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BUSINESS REVIEW

Business Inventories

Prepared by the Research Staff of the Federal Reserve Bank of Cleveland
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Good morning!

Employment is at high levels and salary and wage payments are the greatest in our history. Output of mines, forests and factories continues in record volume, and goods are moving through business channels out into consumers' hands in substantial amounts. As these goods move through our business system, they are the inventories or stocks of goods which enable our factories, jobbers, wholesalers and retailers to do business. As the products of our farms, mines and forests are worked on they become our inventories in process of manufacture. When the articles are completed they become the inventories of finished goods of manufacturers. As they are sold they move into the hands of jobbers, wholesalers, commission merchants and finally retailers where they are put on shelves for display and sale to consumers, as in grocery and clothing stores.

Inventories are necessary for business and it takes a lot of inventories to keep business going. On August 31, 1948, total inventories of manufacturers, wholesalers and retailers were valued at more than $50 billion. That is more than $300 worth of goods for every man, woman and child in the land and nearly $2,000 worth of inventory for every person employed in factories and in transporting and selling the goods. That is a lot of supply -- but, even so, it does not include livestock, foods and animal feed on farms.

We came out of the war with low inventories, too small to really do business. Do you remember trying to buy shirts, sheets, pillow cases, soap, and stoves? Do you remember how difficult it was and has been to get the size, style and color you wanted? That was because merchants did not have adequate inventories; they did not have enough goods on their shelves or on their floors to serve us.

In order to give better service to customers, business had to increase its stocks of goods. From the close of the war to the present, the dollar value of inventories of manufacturers, wholesalers, and retailers has increased by more than 80 percent. A part of the dollar increase, of course, has reflected the higher prices at which successive purchases have been made. But there has also been a substantial increase in the physical volume of goods in warehouses and storerooms and on shelves of business concerns.

Handling these inventories presents problems to businessmen. If inventories are too small they may run short, and businessmen will be unable to supply their customers or even keep their workers employed. This means loss of sales, unemployment and loss of wages. If inventories get too large business suffers the risk of substantial loss through price declines -- as happened with fats and oils last spring -- or through deterioration and spoilage, or changes in fashion or style -- as sometimes happens with items like women's shoes. When inventories become too large businessmen sometimes find it necessary to sell the excessive or unwanted or outmoded stocks of goods at a loss. Excessive inventories in hands of retailers and wholesalers lead to cancellations of orders, to accumulation of stocks of finished goods at manufacturers and to shutdowns or layoffs or short-work weeks, with resulting loss of wages. This happened last summer in the shoe and leather goods industries and in some branches of the textile industry. When these adjustments are scattered and relatively small in amount during prosperous periods, as in the past year, they do not affect seriously the general level of business or of incomes. They are, of course, very serious to the businessmen and to workers immediately affected. When the adjustments become widespread, price cutting becomes general, buying is held off in anticipation or hope of further price declines, production schedules are cut back, unemployment spreads, incomes decline and we have a business recession which sometimes becomes a depression as in 1921 and the early Thirties.

Inventories also present problems to banking and finance. It takes money to run a business. Business has to buy its materials to be processed or worked on. While the materials are being manufactured into finished goods and while the finished goods are being shipped and carried as stock on retailers' shelves and floors, the businessman has his money tied up. He does not get his money back until he sells the goods. In the meantime, he has to continue to pay salaries and wages. In order to keep materials flowing through his plant, and his workers employed the businessman frequently has to borrow. As business has expanded and inventories and payrolls have increased business loans of the nation's banks have risen. Over the past three years these loans have more than doubled. Not all of these loans are for inventory purposes by any means. The cost of carrying these heavier inventories, however, has made it necessary for business to raise more money. Much of that money has been borrowed from the banks.

We have heard a great deal about the effect of inventory growth on our business health. To what extent has the growth of $25 billion in inventories over the past three years contributed to our high levels of business and employment? But I see that my time is up -- so I shall have to imitate the old movie serial which closed each episode with the hero or heroine in imminent peril. And as the screen used to flash the words "Watch for the next episode", I must say "Listen in next week at this time and we shall discuss the extent to which the growth in inventories has affected business trends and how prospective changes may influence the outlook".

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