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BUSINESS REVIEW

What's Behind the Discount Rumpus in Retailing?

Capital Spending—When Will it Turn the Corner?

BUSINESS REVIEW

is produced in the Department of Research. Lawrence C. Murdoch was primarily responsible for the article "What's Behind the Discount Rumpus in Retailing?" and Bertram W. Zumeta for "Capital Spending—When Will it Turn the Corner?" The authors will be glad to receive comments on their articles.

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WHAT'S BEHIND THE DISCOUNT RUMPUS IN RETAILING?

Val-U-Town could be any one of hundreds of huge, hangar-like buildings set in seas of suburban asphalt. Inside, goods to satisfy most of mankind's material wants are displayed over acres of floor space—an area big enough to play and watch several football games simultaneously. Overhead, fluorescent tubes run like staffs of music, shedding a cold impersonal light on the carnival and confusion below.

This cornucopia with a corrugated roof contains a fully stocked supermarket, a furniture department, color TV and appliances, and men's suits for $29. In the large record department there is Welk for grandma, Sinatra for mother, and Darin for daughter. Writers from Shakespeare to Spillane are available in paperbacks. You can find aluminum rowboats, garden supplies, snow tires, and paint-by-number sets for little Leonardos. There is pizza for snacks, a barbershop, a jewelry department, rare coins for collectors, and a case of surplus army rifles from wars long past at $14.95 each.

Many of the shoppers are family groups—mother, dad, and the kids. Small children ride in the shopping cart and the larger ones whoop up and down the aisles. Everybody is informally dressed—jeans, jackets, and sneakers mostly—for they have come right from their living rooms. But if their clothing is casual, there is nothing casual about their shopping. They seem determined and a little keyed up as they jockey their carts for position.

You can paw and maul the merchandise to your heart's content. You pick out what you want, put it in your shopping cart and push it to the check-out counter where you settle for all your "bargains" with one payment.

It is often said that the discount store, such as the one we have described, is revolutionary—a whole new concept. In fact, it is hard to pick up a retail trade publication or to talk with marketing men without reading or hearing the words "the revolution in retailing."

The discount craze is growing fast; it's frantic and it's a bit fantastic but it is not really a revolution. Revolution means a sudden, radical change, and discounting with its corollaries of one-stop shopping and self-service is the acceleration of a long-run trend. Retailing has been building up to the modern discount store for many years. Let's look at some selected branches on the discounting family tree.

VISIGOTHS AT THE GATES

Ever since some caveman made the first retail sale, buyers have wanted the most for the least. Discounting, *per se*, is relatively new, however. During much of recorded history, retail prices were open to bargaining. Without firm prices there was nothing to discount from—no yardstick to measure savings. Then, about a hundred years ago, merchants began posting fixed, take-it-or-leave-it prices on their merchandise. This gave the discounter his first chance.

In 1859, two New York merchants got an idea. By importing tea directly from the Orient and thus eliminating the wholesaler, they were able to sell to the public at substantial discounts from prevailing prices. The name of their store became the Great Atlantic and Pacific Tea Company, subsequently shortened to A. & P.

John Wanamaker, already a successful merchant, bought a railroad freight depot at 13th and Market Streets, Philadelphia, in 1875. His intention was to set up a vast shopping center under one roof. He hoped to lease selling space to cooperating merchants who would run their own departments—a procedure used in modern discount stores and in the present Wanamaker stores. The plan didn't work out in 1875, however, and Wanamaker operated the entire building himself. His ability to buy in huge quantities enabled him to sell below other prices in the area.

A number of other department stores and the major mail order firms were established in the years following the Civil War. Most of these concerns broke into the market by underselling the competition.

In 1912, the A. & P. chain, which by then had grown to 500 units, began featuring an "economy store." It was a low-cost, little-service operation which did not extend credit or make deliveries. As a result, it could sell at discount prices. Did the customers like the idea? Ten years later, A. & P. had almost 10,000 stores.

Some 50 years ago, Filene's, a Boston department store, set up a discount department in its basement. Prices on all merchandise were low to start with and if an item did not sell within 12 days its price was automatically cut 25 per cent. Further reductions were made periodically, and all merchandise unsold at the end of a month was given to charity. The operation is still going strong today.

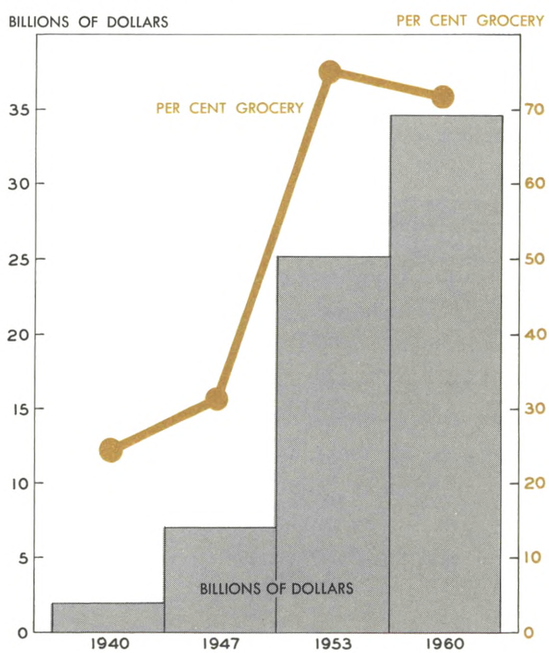
Self-service was pioneered by Clarence Saunders in 1916. He installed check-out counters in a Memphis grocery store that bore the improbable name of Piggly Wiggly. Saunders made the name and the idea available to others on a franchise basis and found thousands of takers.

