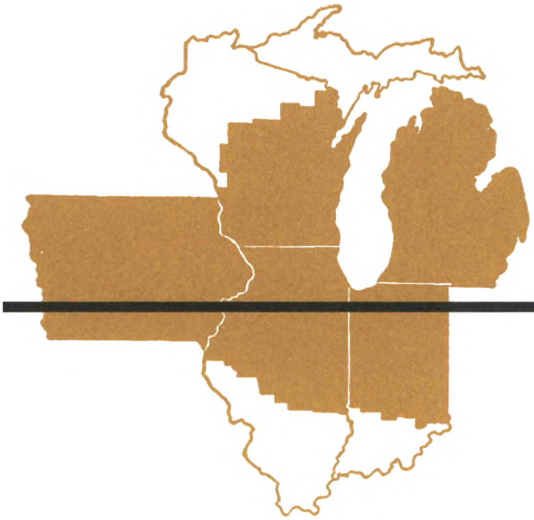
A review by the **Federal Reserve Bank of Chicago**

Business Conditions

1963 May



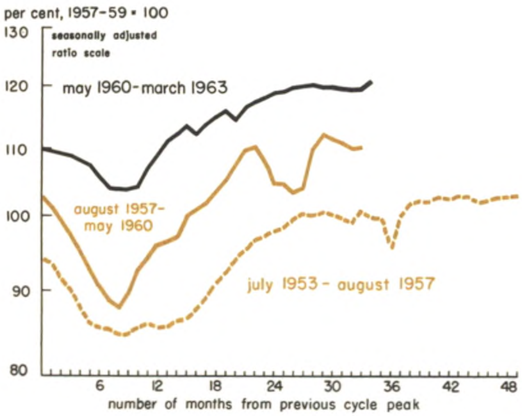
Contents

THE Trend OF BUSINESS

In March industrial production and employment moved up from the plateau reached in mid-1962 and personal income rose to a new high. These developments had been presaged by an improvement in retail sales late last year and a sharp upswing in new orders for durable manufactures in January and February.

It is possible that the dock strike that tied up the East Coast and Gulf ports between December 23 and January 27, together with severe cold in the northeastern United States in January and February, delayed evidence of the strengthening in the underlying business trend. In any case, the economic expansion that began in February 1961 appears to be imbued with new vigor. There continue to be indications that the present cyclical upswing will compare favorably with earlier postwar expansions in terms of magnitude, duration and price stability.

Industrial production
in renewed upswing after several months of stability

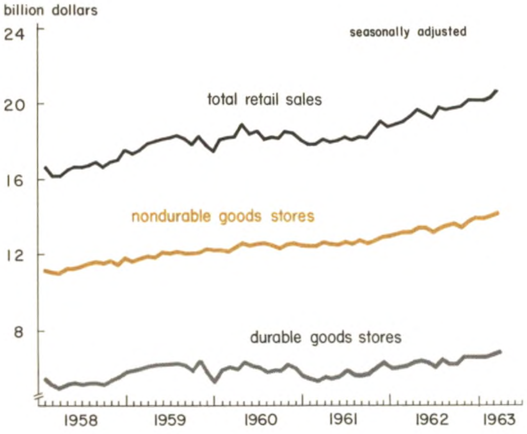


Steel buying important

By mid-April steel production had increased to an annual rate of almost 130 million tons. This was up 30 per cent from January and slightly above the peak rate reached in February 1962 prior to the labor-management settlement concluded at the end of the following month. Inventories of finished steel at the mill, warehouse and consumer levels combined have been rising since early last December and the increase accelerated sharply in March and April. However, inventories in mid-April doubtless were well below the peak reached a year earlier. Output of steel-using industries was about 6 per cent higher in March than a year earlier, indicating a rise in consumption of about this proportion.

Obviously a substantial part of the rise in steel output reflects strike-hedge buying. But this is not the whole story. Order increases were reported in the first quarter by a variety of producers of consumer and business goods. A higher level of output of hard goods normally suggests the need for a larger inventory of finished steel to support operations. Moreover, inventories of steel, until recently, have been geared to the most rapid delivery schedules of the postwar period. These schedules

Since mid-1962, retail sales have risen strongly



were stretching out in April for products in strongest demand such as galvanized sheet, hot and cold rolled sheets and strip. In general the price increases announced in April by several steel producers applied to these products, which, incidentally, do not face strong competition from imports or substitute materials. These factors suggest that a substantial rise in steel output would have occurred in recent months even if the question of a strike had not been raised.

Consumers lead the way

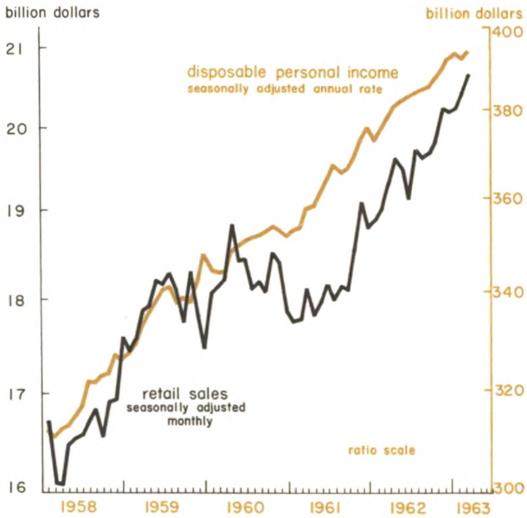
In the first quarter of 1963, retail sales were more than 7 per cent above the level of a year earlier. There was no plateau for consumer buying in the second half of 1962 as in the case of output and employment. In fact the gain in the fourth quarter was the highest for the year. This rate of increase continued in the most recent quarter and sales held up well in April according to preliminary information.

