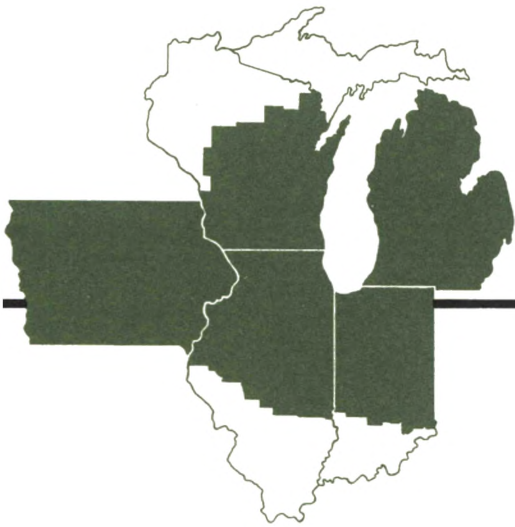
A review by the **Federal Reserve Bank of Chicago**

Business Conditions



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BUSINESS CONDITIONS is published by the Federal Reserve Bank of Chicago. George W. Cloos was primarily responsible for the article "Full Employment in the Midwest" and Charlotte H. Scott for "The Rise of CDs at District Banks."

Subscriptions to **Business Conditions** are available to the public without charge. For information concerning bulk mailings, address inquiries to the Federal Reserve Bank of Chicago, Chicago, Illinois 60690.

TRADING IN FEDERAL FUNDS: Findings of a three-year survey by Dorothy M. Nichols has recently been published. This booklet presents some major findings of a survey in Federal funds transactions from data supplied by nearly 250 banks throughout the country from September 1959 to September 1962 (1965, 116 pp., $1.00 per copy). Copies may be purchased from the Division of Administrative Services, Board of Governors of the Federal Reserve System, Washington, D. C. 20551.

CONSUMER CREDIT: A supplement to **Banking and Monetary Statistics** with consumer credit statistics from 1919 through 1963 has recently been published (1965, 103 pp., $.65). Other supplements available are: Banks and the Monetary System (1962, 35 pp., $.35), Member Bank Reserves and Related Items (1962, 64 pp., $.50), Currency (1963, 11 pp., $.35), Gold (1962, 24 pp., $.35), International Finance (1962, 92 pp., $.65). These booklets may also be purchased from the Division of Administrative Services, Board of Governors of the Federal Reserve System, Washington, D. C. 20551.

MODERN MONEY MECHANICS: A workbook on deposits, currency and bank reserves—Text and "T account" description of the money-creation process and the factors affecting member bank reserves (1961, 32 pp.) is again available without charge from the Federal Reserve Bank of Chicago.

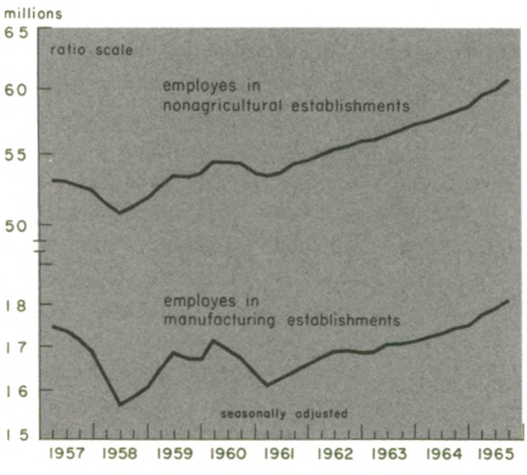
THE TWO FACES OF DEBT: A booklet describing the role of debt in our economy and the distribution of debt among major groups of debtors and creditors (1963, 20 pp.) is also available without charge from the Federal Reserve Bank of Chicago.

Full employment in the Midwest

Employment in the United States has risen rapidly during the past year. In August it was estimated that 72.4 million were at work—up 2.8 per cent from a year earlier. In the five-year period, 1960 to 1965, employment rose at an average annual rate of 1.7 per cent; in the preceding five years, 1955 to 1960, the average rise was 1 per cent.

Unemployment has been reduced gradually in the past four years as demand for workers has risen. In August 1961, as the economy was beginning to recover from a mild recession, about 6.7 per cent of the civilian labor force was unemployed. By July and August 1965 it was 4.5 per cent, the lowest since September 1957.

Manufacturing employment has recently exceeded 1957 peak



The large rise in employment during the past two years has outpaced the accelerated growth in the labor force. From August 1960 to August 1963 the labor force rose about 700,000 per year. From August 1963 to August 1965 the increase was 1.4 million per year.

Younger workers find jobs

In large part the more rapid growth of the labor force reflects the sharp increase in births following World War II. It also reflects the availability of jobs with attractive wages and working conditions that has encouraged additional individuals — many of them women and part-time workers—to seek employment.