King Kullen, one of the first food supermarkets, was established on Long Island in 1930. The Big Bear and others followed quickly. When customer acceptance was well-proved in the latter 1930's, the large grocery chains started converting their own stores. Supermarkets have grown rapidly ever since, on the principles of low mark-up, high-volume turnover, and self-service—the very same principles that the discount stores use today for general merchandise.

For decades, farmers' markets were, as the name implies, places where neighboring farmers could rent stalls and sell their produce. In the 1940's, the farmers went back to their plows and, for the most part, the selling was taken over by professional merchants who added general

SUPERMARKETS REACH MATURITY

Estimated supermarket sales in dollars and as a percentage of all grocery store sales.



merchandise lines—often seconds sold at rock-bottom prices.

In New England, shortly after World War II, a number of abandoned factories were converted into low-overhead stores. Merchandise, mostly soft goods, was strewn around on bare-board tables and plain-pipe racks. Customers served themselves and paid "low, low" prices at the check-out counter.

At about the same time, stores called discount houses began to appear in the big cities. They were generally small and were located just the other side of downtown. They featured radios, major appliances and, later, TV sets. Discount houses gave the customer no delivery, no credit—not even a smile. But their low overhead enabled them to sell below the prices demanded in conventional stores.

The modern, one-stop discount store descended directly from the frowzy factory store and the city-slicker discount house in the early 1950's.

There is a definite pattern in this century of historical development. Aggressive new merchants seem to force their entry into the market with discount prices. That's the way department stores, chain stores, and supermarkets worked their way in and that's the way discount stores are getting in now. Once a new type of retailing gets well-established, however, it costs and its prices usually begin to creep upward. Soon the newcomer, in his turn, becomes vulnerable to the next group of lean and hungry Visigoths waiting to sweep down under the banner of discount prices.

CARROTS AND ONIONS

Discounting may be the most publicized thing in retailing today, but it is far from the only important development. If discounting and one-stop shopping are the meat and potatoes in the stew of retailing, the following are the carrots and onions.

Stores of all types are staying open longer hours.

Evening openings have increased sharply as have Sabbath sales except where the law says "never on Sunday."

Trading stamps are growing more popular all the time. It is estimated that stamps are now given with 15 to 20 per cent of all retail sales.

Vending machines are doing an increasing share of the nation's retail business. About $3 billion worth of coins are dropped into slots each year. The perfection of machines that accept and change paper money should open a vast new horizon for mechanical vending.

Merchandise lines are blurring between different types of stores. Food stores are going deeper into non-food lines, and other stores are adding food. Variety stores are moving up to fur coats and major appliances. Mail order firms are filling prescriptions, and selling world tours. Drug stores have gone into produce and all sorts of general merchandise. Discount stores are selling original oil paintings and automobiles.

Point-of-purchase displays are being used more and more. It is estimated that almost $400 million a year is spent in the highly competitive wooing of the impulse buyer.

Closed-door retailing is booming. These merchants sell, at discount prices, only to card-carrying members. You have to belong to some broad group such as Government workers or teachers to get a card.

Telephone and door-to-door selling are on the upswing. Many stores are leasing departments to independent operators who take over most merchandising functions.

Promotions, sales, and contests are more prevalent than ever. "Just clip the coupon or tear off the box top and state in 25 words or less . . ."

PRESSURES FOR DISCOUNTING

We have tried to show that the present excitement over discounting is the acceleration of a long-run trend. But why did the acceleration happen now? Why not ten years ago or ten years hence? And why are there so many carrot-and-onion developments?

The answers to these questions lie with both seller and buyer. The retail industry itself must initiate any changes, and the consumer must demand or at least accept these changes. So we shall examine both the retail industry and the retail consumer with some thoroughness.

In retailing, competition is the keynote

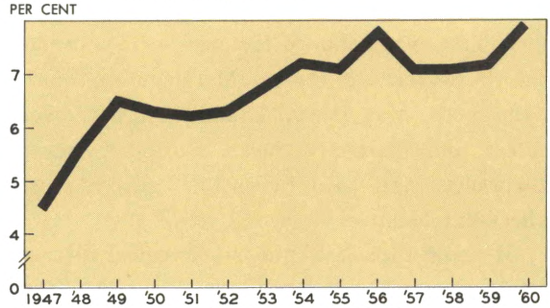
Our collection of clippings from the trade press makes discounting look like a stampede. In the past half-year many new units have started and many established stores have entered the field—Montgomery Ward, Woolworth, Kresge, Penn Fruit, and dozens of others. One might be tempted to say that discounting is something of a fad, a retailer's hula hoop.

Undoubtedly there is a bandwagon effect in operation, but it can't be the main cause. For the most part, experienced levelheaded merchants are embracing discounting. There is a much more basic reason for the recent acceleration of discounting and for the over-all activity in retailing.

We think the basic cause is competition—competition which puts pressure on merchants to become more efficient and to innovate. There is reason to believe that competition among sellers, which has been on the upswing during the past decade, has increased sharply in the past year or two.

SILENT REGISTERS

The number of discontinued retail stores as a percentage of all retail stores in operation.



Evidence of extra competition is the jump in retail failures and the drop in retail profits. From 1959 to 1960, discontinued stores as a percentage of all stores in operation rose almost a point to about 8 per cent. The profits of food and variety chains, department stores, and mail order houses all dipped in 1960.

Several things explain this increase in competition. There was a rapid expansion in retailing floor space during the 1950's. As a result, some experts say that there is now considerable excess capacity in retailing. This is particularly true in the downtown areas which have been sapped by the suburban movement. Excess capacity has much the same effect in retailing that it does in manufacturing. It means increased competition with a downward pressure on prices and profits, and a striving for greater efficiency.

