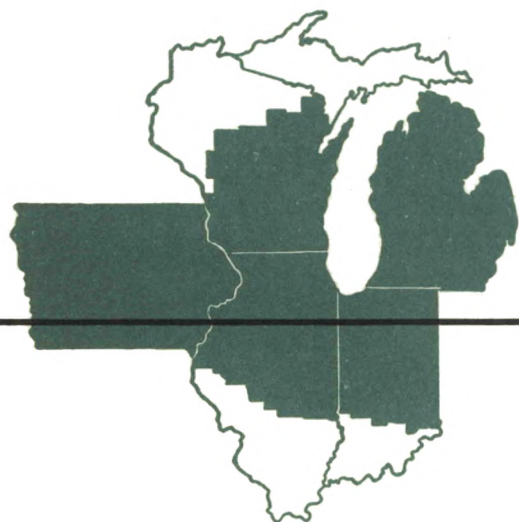


A review by the **Federal Reserve Bank of Chicago**

Business Conditions

1957 February



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THE Trend OF BUSINESS

The usual seasonal layoffs and early year letdown in retail sales have been overshadowed thus far in 1957 by a steady stream of data which documents a continued forward momentum of the American economy.

Retail sales in the final two months of 1956 broke through to a seasonally adjusted rate of 16.4 billion dollars, about 4 per cent above a year earlier. Deliveries of new cars in December remained 14 per cent below the same month of 1955 but moved above the year-ago number in the first ten days of January. Department stores and other purveyors of gift merchandise benefited from a generous Christmas trade, all the more welcome because shoppers had tended to delay their purchases until the final weeks of the season.

Industrial production ended the year at a record level and averaged out the year 3 per cent above 1955. Total wage and salary employment, moreover, rose almost continuously through 1956, on a seasonally adjusted basis, and amounted to 52 million at year-end, up one million in 12 months.

Investment a question mark

That the current momentum will be sustained for awhile at least is indicated by spending prospects for the consumer and government sectors. Consumers are in a position to expand their buying further and are expected to at least maintain their recent volume of purchases. Government outlays are almost certain to rise substantially. Increased spending on foreign aid, the military establishment and domestic welfare measures are indicated. The President's budget calls for an increase of Federal spending of 4.7 billion dollars for the fiscal year beginning next July 1. In addition,

spending by state and local governments continues to increase. If any significant weakness should develop in the trend of activity during 1957, it is generally thought it would stem from the business investment sector.

A few firms have announced postponement of planned outlays. However, any letdown in capital spending during 1957 doubtless would be small in dollar amount. Order backlogs for machinery and equipment remain at a high level, and business firms have reported plans for a larger outlay than last year.

There is greater concern over the course of total business inventories which reached 88 billion dollars on December 1. This stock-on-hand was 6.3 billion greater than a year before — a rise of 8 per cent compared with a 5 per cent rise in sales. Inventories generally have been considered ample, but not too high.

However, in October and November the book value of business inventories was rising at an annual rate of over 8 billion dollars, a fast pace and one not likely to continue. Moreover, virtually all of the rise was occurring in one segment — durable goods manufacturing. The general rise in prices was responsible, in part, for the inventory development, but much of the increase represented a physical rebuilding of steel inventories which had been cut back during the midsummer strike.

Capacity margin expected in steel

On January 1, the steel industry estimated its capacity at 133.5 million tons, allowing for some facilities which were to come into production during the early months of the year. Operations during January were virtually at the new capacity estimate with 2.5 million tons of ingots being poured each week. The more op-

timistic estimates of demand in 1957 called for little over 120 million tons, and most experts looked to a figure closer to the 115 million level of 1956. New ordering by steel users appears to have slowed somewhat. In the case of the automotive industry, demand has not come up to earlier expectations.

Sometime in the months ahead, therefore, steel operations are expected to slip back from capacity rates. As inventory building ceases, it is possible that some users, impressed by the prospect of prompt deliveries and the fact that work stoppages are unlikely until 1959, may seek relief from financial stringency by reducing their inventories. This source of funds apparently is now being utilized in the case of paperboard and certain other materials.

Capital markets remain tight

Yield indexes for all major types of bonds continued to rise through year-end. Seasoned issues of top-grade corporates showed average yields of 3.9 per cent at the start of 1957 compared with 3.1 a year earlier, and lower caliber securities had advanced even more. In January, there was a moderate recovery in bond prices, but calendars remained heavy.

At the height of the demand in the spring of 1953, Standard and Poor's average of A1+ bonds yielded 3.4 per cent after an advance of one-half per cent from the lows of the previous year. In 1955-56 the rise was a full percentage point. Municipals and Governments had advanced at least in step. Shorter-term Governments, pressed down in price by bank liquidation, showed the most spectacular increases in yields.

As usual, newly marketed issues were affected most by declining bond prices. An American Telephone and Telegraph Co. subsidiary sold bonds in January to yield 4.6 per cent, the highest for such an issue since 1929. The quarter-billion flotation of the parent telephone company scheduled for March was expected to arrive amidst a crowd of other offerings which would probably boost total security sales above the record level of the first quarter of 1956.

Pressure for long-term funds for financing

business firms and municipalities held forth little prospect for any improvement in the home-building picture during 1957. Estimates of housing starts this year range downward from 1.1 million, the 1956 level.

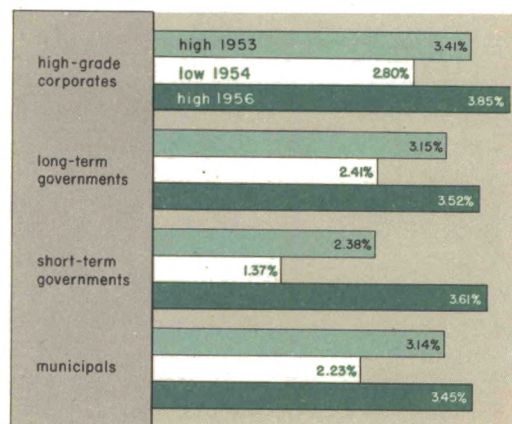
The combined strength of these competing demands for long-term money in an atmosphere of continued price inflation has led to a plea for more savings to fill the gap between creation of capital goods and funds made available from current income. Actually, consumers have been saving a somewhat larger proportion of their incomes than in 1955, but not so large as in the 1951-53 period.