The number of births jumped from 2.9 million in 1945 to 3.8 million in 1947. Persons born in the later year reached 18 in 1965, and many of these graduated from high school and sought jobs.

A year or two ago doubts were raised concerning the ability of the economy to provide jobs for the larger number of young workers starting in 1965. However, the unemployment rate for teenagers (14-19 years) has declined and, at 12.4 per cent in August was the lowest for the month since 1957.

According to state employment service offices, summer jobs were easier to find in 1965 than in other recent years. Moreover, in late summer many Midwest employers were concerned about their ability to maintain adequate work forces when temporary workers returned to high school or college.

Proportion of covered workers receiving unemployment compensation

	July and August, weekly average				
	1955	1957	1960	1964	1965
	(per cent)				
United States	2.9	3.0	4.2	3.0	2.5
Illinois	2.8	2.2	3.1	1.9	1.6
Indiana	1.9	2.4	3.6	1.7	1.3
Iowa	1.1	1.4	1.8	1.2	0.8
Michigan	2.9	4.3	5.8	3.5	2.5
Wisconsin	1.5	2.0	2.9	2.1	1.6

Rates of unemployment always are much higher for teenagers than adult workers. But mostly the unemployed are not the same individuals month after month. Many first and second jobs are of short duration as new workers fill temporary vacancies or seasonal jobs. As teenagers become adults, they acquire experience, skills, acceptable work habits and references to past performance, all of which help in obtaining and holding permanent jobs.

Demand for adult male workers has been particularly strong in recent months. The unemployment rate for men 25 years and over was 2.8 per cent in August, the lowest for that month since 1953 just after the conclusion of the Korean war. Demand for women employes, although strengthening, has not kept pace with the demand for adult males, partly because more of the clerical jobs are being performed by computer systems and high-speed record-processing equipment.

Midwest labor markets

The unemployment rate most compatible with maximum non-inflationary growth varies by locality and with changes in the mix of workers by age, sex and skills. Various observers have offered rough judgments that the optimum unemployment rate might be 3 per cent; others suggest 4 per cent and still others the current rate of 4.5 per cent. Because of changing conditions, a prediction of a minimum unemployment rate consistent with relative price stability cannot be made with complete confidence.

During the second quarter of 1965 when the national unemployment rate averaged 4.9 per cent (unadjusted), rates in four of the Seventh Federal Reserve District states —Illinois, Indiana, Michigan and Wisconsin —were slightly under 3 per cent. In Iowa, the rate was less than 2 per cent.

Unemployment includes all persons who do not have a job and are seeking work, whether or not they have worked previously. For the nation these estimates are based

Classifications of major labor market areas

		May 1957		March 1961		July 1964	
Class	Rate of unemployment	United States	Seventh District	United States	Seventh District	United States	Seventh District
		(number of centers)					
A	Under 1.5	2	0	0	0	0	0
B	1.5-3.0	41	8	0	0	46	17
C	3.0-6.0	85	9	49	4	85	6
D	6.0-9.0	14	4	71	13	17	0
E	9.0-12.0	6	1	17	3	0	0
F	Over 12	1	0	13	3	2	0
		149	22	150	23	150	23

upon a sample survey of 35,000 households. Estimates for the various states and localities are derived from a number of factors: one is the number of persons receiving unemployment compensation payments.

Insured unemployment during the summer is shown in the table on page 4 as a per cent of the number of workers covered by the state programs. Average rates are compared with other recent years of relatively full employment. Insured unemployment was at a very low level in the United States and all District states. Except in Wisconsin, the per cent of covered persons receiving unemployment compensation was the lowest in over a decade. As a result, state unemployment compensation funds—reduced during a number of years of heavy disbursements—have been rebuilding.

Among Midwest centers South Bend, Indiana, has had the most noteworthy decline in unemployment in the past year. Following the closing of the Studebaker auto plant in December 1963, unemployment in South Bend rose sharply and remained high during most of last year. In July 1965, however, unemployment was estimated at only 3.5 per cent of the labor force compared with 6.9 per cent a year earlier. This led to the area's removal from the list of "substantial labor surplus areas", areas with unemployment over 6 per cent.

Although South Bend's future looks brighter because new firms are locating there, decreases in unemployment have been much larger than increases in employment. Many workers have taken jobs in other centers or have withdrawn from the labor force.

In the past four years of rising auto and truck production, most Michigan centers have experienced their strongest labor demand since the earlier boom automobile year, 1955. Changes in the status of these and other industrial centers are reflected in the labor market classifications of the U.S. Department of Labor.