Many retailers now find themselves in a cost squeeze. Wages, a major cost item, have doubled in the postwar period. The new minimum wage law effective last September will increase wage costs even further for many retailers. While manufacturing has attempted to absorb rising wage costs through mechanization, retailing is much harder to automate and has not been able to increase the productivity of its labor nearly so much.

The present lid on over-all sales also makes retailing more competitive. Sales hit a peak in April 1960, and have been in a slump ever since. Some economists say that consumers are sated with goods. Be that as it may, the lid on retail sales has forced merchants to fight harder for business. With no over-all rise to sweeten the pot, one merchant who shows a sales gain does so at the expense of another.

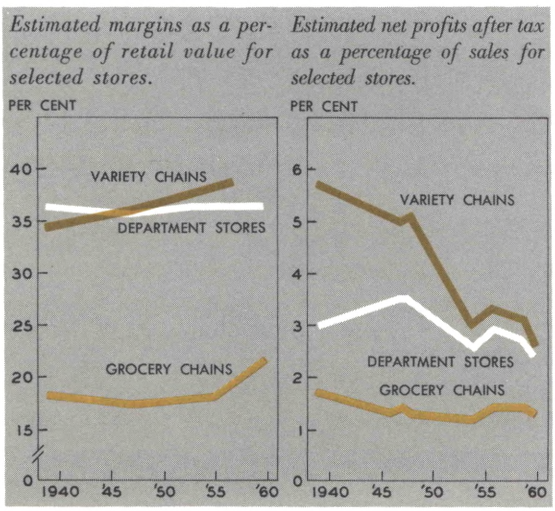
In this environment discounting and most of the developments we mentioned on page 5 are attempts to increase the efficiency of retailing. They are designed to trim costs, increase the productivity of retail labor, sweeten profits, and to jog the consumer into action.

Who buys, and why?

The special interest that consumers are showing in discounting surprised us at first. Today's consumers have more income than ever before. Almost 60 per cent of all American families received an annual income of $5,000 or more in 1960. Consumers are better-educated and are said to be more sophisticated, have better taste, to be fonder of luxuries.

PRESSURES FOR EFFICIENCY

Conventional store markups are on the rise . . . and their profits are falling.



It seemed to us that modern consumers would be more interested in the frills and extras of personalized selling rather than in self-service and stark efficiency. In this age of popular credit, we thought that consumers would favor charging their purchases over paying cash on the barrel head. We would have guessed that consumers would covet fashion, design, and selection rather than the standardization that high-volume selling requires.

Then we ran across a slew of surveys that show who goes to discount stores and why. They made the current craze much less of a paradox to us.

Meet the O'Briens

It is said that you can see chauffeur-driven Cadillacs in discount store parking lots. We have no doubt that many rich people do patronize discount stores; in fact, it was the upper-income groups who first discovered the appliance discount house after World War II. But the mainstays of the modern discount store drive old Chevies, not Cadillacs. They are families like the O'Briens. We first met the O'Briens in the surveys showing typical discount shoppers, and we should like to introduce them to you.

Ed O'Brien is a machinist, about forty years old. He and his wife Cora have three boys aged four, nine, and eleven. Ed makes $5,500 a year and owns his own home and car. His income is higher than it has ever been; in fact, it has doubled in the past 13 years.

The lorelei song of discounting

In spite of his record income, Ed O'Brien is under more economic pressure than ever before.

His aspirations have risen faster than his income. There is the mortgage to pay, the doctor, vacation trips, and installment payments. In addition, Ed is beginning to feel guilty because he has been able to save so little towards sending the kids to college. Ed needs to stretch his income as much as possible, and discount stores are right down his alley. Every dollar saved today is a dollar spent on something extra tomorrow.

Ask Ed and Cora O'Brien what they like about discount stores and they will say, low prices. But they will also mention other things. One is self-service—they actually prefer it. Self-service facilitates browsing and it speeds shopping when you are in a hurry. Do they miss the personal attention they are supposed to receive at the conventional store? They would say, no. Like many householders, they are thoroughly indoctrinated with the do-it-yourself way of saving money. Furthermore, the O'Briens might scoff at the quality of the selling services that some conventional stores offer. "Clerks are often surly and act like they are doing you a favor by waiting on you. Why should you pay extra for that kind of service?"

Discounting implies a lack of service but actually discount stores do offer many services—a different package of services than the conventional store. Discount stores offer the important service of convenience—an accessible location, parking, long hours, and speedy shopping. Credit, delivery, and installation services are also available on the popular, user-pays principle. Factory guarantees are offered on many appliances and other major items.

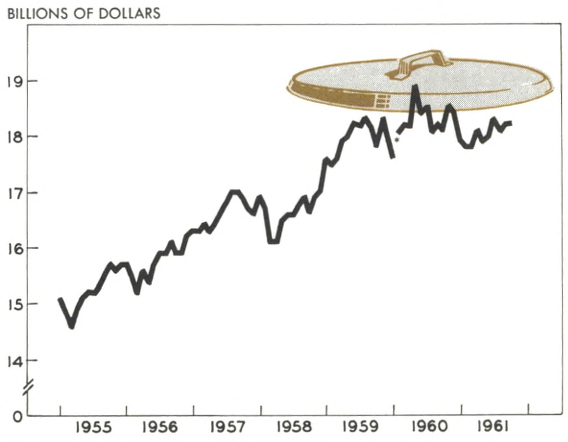
Pierre Martineau, writing in the *Harvard Business Review*, sheds an interesting sidelight on the popularity of discount stores. He indicates that the highly mobile woman who considers her present neighborhood only a stepping stone wants to be very efficient about her shopping. She prefers impersonal stores and wants a minimum of contact with sales personnel. On the other hand, the woman who feels she has settled down to stay prefers the warm personal relationships found in the smaller independent store.