What will consumers do?

If business investment does decline, there is no assurance that the drop would bring about a neat equation of savings and investment. The tendency has been for such movements to feed upon themselves and lead to a general slackening in the pace of business activity. But this is not an inevitable result. If demand from another sector takes up the slack, over-all growth could continue.

Consumption outlays account for about two-thirds of total spending. Every year in the post-

Bond yields up sharply in the past two years; exceed 1953 highs



SOURCE: Standard and Poor's

war period Americans have increased their spending on consumption. This was the case even in the "recession" years of 1949 and 1954. Debt has been incurred to help maintain this spending. Consumer credit rose in each of these years. But the great bulk of the spending and, for that matter, the ability to incur debt has been based upon solid ground—a continuous, if uneven, year-to-year growth in spendable income.

The upward march of personal income has been attributable mainly to its principal component, wages and salaries, which accounts for about 70 per cent of the total. Higher labor income, in turn, has been compounded of two factors, more jobs and higher wages.

Employment declined in a number of post-war years, but in 1956, as in 1955, the gain in labor income was aided by both a rise in employment and higher salaries and wage rates. In each of these years average nonfarm wage and salary employment increased by 1.5 million, or about 3 per cent.

Average weekly wages in manufacturing topped 84 dollars in December compared with less than 80 dollars a year earlier, an increase of 5 per cent. Further boosts of 5-10 cents an hour were scheduled for many industries during 1957 without new negotiations. Additional

millions, moreover, are now covered by cost-of-living adjustments. The steel workers received their first benefits from such a provision in January. Hourly workers obtained a boost of 3 cents an hour and salaried workers an average of 5 dollars per month as a result of increases in the Consumer Price Index.

Factory workers are not alone in achieving yearly wage boosts. Construction workers gained even more proportionately during 1956, and employees of trade, utility and financial establishments also enjoyed substantial increases. The shortage of office workers in many large centers remains acute. Across-the-board raises and continued enhancement of fringe benefits are not uncommon even when collective bargaining is not involved, as management attempt to compete for adequate work staffs.

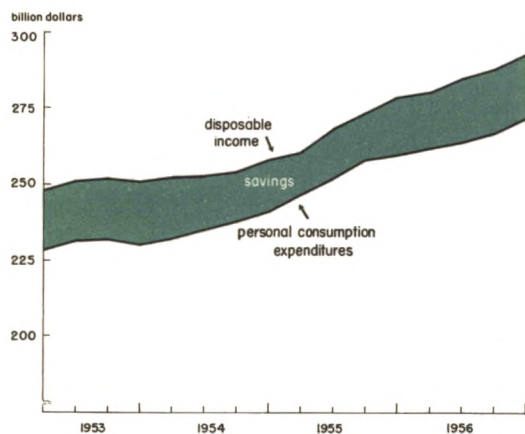
Midwest employment trends vary

Although most Midwest cities were sharing in the growth in income and employment during late 1956, there was a considerable variance in the performance of individual centers. Automobile and farm machinery firms were recalling laid off workers during the fourth quarter, but for most of the cities in which these industries are dominant, employment remained below year-ago figures and unemployment was larger. Nevertheless, the improvement was sufficient to cause the Labor Department to reclassify Flint, Lansing, Racine, Kenosha and South Bend as areas where employment had shown material gains.

Among the larger centers Milwaukee and Chicago reported November 1956 employment to be significantly higher than in 1955. Indianapolis was about the same. Detroit employment was off over 30,000 or 2.4 per cent, and unemployment there was estimated at 81,000 compared with 35,000 twelve months earlier.

The number of persons receiving unemployment compensation recently has been somewhat higher than last year's low level in both this area and the nation. For individual states the situation varied between a 50 per cent increase in Michigan to a slight decline in Illinois.

Individuals' income and spending rose steadily during 1956



Is credit too scarce and too costly?

Probably no questions are asked more often nowadays than, "Is credit too scarce?" and "Are interest rates too high?" Mr. Carl E. Allen, President of the Federal Reserve Bank of Chicago, was asked recently to discuss these questions before The Economic Club of Detroit. His remarks are reproduced below.

The broad objectives of the Federal Reserve System are today generally recognized as:

1. the protection of the dollar's purchasing power by the maintenance of a sound credit and banking system, and
2. the encouragement of economic growth and high levels of employment by reliance on flexibility of credit policy.

In considering the question asked here, we must bear in mind that the responsibilities of the Federal Reserve System have been defined by Congress in acts that represented the wishes of the American people. The major legislation bearing on the System was enacted following periods of serious business and financial difficulties — not immediately following those periods of depression, but several years after. In other words, they do not represent hasty action — rather, they were carefully considered pieces of legislation. Without doubt they reflected the impatience of the American public with the costs of avoidable excesses of expansion and contraction.