Labor market classifications of District centers

	May 1957	March 1961	July 1964
Illinois			
Chicago	B	D	C
Quad Cities	C	C	B
Peoria	B	D	B
Rockford	B	D	B
Indiana			
Ft. Wayne	C	D	B
Gary-Hammond	*	E	B
Indiana	B	D	B
South Bend	C	F	C
Terre Haute	E	D	C
Iowa			
Cedar Rapids	B	C	B
Des Moines	B	C	B
Michigan			
Battle Creek	C	E	B
Detroit	C	F	C
Flint	D	F	B
Grand Rapids	D	D	B
Kalamazoo	C	D	B
Lansing	C	D	B
Muskegon	D	E	C
Saginaw	C	D	B
Wisconsin			
Kenosha	D	D	B
Madison	B	C	B
Milwaukee	B	D	C
Racine	C	D	B

*Included in Chicago area

Unemployment rates for the three largest

District centers—Chicago, Detroit and Milwaukee—were about 3 per cent in the summer. If the labor picture in these areas continues strong, they will move into the B group of "relatively low unemployment." Much depends on developments in the steel and auto industries in the months ahead.

Labor demand generally strong

Starting in 1963 when the current expansion of economic activity was well under way, there have been a rising number of reports from Midwest employers of a gradually tightening supply of skilled workers. At the professional level, engineers of all types, computer programers, medical technicians and accountants have been in short supply. Among the skilled trades, there have been unfulfilled requirements for tool and die makers, machinists, sheet metal workers, welders, electricians, draftsmen and auto, appliance and TV repairmen. In the service industries, demands for social workers, teachers, nurses and hospital aides have remained unfilled. Experienced stenographers and office equipment operators are always in demand.

During the past several months there have been frequent reports of large construction projects being delayed because of inadequate supplies of skilled workmen. Virtually all types of construction workers except laborers —carpenters, masons, glaziers, plumbers, electricians, steamfitters and sheet metal workers —have been in short supply during the summer months of peak demand in the major industrial centers of the Midwest. Seriousness of the shortages varies among areas and among the various trades. One problem is the reduced mobility of workers (partly because of nontransferability of fringe benefits from one locality to another), as compared with the past.

Many construction workers who formerly had been employed by small builders of one- or two-family homes have been drawn into commercial and industrial work by large contractors who can offer year-round employment. Expansion programs in the steel, chemical and petroleum industries typically require large numbers of structural steel workers, electricians, welders and pipe fitters—many of whom can transfer skills learned in factory production. To the extent this occurs, manufacturers' recruitment problems become more difficult.

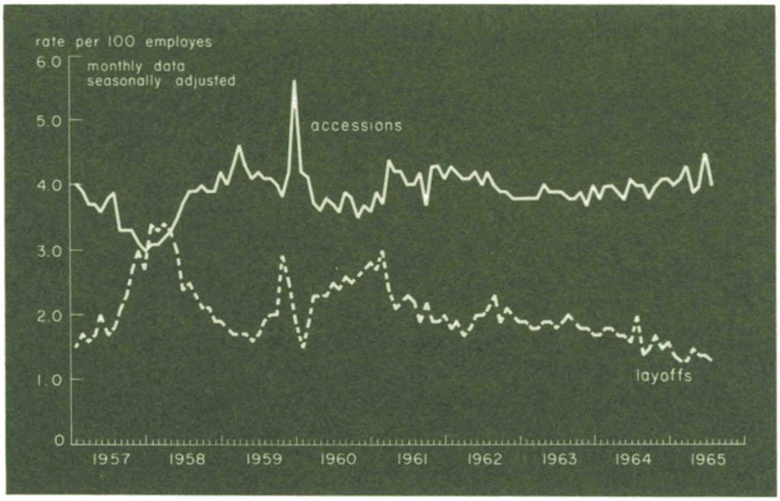
In 1964 there were frequent reports of manufacturers of autos, steel and machinery who had exhausted their layoff lists and had begun to recruit new workers actively, both in the local area and in distant cities. Personnel departments found a growing pinch on supplies of unskilled as well as skilled workers. These reports became increasingly widespread in 1965.

The average workweek in all manufacturing enterprises thus far in 1965 has been in excess of 41

Manufacturing employment rise outpaced total in the last year

	Total nonfarm employment			Manufacturing employment		
	1960-65	1963-65	1964-65	1960-65	1963-65	1964-65
	(per cent increase, June to June)					
United States	11.1	6.6	3.9	7.4	6.0	4.4
Illinois	7.6	5.5	2.9	5.6	6.6	3.6
Indiana	10.9	6.3	4.7	10.6	7.4	6.4
Iowa	9.4	5.5	3.5	6.2	5.6	3.3
Michigan	12.6	9.4	5.4	12.2	10.9	6.2
Wisconsin	10.4	6.5	4.2	5.8	4.9	5.4

Manufacturing layoffs have declined as hirings and employment increased



retail trade and government are finding the competition for employes from industry to be more vigorous.

After the urgent demand of the Korean war had abated, total manufacturing employment reached a peacetime peak of 17.4 million early in 1957. At the high watermark in 1960, manufacturing employment fell short of this total. Employment increases had been centered in government, trade and service jobs.

hours, higher than the average for any full year since 1945. (In July and August the average week was 40.9 hours.) Factory workweeks in recent months have exceeded the national average in all District states except Iowa.