The very high level of sales by automobile dealers reached in the fourth quarter of 1962 was about maintained in the first quarter of 1963. Further gains in retail trade this year, therefore, are attributable to nonautomotive lines, both durable and nondurable.

Heads of families, in response to survey inquiries, have expressed plans to continue to buy hard goods at a high rate in the months ahead. Consumer confidence also is indicated by broader use of credit. Total new extensions of instalment credit were at an annual rate of 59 billion dollars in January and February compared with 52 billion a year earlier. Credit use apparently rose even more rapidly between the early months of 1962 and the comparable period of 1963 than did consumer purchases of hard goods.

After two full years of the present economic expansion it is now possible to compare the rise in consumer income and sales with similar time spans of previous postwar

Retail sales have increased faster than after tax income during the past year



upswings. Retail sales were at cyclical lows in the first quarters of 1954, 1958 and 1961. The following table shows the improvement in this measure after two years from these low points as compared with the rise in personal income after taxes:

First quarter of each year	Retail sales	Disposable personal income
	(per cent increase)	
1954-56	12.6	11.8
1958-60	11.5	10.5
1961-63	14.5	11.6

Retail sales rose at an appreciably greater rate in the latest expansion than in comparable periods of the two earlier cycles. On the other hand, the increase in disposable income in the recent comparison, although larger than in the 1958-60 period, was slightly less than in the 1954-56 period.

26,000 in March, a new record. As a result, despite a high level of production, dealer inventories of American built passenger cars declined slightly in March to 1 million units. Only once before, in 1960, had the industry's inventory exceeded 1 million at this time of year. However, in terms of March sales, the cars on hand represented only a 40-day supply compared with 48 days in 1960 and, by this standard, inventories were the lowest in six years. It should be noted that the adequacy of the current inventory varies widely among car models.

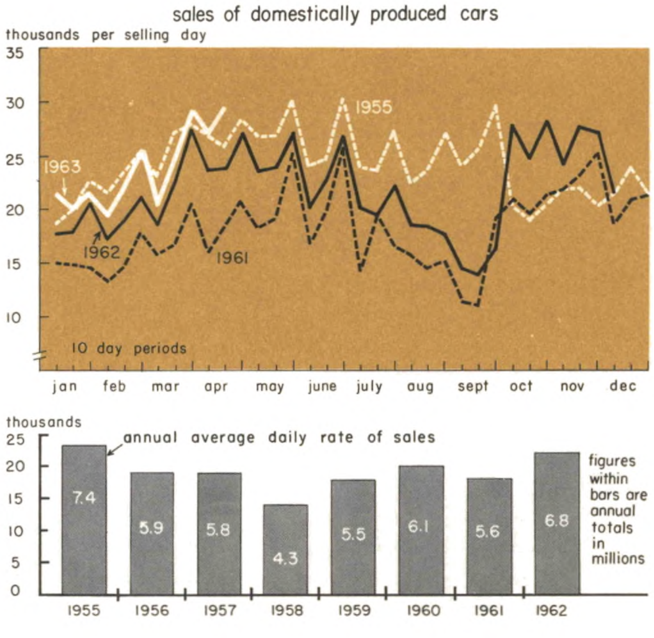
On the strength of the sales performance of the first quarter, some car producers have increased production schedules for the April-June period. Estimates of auto output for the second quarter now run as high as 2 million

Autos continue strong

Auto sales and output in the first quarter of 1963 about maintained the fast pace established late in 1962, allowing for seasonal trends. In the January-March period, according to industry estimates, sales of new cars to American buyers, including imports, were at an annual rate well in excess of the 7.1 million total for 1962. New truck sales were believed to be at a 1.2 million rate. If continued throughout 1963, these trends would produce a record year for both cars and trucks in terms of number of units. The previous highs were recorded in 1955 for the former and 1950 for the latter.

Deliveries of domestic and imported cars to American buyers were at a daily rate in excess of

Car sales have been well above last year and recently have been at record rates



units, a moderate increase from the first quarter instead of a decline as had been expected earlier.

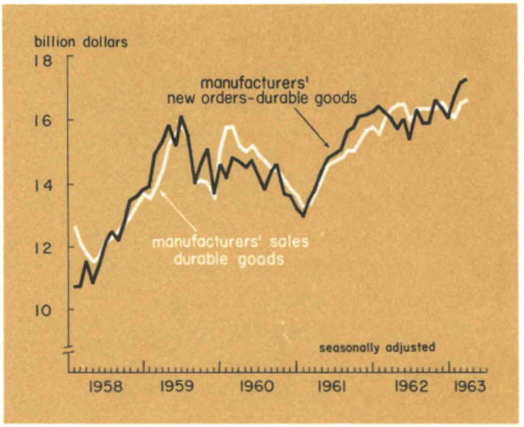
Auto industry analysts have been encouraged by a number of developments in the 1963 model year besides the greater than expected number of cars sold. Demand has been strongest at the top of the line—the larger, more fully equipped models. Second, there appears to have been an acceleration in the rise in the number of families owning more than one car. Third, although used car inventories have risen, prices have remained remarkably firm.

Although car sales in recent months have encouraged hopes for a record year, the most common expectation among industry experts is that new car sales for 1963 will not exceed last year's 7.1 million, the second best year. This implies a decline from current rates of output and sales later in the year. One reason for this view is the fact that the new car market has absorbed an unprecedentedly large number of units during the six-month period ending in March. Sales of domestic cars to United States buyers in this period totaled 3.7 million units—15 per cent more than in any October-March period in the past.