Objective vs. actions

As might be expected, there has been very little disagreement from any quarter with the objective of avoiding excesses. But misgivings have arisen about the actions taken to achieve that end. For example, opinions differ on the diagnosis of economic conditions and prospects which prompt policy actions. There are those, too, who have definite and fixed ideas of a minimum monetary diet regardless of economic conditions. Still others prefer a different timing and

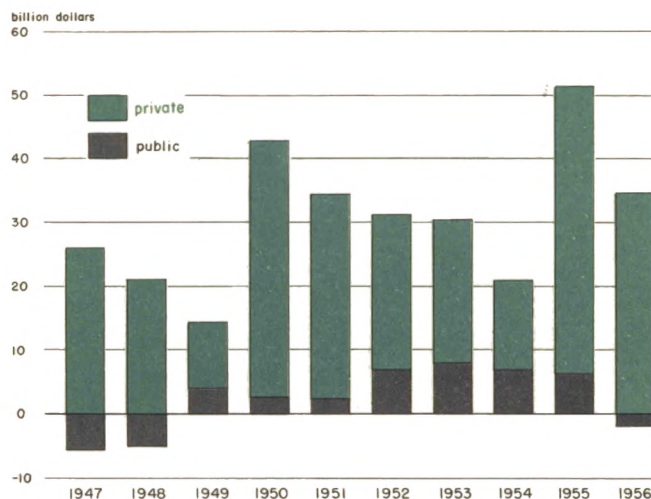
dosage than the monetary authority adopts. And, finally, there are those who really have no opinion on either the need for action, the remedy or the timing, but want, above all, to be sure the costs and inconveniences of any policy are borne by someone else.

As to deciding whether to act, and when and how, it is unfortunate that monetary policy cannot wait until all informed opinion is in agreement. In a sense, that would be almost like fixing a course of medical treatment after the patient had departed this world. Early detection of the evidence of economic bad health simplifies the treatment and brightens the prognosis — it may be the difference between success and failure in averting excesses.

Optimum growth

The problem we face today is to avoid the costs of rates of economic growth in excess of the community's savings — rates of growth which cannot be realized without exposure to inflation. When our resources, both human and otherwise, are fully employed, the Federal Reserve must use its influence to restrain disproportionate growth in money and credit. In these circumstances an expansion fully responsive to demand can only lead to increased prices and to reinforcement of speculative activities. This is because at any given moment we have only so many hands, so many brains to direct them and so many machines for them to work on. When all are fully employed, they can produce only so much goods and so many services. Beyond that point, adding to demand can only force up the price for the existing supply.

Total debt rose 32.8 billion dollars in 1956



Concern over a sluggish rate of economic growth is not now an issue. On the contrary our present day economy is trying to expand its consumption and add to its stock of public and private plant at a too rapid rate. There is too much growth, not too little! Moreover, this is not a harmless excess we can ignore, but one which threatens the worth of our dollar.

Economy under pressure

Let's summarize the present situation in which some say that money is too scarce and too costly. (1) Employment is and has for some time been at record peaks. (2) Many of our basic industries are and have been producing at full capacity and some beyond rated capacity. (3) Wholesale prices of industrial commodities are averaging more than 8 per cent higher than in mid-1955. (4) Consumer prices rose by nearly 2.5 per cent in a year. (5) An old-fashioned capital goods boom is putting a severe strain on savings.

For some months now the demand for credit to finance industrial and commercial plant and equipment expenditures, inventories, public

works and housing has exceeded the available supply of savings. A very large proportion of this demand was met in 1956 as witness the increase in over-all debt of more than 30 billion dollars. Included in that figure is $5\frac{1}{2}$ billion more of loans by banks to business, $5\frac{1}{2}$ billion more in new corporate debt issues, almost 3 billion more to consumers, over 10 billion more in residential mortgages, and 4 billion more to state and local governments. Nevertheless, there is no doubt that some businesses, individuals and governments have had to postpone expansion plans.

Why shouldn't the Federal Reserve meet all of these demands in full — then money would surely not be too scarce and too costly. If this proposition were put as a proposal to start the Government presses rolling

out currency, those crying for enough for everyone would be a pitifully discredited minority. Yet this would be precisely the effect if the Federal Reserve were to provide the banks with enough reserves to meet all the current demand for funds.

Allocating the supply

We hear quite often that, granted there isn't enough for all, there are better ways of dividing up what we have. The burden of a credit restraint policy is said to fall most heavily or even exclusively upon small businesses, home construction and upon state and local governments. Let's examine the apportioning machinery that we use.

On this point I would like to quote Bill Martin, Chairman of the Board of Governors: "The task of the Federal Reserve, under today's conditions, is to determine the volume of credit that needs to be made available in order to keep the economy running in high gear — but not overstrain . . . We do not undertake — and I do not know how it can be otherwise, short of some form of dictatorship — to say how a

given supply of credit shall be allocated." We can put the same thing somewhat differently — resources, human and otherwise, move into one of several alternative uses mainly in response to price. This is true whether we speak of human beings, iron and steel, copper, aluminum, agricultural products or what have you. Human beings still tend to gravitate toward jobs which offer the highest returns — materials into uses bidding the highest for them.

This reliance on the market place to determine the most efficient use of resources is the principal difference between a private enterprise economy and a collectivist society. It is not always perfect, but we believe strongly that it is apt to yield better results over the years than the judgment of any individual or group.

This way of doing things is reflected in the very structure of the Federal Reserve System, our credit and financial institutions, and in our credit and money markets. We have institutions which in competition with each other gather the nation's savings and allocate them to borrowers in a similarly competitive process. Subject to long-established principles of risk and credit-worthiness and to some legal restraints, these funds will tend to go to the highest bidder just as do materials and man power. Using the market system, we cannot make credit more

readily available or cheaper for one set of borrowers without making it cheaper and more plentiful for all borrowers. I am not critical of this way of doing things. Quite to the contrary — I feel it to be the most efficient and the only one wholly consistent with a private enterprise economy.

