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THE CURRENT BUSINESS AND FINANCIAL SITUATION AND THE OUTLOOK FOR 1947

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BUSINESSMEN and bankers are entering a period which will call for exercise of the highest quality of business and financial statesmanship. The goal which faces us in 1947 is that of maintaining a flow of goods and services to our people and the peoples of the world so as to contribute to the further advance of material well-being.

As the year 1946 opened we faced a task of reconversion of staggering proportions. A large backlog of demand existed for goods of all kinds, capital equipment—machinery and tools to be used in the production of goods—consumers' goods, and housing. This demand was supported by the highest level of income and the largest volume of deposits, cash resources, liquid assets and savings in the country's peacetime history. The inflationary threat inherent in the situation on the one hand and fears on the other hand of possible widespread unemployment attending our efforts at reconversion led to developments which increased the already severe stresses and strains to which our economy was being subjected. Work interruptions were numerous, costs increased, severe bottlenecks persisted and prices advanced substantially.

Notwithstanding our difficulties, the year just closed has witnessed the highest levels of peacetime activity in our history, both in the nation as a whole and in the Fourth Federal Reserve District. The output of our farms has been at record levels and the net income of farmers has been higher than ever before. Industrial employment and salaries and wages have been higher than in any other year except at the peak of the war. Net incomes from business operations, before income taxes, while disappointing in some lines and generally below the high level of 1945, have, in the aggregate, also been large. Lower taxes and refunds of some wartime excess profits taxes have provided sufficient financial benefits to bring aggregate profits after taxes to above previously existing records reached during the war. The total volume of money payments of all kinds in the nation has probably been higher than in any other year in our history. These records have not been achieved without some distortion in our business and financial picture. These distortions appear to be particularly pronounced in farm land prices, in urban real estate, in inventories and in prices of some commodities.

The record levels of farm incomes of recent years have caused farm land prices to approach the high levels of 1920. The volume of farm transfers has increased substantially and total farm mortgage debt in the United States has risen during 1946 for the first time since 1927. The rise has reflected primarily

a growth in mortgage loans at commercial banks. The average size of those loans has been substantially larger in 1946 than in prewar years.

The small volume of farm debts on the whole, however, indicates that agriculture does not face the danger of a financial breakdown comparable to that which occurred in 1921 and 1922. Even if the net income of farmers were to decline as it did in the 1919-1921 period, or by more than one half, it would still be at record peacetime levels and most of the farmers would still be receiving incomes sufficient to provide incentives for the planting and harvesting of large crops. A substantial drop in farm prices and farm incomes, however, could seriously embarrass both borrowers and lenders involved in substantial credits predicated on present levels of prices and income. Barring unfavorable weather and substantial reductions in yields, prices of farm products may be expected to show some weakness in 1947.

The shortage of housing throughout the nation and in the communities of this district has brought about one of the most serious real estate booms in our history. The inflation has been particularly severe in the smaller so-called "lower priced" units and has brought prices on existing structures to above reproduction costs. The rise in real estate prices has been facilitated by the extension of liberal credit. Loans on nonfarm real estate have increased more rapidly and have risen to higher levels in 1946 than in any of the past fourteen years. The average size of loans has also been larger than in recent years.

Transfers of existing properties at higher and higher prices with larger and larger loans increase the risks borne by financing institutions and necessitate closer and closer scrutiny of each loan application. Excessive debt may not only bring loss to the lender, but incalculable hardship to the borrower as well. It is our observation that the bankers as a whole are making every effort to see that prospective borrowers do not become involved in debt burdens beyond the borrower's ability to sustain. The utmost diligence will have to be practiced in 1947 to prevent the development of financial difficulties in this field.

As building materials become more plentiful we can anticipate a sustained high level of building throughout 1947, barring work interruptions. The resulting increased supply of residential units should ease the housing situation considerably. As new structures become available in increasing volume, older units, which now command a premium

because of their present availability, can be expected to lose that premium.

The reconversion of industry from war production to civilian purposes has resulted in a substantial expansion in inventories. The larger part of the expansion appears to have reflected the filling of civilian pipelines which were emptied during the war period. These inventories are necessary to maintain a proper flow of goods and services through the industrial structure and to the consuming public and are not a matter of general concern. The uneven flow of materials and products, however, has brought about, in numerous instances, a condition of unbalanced inventories. As bottlenecks are eliminated, some commodities could come onto the market in such volume as to bring about substantial reductions in prices and losses on excessive inventories.