Business investment rises

Comparisons between trends in retail sales and disposable income during the past three cyclical revivals suggest that sluggishness in the recent recovery cannot be laid at the door of the consumer. The record indicates that spending programs of consumers have been influenced more by current and prospective income than by the forebodings of an imminent recession. Fears of a business decline had become widespread in business and financial circles in the second half of last year, largely because of the sharp break in the stock market and adverse readings of other

In the first quarter new orders of durable goods manufacturers were well above shipments



widely accepted "leading indicators."

Recent evidence suggests that business investment, the lagging segment of the economy, is showing renewed strength. Construction contracts were at successive all-time highs by wide margins for each month in the period from November through February. Orders for trucks, freight cars, construction machinery, machine tools and other producers' durable goods also have increased substantially in recent months.

Total business inventories which increased moderately in the second half of 1962 now are rising at a faster rate. Outlays on construction and producers' durables together with the change in inventories are the components of "gross private domestic investment" as defined by the Department of Commerce. This portion of total spending was virtually stable throughout 1962 and early 1963.

The need for caution

Throughout the history of cyclical fluctuations the ebb and flow of business confidence has played an autonomous role in influencing developments. Excessive optimism or pessimism often has caused the pendulum to swing too far.

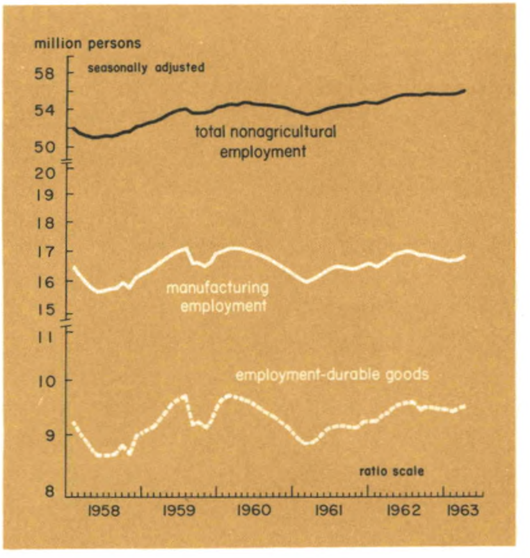
At the start of 1962, high hopes for a rapid expansion in activity soon required modification as sales and profits failed to match expectations. As the year moved on and production and employment ceased to show further improvement, the view that a general decline in business was in process or would soon develop gained acceptance. Plans for capital expenditures, inventory investment and hiring of personnel were adjusted downward.

These retrenchment programs were under way in many firms when the strength of retail sales in the fourth quarter convinced some doubters that a recession would be avoided. Even then the common view saw no appreciable spur to activity before the second half of 1963, and this prospect often was predicated on a substantial tax cut becoming effective by midyear. The record of the first third of 1963 has shown greater strength in the private economy than had been generally expected, thus reversing the relationship between expectations and developments which existed a year earlier.

It remains to be seen whether the pendulum of confidence, energized by recent favorable business news, will be propelled once more toward excessive optimism. Some hint of this may be seen in the exuberant rise of stock prices, no doubt reflecting expected additional stimulus to the economy from a further rise in Government spending, a possible tax cut and business plans to boost investment in plant and equipment. However, the economic horizon is not free of clouds.

First, the present level of employment and output owes a good deal to the extremely high demand for steel and autos. Declines in production of these items may occur later in the year.

Manufacturing employment leads rise in total employment in March



Second, there is a possibility of extended work stoppages in both the steel and railroad industries which could have a significant effect upon general activity later in the year.

Third, the improvement in manufacturers' orders has encouraged price increases in some lines. An appreciable rise in the general price level appears unlikely in the face of large unused resources of men and materials, but a rash of attempted price increases, even if these proved abortive in the long run, could dampen the business expansion.

Finally, the still unsolved problem of the substantial deficit in the international balance of payments remains a cause of uneasiness for the domestic economy.

Trends in banking and finance

Financial developments in the first quarter 1963

The strengthening optimism which was evident in some sectors of the economy in the first quarter of 1963 was generally not reflected in the financial sectors. The money supply—private demand deposits plus currency outside banks—showed little further increase after mid-January and at the end of March was about 2 per cent larger than a year earlier. The public continued to show a strong preference for interest earning liquid assets over demand deposits and added substantial amounts to their holdings of time deposits, savings and loan shares and similar assets.

Bank loans decline

Weekly reporting member banks in leading cities in the nation experienced greater than usual seasonal declines in loans and demand deposits. Loans declined 1.6 billion dollars between January 2 and March 27, 1963—1.3 billion more than in the same months a year earlier. Over half of the decline resulted from a drop in loans to dealers and brokers. Commercial and industrial loans decreased slightly in the first quarter of the year in contrast with a slight rise in the first three months of 1962. Real estate loans, on the other hand, rose 400 million dollars in the first quarter of 1963, almost twice as much as in the same period of the preceding year. These loans increased a record 16 per cent in the full year of 1962.

Banks' investments in Treasury securities in the early months of 1963 also declined but not as much as last year. The average maturity of these securities was lengthened somewhat as the weekly reporting member banks added more than 1.5 billion dollars to their holdings of Government bonds maturing in over five years. Investments in other securities, primarily obligations of state and local governments, rose 1 billion dollars in the first quarter of the year, somewhat less than the same quarter of the preceding year. In the first quarter of 1962, these investments increased a record 1.2 billion dollars.