Small business, local governments

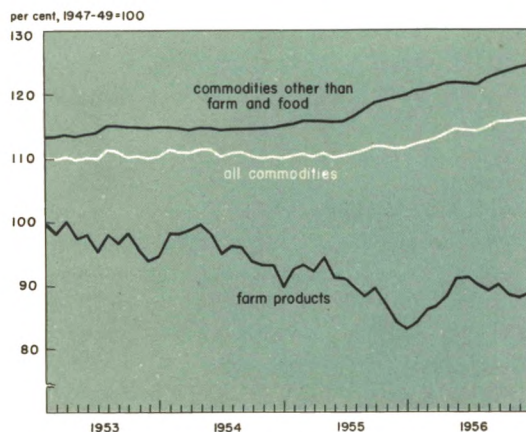
I have tried to find out whether small businesses in the Seventh Federal Reserve District are bearing the brunt of current credit restraint policies. The statistics are fragmentary and not directly to the point. But they seem to indicate that small businesses have participated in the unprecedented expansion in credit of the past few years. More than 50 per cent of the business loans at large banks are being made to small businesses. Many bankers have told me that as a matter of policy they make a special effort to accommodate their small business customers.

State and local governments undertaking very large programs of public works, including urgently needed schools, are said to be caught in a vise. A strong demand for funds has raised interest costs above what they are legally permitted to pay. Some issues have been postponed. Among these have been some revenue bonds for purposes which apparently are not urgent enough to make the enterprise self-liquidating at current interest rates.

Government must compete for the use of savings just as it must compete for man power and materials and for the same reasons. As you know, state and local issues have an important tax advantage. It seems to me that one jaw of the vise is of our own making — namely, the legal restrictions which provide for upper limits to interest rates. Such limits in some cases effectively prevent bidding for needed funds. I am in no position to advise the affected state and local governments, but surely taxpayers must know that higher interest rates are a much smaller cost than inflation of building costs.

The record shows that in the last fifteen years building costs, as measured by labor and material costs, have risen nearly one and one-half times. A school building which cost 1 million

Wholesale prices have advanced since mid-1955



Big, thriving economies

Indianapolis

BIG TOWN, BOOM TOWN

The Bank's 1956 Annual Report, just out, features reviews of the economic structure of Indianapolis and Milwaukee, two large and prosperous Midwestern cities.

The Report highlights the distinctive features of each metropolitan area's economy — the industries in which the cities specialize and the firms in those industries. The factors behind the recent growth and the prospects for the years ahead are appraised in a 35-page illustrated review.

This review is the third in a series of studies concerning the distinguishing characteristics of the Seventh District economy to appear in the Bank's Annual Reports. The 1955 Report discussed "Growth and Prosperity in Five Midwest Cities" — Decatur, Fort Wayne, Waterloo, Flint and Madison. The 1954 Report presented a perspective on Midwest agriculture.

Milwaukee

OLD FIRMS AND NEW INVESTMENT

The 1956 Report, like its predecessor, concentrates on each area's "export" industries. These are the industries which produce substantial quantities of goods and services sold outside the community's boundaries, thus enabling its citizens to buy things not produced locally.

The accompanying tables illustrate the

Where the "export" earnings come from —

	Indianapolis	Milwaukee
	(per cent of total)	
Manufacturing	78	90
Producer durables	35	54
Consumer durables	20	15
Consumer soft goods	17	14
Other manufacturing	6	7
Nonmanufacturing	22	10
Utilities (including transportation)	7	4
Trade	5	2
Government	7	2
Finance, services, etc.	4	2

dollars in 1941 would cost around 2½ million dollars today, and about 85 per cent of that increase came during the long periods of plentiful and cheap money during the war and the early postwar years. The additional borrowing costs of building a school which result from a credit restraint policy are only a fraction of the increased building costs which were caused not by tight money, but by the reverse.

The "price" question

The assertion has been made in recent months that higher interest rates add to inflationary rises in prices since they enter into business

costs. It seems to me that this superficial observation overlooks the economic role played by price. Rising interest rates reflect a growing demand for credit relative to the amount of funds available for lending. In this process a basic economic adjustment takes place. A number of consumers and businesses, attracted by the higher rates, will forego their own expenditure plans and make their funds available to others. Others will postpone expenditure plans because the rates are too high. In this way higher rates tend to reduce the demand for funds while adding to the supply. The pearl in the oyster is not what happens to interest rates but the

methods and findings for Indianapolis and Milwaukee. The adjacent table traces the flow of earnings from productive effort, for both local and "export" markets, and disposition of these earnings — for "imported" and locally produced goods and services, taxes and, in Milwaukee's case, net "exports" of capital funds. The table on page 8 indicates the main sources of "export" earnings in the two metropolitan areas.

The 1956 Report contains several new features. One is an analysis of capital formation in the past two years in Indianapolis and how it is being financed. A second is a brief summary of some of the findings of a special study of personal income in Milwaukee County, based on income tax returns. Copies of a more extensive summary of the income study are available on request. Also, there is a comparison of per capita state and local government tax and spending levels in

How the cities make their way

	Current rate	
	Indianapolis	Milwaukee
(million dollars)		
The community's earnings —		
from "export" activities.....	1,110	1,975
from local activities.....	800	1,275
total	<u>1,910</u>	<u>3,250</u>
less: portion not available to the community..... (profits earned by local branches of outside firms, wages and salaries earned by commuters)	310	120
plus: funds from outside the community..... (profits earned by outside branches of local firms, transfer payments from state and U. S. Governments)	160*	190
The community's available funds.....	<u>1,760</u>	<u>3,320</u>
spent for —		
purchase of local production.....	800	1,275
"imports" for final use.....	630	1,100
payment for state and U. S. Government services (via taxes).....	330	600
capital surplus	—	345
(funds spent by local firms for capital formation elsewhere and net additions to locally owned financial assets)		

*Includes net inflow of outside funds for capital formation.

the five Seventh District states. The purpose of the comparison is to indicate in general the extent to which state and local taxes and services create or respond to distinctive economic environments in states with roughly comparable access to raw materials and markets.

Copies of all the Reports are available on request from the Research Department, Federal Reserve Bank of Chicago, Chicago 90, Illinois.

induced postponement of expansion plans; thus the excessive demand for resources is reduced and the upward pressures on prices abated.

