BUSINESS REVIEW

1914

1964

FEDERAL RESERVE BANK OF PHILADELPHIA

Consumer Spending and the Inverted Wedding Cake Theory

Home, Suite Home

The Market for Office Space in Philadelphia

MARCH

BUSINESS REVIEW is produced in the Department of Research. Evan B. Alderfer was primarily responsible for the article, "Home, Suite Home," J. Allan Irvine and Evan B. Alderfer for "The Market for Office Space in Philadelphia," and Lawrence C. Murdoch, Jr. for "Consumer Spending and the Inverted Wedding Cake Theory." The authors will be glad to receive comments on their articles.

Requests for additional copies should be addressed to Bank and Public Relations, Federal Reserve Bank of Philadelphia, Philadelphia, Pennsylvania 19101.

With all the new high-rise apartment buildings in downtown Philadelphia and the profusion of garden apartments in the periphery, the theme of an old song may have to be changed to:

HOME, SUITE HOME

Philadelphians who read their Sunday papers "in depth" sooner or later come upon the section telling about the glorious opportunities for luxurious living in downtown apartments. Open for inspection are plush, midtown, high-rise apartments where you can live with "verve" on "Philadelphia's cultural crossroads," with "urban sophistication," at "the finest addresses," or "around the corner from everything."

Along with the news tuned in over their breakfast coffee cups, Philadelphians often hear sweetly spoken words about the grandeur of garden apartments in the suburbs. Ready for immediate occupancy are apartments "meticulously planned with utmost intelligence," offering "the European concept of elegance," and "exciting interior arrangements," with "individual climate control in each room," along with "free bus service to trains," and "owner-management assurance of complete attention to all requests."

An apartment is a many-splendored mass of masonry, plain or fancy. To the builder, an apartment is the hope of a profit; to the owner it is the promise of a continuing source of income; to the tax authority it is a flow of revenue; to the manager it is full or over-full employment; to the occupant it is elegance in capsule captivity—a carefree, mechanized, automated, slot-machine way of life. And to the amazing and amorphous residential construction industry the construction of apartments has been the major source of growth during the past several years.

Apartments in the sky

Former residents of the Philadelphia area returning for a visit after a long absence are amazed at the transformation of the city's skyline. Gone are lamented or unlamented structures like Broad Street Station and the "Chinese Wall." These and other period pieces have been replaced by tall, modern office buildings, like the Penn Center family of skyscrapers. Competing with the high-rise office buildings in the heart of the downtown area is an efflorescence of high-rise rental apartment buildings.

A central-city apartment building, like a central-city office building, sits on high-priced ground; so it must go sky-high to provide enough revenue-yielding apartment units to compensate for the high-priced standing room it occupies. Like the tall office buildings with which some of the apartment structures compete for standing room, they are many-storied structures whose uppermost floors may disappear in early morning mists.

Standing on top of City Hall and facing Pennsbury Manor to the northeast, William Penn is looking in the wrong direction to see the central city apartment buildings. Rittenhouse Square is a particularly attractive location, but the Square isn't large enough to accommodate all the big apartment buildings that have gone up in recent years. Some have been built just off the Square or nearby. Still others have been erected on the John F. Kennedy Boulevard, on the Parkway, and in the redevelopment area of Society Hill.

Philadelphia's outstanding downtown apartment buildings are located between the Delaware and Schuylkill rivers on the east-west axis, and between Spring Garden Street on the north and Pine Street on the south. Within this area are 29 distinguished rental apartment buildings, recently surveyed by the University of Pennsylvania's Institute of Urban Studies. Most of the apartments included in the survey are within easy walking distance of City Hall. All of them are of the luxury type, have distinguished names, and command substantial rentals.

The appearance of swank midtown, multistory apartments is not a new phenomenon. The first of these residential queens is of 1918 vintage. It was built on Rittenhouse Square, its portal is graced with ornamental wrought iron, and it has 44 apartment units. In those days, a 12- or 15-story structure was considered—though not yet so called—high-rise.

During the 1920's a dozen more smart apartments appeared. They were constructed either on Rittenhouse Square or as near to the Square as they could get. During the period there was a tendency toward larger and taller structures, some of which went up to 18 and 20 floors.

Only two apartment buildings were erected during the troubled 30's, and apartment construction came to a complete standstill during the 40's because of World War II with its attendant shortages of materials and labor. Construction was resumed during the decade of the 50's when six new apartments were completed. Most of these were larger and higher and, of course, more modern than their predecessors.

Thus far in the 60's, high-rise construction in the downtown area has accelerated so vigorously as to take on the semblance of a boom. Six new apartments have been completed or are sufficiently completed to begin accommodating tenants; and two additional structures, still under way, are scheduled for completion early next year or sooner.

The boomy aspect of midtown apartment construction is even more apparent when viewed in terms of newly created apartment units, rather than in the number of structures, because the newer buildings are significantly larger than those built earlier. The eight buildings completed, or to be completed, in the period beginning with 1960, contain almost as many apartment units (3,614) as the 3,886 units in the 21 complexes completed during the earlier period of more than four decades.