We believe that there might be a high percentage of the first type of woman in the sprawling middle-class suburbs where the discount stores are now proliferating.

Ask the O'Briens whether they feel discount stores offer real bargains or just low prices. They probably would mention the many national brands available at shaved prices—"real savings there." But how about all the other stuff, soft goods mostly, with name tags nobody ever heard of? On this score the O'Briens and shoppers like them have some nagging doubts. Surveys show that discount stores have not convinced the general public that they offer quality right down the line. But obvious savings on nationally branded goods, the over-all convenience, and confidence in their ability to judge

THE LID ON SALES

Total retail sales, seasonally adjusted, monthly rate.



* 1960–1961 include Hawaii and Alaska.

merchandise are enough to bring people back again and again.

Down the aisles together

Discount stores are part cause, part effect of a new sociological development—the family shopping trip. It used to be that the woman of the house did most of the family shopping during the day. Now dad and the kids often come along, and shopping takes place evenings and week ends.

Perhaps it's because mother works more often these days or because dad has to use the car to get to his job. Maybe dad is trying to be more helpful at home or maybe he just wants to get in on the spending of large sums of his own money. Whatever the cause, family shopping is having important effects on the retailing industry.

Family shopping means increased peaking of traffic in the evenings and on Saturdays. For the store, this adds up to longer hours and increases the need for the part-time help.

Family shopping means growing pressure for Sunday openings where they are not now legal. Sunday selling is a controversial topic in Pennsylvania and in spite of recent court decisions against it the issue is far from dead.

Advertisers who have long slanted their appeals to women may have to change now that dad is getting in on the selection of merchandise. Men won't buy a soap because it gives them "the hands you love to touch."

There could be more on-the-spot buying of big-ticket items because the whole family is right there to make the decision. And the amount of returned merchandise could decline for the same reasons.

With dad behind the shopping cart, there could be an upsurge in impulse buying. Surveys have shown that it is men, not women, who are most prone to pick up "goodies" that catch their eye.

The sale of meals in retail stores will probably become less important, for the family is likely to eat at home before or after their shopping trip. With dad and the kids along, however, the sale of snacks should be up.

IT'S TIME TO MAN THE RAMPARTS

Whenever a new type of retailer tries to break into the market the established merchants seem to go through three stages of reaction. First, they ignore the invader in the hope that he will go away. This often gives the newcomer the foothold he needs. Second, the established merchants start worrying and complaining and shouting "unfair competition." Finally, they begin fighting back. By then it may be too late, for the invader often is across the moat and into the castle.

Many established merchants have now begun fighting the discount store. As far as we can see, there are two general tactics: the if-you-can't beat-'em-join-'em type, and the emphasize-your-own-strong-points type.

Many established stores are converting themselves to discount methods or acquiring their own discount branches. Some stores, however, are attempting to match the discounters' prices while retaining their existing selling procedures. This seems to us to be fighting where the opposing line is strongest—as Pickett did at Gettysburg. Rigid cost structures may prevent conventional stores from matching the discounters' prices for an extended period. The discounter can offer low prices because he is specifically organized to do so, and many other stores are not so organized.

A large number of established stores are striking at the enemy's weak spots—as Jackson did at Chancellorsville. The discounter does not give personal selling service, so they do; and they make sure the service is all that it's supposed to be. They hire better clerks—friendly courteous clerks who can sell. Some stores are even sending their clerks to school.

The discount store is a Coney Island type of place. Its vast, elbowing crowds can be irritating and a bit nerve wracking. As an offset, many conventional merchants are emphasizing an inviting, relaxing appearance.

The discounter does not sell much style and fashion merchandise, and some competing merchants are emphasizing that type of goods in their own lines.

Although the discounter can usually arrange credit for major items through a bank or finance company, he often does not offer charge accounts. Some conventional merchants are therefore liberalizing their own credit plans.

Most long-established stores have built up a public image—usually a favorable one. The discounter does not have this advantage. The general public may like discount prices but as yet is not quite sure what to think about the discount stores themselves. Thus, a well-known store name with a reputation for quality and integrity behind it is a great competitive asset. For one thing, it helps to put across private brands. Low-cost private brands are one way to compete effectively with the discounter.

A number of conventional stores are carrying the fight to the discounter's own home ground—the suburbs. Suburban branches are nothing new—one local department store had two of them by 1931—but the branch movement seems to have accelerated recently. While this article was being written, two department stores opened new branches outside of Philadelphia. Specialty stores, variety stores, and many others are expanding to the suburbs with increasing frequency.

The twig store, too small to be a branch, is another effective way to follow the suburban consumer. Twigs can be set up on a self-service, discount basis while the parent store retains its regular procedures.

There are many other ways to fight the discounter. An all-weather shopping center—a cluster of stores around an enclosed mall—has been opened recently in our area. Downtown shopping malls are also being created by blocking off city streets. Some stores are becoming discounters for a day by holding warehouse sales.

The battle has been joined and the strategy is well-conceived on both sides. The conclusive engagements, however, are yet to be fought.

WILL SUCCESS SPOIL THE DISCOUNTER?

Discounting is still in the experimental stage. It is still feeling its way toward the best merchandise mix. There is, as yet, no indication whether leasing departments is the best method, or whether sales should be restricted to card holders. There are few accounting ratios to serve as guides and few profit norms to shoot for.