Viewing recent restiveness with monetary policy as a comparative newcomer on the scene, I am left with two general impressions. The first is that attaining the goal of orderly economic growth is not without immediate "costs." In a period of credit restraint all users of credit can expect to pay more for funds. Some may not get all that they want and feel entitled to. Still others may be denied credit accommodation. In a word, these are times when rationing in some form — by price or regulation — is essential.

The second is that we ought not to "go soft" on the damages which chronic inflation can cause us. I think that I am on safe grounds when I say that never before in our history have so many people had such a direct and compelling stake in economic growth and the avoidance of fluctuations in purchasing power which often have accompanied it. This is because of the spectacular increases in pension and retirement plans that are built on the assumption of a stable dollar. As of now, there are few people working who are not currently accruing pension benefits in dollar terms. Twenty-five years ago fewer than 2½ million persons par-

ticipated in private pension plans — about 1½ million Government workers were also covered. Private plans have risen from 2½ to 12 million. Social security covers nearly all of these and over 50 million others, and other public plans cover an additional 7½ million persons. It is estimated that balances in such funds now total more than 65 billion dollars.

Big stake in savings

No one can question the stake in a stable dollar of life insurance policyholders or of individuals' holdings of Government bonds. In the last ten years the number of policyholders in life insurance companies has risen from 71 to 115 million and insurance in force from 152 to 372 billions of dollars. Individuals' holdings of Government bonds amount to about 65 billions of dollars.

If we add these three forms of dollar savings for future dollar benefits, we arrive at a figure of about one-half trillion dollars. Nor is this all. A sizable proportion of the investors in savings and loan associations, in mutual savings banks and in savings accounts at commercial banks consider such savings as long-term investments. These have expanded rapidly in recent years in both numbers and amounts and now add up to about 104 billion dollars.

Funds set aside in these ways represent, for the most part, security for the retirement age and for emergency use. Those of us now contributing to such funds or holding other forms

of dollar claims — and that includes virtually every adult as well as the oldsters now receiving the benefits — have an obvious and enormous stake in seeing to it that the value of these dollars is not eroded. So far as I know, the surest way to accomplish this is to work for stable, orderly economic growth, and when I say stable and orderly, I mean without the excesses of either inflation or deflation.

I have mentioned some pretty big figures as representing the huge — and the steadily increasing — stake which most of us, and the so-called average citizen most of all, have in the stability of the dollar. And I think there is increasing awareness of the dependence of that stake upon proper monetary policy.

Before closing I should like to make an observation which is by no means original but which can bear repeating. It is that an appropriate monetary and credit policy cannot by itself assure stable, orderly economic growth. The decisions of business, labor, agriculture, consumers and Government bear heavily upon the outcome. This is necessarily so in a private enterprise economy. For these reasons each of these interests in our population must shoulder partial responsibility for the over-all outcome. Their understanding that there are short-run limits to our capacity to expand — whether it be in plant and equipment, profits, wages and salaries or in consumption — should temper their demands for credit accommodation and price boosts in times such as these.

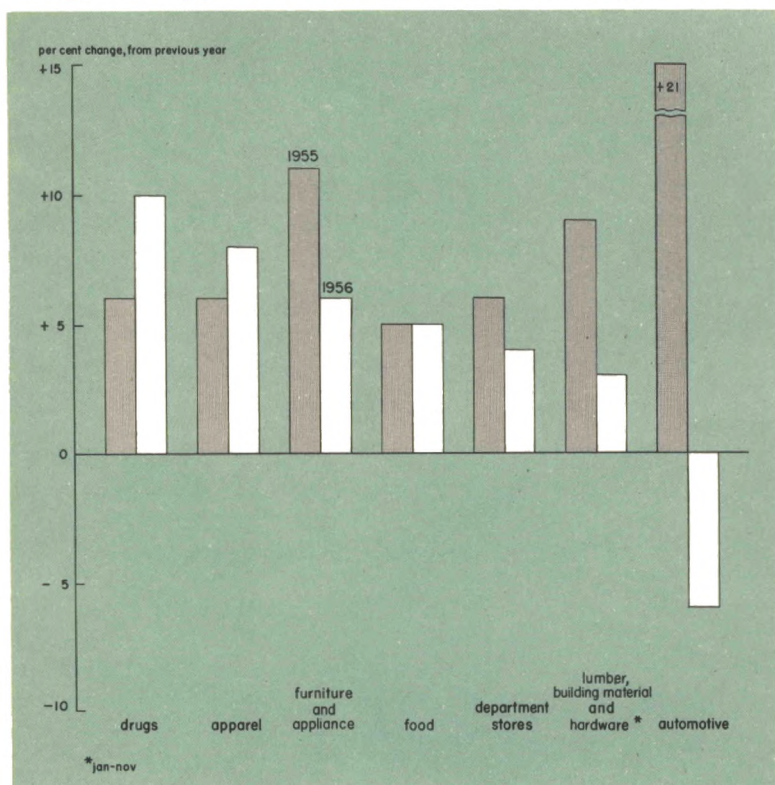
Retail trade gains momentum

Sales comparisons with earlier periods, a time-worn performance yardstick, are looked to by retailers as a significant indicator of how well they're doing. Disappointment is rampant when current sales fail to top previous figures. For in a growing and prosperous economy,

retail merchants know that merely equaling last year usually indicates loss of position to competitors.

After a relatively lethargic start early in 1956, sales picked up momentum as the months wore on. Finishing the year under a full head of

Drug and apparel stores led in 1956 sales gains



a 4 per cent gain over the high level of the year before and matched November's very good seasonally adjusted dollar volume.

All major categories except autos chalked up gains in 1956. However, not all the advance reflected larger physical volume. Higher prices accounted for about half of the 3 per cent increase in total retail sales for the year as a whole. This contrasts with the 9 per cent gain in 1955, a year in which prices remained about stable.