The newest of these apartments have the

latest in decor and urban niceties. Seeing is believing—parquetry wood flooring, carpeted halls, sound-conditioned walls, individually controlled heat and air conditioning, dishwashers, washer-dryers, garbage disposal units, push-button fume exhausters, FM radio and TV channels providing reception of New York telecasts, penthouse swimming pool, underground garage, balcony, maid service, and uniformed doormen.

Midtown apartmental luxury has its price. Rentals asked range from slightly under $100 a month for the efficiency units to $400 and over depending upon the number of bedrooms, the de luxe accommodations, and number of floors above street level desired by the tenant. The higher you dwell the more you pay. Garage rent ranging from $23 to $37 a month is extra.

Although high-rise apartments in the commonly accepted sense of the term are confined to the newer skyscrapers that push up 30 stories, numerous elevator apartments of substantial loft have been built in other parts of Philadelphia and its surrounding metropolitan area. Multi-story apartment accommodation is available in steadily growing volume just a few minutes from downtown Philadelphia. Most of these are on or near main traveled routes in areas such as Germantown, Mt. Airy, along the Wissahickon, City Line, and in suburban communities along the Main Line, as well as across the Delaware River in New Jersey. The newer apartments in many of these communities offer many of the attractions of the downtown apartments at somewhat lower cost. Special attractions offered by some of these peripheral apartments are such things as greater amplitude of space, swimming pool, cabana club, shopping colonnade, club facilities, panoramic views, and free bus service to town.

Suburban garden apartments

It has been said that a boy can be removed from the farm but the farm cannot be removed from the boy. For people who want the convenience of city living in a rural setting, the garden apartment is just the thing. And there are many people like that—witness the growing popularity of garden apartments.

A garden apartment complex is usually a family of similar but not identical two- or three-story, walk-up buildings thoughtfully distributed with a studied carelessness over a regular or irregular plot of ground of considerable acreage of rolling contour, on which as many as possible of the mature trees have been preserved in the course of constructing the apartment buildings. If the acreage includes a shallow lake or has a winding stream coursing through it, all the better. A former golf course, for example, makes an ideal site on which to build garden apartments. The irregular dimensions of the plot are no drawback; neither is an irregular topography. Both are assets for landscaping after the buildings are erected. Such a setting is perfect for split-level construction, with flower gardens, shrubbery, trees, outdoor fireplaces, and vistas of green grass manicured by the management. Some of the garden apartments have country club facilities, including golf, tennis, swimming, ice skating, and other forms of diversion.

The interiors of these apartments contain most of the appointments and domestic appliances designed to keep the occupants cool in summer, warm in winter, and happy at all times as far as possible.

Brand-new garden apartments have been appearing in great numbers during the past few years. A large number of these have been built

(Continued on Page 7)

THE PREVAILING METROPOLITAN TREND

The Philadelphia region is by no means unique in the recent upsurge in the construction of apartments. It is a development of nationwide proportions; a phenomenon especially characteristic of the 60's. This is readily apparent in the accompanying chart of Private, Nonfarm Housing Units authorized by building permits.

For the past three years, permits for the construction of one-family housing units have been practically stationary, showing no growth whatsoever. That is in sharp contrast with the issuance of permits for housing units of five or more families, which have grown from a monthly level of less than 200,000 in 1960 to well over 400,000 in 1963. In other words, virtually all of the recent expansion in residential construction has been coming from the multi-family type of dwelling.

BUILDING PERMITS FOR APARTMENT UNITS (PER CENT OF TOTAL)

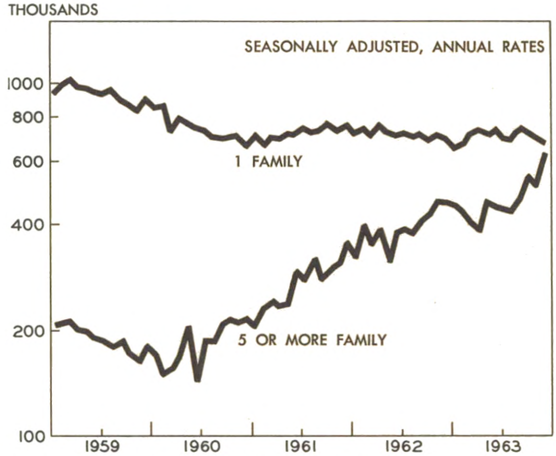
	1960	1961	1962	1963 (8 mos.)
United States, total	19.9	27.2	33.8	35.5
Large metropolitan areas				
New York City	54.7	64.2	64.2	52.4
Los Angeles-Long Beach	41.7	46.1	50.0	52.5
Chicago	27.1	36.6	42.4	37.9
Philadelphia	23.6	32.5	46.9	36.6
Detroit	6.4	8.6	23.2	24.1
San Francisco-Oakland	37.0	47.0	50.2	47.3
Boston	18.2	38.0	47.7	48.4
Pittsburgh	3.8	7.7	15.9	23.4
St. Louis	12.2	19.5	21.9	26.0
Washington	45.2	51.0	65.0	62.9
Cleveland	24.7	40.0	54.1	71.0
Baltimore	13.8	36.7	39.6	56.2
Minneapolis-St. Paul	26.8	40.5	49.2	51.6
Buffalo	2.8	4.3	11.3	6.0
Houston	21.0	38.0	65.0	63.5
Milwaukee	35.2	37.7	39.0	40.5
Dallas	22.9	28.1	46.2	52.2
Cincinnati	23.2	21.2	38.8	37.4
Kansas City, Mo.-Kans.	8.3	18.0	15.6	20.4
Atlanta	32.3	28.7	40.7	54.5
Seattle	12.4	15.5	26.1	31.6
San Diego	13.3	24.3	31.6	23.1
Denver	31.7	40.0	22.6	26.4
Miami	23.5	32.6	48.3	46.6
New Orleans	9.3	19.6	25.9	26.5