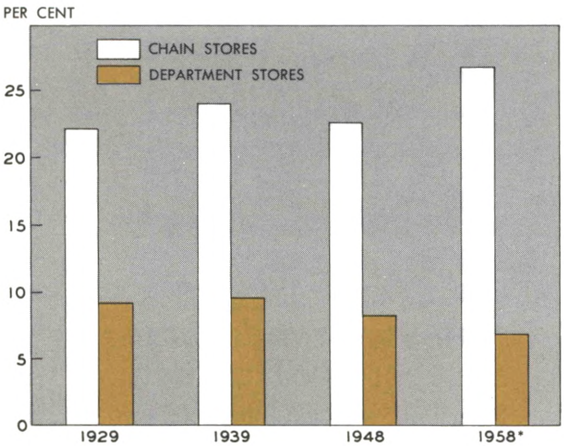
Nevertheless, discounting is definitely here to stay, say the great majority of experts, and it will continue to grow for quite some time. An evolution is often harder to stop than a revolution.

This leaves important questions unanswered, however. How far will discounting ultimately go? Will it take over all of retailing? What will the store of the future be like?

Retailing has a way of civilizing its invaders. After cracking in on the power of low prices, newcomers' costs tend to increase and so do their

SLICES OF THE MARKET

Chain store (4 or more units) and department store sales as a percentage of total retail sales.



markups. Perhaps success makes them a little sluggish. Their market penetration, which was rapid at first, slows significantly and sometimes declines. In 1929, chain stores (four or more units) accounted for about 22 per cent of all retail sales. Since then they have gained only a few points. The department stores' share of total retail sales has actually declined since 1929.* Even the supermarkets, which have had things pretty much their own way since the late thirties, have not been growing so fast lately. Their estimated percentage of all grocery sales dropped three points to 72 per cent from 1953 to 1960.

Over the years, the small independent merchants have taken a lot of hard knocks and many of them have failed; but as a group they are surprisingly tenacious. Chances are they will survive discounting, too.

It may happen that the discounter will carve his niche, probably a large one, and then settle down with a relatively constant share of the market.

Some experts, however, seem to think that retailing will absorb the discounter completely—as China has absorbed her invaders over the centuries. They hold that retailing is evolving toward a huge all-purpose type of store. Already the lines between stores are blurring, these students point out. Their prediction is that the discounter will have to give more and more service and thus raise his prices, while conventional stores will give less and less service and lower their prices. All stores will continue to broaden their merchandise lines and will meet on some common ground to blend into an amorphous, everything-for-everybody store.

We won't buy the idea. It assumes that consumers are all the same, or at least similar enough so that their needs can be satisfied by the same store. This is not true. Actually, the consumer market has been splitting up into many diverse parts. We dealt with this phenomenon in some detail in the article "The Royal Family Grows Restless," in the February, 1961, *Business Review*.

The everything-for-everybody store may be suited to serve a sizable segment of lower- and middle-income consumers. But many others are going to want prestige, service, personal contacts, selection, style, credit, deliveries, and ever so much more. And they will be willing to pay for it. We feel that there will be room for many different kinds of stores in retailing, especially since more and more consumers are moving into the really high-income brackets.

No, the discount store or what it ultimately evolves into is not the only store of the future. As a matter of fact, we look for new types of retailing to appear with increasing frequency. The fully automated store, now in the prototype stage, may make the next big noise in retailing. It might work something like this: You go into a showroom with one of each item on display.

* The latest figures may not be strictly comparable with earlier data due to changes in statistical methods.

You push buttons under whatever you want and when you leave, your order has been automatically assembled and is waiting for you in your car. Perhaps the bill could be sent to your bank where it would be paid automatically.

Or telephone buying may be the wave of the future. You could select from samples shown on closed circuit TV and have the merchandise delivered within the hour by jet copter from automated warehouses.

CAPITAL SPENDING - WHEN WILL IT TURN THE CORNER?

Manufacturers in the Philadelphia Metropolitan Area plan to spend $289 million on plant and equipment in 1962—10 per cent less than in 1961. In the combined Lehigh Valley, Trenton, and Wilmington areas, manufacturers anticipate 14 per cent less capital spending in 1962 than in 1961. The projected declines extend to every region included in our capital spending surveys, and to all but a few industries.

