued to characterize most segments of industry.

Smalls vs. bigs

Very large firms have made somewhat larger improvements in profits than the totals this year, just as they suffered less decline in the 1953-54 comparison. Profits of the 200 large manufacturers tabulated by the Federal Reserve Board, for example, increased 39 per cent in the first half compared with the 31 per cent gain estimated for all producers. All corporations, including the less profitable retailing and construction lines, rose only 27 per cent in the first half.

Taking the 100 million asset size in manufacturing as a dividing line, the larger firms increased sales 14 per cent and profits 34 per cent in the first half whereas for the smaller group the figures are 6 per cent and 24 per cent, respectively. In part, these better results for very large firms merely reflect the fact that prosperity has benefited especially the steel and automotive lines which are heavily domi-

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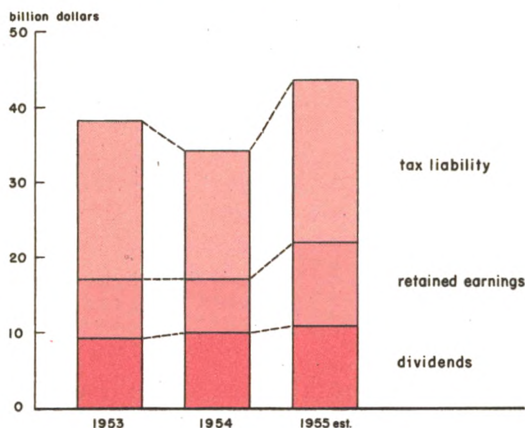
Corporate earnings spurt boosts taxes and retained earnings; dividends rise less



nated by firms in the upper bracket. Nevertheless, within most categories there is some tendency for the largest producers to achieve higher earnings. In fact, certain firms have actually lost money.

General Motors earned net profits after taxes of 913 million dollars in the first nine months of 1955, up 56 per cent over 1954 and more than in any previous full year; Ford also reported earnings to be at record levels, and Chrysler stated that its nine-month net had been raised to 70 million from last year's meager 2 million. American Motors and Studebaker-Packard, on the other hand, are expected to show red ink figures.

Where the money goes

The record levels of corporate earnings this year will benefit the stockholder as well as the Federal Treasury. Dividends may reach 11 billion, up 10 per cent from the record 1954 level. This would mean about a 50 per cent payout and leave an equal amount of undistributed profits for future use in the business. Retained earnings averaged only about 7 billion dollars from 1952 through 1954. The substantial rise in retentions together with an even larger sum from ever-rising depreciation allowances will continue to dominate the financing of capital expenditures, apparently heading for a record year in 1956.

The very favorable corporate earnings reports covering the third quarter played an important part in the stock market recovery in late October and November. Despite the 70 per cent advance in stock prices during the past two years, price-earnings ratios remain low relative to bull market peaks in the past. High-grade issues are selling at about 12 times current earnings compared with 19 times in 1929 and 16 in 1946. Dividend yields on these shares average better than 4 per cent. Stocks of firms in industries expected to experience some drop in earnings next year are capitalized more conservatively than these averages.

It is generally believed that the level of business activity in 1956 will average higher than 1955 but that a leveling off will occur as the year proceeds. Should this pattern prove to be correct, costs probably would rise further. On balance, it would appear that next year's profits will approximate those of the current year—a favorable prospect for "the tax collector" and shareholders alike.

Exports—*continued from page 7*

agricultural production in sugar and thus depends to a large extent on imported foodstuffs. About 30 per cent of its purchases from the United States are made up of food products with grains amounting to 50 million of the 125 million dollar total food purchases. Textiles also take a bigger share than is the case in most other Latin American nations. Last year, one-ninth of Cuban expenditures in this country was for manufactured cloth and fibers.

Exports to *Brazil* have been notable for their sharp fluctuations in the postwar period. Sales to our major coffee supplier declined from 1948 to 1950 as dollar reserves had been depleted and restrictions were imposed on imports from the United States. These controls were eased in early 1950, and our shipments to Brazil rose

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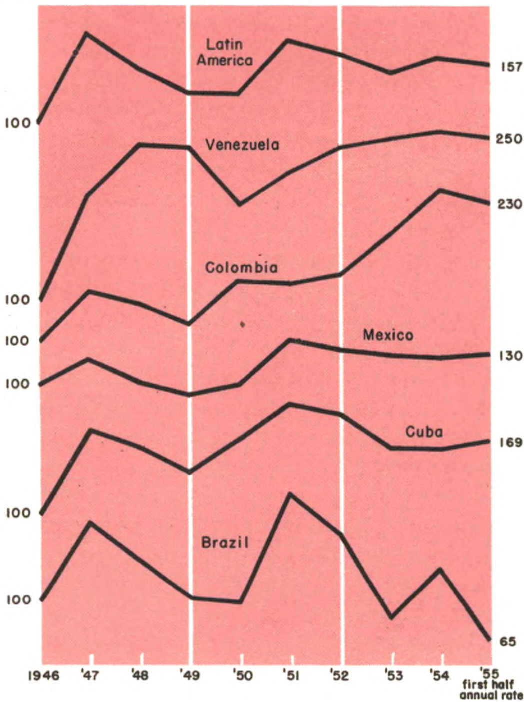
U.S. exports to major Latin American customers show varying trends



dramatically. By 1951, exports to that nation reached 700 million, more than double the 1950 level. This buying spree continued into 1952, but by the end of the year it was again necessary for Brazilian authorities to clamp down on imports.