Contributing to the smaller advance last year was the smaller increase in consumer debt, especially for the purchase of autos. Although disposable income rose by 6 per cent in both years, the lesser

steam, fourth-quarter sales pushed to a new high. But many merchants had set their sights even higher. Utilizing the conventional "year-ago" comparisons, 1956 sales appeared to lack vigor, partly as a result of very good gains the preceding year. Nevertheless, on a seasonally adjusted basis, retail sales moved up 4 per cent from the first to the fourth quarter of 1956 — a pretty good showing.

A spirited close

The all-important Christmas season traced a pattern not unlike that for the entire year. Following a shaky start, holiday trade became more spirited as the year drew to a close. Unseasonably warm weather was thought by some to account for the slow beginning. But the month ended happily as December sales scored

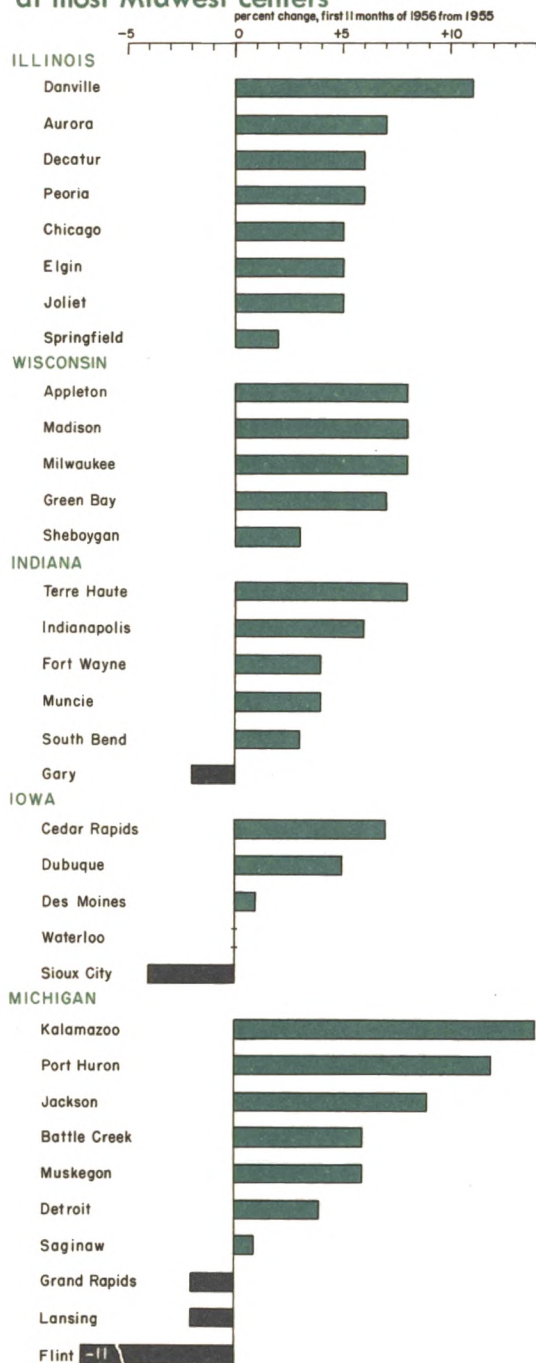
debt rise in 1956 worked to push aggregate consumer purchasing power up less rapidly. Disposable income plus the addition to consumer credit outstanding rose 5 per cent last year compared with 8 per cent in 1955.

Autos, up and down

The decline in automotive sales from their extremely high level in 1955 was a dominant factor in the retail sales picture. Exclusive of the volatile automotive component, retail sales registered gains of about 6 per cent in both 1955 and 1956.

Purchases of automobiles and things automotive have consistently stolen the limelight in the postwar period. Although accounting for about one-twentieth of total consumer spending, year-to-year changes in automotive sales

Department store sales rise at most Midwest centers



have exceeded by far the ups and downs in most other retail categories. For example, the yearly dollar changes in outlays for automobiles and parts have rivaled even the changes in spending on food and alcoholic beverages, which account for about one-third of total consumer expenditures.

Automotive dealer sales, as reported by the U. S. Department of Commerce, dropped nearly 6 per cent in 1956 after gaining a whopping 21 per cent the previous year.

Soft goods "shine"

Recording the sharpest year-to-year gain since 1951, apparel store sales ran 8 per cent ahead of 1955. Women's apparel outpaced men's clothing by a small margin as both turned in good showings. Children's wear apparently led other apparel gains in 1956, while shoe sales barely managed to top the previous year.

Furniture and appliance sales turned in a 6 per cent increase, and lumber, building materials and hardware recorded only a slight gain (see chart). Both increases were significantly smaller than those turned in a year earlier, apparently reflecting the 1956 decline in home building. The total value of residential construction put in place last year, including new dwellings and additions and alterations, ran 8 per cent below 1955. In the furniture and appliance group, furniture did somewhat better than appliance stores, though falling short of the very vigorous gains recorded the previous year.

And in the Midwest

For the Seventh District, the most up-to-date indicator of changes in retail trade is department store sales. At best, however, such sales are broadly representative of general merchandise and apparel groups only. District department store business topped 1956 by 4 per cent, about matching the U. S. "big store" experience.

Individual departmental sales at Midwest department stores traced a pattern somewhat similar to that of specialty stores in comparable lines during 1956. Sales gains in January to November, relative to the year-earlier period

for selected departments of Midwest stores were as follows:

	Per cent gain
Girls' wear.....	7
Boys' wear.....	6
Men's clothing.....	4
Women's and misses' apparel.....	6
Women's and misses' accessories.....	4
Major household appliances.....	2
Furniture and bedding.....	3
Floor coverings.....	4
Radio, TV, records.....	11
Furs	7
Toilet articles and drugs.....	7

Department store sales gains were not uniform for all Midwest cities. Comparisons with 1955 ranged from minus 11 per cent in Flint to plus 14 per cent in Kalamazoo (see chart). Illinois and Wisconsin centers recorded the most uniform gains while both Iowa and Michigan displayed wide variations as changes in farm income and the slide-off in auto output hit these areas with uneven impact. Sioux City and Flint, registering the sharpest sales drops from a year

ago, also recorded the largest District declines in checkbook spending.