Earlier in the current expansion many firms found it cheaper to pay time and one-half for overtime than to hire and train additional workers for what were thought to be temporary demand increases. But requirements have continued to rise, and this year the need to maintain production schedules often has required additional overtime as well as large additions of new workers.

Through much of the period 1957-64, a dearth of opportunities in the goods producing lines—manufacturing, construction and mining—and in transportation caused many young men who were not college bound to seek white collar employment. This year personnel managers seeking workers for factory offices, financial institutions, public utilities,

Not until November 1964 was the 1957 peak in manufacturing employment exceeded. In the summer of 1965, the total went well over 18 million. Employment gains in the states of the industrial Midwest, as a group, have about matched the increase for the nation during the current economic expansion. Illinois has lagged somewhat, while Michigan has reported dramatic gains. Increases in employment in manufacturing have been associated more with the rate of layoffs than the rise in hiring (see chart). New hirings, as indicated earlier, have been limited by the available supply of workers.

Needs for male workers

The rise in number of available workers, although rapid, has been limited by several factors in recent years. Some of these have been of growing significance for a decade or more; others are of relatively recent origin. These developments particularly affect the number of adult men available.

Throughout the postwar period, there has been a steady rise in the proportion of high school graduates who seek further training in colleges or technical schools. For the Midwest this proportion now approximates 50 per cent and is much larger in high-income communities. Many of these persons could easily fill vacancies for inexperienced workers but prefer to acquire education and skills that may fit them for more attractive positions later.

One of the most significant labor market developments of the past decade has been the lengthening of vacations. Both white and blue collar workers today commonly are eligible for annual vacations of three or four weeks, occasionally even more, after completing a given term of service. To accommodate such schedules, many firms hire seasonal replacements, or maintain a larger average employment throughout the year.

A more recent development relates to earlier retirement under public or private pension arrangements. As a result of last year's labor-management agreement in the auto industry, for example, thousands of workers are applying for early retirement this autumn, some as young as 55 years of age. Not all of these, of course, will withdraw from the labor force; some will take jobs elsewhere.

Another factor has been the recent step-up in draft calls associated with hostilities in South Viet Nam. A year ago about 6,000 young men, mainly between 20 and 26, were called into the armed services monthly. Currently the number is about 34,000 per month.

Employers have taken various measures to obtain the services of the desired number of workers. One obvious method is to raise compensation and fringe benefits, to improve working conditions and to adjust work schedules to the availability of workers. Doubtless, hiring standards have been lowered in some cases. Another step has been to increase advertising and recruiting efforts, although this does relatively little to relieve the overall problem and may tend to increase voluntary separations (see chart).

Where feasible, average workweeks have been lengthened. Workers have been upgraded, and in-plant training programs have been expanded and accelerated. Most workers, of course, learn their specific skills on the job.

Midwest manufacturers during recent months have been recalling retirees, especially those with metal working skills. Some of these men had been retired for five years or more, often because of arbitrary maximum age regulations.

Matching workers and jobs

The July 1964 issue of *Business Conditions* was devoted to a discussion of "Why Unemployment Amidst Unfilled Jobs?" One of the study's major conclusions was that, although further increases in aggregate income could reduce unemployment appreciably, there was also a "structural" problem of matching workers and jobs through better education and training and improved communications between employers and persons seeking work. In recent months the structural aspects of the unemployment problem seem to have become the more important, following the substantial increase of employment in the past year. Numerous signs that appear in shop windows in suburban shopping areas and on the main streets of large Midwest cities currently offer jobs to waitresses, sales persons, cashiers and stock room helpers. Presumably, such signs are used in an effort to recruit workers despite the possibility that patronage may be discouraged by the expectation of sluggish service.

In the low-income sections of the cities, there are many unemployed who are hampered by lack of training and education. Frequently, the barriers between these persons and the vacant jobs are not insurmountable. Methods of reducing these barriers are being explored under the auspices of both public and private organizations.

Government efforts to match jobs and workers have been expanded under the Manpower Development and Training Act (MDTA). Since 1962 over 200,000 persons have been trained in a variety of occupations while receiving subsistence pay under the MDTA. In the Chicago area 4,500 persons have been assisted in training and job placement and another 7,000 currently are enrolled in courses fitting them for 30 different occupations for which workers are in short supply.

A portion of the MDTA funds are being channeled to the Labor Department to expand the programs of the Bureau of Apprenticeship and Training (BAT). Since the time of the Korean war, there have been frequent warnings of future stringencies of skilled workers because of the small number of young men serving apprenticeships, particularly in the metal working trades. Independent shops employing critically short tool and die makers are said to be too small—averaging about 30 workers—to offer formal training programs without Government aid.