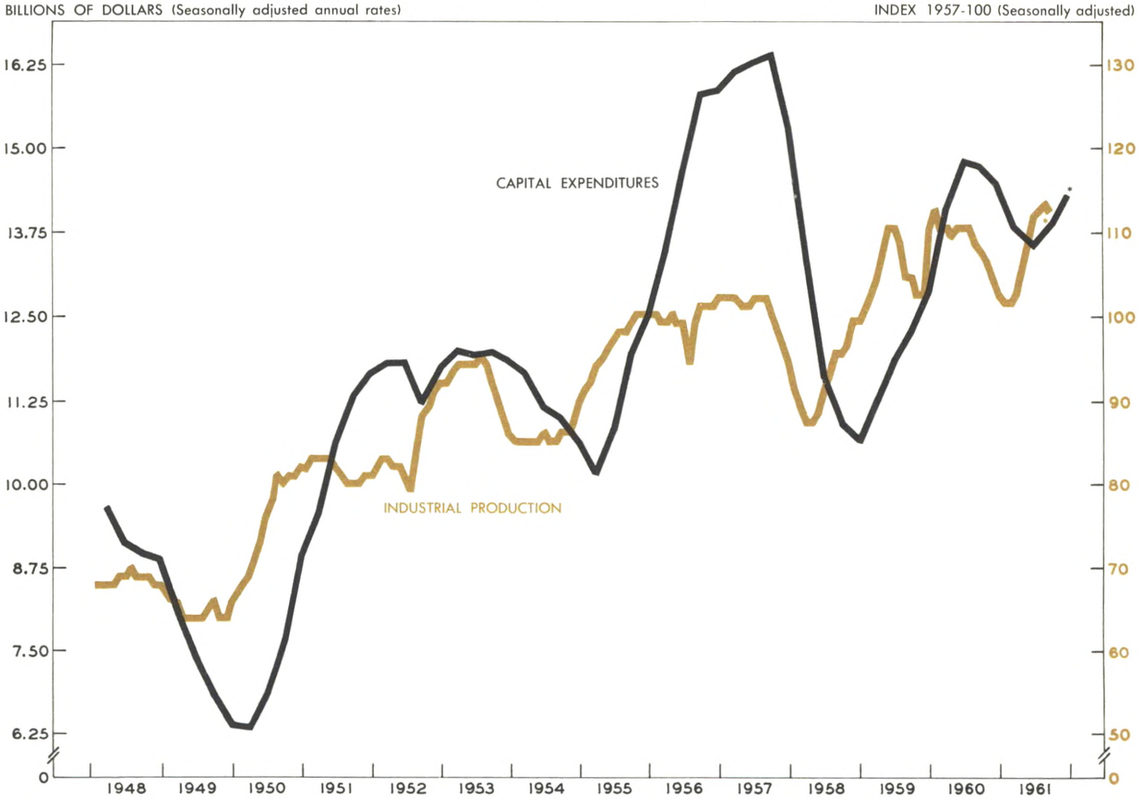
These findings are, to put it mildly, a disappointment. Capital spending should be stimulated by and in turn should support and extend the business recovery which got under way early this year. Augmented capital spending would create new orders for industries which make capital goods—the machines and equipment required for modernization and expansion. New business for these capital goods industries is particularly stimulating to the economy generally, because their sales are volatile, swinging higher than most in good times and lower in bad. The swing back when orders flow in generates widespread recalls to work, overtime pay, buying of materials. A modest increase in total capital spending may double the order backlogs of firms which supply producers with equipment. Thus, increased spending on plant and equipment exerts a powerful leverage which is

ESTIMATED CAPITAL EXPENDITURES OF MANUFACTURERS

Delaware and Lehigh Valleys

	Expenditures (Millions $)		Percent Change
	1961	1962	1961–1962
Philadelphia Metropolitan Area			
All manufacturing	320.7	289.4	— 9.8
Durables	135.6	112.9	—16.7
Lumber & furniture	2.6	1.0	—61.5
Stone, clay & glass	6.6	8.6	+30.3
Primary metals	44.7	37.7	—15.7
Fabricated metals	18.6	10.9	—41.4
Machinery (excl. elec.)	16.9	16.4	— 3.0
Electrical machinery	31.8	26.2	—17.6
Transportation equipment	6.2	3.5	—43.5
Instruments & misc.	8.2	8.6	+ 4.9
Nondurables	185.1	176.5	— 4.6
Food & tobacco	33.6	26.2	—22.0
Textiles	7.4	4.0	—45.9
Apparel	2.9	2.3	—20.7
Paper	22.8	15.8	—30.7
Printing & publishing	17.6	22.6	+28.4
Chemicals	46.3	51.4	+11.0
Petroleum & coal	42.1	46.2	+ 9.7
Rubber & leather	12.4	8.0	—35.5
Lehigh Valley			
All manufacturing	52.4	44.1	—15.8
Durables	39.9	33.5	—16.0
Nondurables	12.5	10.6	—15.2
Trenton			
All manufacturing	22.6	13.9	—38.5
Durables	11.7	9.9	—15.4
Nondurables	10.9	4.0	—63.3
Wilmington			
All manufacturing	68.1	65.4	— 4.0

CAPITAL EXPENDITURES AND INDEX OF INDUSTRIAL PRODUCTION ALL MANUFACTURING INDUSTRIES, UNITED STATES



* Estimated

Sources: Securities and Exchange Commission—Department of Commerce; Federal Reserve Board.

felt in precisely the sector of the economy that most requires stimulus, having been most affected by recession.

Should not this stimulus accompany the present business recovery?

A look at the record

The fact is that capital spending is a "lagging indicator." It takes resurgent business activity to bring into use the less modern equipment of a firm, to generate confidence along with the realization that better machines and the better methods they often make possible could help reduce costs, make the company more competitive. Therefore, rebounds in capital spending follow upturns of production. It happened so in the United States in 1950, 1952, 1955, 1958, and appears to be happening again in 1961, judging by estimates recently published.

Local surveys conducted by this Bank reveal patterns similar to the national experience. The

DELAYED ACTION

(The Lag in Capital Expenditures)

Date of Production Upturn	Date of Survey Revealing Upward Revision of Plans for Capital Spending	Date of Survey Indicating Capital Expenditures in Excess of Recession-Year Totals
May, 1954	September, 1955	September, 1956
April, 1958	March, 1959	March, 1959
January, 1961		