Inflation has aggravated Brazil's already difficult balance of payments situation. The cost of living in Rio de Janeiro, the capital, has increased at an annual rate of 16 per cent from 1951 through mid-1955. Restrictions imposed on Brazilian imports from the United States have hit most consumer goods severely. Exports of autos and parts, for example, are now at one-half the 1952 level. In 1947, machinery purchases from the U.S. accounted for 24 per cent of total imports from this country and in 1951 represented 30 per cent. Machinery exports last year represent more than one-third of our sales to Brazil.

Latin America has been one of the fastest growing markets for U.S. exports in the last two decades. Economic activity, in real terms, has increased at the very rapid rate of 4 per cent per year since the mid-Thirties. Since 1945, the growth rate has exceeded 5 per cent. The economies of Latin America should expand substantially in the next two decades. Even at the lower 4 per cent annual rate of increase, 1975 output would total 100 billion dollars, two and a half times the present level.

Along with the growth will go an expanded demand for imports. No doubt the composition of purchases will shift. As incomes rise, a larger share will be devoted to semi-luxury items—automobiles for instance—that would allow the U.S., and the Midwest, to maintain their position as suppliers. Nevertheless, competition in these markets will remain stiff. All the industrial countries of the world are aware of the potential demand of Latin America and can be expected to attempt to boost their sales in that area.

In the next few decades, the dollar earnings of Latin America should continue to increase as the U.S. comes to rely more and more on foreign sources of raw materials. The recent discoveries of iron ore in Latin America have added another commodity to the list of important industrial materials for which the countries to our south will be an important supplier. If, in this environment, the U.S. exporters can continue to at least hold their own as they have done in the past few years, requests from Latin American importers to "please ship . . ." will become increasingly frequent.

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

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Christmas cash

Equipped with a pocketful of cash, in addition to checkbook and charge plate, the American consumer sets out shortly after Thanksgiving on the serious business of Christmas shopping. In the ensuing weeks before December 25, his gift purchasing, increased travel and entertainment expenditures, gifts of money, and other special outlays connected with the holiday season combine to produce a seasonal peak in the amount of money in circulation. If currently mounting cash requirements approximate those of recent years, between 300 and 400 million dollars will be drawn into circulation over the three weeks preceding Christmas 1955.

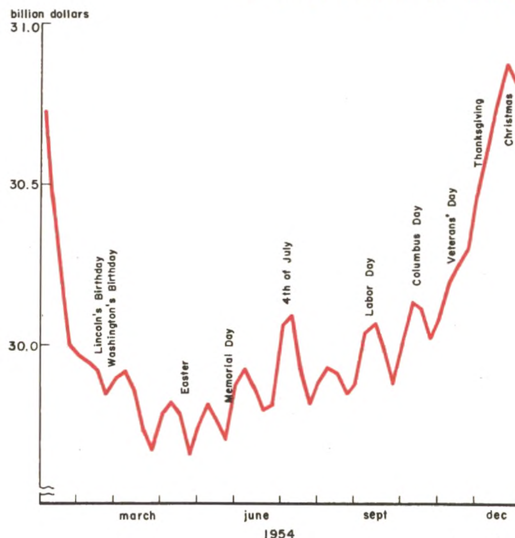
Apart from fluctuating seasonal demands, however, changes in the amount of cash in circulation—defined as all currency and coin outside the Treasury and the Federal Reserve Banks—have been relatively minor during the past three years. The explanation for this relative stability during a period which brought significant change in many other economic indicators lies in the comparative steadiness of prices and expenditures for goods and services which normally involve payment of cash.

Over the years, circulation of currency and coin has tended to follow somewhat the same pattern as consumer spending. In particular, the volume of consumer outlays for nondurable goods seems to influence the volume of cash in circulation, especially coin and the smaller denominations of bills. Making such purchases, after all, is probably the most important single use of cash. Unlike outlays for durables, expenditures for nondurables—food, clothing and the like—tend to be more regular, are usually made in smaller lump sums and involve credit or payment by check less frequently.

The increased demand for cash during the Christmas season typically extends to coin and all denominations of currency up to and including $100 bills. In general, the smaller the denomination, the bigger is the holiday bulge in the amount in circulation. Consumer expenditures, particularly for nondurable goods and the less costly durable items, typically reach their annual peak during the Christmas season and involve mostly the "commercial" denominations of $20 bills and under. Once the holiday is past, however, cash needs dwindle and the surplus flows back rapidly to commercial banks and the Reserve Banks. Before the end of January, outstanding currency totals are typically back to pre-holiday levels.

The amount of cash in circulation depends solely upon the combined decisions of private users, subject of course to the fact that they can obtain no more than they can pay for. As individuals and businesses cash checks drawn upon demand deposit accounts, the volume of cash in circulation expands; conversely, as the public builds up checking accounts with cash deposits, the volume of cash contracts. This expansion and contraction is largely automatic with the commercial banks, the Treasury and the Federal Reserve Banks serving as agents to satisfy the composite choice of individuals and business for a greater or lesser amount of cash.

Seasonal patterns in circulation of cash



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Business Conditions

a review by the Federal Reserve Bank of Chicago

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