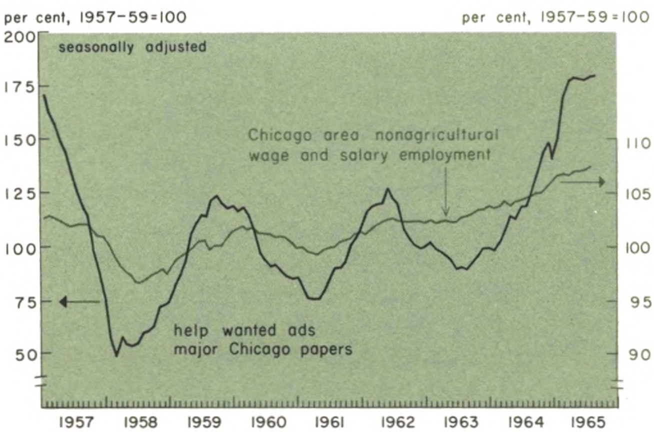
BAT is empowered to help finance the cost of employers' apprenticeship programs including subsistence pay, instructors' salaries, wear and tear on machines and usage of materials. Employers usually must provide a period of formal training lasting at least two years to be eligible for such payments.

A variety of projects have been launched this year under the anti-poverty program, administered by the Office of Economic Opportunity and the Department of Labor. One of these is the Job Corps which places young men and women in camps where they can be taught basic skills under a regime calculated to develop acceptable work habits. Another program is the Neighborhood Youth Corps which employs young persons, who cannot otherwise obtain jobs, through assignments with government bodies and nonprofit organizations.

Various organizations, public and private, are attempting to convince employers that it is profitable to hire members of minority groups, the physically handicapped and the retarded. Some firms have found that workers in these groups perform certain jobs more diligently than persons who have had greater developmental advantages.

Many firms require that prospective employes possess a high

Rising labor demand boosts "help wanted ads"



school diploma but, in lieu of this, are willing to accept a "Certificate of Equivalency." Some of the community action programs financed by the anti-poverty program are specifically directed towards training "disadvantaged" persons in the "language and numbers" skills required to obtain such a certificate.

Social workers and personnel managers find that many potential workers are functionally illiterate (defined as unable to read a newspaper with ease) regardless of the number of years in school. Others who have difficulty holding jobs do not appreciate the value of personal grooming and manners deemed essential in an ever growing number of jobs involving close association with other workers. Moreover, some must be brought to understand the need for energetic application, punctuality and taking orders from a boss.

Experiments are being made by public and private groups to improve communications between localities with surplus workers of various abilities and places that need such workers. In some cases, help may be available to finance moves of workers and their families to new locations. Unemployed persons often are unable to move to jobs because of lack of information and/or ready cash to finance their transportation and resettlement.

Employment outlook in the Midwest

The vigorous economic climate of the Seventh District is based to an important extent upon strength in the steel, automobile and capital goods industries. Labor requirements in two of these prime movers are likely to ease somewhat in the months ahead.

Many of the producers of machinery and equipment are working at practical capacity and report growing order backlogs. With many business firms accelerating programs of expansion and modernization, labor requirements of capital goods manufacturers can be expected to be maintained or rise further.

Auto and truck output is expected to be at virtual capacity in the early months of the 1966 model year. Late in the fourth quarter as inventories of new model vehicles reach desired levels, reductions in auto output are likely to occur. If sales should weaken, the cutbacks would be greater than seasonal.

Steel output declined in September after the labor settlement and a further drop is expected in October. Early evidence suggests a smaller and more gradual reduction in swollen inventories of steel than had been indicated earlier. Nevertheless, steel's labor requirements probably will be reduced slowly through the remainder of the year.

The economic outlook is normal in that there are important uncertainties. But these uncertainties, particularly in autos and steel appear less foreboding with the fourth quarter at hand than several months ago.

Developments during the past year provide some reassurance that the American economy can operate at relatively full employment without generating the inflationary pressures that might lead to a reaction accompanied by declines in output and income. The testing period, however, will continue.

Additions to the labor force in the years ahead will approximate the large increases of 1964 and 1965. Meanwhile, more efficient new equipment will reduce needs for workers in some lines. Rapid growth in output and income will be needed if additions to the labor force are to continue to be utilized productively and the trend toward lower levels of unemployment is not to be reversed.