Demand deposits, which like loans tend to decrease seasonally following the year-end bulge associated with the Christmas season, declined 11.7 billion dollars in the first quarter of 1963 compared with a decrease of only 8.9 billion a year ago. Deposits of individuals and businesses and domestic interbank balances accounted for most of the decrease.

Time deposit growth slows

Time and savings deposits at these large banks have continued to expand rapidly but at a slower pace than in the first quarter of 1962 when these deposits were given a boost by the increase in interest rates offered by many banks. In the first quarter of 1963, total time and savings deposits rose 2.8 billion dollars compared with a record increase of 3.5 billion a year earlier.

—continued on page 14

Export aids play a key role

Organization	Major Purposes	Capitalization
Export-Import Bank (Eximbank)	To provide credit to U. S. exporters and foreign importers where private credit is not available on "reasonable" terms and to guarantee loans.	$1 billion capital stock subscribed by U. S. Treasury. Authorized to borrow $6 billion from Treasury, based on cost of the money to the Treasury.
Foreign Credit Insurance Association (FCIA)	To provide insurance to U. S. exporters on credit sales overseas.	No separate corporate existence. Operating funds provided by member companies.
Agency for International Development (AID)	To administer all governmental foreign aid activities. To provide loans or grants when funds not obtainable from other free world sources.	Resources based on annual Congressional appropriations and on Public Law 480 foreign currency proceeds.
International Bank for Reconstruction and Development (IBRD, or World Bank)	To make or guarantee loans for productive (reconstruction and) development projects, with own funds and borrowed funds, where private capital not "reasonably" obtainable.	Authorized capital of $21 billion ($10 billion before 1959). Of $20.7 billion subscription, 1/10 paid in and 9/10 subject to call. Authorized to borrow in capital markets of member countries; funded debt $2.5 billion.
International Finance Corporation (IFC), affiliate of IBRD	To supplement activities of IBRD by encouraging the growth of productive private enterprise in (less developed) member countries.	Authorized capital of $100 million, of which $98 million subscribed.
International Development Association (IDA), affiliate of IBRD	To promote economic development, and — by increasing productivity — to raise standards of living in the less developed areas of the world.	Provided for initial capital of $1 billion, of which $968 million subscribed and $595 million paid in. "Advanced" countries pay their subscriptions in convertible currencies; "less developed" countries 10 per cent in convertible funds, 90 per cent in their own currency.
Inter-American Development Bank (IDB)	To promote the general economic development and economic integration of Latin America.	"Ordinary" capital, $813 million ($382 million paid in), and Fund for Special Operations, $146 million. IDB also administers $394 million Social Progress Trust Fund (Alliance for Progress) for U. S. Government. Has borrowed some $100 million in capital markets.

The U. S. Government attempts to provide financial assistance to U. S. exporters and to foreign countries in various ways through a number of specialized institutions. However, the main purpose of participation by the United States in international institutions is not to broaden the markets for our exports. The essential characteristics of the various financing aids are described below.

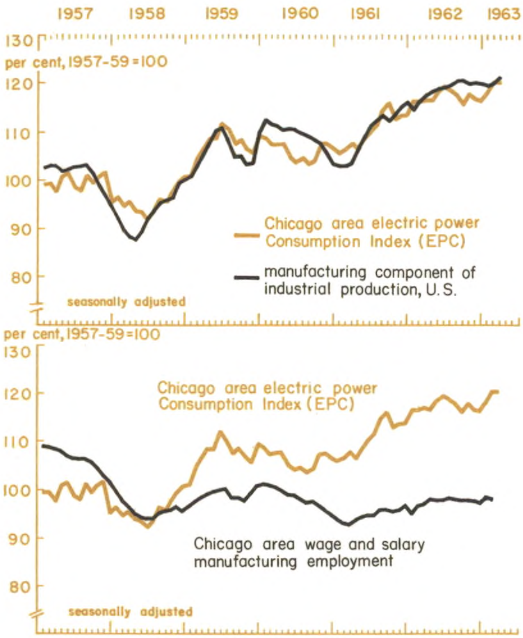
Date of formation (Membership)	Operation	Loan terms
1934. Greatly expanded in 1945.	Only U. S. Government agency having sole purpose of financing foreign trade. Makes loans for development and other purposes. Since 1934, has authorized loans of more than $13 billion and has operated profitably.	Rate varies with changes in the capital market (presently 5¾ per cent). Most maturities 7-20 years.
Began operating February 1962. Sponsored by Eximbank. 74 insurance companies are members.	Offers insurance covering both political and credit risks in short- and medium-term transactions. Political risks carried 100 per cent by Eximbank; commercial-credit risks shared by Eximbank and FCIA. Insured retains liability of 5-15 per cent. FCIA insured exports exceed $600 million so far.	Rate varies by country and credit terms, lower for separate political-risk policies. Reduced about 10 per cent February 1, 1963.
November 1961. Combined the previous ICA and the Development Loan Fund.	Loans (55 per cent in fiscal 1962) and grants to foreign governments and private firms, mostly for projects not suitable under conventional credit terms. Loans ordinarily tied, i.e., proceeds must be spent for purchase of U. S. goods. Separate investment guarantees program to encourage private enterprise and capital in less developed countries.	Loan maturities generally have been for 40 years, with 10 years of grace, at ¾ of 1 per cent interest.
1944, opened for business 1946. 84 countries are members.	Lends to governments and private firms (with government guarantee) in member countries. Finances foreign exchange requirements of specific projects of high priority. Loans not tied (see above). Risk of default shared by members. Loans, almost $7 billion, have financed mostly basic facilities for economic growth (transportation, power, etc.)	Interest rate, including 1 per cent annual commission charge, recently 5¾ per cent. Varies with conditions in capital markets in which World Bank bonds are sold. ¾ of 1 per cent commitment fee charged on undisbursed portion of loans. Maturities generally up to 25 years.
1955, opened for business 1956. 73 countries are members.	Provides financing in association with private investors, brings together investors and experienced management. Lends mostly to manufacturing firms, requires no government guarantee. Revolves funds by selling investments to private interests. Since 1960 authorized to make equity investments.	Rates on loans vary and loans carry option on shares. One per cent commitment fee charged on undisbursed portion of investment (including both loan and equity features). Loan maturities usually 7-15 years.
September 1960. 74 countries are members.	Provides capital on more liberal terms of repayment and finances wider range of projects than IBRD. Relatively poor countries given priority in allocation of funds. Has extended development credits in excess of $450 million.	So far has charged no interest on development credits. Levies a service charge of ¾ of 1 per cent on amounts withdrawn to meet administrative costs. Credits repayable over 50 years, with a 10-year grace period.
1959, began operations in 1960. 20 countries are members, all also members of Organization of American States.	Loans from "ordinary" capital and borrowed funds to governments and private enterprises on commercial terms to finance immediately remunerative projects. Fund for Special Operations provides credit to countries in special need, finances undertakings that pay for themselves slowly. Has made loans exceeding $600 million.	Variable rates, generally lower for Special Fund projects. Loan maturities: 12-20 years.