Source: U.S. Department of Commerce, Office of Business Economics, based on Census data, as reproduced in the December, 1963, *Survey of Current Business.*

Despite all the construction of apartments in the Philadelphia metropolitan area this region is not in the lead. Compared with other major metropolitan areas of the country, Philadelphia was a bit slow in starting and has been handsomely overtaken by others. This is shown in the table entitled Building Permits for Apartment Units, in which units of five or more family structures are expressed as a percentage of total permits by major metropolitan areas.

Since 1960, as the table shows, the proportion of permits for construction of apartment units expressed as a percentage of total permits issued has increased in 23 of the country's 25 leading metropolitan areas. It should also be noted that Philadelphia was not among the nine metropolitan areas in which permits for multi-family construction in 1963 (eight months) represented over half of the total of permits issued. Nevertheless, Philadelphia did right well.

PRIVATE NONFARM HOUSING UNITS AUTHORIZED BY BUILDING PERMITS (In 10,000 permit issuing places)



Source: United States Department of Commerce.

(*Continued from Page 5*)

in the northeast section of Philadelphia County and also in the Germantown area. In the counties surrounding Philadelphia on both sides of the river, new garden apartments are flourishing outside the city limits, where available land for development is more plentiful and less costly. This is reflected in the more modest rentals, which account in part for the popularity of suburban garden apartments. Odd-shaped plots have been available at prices which have enabled builders to erect apartments for published rental rates as low as $86.50 for a one-bedroom apartment, $110 for a two-bedroom apartment, and $125 to $150 for a three-bedroom apartment.

The lure of apartment living

The resurgence in popularity of apartments is associated with a number of closely interrelated economic and social changes; indeed, it is often difficult to tell which are economic and which are social. For example, the increasing participation of women in the labor force is motivated largely by the need or desire for augmenting the family income. When husband and wife are both gainfully employed, the wife finds it easier to participate in social activities if she is relieved of the onerous work and care of "running a house."

One of the economic factors related to the apartment-building boom is the rising cost of land. With population on the increase and land area practically fixed, the cost of the land required to build a home has a long-run tendency to rise. In the construction of an apartment building the land required is utilized more economically.

Apartment construction has been favored by the availability of funds. Not so long ago an insurance company executive made the remark that he wakes up every morning with the horrible thought that another million dollars has accumulated for which he must find a safe and profitable investment haven. The apartment-building boom has helped to relieve some of those burdens of insurance companies. Smaller lenders, such as savings banks, savings and loan associations, and pension funds have also participated in supplying capital. Moreover, the construction of apartments has also been facilitated to some degree by FHA financing; that is, FHA insurance of funds used in financing of apartment construction.

Apartment construction is a relatively easy field to get into and it has attracted numerous builders with limited experience and little equity, desirous of creating an income-producing property. During the early postwar years when the housing shortage was acute, speculative building entailed comparatively small risks. Now, however, new ventures are attended with greater risk; lenders are becoming more chary as the supply of apartments grows.

The ever-changing age composition of the population will soon sprout a host of potential apartment dwellers. What was a postwar tidal wave of infants will be a grown-up generation of young people in the 20- to 25-year age bracket by 1965 and in the market for housing. Among these, especially the young married couples with limited funds will find modest-priced apartments a desirable way of setting up housekeeping before the arrival of children.

Apartments also have an appeal for older couples whose children have grown up, married, and left home. After all the children have flown the coop, the aging parents, finding themselves over-housed and over-burdened with the cares of maintaining an over-sized homestead, begin to dream of the comforts and convenience of an apartment—of a luxury apartment, which many of these people can afford, particularly after they dispose of the homestead. Apartments likewise have an appeal for the unmarried, the surviving widow or widower, or for individuals going their separate ways after a divorce. For retired people living on fixed incomes of moderate proportions, an apartment is attractive because it offers known and fixed housing costs, in contrast with the vagaries of maintaining a homestead with all the unpredictable costs of its maintenance.

Another source of demand for apartments is young men working for large corporations that frequently transfer their able young executives from one branch plant to another in various parts of the country, in the course of going up the executive ladder. Rather than incurring the financial risks and inconvenience of periodic buying and selling of a home, many of these roaming businessmen choose an apartment.