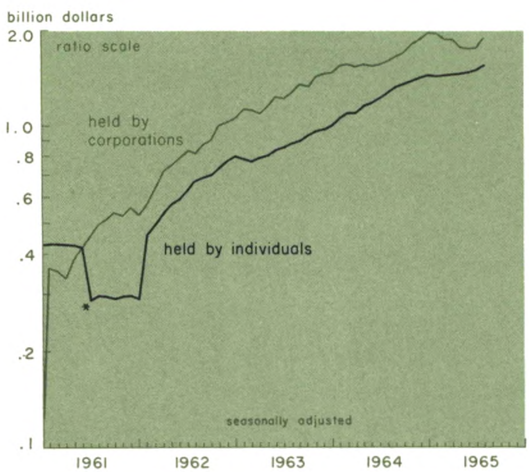
The rise of CDs at District banks

One of the most striking developments in commercial banking in recent years has been the dramatic growth of time certificates of deposit (CDs). At midyear, the CDs outstanding at commercial banks in urban areas of the Seventh Federal Reserve District accounted for almost 20 per cent of total time deposits, compared with about 5 per cent in mid-1960.[1] While passbook savings—the largest segment of the time deposit total—rose a substantial 70 per cent between mid-1960 and mid-1965, this was relatively a much smaller gain than was recorded by CDs.

The CD—a time deposit of specified maturity—now encompasses a variety of forms. Included are "negotiable CDs" as well as the nonnegotiable "savings certificates." One class may be set apart from another at a given bank by restricting it to a particular group of holders, such as individuals, or by combinations of other characteristics. The development of a number of forms of CDs reflects the efforts of banks to attract funds from a broad range of depositors.

At the larger banks, CDs issued to corporations are usually in denominations of 100,000 dollars or more, negotiable and readily marketable. By contrast, the savings and other time certificates issued to individuals typically are in much smaller denominations, often are not negotiable and, even if negotiable, are not readily marketable. Rates and maturities on CDs issued to corporations frequently are tailored to meet individual requirements, while the terms of savings certificates normally are fairly standardized.

CDs increase sharply
at District banks
until early 1965



*Reflects in part transfers from personal CDs to passbook accounts when several large banks began to offer the same rates on both types of time accounts.

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[1] The data used in this article include CDs issued to corporations and to "others" (largely individuals) by member and nonmember banks in 51 urban areas in the Seventh Federal Reserve District. CDs issued to public bodies (state and local governments, foreign institutions, etc.) are excluded. About 22 per cent of total time deposits of individuals and businesses at these urban banks were in the form of deposits other than passbook savings as of June 30, 1965—slightly less than the 24 per cent for all Seventh District member banks.

Interest rates and balances of passbook savings and personal CDs, June 30, 1965

Urban area	Yield spread[1] (per cent per annum)	Personal CDs as proportion of total personal time deposits[2] (per cent)
Illinois		
Bloomington	0	8
Champaign-Urbana	0.1	8
Chicago	0.1	6
Danville	—	—
Decatur	0	6
Peoria	0	7
Quad Cities[3]	1.0	39
Rockford	0.5	14
Springfield	0	4
Total[3]	0.1	7
Indiana		
Anderson	0.5	18
Fort Wayne	0.6	16
Gary-Hammond	1.2	27
Indianapolis	0.7	21
Lafayette	0.9	44
Muncie	0.6	39
Indiana—*continued*		
South Bend[3]	0.6	19
Terre Haute	0.5	22
Total[3]	0.7	23
Iowa		
Burlington	1.0	58
Cedar Rapids	0.9	7
Clinton	1.0	32
Council Bluffs	1.0	44
Des Moines	0.1	25
Dubuque[3]	1.0	28
Marshalltown	0.5	18
Mason City	0	44
Muscatine	1.0	39
Ottumwa	2.0	65
Sioux City	0	7
Waterloo	0.7	38
Total[3]	0.5	27

Deposits of individuals

As of June 30, 1965, 90 per cent of the banks in the District's 51 urban areas had CDs outstanding to individuals, although in many instances the amounts were small. Five years earlier, 70 per cent of the banks had personal CDs outstanding. Hence, most District banks have offered CDs to individuals for a number of years. The big push in CDs for corporate deposits, however, did not come until 1961 when a number of the larger banks began to seek such deposits aggressively.

Since early 1962, personal and corporate CDs have shown roughly comparable growth (see chart). By mid-1965, 1.5 billion dollars of personal CDs and 1.8 billion dollars of corporate holdings were outstanding at District banks.

The growth of personal CDs has varied greatly in different areas of the District, depending in part on the relationship between

Urban area	Yield spread[1] (per cent per annum)	Personal CDs as proportion of total personal time deposits[2] (per cent)	Urban area	Yield spread[1] (per cent per annum)	Personal CDs as proportion of total personal time deposits[2] (per cent)
Michigan			**Wisconsin**		
Adrian	0	24	Appleton	1.0	40
Ann Arbor	0	7	Green Bay	1.0	32
Bay City	0	10	Kenosha	1.0	17
Detroit	0	4	Madison	1.1	43
Flint	0	8	Manitowoc	1.0	23
Grand Rapids	0	8	Milwaukee	0.9	16
Jackson	0.7	22	Oshkosh	1.0	41
Kalamazoo	0.5	29	Racine	2.1	45
Lansing	0	7	Sheboygan	1.0	34
Muskegon	0.6	25	Total	0.9	24
Port Huron	0	5			
Saginaw	0	10	**51 areas[3,4]**	0.2	10
Total[4]	0.1	7			

[1]Rate on personal CDs minus rate on passbook savings.