Manufacturing at record level in Chicago metropolitan area

Production by manufacturing firms in the Chicago standard metropolitan area was at a record level in the first quarter of 1963. This development was indicated by the Federal Reserve Bank's seasonally adjusted index of electric power consumption (EPC) for manufacturers which reached a high about 20 per cent above the 1957-59 average in February and March.

There was a mild slowdown in production by manufacturing firms in the Chicago area in the third quarter of 1962, with the EPC index slipping from about 119 in June to a low of 116 in September. The food products, chemicals, primary and fabricated metals and nonelectrical machinery industries experienced declines shortly after midyear but were reversed in October. The electrical machinery and the printing and publishing industries drifted downward throughout most of the second half.

Chicago area electric power consumption index at a record high



The upswing in Chicago manufacturing which got under way toward the end of 1962 has continued in the first quarter with most of the area's major industries participating in the advance. Production of food products increased throughout the quarter to 108 per cent of the 1957-59 base period in March, up from 104 in December. The printing and publishing industry made large gains in January and February but declined in March to about the average level of the fourth quarter of 1962. Sizable gains were scored by chemicals firms as production increased from an index of 116 in December to 125 in March. Most of the other nondurable goods manufacturers in the area had similar gains.

Since October 1962, Chicago standard metropolitan area primary metals production has been at a relatively high level. Steel production in this area, as in the Gary-Hammond-East Chicago area, has been on the upswing while the other components of the category—nonferrous metal processing and forging operations—have lagged somewhat.

An advance was recorded in the fourth quarter for producers of metal products, such as fabricated structural steel and plate, sheet

The Chicago area electric power consumption index

The electric power consumption index (EPC) is a new measure of regional manufacturing production based on electric power used by manufacturing firms. The index for the Chicago standard metropolitan area—Cook, Du Page, Kane, Lake, McHenry and Will counties—is published here for the first time. Indexes for the Detroit, Indianapolis and Milwaukee areas were published in earlier issues of *Business Conditions* (April 1959, January 1961 and April 1962, respectively).

The EPC indexes are believed to be reliable indicators of changes in industrial production. Electric power figures have been used for many years as a rough measure of changes in economic activity. This use has been based on the fact that changes in the industrial consumption of electric power in the United States have closely paralleled changes in manufacturing activity. The direction of movement has generally been the same although manufacturing output has tended to show wider swings than the simple total of electric power used.

The EPC index is an improvement over the measures of electric power consumption previously used for indicators of production in local areas. The index is based primarily on purchased power but includes a small amount of "on site" generated power. In addition the data are available for various manufacturing industries. This makes it possible to analyze activity changes on an industry by industry basis and to take into account differences in power used per dollar of output when combining the indexes for individual industries into an index of total manufacturing.

The amount of electricity consumed in relation to output varies greatly among industries, impairing the reliability of an area index based on a simple total of electric power used. The primary metals industry in the Chicago area, for example, uses more than five times as much electricity for each dollar of output as the food products industry does and about twice the amount used by firms producing electrical machinery. In order to take this into account, the amount of power consumed by each industry is weighted with a measure of "value added" per kilowatt hour to provide the total index for the area.