In addition to these economic inducements favoring apartment dwelling there are also numerous social reasons. One of these is the growing disenchantment of suburban home ownership. There was a time when home ownership was a status symbol, and probably still is—especially to the brand-new owner of a mortgaged home. But as the equity-building, interest-paying years roll on and on the initial pride and glamor of home ownership may pall. Every credit has it debit, as Emerson pointed out in his essay on Compensation. By and by the joys of home ownership may be counterbalanced by such annoyances as ever-rising taxes, mowing grass, raking leaves, shoveling snow, fighting crabgrass and possibly termites, screening, weatherproofing, re-roofing, painting and pointing, shoring up sagging gutters, refinishing floors, fortifying electric wiring, repairing the plumbing, and battling daily bottlenecks incident to commuting to and from work. Oh, for the life in a downtown apartment where you buy off these vexations with a monthly check!

Of course, apartment life isn't all "apples of gold in pictures of silver." To begin with, not everyone can live in a downtown apartment even if he has the means—there simply isn't enough room. In an apartment, you have neighbors to the left and neighbors to the right; neighbors above and neighbors below, and it is unlikely that they all subscribe to the same values of life you hold dear. With so many neighbors so close, you may get awfully lonely; or, if you are fortunate enough to have congenial neighbors there is always the hazard that some may be too congenial.

Economy of space is, of course, the basic virtue of an apartment; but a virtue carried too far ceases to be a virtue. In an apartment, you do not have your own cellar; and you have no attic to store empty jars, quilts, Christmas tree ornaments, fishing tackle, spare mattresses, old furniture, out-of-season apparel, extra floor lamps, old books and magazines, picture frames, wedding presents, family heirlooms, loving cups, and miscellaneous memorabilia. Attics are doomed to go the way of grandmother's spinning wheel, if the present trend toward apartment living continues, because there is no room for spinning wheels in an apartment where storage space is measured in square feet instead of square yards.

Is the boom weakening?

It is both alleged and denied that apartments are appearing faster than the market can absorb them. Whether the builders have been over-optimistic depends largely on the particular market in question. A good measure of the relation between the apartment demand and supply ought to be the vacancy rates. Vacancy rates, however, have a tendency toward a downward bias. If the occupant of an apartment is signed up to move from one apartment to another at the time of an occupancy survey, he may be recorded as occupying two apartments simultaneously, thus giving rise to double accounting.

The July 1963 vacancy rate in Philadelphia's midtown high-rise apartments was reported at 3.3 per cent in the survey of the Institute of Urban Studies. That looks very good indeed, but it was above the 1.2 per cent rate prevailing in the Institute's January 1958, survey.

In contrast with the over-all rate of 3.3 per cent last year, vacancies in efficiency apartments were only 0.4 per cent. In the 2-, 3-, and 4-bedroom apartments, however, vacancy rates ranged from 4 to slightly over 5 per cent. That is rather typical because the small efficiency apartments always rent faster than the larger, more spacious, and more expensive units.

With over a thousand additional apartment units coming on the market in downtown Philadelphia this year and next, the question is: will they find occupants or will they push up the vacancy rate? There is some evidence that the former out-of-town movement into the suburbs has been reversed, that people in the suburbs are moving back into the city; however, the downtown apartments, it will be recalled, are in the high-priced brackets and there is some skepticism about the ability to find enough tenants for the additional luxury apartments now in process of completion. In time, of course, they will no doubt be occupied. But a finished apartment building is a big fixed investment which has its own break-even point, and not until that point is passed does the investment begin to sweeten.

The garden apartment boom in the outlying sections of Philadelphia and in Delaware and Montgomery counties appears to have outrun its market even more than in center city, according to a study of vacancies made by Jim T. Davis of the Graduate Division of the Wharton School. His study, not yet published, shows a vacancy rate averaging 14 per cent in garden apartments. The higher vacancy rates in garden apartments reflects the participation of numerous smaller builders, the availability of cheaper land, and the ease of getting financing from smaller lenders.

The increased popularity of apartments is nationwide and the construction industry has eagerly accommodated the demand. Although construction in the Philadelphia region has not been so great as in some other metropolitan areas, there has been enough local apartment construction to afford prospective tenants considerable choice. Philadelphia is among the 10 leading metropolitan areas of the country that show some tapering off. Rising vacancy rates, the profusion of advertisements, and the offering of special inducements and concessions to get tenants are also indications that the region is adequately if not over-adequately supplied for the present.

THE MARKET FOR OFFICE SPACE IN PHILADELPHIA

What makes Philadelphia so Philadelphian is illustrated in many ways—even in its office architecture and its office-building economy.

A city is never finished. It is in endless transformation, forever tearing down and building up. There is a ceaseless tug of war between decay and renewal; between obsolescence and recrudescence; between degeneration and regeneration.

In times of war, business depression, or just plain neglect, the ravages of age leave their marks. Caulking crumbles, paint peels, wood warps, plaster cracks, steel rusts, and stone corrodes. Roofs spring leaks, facades get dirty-faced, stairways sag, water mains break, flagstones part company, streets cave in, and the city takes on a forlorn and woebegone appearance.