Sharp sales gains ahead?

This year, most retailers appear moderately optimistic about their sales prospects. But as always consumers will have the last word. Noted late in 1956 was "extremely selective" consumer buying — a trend which is expected to continue in the months ahead. Moreover, the retail customer's reaction to prospective price increases remains to be determined.

Leading merchants are reportedly planning for sales gains about matching the 1956 increase of 3 to 4 per cent. With prospects for a further rise in disposable income, such a performance could well be in the cards. The outlook for even sharper gains, however, hinges on two important questions: (1) will consumers be willing to take on much additional debt during the year and (2) will the personal saving rate decline from the high level recorded in 1956? An affirmative reply to either or both questions could spell sharply higher 1957 sales.

Bank loans in 1956— another year of expansion

The nation's banks, like many industrial firms, were unable to fill all of the "orders" they received in 1956. Some customers had to go unsatisfied, for resources were not adequate to meet all demands. This situation has continued in the early months of 1957.

Nevertheless, banks did a booming business in the past year. As 1956 closed, outstanding loans totaled 90 billion dollars, reflecting an 8 billion gain over the beginning-of-year level. While this rise was substantially smaller than the whopping 12 billion bulge recorded in 1955,

it still represented a sizable 10 per cent boost.

A large part of the loan increase was made possible by a reduction in security holdings. Commercial banks' portfolio of Governments dropped 3 billion dollars, and holdings of other issues were reduced an additional 500 million. As a result, *total* bank credit rose 4.6 billion, matching the 1955 gain (see table).

Businesses fared well

Business borrowing slowed down proportionately less than most other kinds of loans.

1956 gain in commercial and industrial outstandings reached 5.5 billion dollars, second only to the 6.3 billion surge in 1955. During the first half of last year, the rise in business loans was running well ahead of 1955. By fall, however, the climb in loan totals had begun to slow, in contrast to the upsurge in lending over the same period a year earlier (see chart).

A substantial share of the 1956 rise in business loans was concentrated in the large banks.

	Per cent increase in business loans during 1956
All commercial banks	16
New York banks	25
Chicago banks	16
All others	13

New York lenders boosted their commercial and industrial outstandings by 2.3 billion. These banks, which at the start of the year held 28 per cent of all business loans on commercial bank books, alone accounted for over 40 per cent of the total increase. The New York gains reflect the unusually large net increase over the year to the seasonal borrowers and to petroleum, coal, chemical and rubber firms and public utilities. Much of the borrowing of each of these groups is concentrated in the New York money market banks.

Within the Seventh District, there were also some striking differences in business loan performance.

	Per cent increase in business loans during 1956
Leading Seventh District banks	18
Chicago banks	16
Detroit banks	29
Other leading banks	10

Two borrowing groups are mainly responsible for the hefty increase recorded at Detroit banks. Loans to metals and metal product firms (excluding transportation equipment) increased by 50 per cent and accounted for one-third of the 1956 rise. Borrowing by public utilities at leading Detroit banks doubled during 1956 and represented 20 per cent of the total gain in the year.

The growth last year in real estate mortgages — second largest loan category — was one-

fourth under the gain recorded in 1955, a reflection of the dip in home-building activity. The 1.8 billion rise, however, about matched the average annual increases for the postwar period.

While borrowings by sales finance companies declined last year, consumer loans showed an increase, though at a less rapid pace. The lower level of auto sales was offset in part by the increased share of autos sold on credit. In fact, bank *extensions* of instalment loans exceeded the 1955 volume. However, *repayments* rose 9 per cent and limited the gain in outstandings to a third that of the previous year.

Loans for purchasing or carrying securities was the only category to show a drop. This probably reflects, in part, the effects of the higher margin requirements instituted in 1955 as well as the increasing cost of such borrowing. These factors, combined with the declining yield on corporate stocks, have made margin purchases less attractive. The 30 per cent decline in security loans at the leading New York lenders accounted for virtually the entire drop in this type of credit.

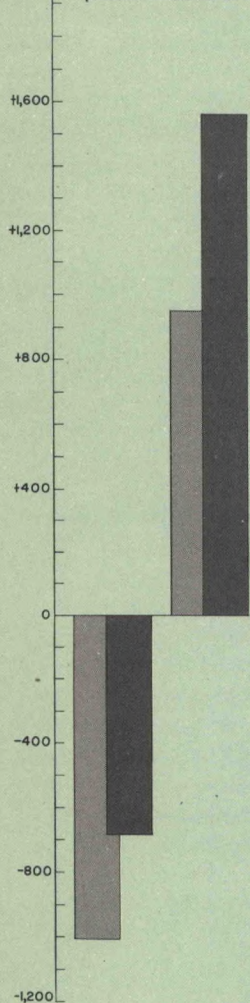
Small banks gain deposits

Although the rise in loans at big banks generally matched or surpassed the percentage increase for the nation, this did not hold true for total loans and investments. At leading Chicago banks, the entire expansion in loans was offset by a decrease in security holdings. As a result, earning assets of these banks showed little change over the year as a whole. In New York, a billion dollar increase in earning assets during December more than offset the 400 million decline in the first eleven months with the result that a gain was recorded for the year. Between year-end and mid-January, however, their loan and investment total dropped more than in the comparable 1956 period.