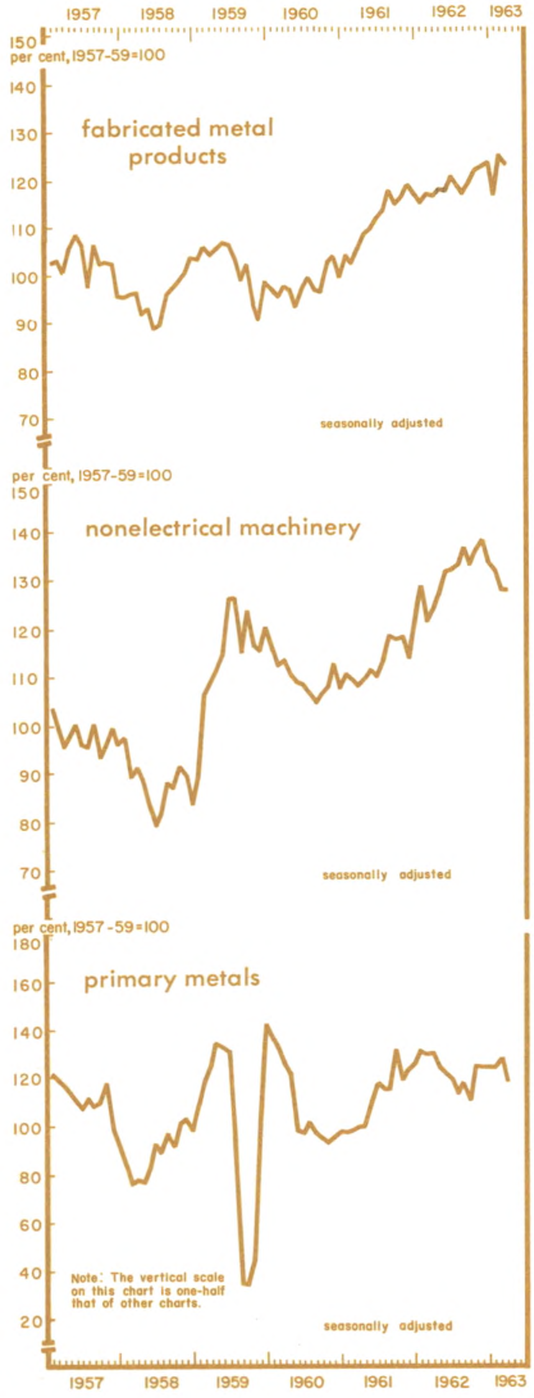
Most of the electric power data used in this article were furnished by the Commonwealth Edison Company.

metal products, heating apparatus and metal stampings. However, these firms showed a 2 per cent decline in the first quarter.

Production of nonelectrical machinery, as indicated by electric power consumption, declined during the first three months of 1963. Chicago area firms in this industry had attained a record level of production in November 1962, but by March the pace had slackened to approximately that prevailing last April.

Much of the gain in the Chicago EPC index since year-end is accounted for by the electrical machinery industry which produces more than 14 per cent of the total manufacturing output of the area. Since December, production in this industry has increased more than 4 per cent.

An upswing in manufacturing activity during the early months of 1963 also is indicated by an alternative measure—seasonally adjusted Chicago area manufacturing employment. Over a longer period of time, however, trends in the manufacturing employment and



the EPC indexes differ considerably.

By March, Chicago's EPC index had risen 20 per cent from the 1957-59 period while wage and salary manufacturing employment had declined approximately 1.5 per cent. This difference largely reflects gains in production per worker and, to some extent, a rise in consumption of electric power per unit of production. These trends also have been evident for the nation and the other Midwest centers for which EPC indexes have been prepared—Detroit, Indianapolis and Milwaukee.

Cyclical behavior of the Chicago EPC

As is true of the EPC indexes for these three Seventh Federal Reserve District areas, movements in the Chicago index closely approximate the long-run trend of the manufacturing component of the industrial production index for the nation. The major interest in the EPC indexes for local areas, however, is in the comparison of short-run cyclical changes in production.

The EPC index indicates that manufacturing activity in the Chicago area declined less in the 1957-58 recession than did national manufacturing output. The Chicago area index reached a high at 102 per cent in November 1957, then fell 10 percentage points to the June 1958 low. In contrast, both the decline and recovery of national manufacturing production preceded the corresponding movements in Chicago by about two months and declined 15 points.

During the 1960-61 downturn, manufacturing activity in the Chicago area differed even more from that at the national level. Possibly this was because the recovery that followed the 1959 steel strike had been much less vigorous in the metropolitan area than in the nation as a whole. The Chicago area EPC index reached a low of 103 per cent during the 1960-61 downturn or very nearly the same as the low for the manufacturing component of the U. S. index of industrial production. The Chicago area decline, however, was only about 6 per cent, as compared with about 9 per cent nationally.