[2]Total personal time deposits include personal CDs and passbook savings.

[3]Includes adjacent communities in neighboring state.

[4]Includes Battle Creek for which figures are not published separately.

NOTE: The maximum weighted interest rate on CDs issued to individuals as of June 30, 1965, was 4.5 per cent in Kalamazoo; 4.2 per cent in Indianapolis and Milwaukee; and 4.1 per cent in Fort Wayne and South Bend. In all other areas it was 4.0 per cent, except in Danville where CDs have not been offered to individuals.

rates of interest paid on CDs and the rates applicable to passbook savings. In June, 86 per cent of the banks in the District's urban areas were paying 4 per cent on personal CDs of one year or longer maturity. This rate exceeded the top rates on passbook savings in 34 of the 51 urban areas. All of Indiana's urban areas were included in this group. (The maximum rate permitted on passbook savings is 3.5 per cent in Indiana and 4 per cent in the other District states—Illinois, Iowa, Michigan and Wisconsin.) In a small but increasing number of communities, banks have raised rates on personal CDs above 4 per cent. In June, however, only 2 per cent of the banks offered 4.5 per cent, the top rate permitted on certificates of deposit.

Changes in rate relationships induce some transfers from one form of time account to another. Also, a relatively attractive rate on CDs usually results in net gains in *total* time deposits, at least temporarily. Such developments were evident during the first half of 1965, for example, in the rise of 60 million dollars in certificates held by individuals in Indiana's urban areas, compared with an increase of 18 million dollars in lower-yielding passbook savings.

Some of the District's banks during the first half of 1965 reported declines in personal CDs. This occurred in Detroit and most other urban areas of Michigan and reflected in large measure recent rate increases on passbook accounts, which brought rates on these accounts into line with those on certificates of deposit. While passbook savings rose 505 million dollars at Michigan's urban banks, personal holdings of CDs declined 24 million dollars.

Competition leads most banks within urban areas to offer the same rates on comparable types of time deposits. This tends to result in fairly standard proportions of personal time deposits in the form of CDs for all banks within an area, irrespective of bank size. From one area to another, however, these proportions may vary widely as they reflect differing relationships within time deposit rate structures. For example, the average ratio of CDs to total personal savings-type deposits (passbook accounts and personal CDs combined) as of mid-1965 at the Michigan banks was 14 per cent; in Indiana, by contrast, the share was twice as great, 27 per cent.

Attracting corporate funds

The larger banks in the District compete with banks in many other sections of the country for the time deposits of large business firms. It is at these banks that corporate CDs account for a large proportion of the total outstanding (see table). The smaller banks, serving more localized markets, appear to find their business depositors less disposed to hold funds in CD form. At the end of June only 20 per cent of the "small" District banks (those with less than 50 million dollars in deposits) reported that corporations held half or more of all CDs outstanding.

In Chicago—where bank promotion of personal CDs has been limited—nearly 80 per cent of the banks in the largest size group (total deposits of 100 million dollars or more) had more than half of their CDs outstanding to corporations. Moreover, the proportions of banks for which corporations held 50 per cent or more of total CDs outstanding were appreciably higher in Chicago for all deposit-size classes than in other urban centers in the District.

Higher withdrawals

CDs are often renewed at maturity, fre-

Distribution of banks by size and proportion of CDs issued to corporations

Banks by deposit-size groups (million dollars)	Proportion of corporate CDs to total CDs outstanding[1] June 30, 1965: Under 10 per cent	10-50 per cent	50 per cent and over
	(per cent of banks)		
Chicago			
Under 10	50	23	27
10-50	53	20	27
50-100	23	27	50
100 or more	5	16	79
50 smaller urban areas			
Under 10	55	27	18
10-50	54	31	15
50-100	40	36	24
100 or more	17	46	37

[1]Excludes CDs held by state and local governments and foreign institutions.

quently as a result of an automatic renewal clause in the deposit agreement. The "nominal" maturity schedule of a bank's CD liabilities consequently may bear little relationship to the pattern of cash outflow actually experienced. Furthermore, withdrawals may rise while the volume of CDs outstanding remains stable, as banks succeed in replacing maturing certificates with new deposits.