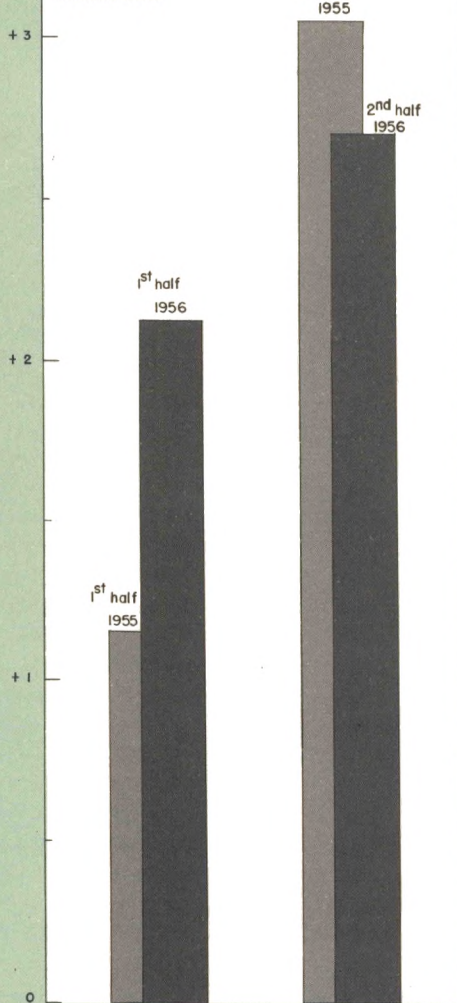
The stability in loans and investments of large city banks is related to the fact that deposits in these institutions have lagged behind the increase recorded in the smaller institutions. In 1956, New York and Chicago banks experienced a deposit decline, whereas "country" banks had a 2 per cent rise.

Business loan increase in second half less than in 1955 as metals and sales finance borrowing drops

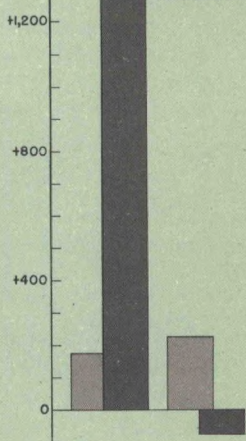
change in million dollars
farm product processors and dealers



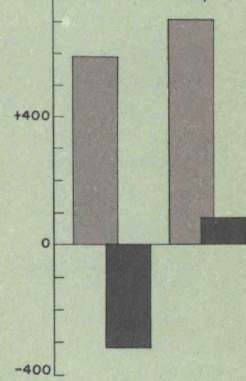
change in billion dollars
total classified business loans



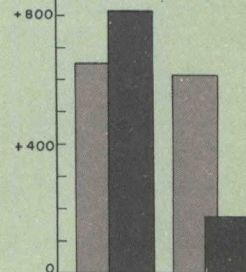
change in million dollars
metals and metal product manufacturers



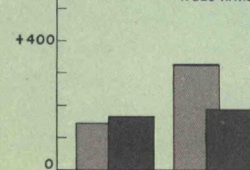
change in million dollars
sales finance companies



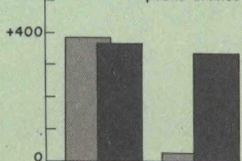
change in million dollars
all other



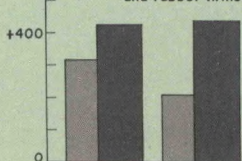
change in million dollars
wholesale and retail trade firms



change in million dollars
public utilities



change in million dollars
petroleum, coal, chemical and rubber firms



Major banking trends in 1955 and 1956

	All commercial banks		New York City banks		Chicago banks		Large banks outside New York & Chicago		All other banks	
	1955	1956e	1955	1956	1955	1956	1955	1956	1955	1956e
Amount outstanding, end of year, in billion dollars:										
Loans	82.0	90.1	14.2	15.9	3.5	4.0	30.7	33.9	33.6	36.3
U. S. Government securities	61.6	58.6	6.6	5.9	2.8	2.4	20.7	18.3	31.5	32.0
Other securities	16.7	16.2	2.1	1.7	.8	.7	5.3	5.1	8.5	8.7
Total loans and investments	160.3	164.9	22.9	23.5	7.1	7.1	56.7	57.3	73.6	77.0
Total deposits, excluding interbank	175.7	176.1	23.7	23.5	7.3	7.1	61.6	61.7	83.1	83.8
Per cent change over the year:										
Loans	16	10	19	12	17	14	18	10	14	8
U. S. Government securities	-11	-5	-29	-11	-20	-14	14	-12	-2	2
Other securities	2	-3	-3	-19	14	-13	-2	-4	10	2
Total loans and investments	3	3	-3	3	-1	0	2	1	6	5
Total deposits, excluding interbank	5	*	-*	-1	0	-3	4	*	7	1

e Estimated.

* Less than 0.5 per cent.

In part, the movement to the suburbs by both industry and consumers is responsible for the varying deposit trends. Many companies and individuals like to deal with banks in the area in which they are located. Moreover, the competition among savings institutions in the downtown areas has become increasingly strong.

Little slack left

By the start of 1956, much of the "slack" in the banking system that had come as an aftermath of the 1953-54 drop in business activity and the Federal Reserve's policy of "active ease" had already been absorbed. In order to meet the mounting backlog of higher-yielding loans as business expansion got under way, most banks drew down substantially their bulging portfolio of Governments. Bank holdings of Government securities dropped almost 8 billion dollars during 1955 and were the major source of funds behind the 12 billion rise in loans.

The loan rise in 1956 reduced bank "excess capacity" even further. Commercial banks are

now increasingly reliant upon additions to their resources as the basis for additional loan expansion. With banks actually aware of the decline in their liquidity positions and with capital losses almost inevitable on security sales, further depletions in Government portfolios will be made with great reluctance. Hence, banks will be more and more dependent upon the continued growth in deposits as a means of expanding their outstanding loans.

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