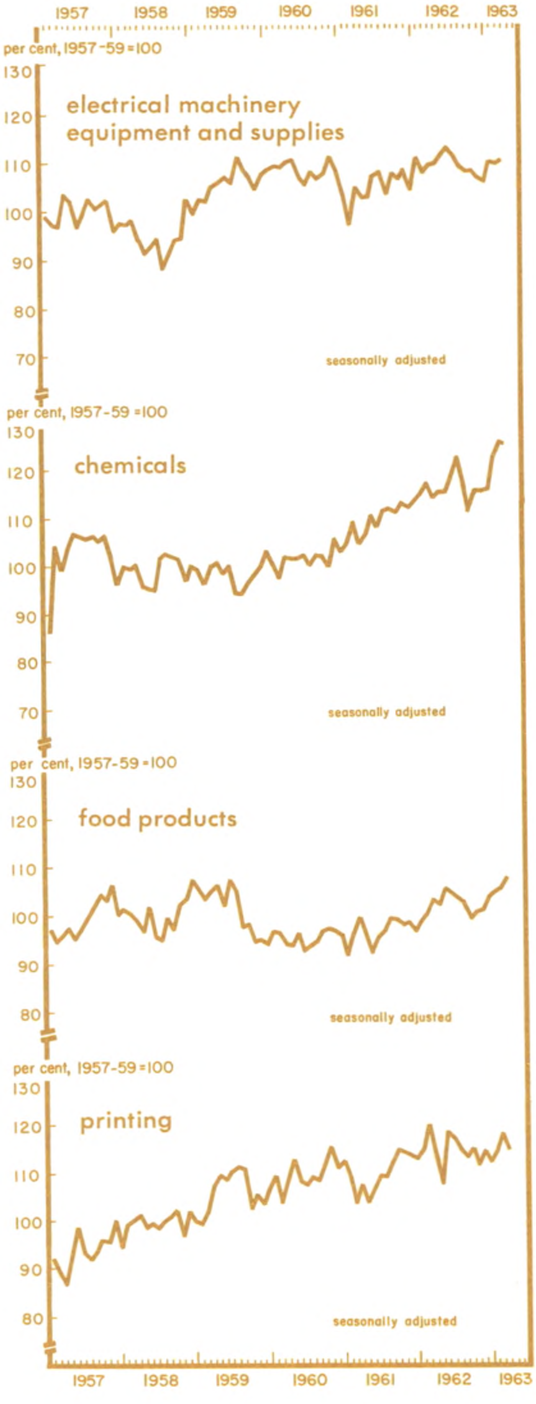
Differences in industry performance

About 45 per cent of the total manufacturing output in the Chicago area is produced by electrical and nonelectrical machinery, and primary and fabricated metal products firms. The wide cyclical swings experienced by these durable goods producers account for much of the cyclical pattern evident in the EPC index. For example, differences in both timing and magnitude of the swings of national and Chicago area manufacturing activity during the 1957-59 and the 1960-61 downturns can be traced to these four industries.

Of the four, only the primary metals industry reached a 1958 low at about the same time as the corresponding national manufacturing components; the other three reached their low points in June or later. Similarly, manufacturing activity had begun to rise in the latter half of 1960 for all of the major durable goods industries except electrical machinery which reached a low in February 1961.

Three nondurable goods industries—food products, printing and publishing, and chemicals—account for almost 30 per cent of the Chicago area's total manufacturing output. These industries typically do not experience pronounced cyclical swings and therefore add stability to Chicago area manufacturing.

In conjunction with the electrical machinery industry, these three nondurable goods industries accounted for much of the first quarter advance. If the fabricated metals and nonelectrical machinery firms in the Chicago area join in the production upswing during the second quarter, manufacturing activity should rise further in the coming months.

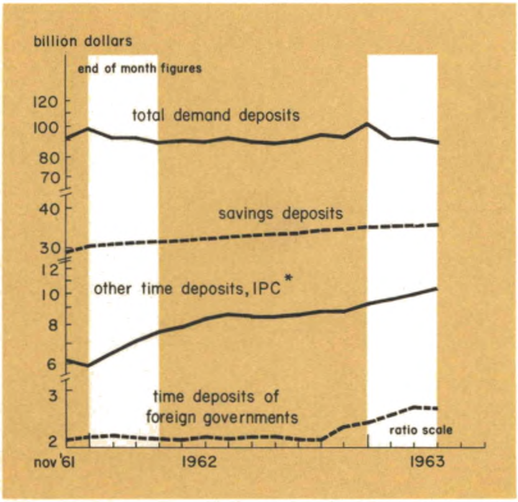


BANKING—*continued from page 7*

Time deposits of individuals and business firms other than "passbook" savings rose 1.2 billion dollars during the quarter in contrast with a record 1.7 billion rise in the first quarter of 1962. At the end of March 1963, weekly reporting member banks in leading cities had 10.4 billion dollars of such deposits, a gain of 35 per cent from a year earlier. Negotiable time certificates of deposit, which account for a sizable proportion of these deposits at large banks, continued to expand rapidly at banks in New York City but increased only slightly at Chicago banks.

Passbook type savings, which account for almost 70 per cent of total time and savings deposits, also increased less in the first three months of 1963 than in the same period in 1962. These deposits rose 1 billion and 1.4 billion dollars in the two periods, respectively.

Time deposits continue to expand rapidly in 1963 at weekly reporting member banks



*Individuals, partnerships and corporations

Only the time deposits of international institutions and foreign governments and central banks, which were freed from interest rate ceilings by congressional action in October 1962, expanded faster in 1963 than in the early months of the preceding year. At the end of March, these deposits were up 25 per cent from a year earlier and accounted for 5 per cent of the total time deposits at these banks.

Free reserves decline

Member bank free reserves declined during the quarter, averaging more than 380 million dollars in January, 300 million in February and about 270 million in March. For the quarter as a whole, excess reserves at member banks exceeded borrowings by about 320 million dollars compared with 450 million in the same period a year earlier. The reduced level of free reserves indicates a slightly less easy monetary policy relative to the prevailing demand for credit. Average weekly free reserves have fluctuated considerably as the Federal Reserve has continued to cushion downward pressures on short-term interest rates in order to minimize the flow of capital abroad.

Treasury financings

The Treasury tapped the money market five times during the first quarter of the year in addition to the regular weekly bill auctions. Particularly gratifying to the Treasury was the response to the initial auction of 250 million dollars in long-term bonds in January. The interest cost to the Treasury was less than 4.01 per cent which compared favorably with market yields on outstanding long-term issues.

In its other financing operations during the quarter, the Treasury sold 2.5 billion dollars each of June tax anticipation bills and

Sources and uses of funds in 1962

Total assets of United States commercial banks increased 16 billion dollars in 1962. Only in 1961 had there been a larger increase in the postwar years. Time deposits were the major source of the gain in bank funds, rising 15 billion dollars or about 50 per cent more than in the preceding year. Demand deposits, which had contributed almost as much as time deposits to the net addition to bank resources in 1961, declined somewhat last year.[1]

Loans increased 14.6 billion dollars in 1962, nearly as much as the total new funds acquired. In the preceding year the rise in loans was only about half as large.