Sooner or later such a period of stagnation is followed by an era of active renewal, repair, renovation, and rebuilding. Philadelphia, like many other cities, is now and has been for some time in a period of face-lifting, modernization, and redevelopment.

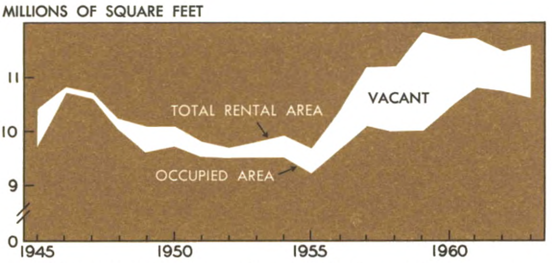
Office buildings play an important role in Philadelphia's downtown program of urban redevelopment. In the construction of office buildings, however, Philadelphia follows no leader but goes about the task in its own individual way, which is perhaps best characterized by the term *moderation.*

Philadelphia has no Pentagon, no Empire State Building. The biggest office building is the Philadelphia Savings Fund Society's 36-story structure which stands 491 feet high. Only three other office buildings rise above 30 stories.

Nor does Philadelphia go in for wedding-cake construction. The growing family of new office buildings in Penn Center may strike Nathaniel Burt as "miserable packing boxes" but they were built to serve as efficient, modern offices—not as conversation pieces. When Philadelphia puts up a new office building the functional takes precedence over the fanciful.

Moderation also characterizes Philadelphia's activity in office-building construction. The city may be several steps ahead of the demand for office space but overbuilding here has not been so great as in some other cities. The present and past relationship between supply and demand is shown in the accompanying chart.

COMMERCIAL SPACE IN PHILADELPHIA OFFICE BUILDINGS



Philadelphia has about 11.5 million square feet of office space. That is the equivalent of 1¾ Pentagons—to give you a colossal point of reference. The 11.5 million square feet refers to office space either rented or for rent. We are not concerned here with the approximately 5.5 million square feet in the city's 35 single-purpose office buildings occupied by their owners, such as the Philadelphia Electric Company, Bell Telephone Company, and the Federal Reserve Bank. Excluded also are the buildings on the sunset side of City Line, just beyond the reach of the City Fathers' mercantile tax and wage tax.

All of the 11.5 million square feet of commercial office space is downtown, defined as the area between the Delaware and Schuylkill rivers, and between Spruce and Spring Garden streets.

Of the 11.5 million square feet available, 10.3 million are occupied; so the vacancy rate is 10 per cent. The chart shows the postwar history of the city's commercial office vacancy. The top line is the total rental area, the supply; the bottom line is the occupied area, the demand. Trapped between the two lines is the vacant office space—roughly equivalent to what is termed "excess capacity" in manufacturing industries.

The big bulge in postwar construction, you will note, occurred between 1955 and 1960, and it was accompanied by an increase in the vacancy rate. The narrow band of vacancy in the years prior to 1955 portrays an exceedingly tight situation, and the subsequent widening of the band reflects the subsequent easing. Thus far in the 1960's not much change has taken place; that is, the over-all relationship between supply and demand has neither improved nor degenerated, materially.

For an individual building, a 10 per cent vacancy rate is just about normal, with the going and coming of tenants. For the total market, a 10 per cent vacancy rate is not too bad, either; but the vacancies fall with unequal impact on various classes of buildings. Overall quantitative measures sometimes conceal as much or more than they reveal.

The best office buildings have a vacancy rate of only 4 per cent. These are known as Class "A" buildings. They include the new structures like those now gracing Penn Center and others that have been modernized with air conditioning, up-to-date lighting and plumbing, automatic elevators, and related improvements. Some meticulous husbands permit their secretarial spouses to accept employment only with firms occupying Class "A" structures.

Class "B" office buildings are the older ones which have been well maintained but lack the very latest in modernization, though some are air conditioned. Buildings in this group have a vacancy rate of 15 per cent.

All others are Class "C" which are the more aged and obsolescent structures that have just failed to make the "B" classification, as well as the shopworn, weatherbeaten, forlorn-looking veterans of bygone glory. Class "C" vacancies are 19 per cent.

Fortunately, the city's Class "C" square footage is only 11 per cent of the total. Class "B" space accounts for 39 per cent of the total office space; and Class "A," 50 per cent. Quality varies inversely with quantity.