PHILADELPHIA MANUFACTURERS' EXPECTATIONS CONCERNING EMPLOYMENT, PRODUCTION, AND INVENTORIES

	Employment Projections by Quarters (Index: Third Quarter=100)				Production as Per Cent of Capacity by Quarters				Inventory Expectations, 1962 Per Cent of Total Firms Expecting:		
	1961 Third	1961 Fourth	1962 First	1962 Second	1961 Third	1961 Fourth	1962 First	1962 Second	Increase	No Change	Decrease
All manufacturing	100.0	100.6	99.8	99.8	76.2	78.7	79.1	79.4	15.2	72.0	12.8
Durables	100.0	101.4	100.4	100.2	71.0	75.1	75.0	75.2	16.5	67.6	16.0
Lumber & furniture	100.0	95.2	94.2	99.3	86.5	78.7	78.3	90.8	6.7	86.7	6.7
Stone, clay & glass	100.0	102.5	103.9	105.7	66.8	75.5	77.7	78.3	22.2	72.2	5.6
Primary metals	100.0	101.5	102.1	102.1	70.3	78.0	80.6	81.7	11.1	61.1	27.8
Fabricated metals	100.0	98.3	95.6	95.8	70.3	71.0	69.0	71.6	17.9	71.8	10.3
Machinery (excl. elec.)	100.0	100.0	99.4	99.1	74.8	76.6	77.1	77.1	18.2	70.5	11.4
Electrical machinery	100.0	100.3	100.9	100.9	83.1	84.8	83.4	83.7	17.4	56.5	26.1
Transportation equipment	100.0	109.0	103.0	100.7	41.3	54.4	51.7	48.7	10.0	50.0	40.0
Instruments & misc.	100.0	101.1	102.5	102.9	76.3	81.4	85.9	82.4	19.0	61.9	19.0
Nondurables	100.0	99.8	99.0	99.4	81.9	82.7	83.7	84.1	14.2	75.5	10.3
Food & tobacco	100.0	100.3	98.9	98.8	85.4	83.8	82.7	85.3	5.9	85.3	8.8
Textiles	100.0	97.0	97.3	103.3	77.9	76.4	76.5	79.8	8.9	73.2	17.9
Apparel	100.0	102.9	103.0	99.7	85.7	90.5	91.8	88.3	10.8	81.1	8.1
Paper	100.0	99.9	98.7	99.5	88.5	89.6	88.5	89.6	15.4	80.8	3.8
Printing & publishing	100.0	99.7	96.7	94.7	89.1	87.4	87.2	88.5	26.1	65.2	8.7
Chemicals	100.0	99.2	99.4	100.2	72.9	76.0	78.6	83.1	33.3	58.3	8.3
Petroleum & coal	100.0	99.9	99.7	101.4	79.3	80.5	85.4	77.0	12.5	75.0	12.5
Rubber & leather	100.0	100.1	100.3	100.6	80.8	82.9	83.7	82.7	12.0	80.0	8.0

first year of business upturn included in our surveys of the capital spending plans of manufacturers in the Philadelphia area was 1954. It was not until 1956 that plant and equipment expenditures increased, reflecting the production gains which began in 1954. In 1958 production turned up in the beginning of the year, but capital spending plans were not revised upward until the spring of 1959. The accompanying table shows what happened. Dates of production turns were determined from the electric power consumption of manufacturing firms in the Philadelphia area, and the capital expenditures dates refer to our surveys of manufacturers' plant and equipment expenditures in the Philadelphia area.

"Hope springs eternal . . . ."

What are we to conclude from the record? It is tempting to say that history will repeat itself, that plant and equipment spending will recover in the spring, following a dip similar in length and strength to the one-year lag that occurred in 1958–1959. Such a conclusion finds support in the national capital spending estimates shown in the chart on page 13. They indicate, tentatively, a capital spending revival only four months after production recovered, compared with an eight-month lag in 1958.

On the other hand, despite the persuasively optimistic indications we can deduce from past patterns, the simple truth is that future events never are fixed until they become past events. It is quite possible that continued softness in retail sales, coupled with uncertainty concerning the international situation, could cause manufacturers to hold back new spending on

ANTICIPATED CHANGE IN CAPITAL EXPENDITURES, 1962–1963

Philadelphia Area

	Per Cent of Firms Expecting:		
	Increase	No Change	Decrease
All manufacturing	20.4	62.9	16.7
Durables	21.6	62.1	16.3
Lumber & furniture	20.0	73.3	6.7
Stone, clay & glass	16.7	72.2	11.1
Primary metals	15.8	68.4	15.8
Fabricated metals	32.5	55.0	12.5
Machinery (excl. elec.)	26.1	52.2	21.7
Electrical machinery	30.4	47.8	21.7
Transportation equipment	0	77.8	22.2
Instruments & misc.	0	85.0	15.0
Nondurables	19.5	63.5	17.0
Food & tobacco	21.6	59.5	18.9
Textiles	18.6	72.9	8.5
Apparel	15.8	71.1	13.2
Paper	23.1	53.8	23.1
Printing & publishing	20.0	52.0	28.0
Chemicals	16.7	66.7	16.7
Petroleum & coal	12.5	62.5	25.0
Rubber & leather	25.0	54.2	20.8

equipment for a while longer. Productive capacity is now more adequate than at any time since World War II, and this fact undoubtedly makes for lower levels of capital spending. But the pressures for cost-cutting modernization of productive equipment are great. Total corporate cash flow is adequate to support considerable capital expenditures. What is needed is confidence, and at this stage of a business recovery the confidence required for firms to approve large capital improvement programs waits upon firmer indications of business strength than have yet appeared. Paradoxically, one indicator of strength that is closely watched is capital spending.

Uncertainty

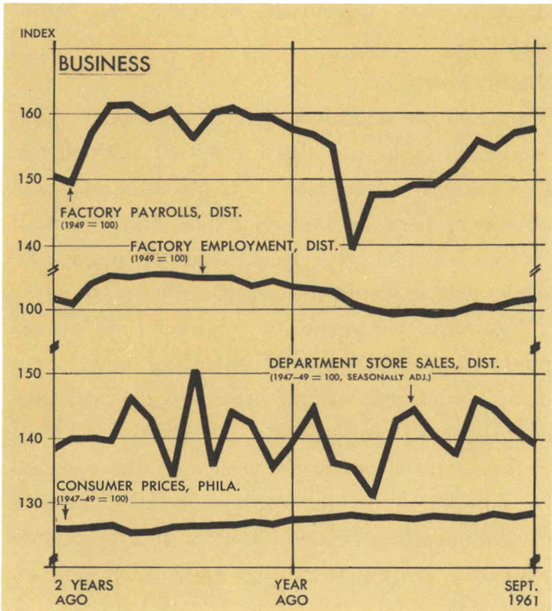
We asked the manufacturers in the Philadelphia region to look into the futures of their firms. How would employment and production probably vary between now and next June? Would inventories change? And what of plant and equipment expenditures in 1963?