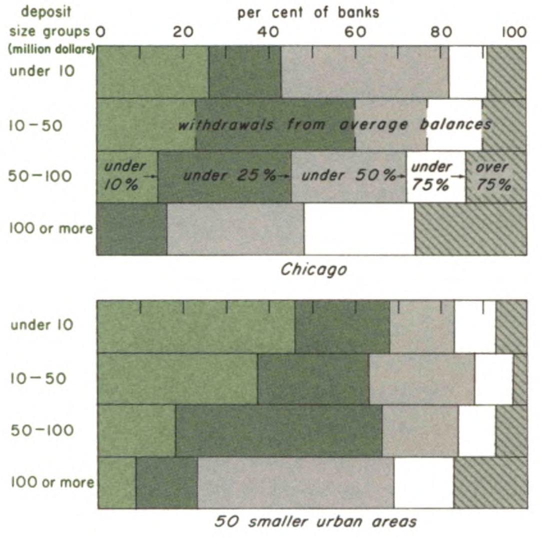
Personal CDs tend to have lower withdrawal rates than corporates. During the first half of 1965, withdrawals of personal CDs accounted for 29 per cent of the average amount outstanding. The withdrawal of corporate certificates was equal to 74 per cent of average outstandings.

CD withdrawals as per cent of average balances

First six months	Personal deposits Passbook	CDs	Corporate CDs
			(per cent)
1961	26.8	58.9	45.7
1962	30.1	21.7	36.5
1963	24.9	24.1	41.8
1964	24.8	18.8	66.8
1965	26.3	29.3	74.1

CD withdrawals by both personal and corporate depositors during the first half of 1965 were higher than in most earlier periods but not as high as in late 1961. In that period, rates offered by banks ceased to be competitive with yields on alternative investments. After the January 1962 revision in Regulation Q and upward adjustments in rates paid by banks, CD withdrawals dropped sharply. Recent increases in withdrawals, in part, appear to reflect changes in interest rate relationships that make it difficult for some banks to attract new funds. This may also reflect reduced supplies of corporate funds available for investment in certificates of deposit and other liquid assets.

Most District urban banks had CD withdrawal rates of 50 per cent or less in first half of 1964



For all District banks with deposits of 100 million dollars or more, withdrawals from corporate CDs for the first half of 1965 amounted to 81 per cent of balances, implying an average maturity of approximately seven months. Almost half of the District's urban banks had withdrawal rates during the first six months of less than 25 per cent in corporate as well as individual time deposits, and another 25 per cent had withdrawals between 25 and 50 per cent. Banks that have had a large proportion of time deposits in the form of CDs since early 1962 almost invariably have had lower CD withdrawal rates than those with smaller proportions of such deposits. The generally lower rates suggest that the funds attracted into these accounts have been interest-sensitive but relatively inactive, especially at the smaller banks (see chart.)

Determinants of growth

Continued popularity of CDs will depend much on comparative interest rate movements. The most relevant rates include those on passbook accounts, savings and loan shares and Treasury bills. Even at banks that have paid higher rates on CDs than on passbook savings since early 1962 (as in Rockford, the Quad Cities and most urban areas in Iowa and Wisconsin), the bulk of personal time deposits has remained in passbook accounts.

Growth in CDs may become sensitive also to rates on the newly developing unsecured promissory notes and long-term debenture issues. Higher returns can be offered on notes and debentures than on CDs at about the same net cost to the banks. This is chiefly because funds raised by issuing notes and debentures are not deposits (under existing regulations) and therefore are not subject to reserve requirements and deposit insurance assessments.

Notes and debentures, however, are not likely to replace CDs completely since they constitute borrowed funds, which are subject to regulatory limitation. In addition, management policies and customer attitudes may limit the borrowings that can be accommodated. Those few District banks that have issued unsecured notes also issue certificates of deposit. Note issues frequently have been used to acquire funds for periods of less than 30 days—a maturity for which, by regulation, interest bearing CDs cannot be issued. For the nation it is estimated that only about 200 million dollars of short-term notes were outstanding at the end of June. The amount was increasing rapidly in September following the announcement that a special form of non-negotiable instrument was permitted under New York state laws.

A sizable portion of all recent debenture issues, and especially those of smaller banks, have been sold privately to such large national investors as insurance companies and corporate pension funds. Notes and debentures, however, could have a marked impact on CDs if banks were to find it difficult to compete for funds at the maximum rates permissible under Regulation Q.

Rate relationships have changed very little since the end of June 1965. Only a few banks, mostly in Chicago, boosted rates paid on personal CDs as of July 1, while rates of return on passbook savings, savings and loan shares and short-term Treasury securities remained quite stable. Some downward adjustments were made during July in rates paid on negotiable CDs with longer maturities, but in early September rates moved up to new high levels with negotiable CDs of one year and more commanding rates close to the maximum permissible rate of 4.5 per cent.

Growth in CDs in the District's urban areas combined accelerated somewhat during July and remained at a high level in August. Personal CDs, seasonally adjusted, rose 2.5 per cent on the average during the two-month period compared with a 1.6 per cent average increase in the preceding four months and decreases in January and February. Corporate CDs, seasonally adjusted, rose 6 per cent following declines in all earlier months of 1965 except June. The gains of the latest two months point to continued interest in this source of funds on the part of banks and widespread investor demand for certificates of deposit.