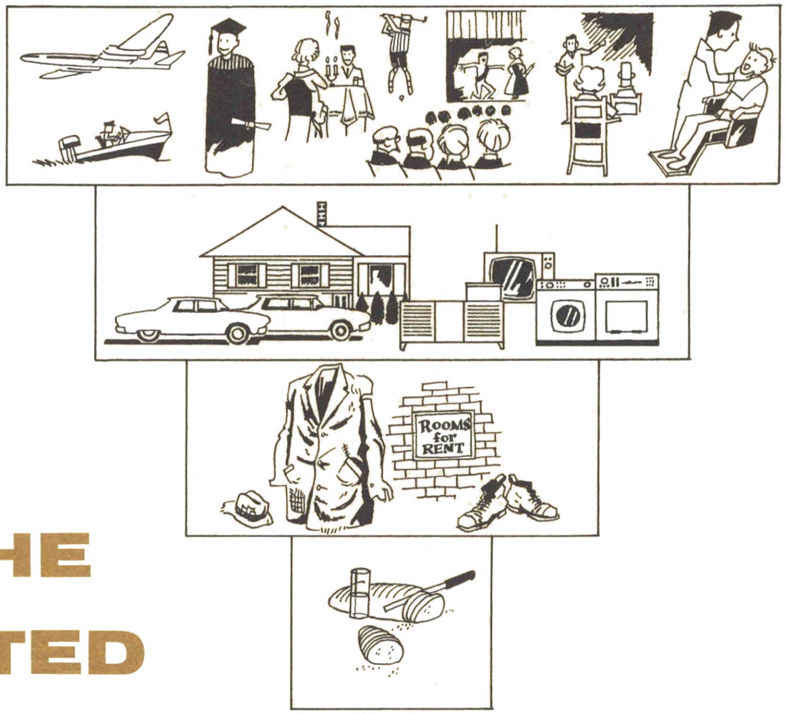
The current rental situation, as reported to us by the trade, is only moderately active. A substantial part of the demand is from present tenants in need of more space. Large companies often underestimate their office space requirements, and as they grow they do a lot of re-partitioning and huddling people into closer quarters. By and by the congestion becomes intolerably inefficient and then the firm is forced to seek more space. Some of the demand also arises from smaller tenants looking for small blocks of space. Practically none of the demand, it is reported, is from outside concerns moving into the area.

The over-all supply of office space is more than adequate, but the supply of Class "A" space is definitely too limited. Most of the shifting is "trading up"—moving into the modern office buildings, which increases the pressure where vacancies are already small and leaves larger vacancy rates in the other classes.

About 700,000 square feet of new office space is scheduled for completion this year. A large part of the new square footage will be contributed by Four Penn Center, the new I.B.M. Building, and the new Rohm and Haas office building which, in the course of construction, offers large picture windows to the "sidewalk superintendents." The new, company buildings will offer some commercial office space. The newly modernized Widener Building is also nearing completion.

Looking beyond 1964, the trade anticipates continuation of new construction, tenants shifting into the preferential structures, and intensified selling and greater modernization of older office buildings.

CONSUMER SPENDING AND THE INVERTED WEDDING CAKE THEORY



A well-known explanation of our recent below-potential rate of output is that the American consumer is sated with goods. Total demand is said to be lethargic because so many families have all the houses, cars and washing machines they need. If true, this could influence the way people spend their tax savings and, in turn, the over-all effectiveness of the cut.

At first thought, this argument seems in conflict with common sense. We know human wants are capable of almost infinite expansion. Once the income to satisfy a certain want becomes available, another appears quickly. When a starving man gets a meal, he begins to think about an overcoat; when an executive gets a new sports car, visions of country clubs and pleasure boats dance into view.

So how can consumers be sated? Yet the argument persists—and our production rate *is* below potential.

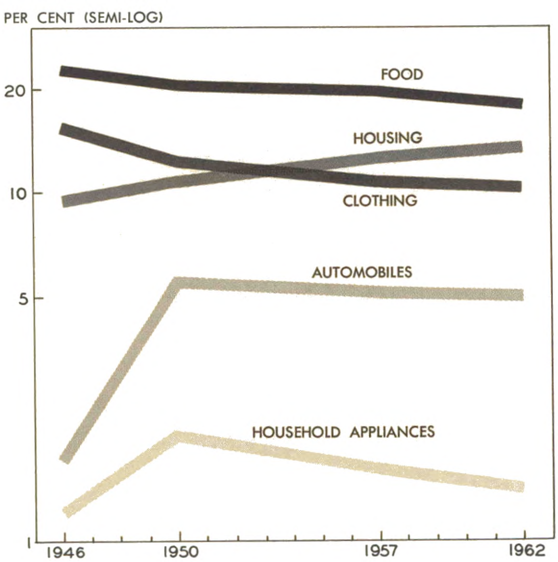
Old-time economists observed that patterns of consumer spending changed as income increased over the long sweep of history. Perhaps this also is true in short periods of time. The myriad wants of individuals can be grouped loosely into several basic levels. Recent experience seems to indicate that when income is available to satisfy one level another level appears very quickly. The levels build up like the layers of a cake. Since each new level involves a greater number of increasingly complex wants, the layers might resemble an inverted wedding cake.

Thus consumers can be sated at one level of wants but not in the over-all sense. Even this may have an important effect on growth, however.

The first and most fundamental level of wants involves food. Once this want is satisfied, a second level appears—clothing and some sort of shelter. Since these physical wants are essential to survival, they often are called "necessities." By the end of World War II, necessity wants were satisfied and on a replacement basis for a great majority of our population. In 1946 consumers spent about 23 per cent of their budget on food and 15 per cent for clothing. The most recent figures are 18 per cent and 10 per cent, respectively. People are devoting a larger share of income to housing today than they did in 1946 but this reflects the great increase in suburban home ownership, a relative luxury compared to basic shelter.