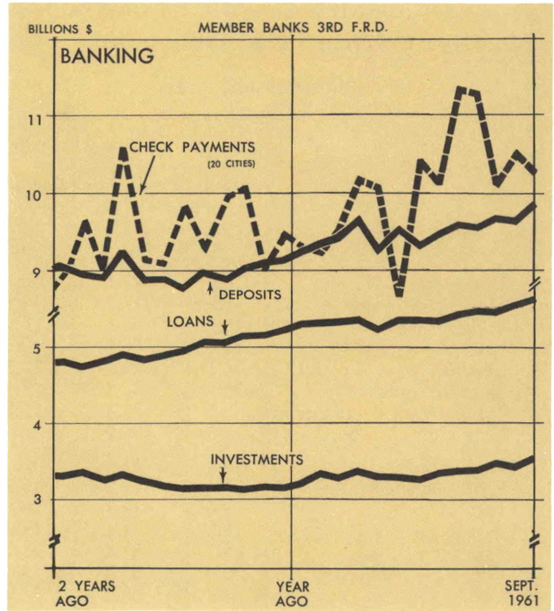
One word—uncertainty—characterizes the replies. Concerning capital spending and inventories, two-thirds of the firms did not feel they could hazard an estimate of the direction of change, and they simply indicated there would be no change in inventories in 1962 and in capital spending between 1962 and 1963. Those who were willing to hazard an opinion split almost evenly into "up" and "down" groups.

Production gains are anticipated, but the gains are expected to be small, and not to improve employment significantly.

The findings of our surveys of manufacturers' capital spending prospects reveal a prevalent caution, extending to all regions and to the great majority of industries. If business activity does not dip, if reasonably satisfactory profit margins are maintained, the history of the surveys suggests that a turn to augmented plant and equipment spending is not far off. But for the upturn to occur will require a higher degree of confidence concerning the business outlook than existed in September, the survey month.

FOR THE RECORD...





SUMMARY

	Third Federal Reserve District: Per cent change, Sept. 1961 from mo. ago	Sept. 1961 from year ago	9 mos. 1961 from year ago	United States: Per cent change, Sept. 1961 from mo. ago	Sept. 1961 from year ago	9 mos. 1961 from year ago
MANUFACTURING						
Production	....	....	....	+ 2	+ 5	− 2
Electric power consumed	+ 1	+11	0	....	....	....
Man-hours, total*	0	− 3	− 7	....	....	....
Employment, total	0	− 2	− 4	+ 1	− 1	− 4
Wage income*	0	0	− 4	....	....	....
CONSTRUCTION**	−17	+13	+11	−15	− 4	+ 3
COAL PRODUCTION	+ 8	+15	− 9	+ 2	+ 6	− 7
TRADE***						
Department store sales	− 1	0	0	0	+ 3	+ 1
Department store stocks	+ 3	+ 3	....	+ 1	+ 1	....
BANKING (All member banks)						
Deposits	+ 2	+ 7	+ 6	+ 3	+ 7	+ 6
Loans	+ 1	+ 6	+ 7	+ 2	+ 4	+ 4
Investments	+ 3	+11	+ 6	+ 3	+17	+13
U.S. Govt. securities	+ 4	+14	+ 8	+ 3	+17	+14
Other	+ 1	+ 4	+ 3	+ 3	+17	+11
Check payments	− 2†	+11†	+ 9†	− 3	+ 2	+ 8
PRICES						
Wholesale	....	....	....	0	0	0
Consumer	0‡	+ 1‡	+ 1‡	0	+ 1	+ 1

*Production workers only.
**Value of contracts.
***Adjusted for seasonal variation.

†20 Cities
‡Philadelphia

LOCAL CHANGES

	Factory*: Employment, Per cent change Sept. 1961 from mo. ago	year ago	Factory*: Payrolls, Per cent change Sept. 1961 from mo. ago	year ago	Department Store†: Sales, Per cent change Sept. 1961 from mo. ago	year ago	Department Store†: Stocks, Per cent change Sept. 1961 from mo. ago	year ago	Check Payments, Per cent change Sept. 1961 from mo. ago	year ago
Lehigh Valley	0	− 2	+ 3	+ 2	....	....	....	....	− 1	+ 9
Harrisburg	+ 1	− 2	+ 1	+ 2	....	....	....	....	− 8	+ 3
Lancaster	− 1	− 2	+ 3	+ 5	+11	+ 2	+ 1	+ 2	− 2	+ 4
Philadelphia	0	− 2	+ 1	+ 2	− 6	− 1	+ 4	+ 5	− 3	+10
Reading	+ 1	− 2	+ 2	+ 5	+ 1	+ 3	0	− 6	− 6	+19
Scranton	0	− 1	− 4	− 3	− 7	− 2	− 2	− 4	− 6	−11
Trenton	0	− 6	−12	−13	+ 5	+ 4	+ 6	+14	−20	+ 9
Wilkes-Barre	− 3	− 7	− 7	−12	− 3	− 5	+ 1	+ 1	− 3	+ 2
Wilmington	+ 4	− 5	+ 5	+ 2	+ 2	+ 4	+ 4	+ 7	+15	+42
York	− 2	− 3	− 3	+ 5	+13	− 1	+ 5	− 1	−10	+ 4

*Not restricted to corporate limits of cities but covers areas of one or more counties.
†Adjusted for seasonal variation.