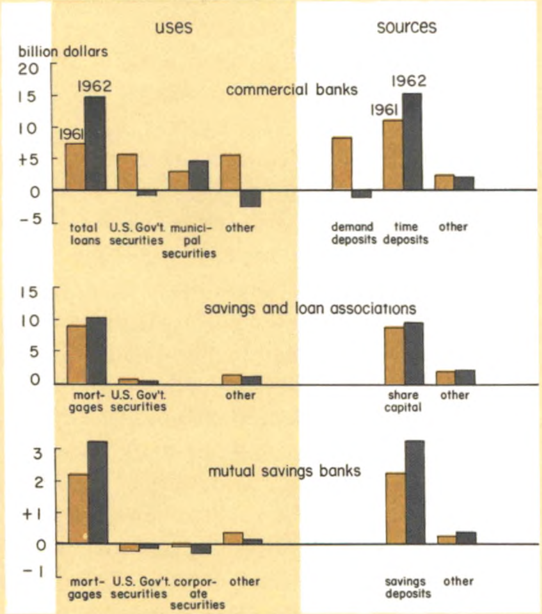
Commercial banks increased their holdings of real estate loans and securities issued by state and local governments by greater amounts than in 1961. On the other hand, their holdings of Treasury securities and other assets, which together increased more than 10 billion dollars in 1961, declined 3 billion in 1962. The decrease in other assets was primarily attributable to a decline in bank holdings of cash following the reduction in reserve requirements on time and savings deposits in the fall of last year.

Despite the rapid increase in time deposits at commercial banks, both savings and loan associations and mutual savings banks had record gains in savings. Share capital at savings and loan associations rose 9.5 billion dollars in 1962 compared with 8.7 billion in 1961. Almost all of the inflow was invested in mortgage loans.

The deposit increase at mutual savings banks, located largely in the New England and Middle Atlantic regions, was 45 per cent greater in 1962 than the year before. As with commercial banks, the rise in savings deposits at mutual banks can be attributed, at least in part, to increases in interest rates.

New York state, home of one-fourth of all mutual savings banks and 60 per cent of all deposits at such banks, raised the rate these institutions may pay on savings deposits held less than one year to 3¾ per cent effective January 1, 1962. At the same time all rate restrictions were removed on deposits of more than one year. The savings banks, which along with savings and loan associations specialize in mortgage lending, increased loans on real estate 50 per cent more in 1962 than in 1961. Investments in other assets increased slightly, while holdings of Treasury securities declined somewhat.

Sources and uses of funds at selected financial institutions in 1961 and 1962



[1]December 31 data are not available for 1962. Changes for the year are measured from December 27, 1961, to December 26, 1962.

one year bills, refinanced more than 9 billion dollars of maturing securities and refunded a record 8 billion of securities maturing within four years into longer-term issues.

One effect of the Treasury's financing operations in the quarter was to increase the average maturity of the public debt from 58.7 months to 61.1. To minimize the downward pressures on short-term rates arising from such a shift in maturity, the Treasury aimed the majority of its new money financings at the short-term sector while moving outstanding issues out to longer-term areas.

Interest rates mixed

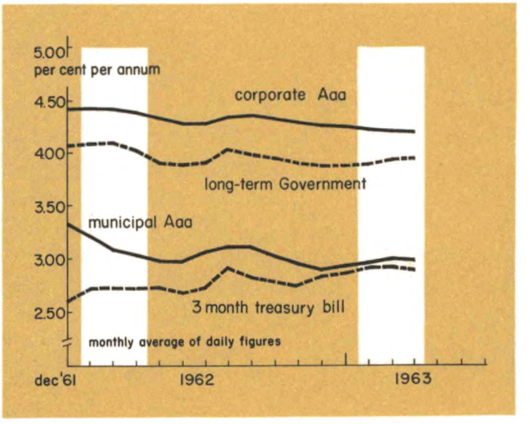
Interest rates, which reflect the sum of all the forces operating in the money and capital markets, fluctuated within narrow limits during the first quarter of 1963. While rates on three-month Treasury bills at the end of the quarter approximated those at the beginning, rates on intermediate- and long-term Government bonds moved up moderately to the highest levels since September 1962.

Open Market Operations, 1962

The open market operations of the Federal Reserve System during 1962 are described in considerable detail in the April 1963 issue of the Federal Reserve Bulletin. The operations are reviewed against the background of broad System policy objectives and money and capital market developments. The report includes a chronological review of open market operations as seen from the Trading Desk of the Federal Reserve Bank of New York and supplements the Annual Report of the Board of Governors of the Federal Reserve System in which the policy actions of the Federal Open Market Committee are described.

Reprints of the article are available on request either from this Bank or from the Board of Governors of the Federal Reserve System.

Interest rates show little change in first quarter 1963



However, until the last days of the quarter, intermediate- and long-term rates remained below the levels of a year earlier, reflecting a large supply of long-term funds relative to investor demand. Market yields on three-month Treasury bills were almost 20 basis points higher at the end of March 1963 than at the same time a year earlier.

Rates on long-term corporate and municipal securities and on mortgage loans did not follow the upward drift in long-term Government rates. On the contrary, rates on corporate Aaa securities fell to their lowest point since early 1959 in the first week of February and remained there throughout the remainder of the quarter. Market yields on municipal securities retreated in March after advancing sharply in February and ended the quarter at about the same level as at the beginning of the year. Interest rates on conventional mortgages on residential properties eased slowly during the quarter while maturities lengthened and loan to value ratios rose somewhat.