THE CHANGING BUDGET

Spending for various items as a percentage of total consumer outlays.



Then in the early postwar period a third level appeared. In it were such things as automobiles, appliances and new houses. People were unable to satisfy such wants during the depression for lack of income, and during the War for lack of production. In the latter 1940's, production met pent-up demand and easy credit in the market place. A decade-long buying spree resulted and the economy enjoyed substantial prosperity.

By 1957 or 1958 this third tier of wants was fairly well satisfied. There was one car on the road for every two people over 18; more than 90 per cent of all homes had major appliances, almost two-thirds of all families owned their homes. Most durable goods and houses purchased since the 1950's have been to take the place of an older item already in use. In spite of the recent glowing reports from Detroit, consumers are using less than 5 per cent of their budget to purchase automobiles, compared with 6.1 per cent in 1955 and 5.5 per cent in 1950.

Then, in the late 1950's, a fourth level of wants received increasing emphasis. It could be called the "life-enriching" strata. If the other levels might be said to feature physical satisfactions—the nourishment, comfort, safety and transportation of the human body—this one emphasizes psychological needs such as recognition, achievement, and self-realization. This fourth level includes a tremendous variety of goods and services, many with a strong element of "luxury." Among them are vacation trips, hunting and fishing paraphernalia, the best medical and dental care, hi-fi, "Ivy League" college education, entertainment, domestic help, hobbies and all manner of things cultural.

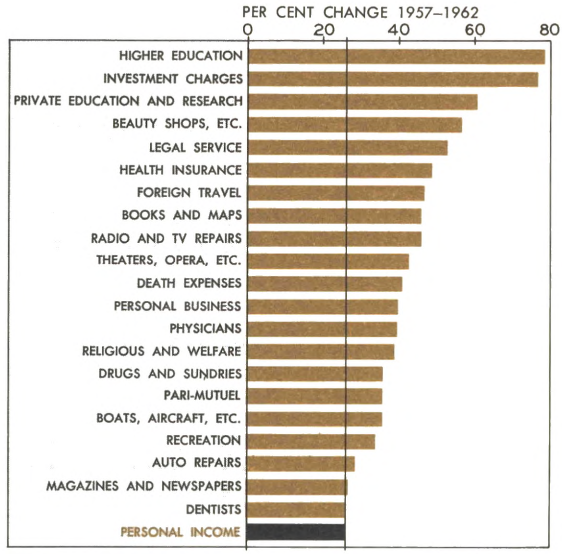
Luxury versions of basic necessities also are covered here: gourmet foods, professionally decorated homes by Sears, Roebuck or Dorothy Draper, and the latest styles in clothing.

We don't mean to imply that the consumer never before bought such items or that he is no longer interested in things on the first three levels. The point is that the average family is devoting a significantly larger percentage of its income to satisfying these fourth-level wants. From 1957 to 1962 personal income increased 26 per cent. In comparison, expenditures for medical expenses increased 40 per cent; foreign travel, 47 per cent; higher education, 80 per cent.

Because there is a great variety of almost-interchangeable goods and services on the fourth level, demand does not seem to have the single-minded focus that it does on the lower levels. There is no substitute for food, clothing and shelter if you haven't any; neither is there an effective substitute for an automobile or television set if you have your heart set on one. On the other hand, many fourth-level luxuries are substitutable, one for another. A vacation trip to Atlantic City could well be a last minute replacement for an outboard motor boat. Or you could easily change your mind and grill a steak in the backyard instead of taking the family out to a restaurant.

With consumers devoting a greater portion of their budget to such mercurial wants, marketing has become more difficult. The consumer of today is harder to figure out, more difficult to anticipate, harder to sell. Possibly our economy would grow faster if more marketing and advertising efforts were raised from a type of "hammering" appropriate for the third level to relatively sophisticated and subtle fourth-level appeals.

THE FAST-GROWING FOURTH LEVEL



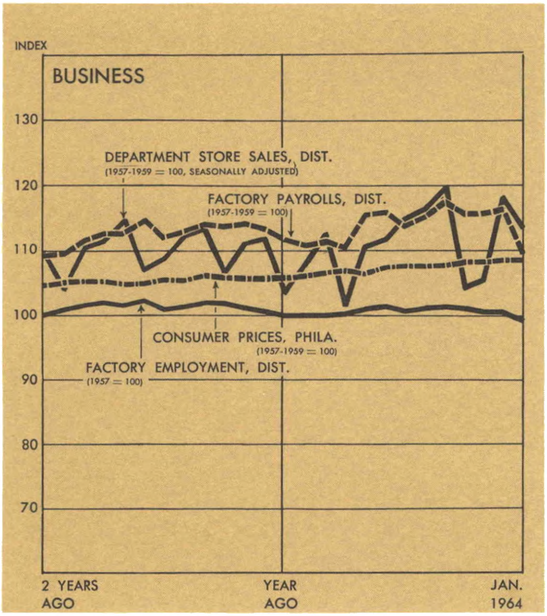
The step up to the fourth level means that a greater percentage of total consumer spending is devoted to services which bulk large there, while goods dominate the first three levels. As a result 41 per cent of the consumer budget now goes for services compared to 32 per cent in 1946.