If our major bottlenecks can be broken and a large output of goods maintained, the year 1947 should see the development of increasingly severe competitive situations which will test the skill and ingenuity of businessmen. Probably every house and every automobile that is built in 1947 can be sold. The limitations on output of these articles will be set not so much by market demand as by the availability of materials and skilled manpower. The same will probably be true of transportation equipment, farm equipment, and some household equipment. In other lines, however, particularly in some of the so-called soft goods or nondurable goods lines where inventories have been accumulating rapidly, we cannot overlook the possibility of supplies becoming excessive at present prices. As a consequence, reductions in prices of numerous consumer items loom as a distinct possibility in 1947. Businessmen will need to give increasing attention to their inventory problems. Competitive pressures will react particularly severely on concerns with high costs and limited financial resources.

The bankers and financiers of the nation and of this district have done an outstanding job in financing the reconversion of business to a peacetime footing. Notwithstanding the largest aggregate cash resources in their history, business has required substantial additional credits. The volume of new corporate issues in 1946 was the largest of any year since before the depression of the Thirties, the volume of business loans of banks throughout the nation and in the Fourth District has expanded more rapidly than ever before, and the amount outstanding probably has reached the highest figure on record.

As goods have become more plentiful, the volume of consumer credit has expanded. The growth in consumer credit has been more rapid in 1946 than in any other year of record and further increases are indicated for 1947, possibly to levels exceeding the highest heretofore achieved.

Bank loans on securities and their holdings of obligations of the United States Government declined substantially during the year, reflecting a change in the financial position of our Federal Government with the cessation of armed conflict. The rapid curtailment of wartime expenditures brought cash receipts and disbursements of the Government into approximate balance and permitted a reduction in the public debt of about \$23 billion during the year. The reduction was effected chiefly by drawing down the Treasury's large deposit balances carried with the banks of the nation. As a consequence, total deposits of the banks were reduced, even though holdings of cash assets of all kinds—currency and deposits—by individuals and businesses increased, both in this district and in the nation as a whole, to the highest levels on record.

The volume of United States Government financial transactions is so large and the impact of Government fiscal operations on our economy is so great that any analysis of financial developments would be incomplete without some reference to the role played by Government finance.

During the calendar year 1946, approximately \$70 billion of U. S. Government marketable issues matured or were called for payment. Of the \$70 billion maturing, about \$23 billion were retired. The remaining \$47 billion were exchanged for \$17 billion of Treasury bills and \$30 billion of Certificates of Indebtedness.

In this district alone, the Federal Reserve Bank handled more than 60,000 individual securities or pieces aggregating more than \$4 billion of marketable issues in connection with the Treasury's issue and redemption of securities. More than 11,000,000 sales of "E" bonds totaling \$700 million and 18,000,000 redemptions amounting to \$600 million were handled by the Federal Reserve Bank either directly or through nearly 2,000 agencies—chiefly financial institutions.

The Federal Reserve Bank of Cleveland, acting as the paying agent of the Bureau of Supplies and Accounts of the United States Navy with personnel all over the world and for other Government agencies has handled nearly 23,000,000 checks for a total of more than \$2 billion. Govern-

ment checks of all kinds handled by the Federal Reserve Bank numbered 40,000,000 for payments exceeding \$6 billion. While these amounts are smaller than during the peak of the war activity when Treasury payments to the industrial heart of the nation were of record-breaking proportions, they are nonetheless larger than in any other peacetime year of our history.

Other operations of the Federal Reserve Bank have reflected the high levels of activity of business and finance in this district. Checks cleared through the Federal Reserve Bank numbered about 200 million and involved the transfer of about \$60 billion. The demand for currency in this district and in the United States as a whole was of record-breaking proportions and the year 1946 closed with the volume of currency in circulation the highest ever recorded (\$29.1 billion for the nation on December 24.)

The banks of the Fourth Federal Reserve District have handled skillfully a record-breaking volume of financial transactions, and have served effectively the credit needs of industry, commerce, agriculture, consumers, and Government. While the year 1947 will impose even greater problems and responsibilities, I am confident that the financial community can, through the exercise of imagination and forethought, continue to serve all constructive financial needs of our economy and contribute to the maintenance of high levels of production and consumption and to the preservation of our economic health. The task confronting us will call for wisdom and courage. While I am a relative newcomer to the Fourth District, I have had an opportunity to meet virtually all of the bankers of this region and believe that these qualities will not be found lacking.

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