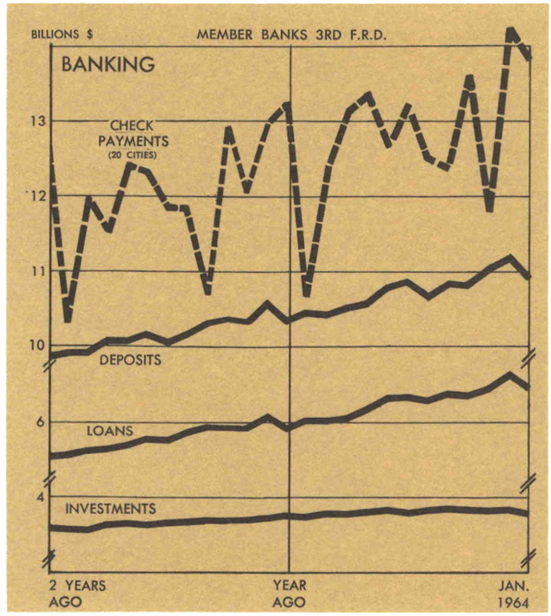
Will consumers raise their sights to a fifth level of wants as their income increases, or will they continue to embrace a never-ending procession of luxuries and personal services—many still to be invented—on the fourth level?

A fifth level probably would involve wants that can be achieved best by collective action. In other words, consumers may be spending more of their incomes on taxes with which to pay for Government action against such universal enemies as disease, ignorance, crime and prejudice. Indeed the trend has already begun. In 1957, federal and state and local personal taxes paid came to 12 per cent of personal income. In 1962 the figure had risen to 13 per cent with the state and local bite increasing most rapidly. It is likely that this trend will continue as reductions in federal income taxes are more than offset by growth in tax rates levied by other units.

After filling our stomachs, our clothes closets, our garages, our teeth and our minds, we now may seek to insure the health, safety and leisure to enjoy more fully the good things on the first four levels.

FOR THE RECORD...





SUMMARY

	Third Federal Reserve District		United States	
	Per cent change		Per cent change	
	Jan. 1964 from		Jan. 1964 from	
	mo. ago	year ago	mo. ago	year ago
MANUFACTURING				
Production	....	....	0	+ 7
Electric power consumed	0	+10	....	....
Man-hours, total*	− 6	− 6	....	....
Employment, total	− 1	0	− 1	+ 2
Wage income*	− 5	− 2	....	....
CONSTRUCTION**	−20	+ 1	− 2	+20
COAL PRODUCTION	− 1	+ 9	0	+10
TRADE***				
Department store sales	− 4	+ 8	− 4	+ 7
Department store stocks	− 1	+ 3	....	....
BANKING (All member banks)				
Deposits	− 2	+ 5	− 3	+ 7
Loans	− 2	+ 9	− 2	+12
Investments	− 1	0	− 2	0
U.S. Govt. securities	− 2	− 8	− 2	− 8
Other	0	+21	− 1	+18
Check payments	− 3†	+ 4†	+ 1	+11
PRICES				
Wholesale	....	....	+ 1	0
Consumer	0‡	+ 2‡	0	+ 2

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

†20 Cities
‡Philadelphia

LOCAL CHANGES

	Factory*				Department Store†				Check Payments	
	Employment		Payrolls		Sales		Stocks			
	Per cent change Jan. 1964 from		Per cent change Jan. 1964 from		Per cent change Jan. 1964 from		Per cent change Jan. 1964 from		Per cent change Jan. 1964 from	
	mo. ago	year ago	mo. ago	year ago	mo. ago	year ago	mo. ago	year ago	mo. ago	year ago
Lehigh Valley	− 1	0	− 5	− 1	....	....	....	....	− 6	+13
Harrisburg	− 1	0	− 5	0	....	....	....	....	− 6	+ 8
Lancaster	− 1	− 2	− 6	− 5	− 3	+ 7	− 2	+ 2	+ 5	+14
Philadelphia	− 1	− 2	− 5	− 3	− 6	+11			− 7	0
Reading	− 1	+ 1	− 6	+ 5	0	+ 8	− 3	+ 3	− 2	+10
Scranton	0	+ 1	− 6	− 1	− 8	− 2	0	+ 2	− 3	+ 1
Trenton	0	+ 5	0	+ 7	+ 5	+11	− 3	+ 7	+27	+33
Wilkes-Barre	− 1	− 2	−10	0	− 5	− 1	− 1	+ 2	− 6	+ 2
Wilmington	0	+ 5	+ 2	+ 8	− 4	+ 8	− 3	+ 8	+11	+13
York	− 1	− 1	− 9	− 5	+ 1	+ 4	+ 9	+ 1	− 1	+ 2

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