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# Uniform Price and Banking Market Delineation

by Charles D. Salley

*This study tests the service area method of geographic banking market delineation, using a uniform price criterion. Secondly, the study seeks to identify other uniform performance variables that may coexist with geographically uniform prices. These other variables include banks' return on assets and capital, measures of portfolio mix, and measures of operating efficiency. There is no theoretical expectation that most of these variables, apart from profit and output measures, should be uniform in separate geographic markets. Coincidental uniformities are sought primarily for future investigation, although they might serve as proxies for price measures that are difficult to obtain. The study attempts to delineate objectively numerous local markets that can be used to evaluate proposed bank mergers. Previous studies have used the more readily available county and SMSA boundaries or subjective estimates of economic trade areas.*

Market definition bounds antitrust jurisdiction both theoretically and administratively. The Anti-Merger Act of 1950 prohibits mergers which substantially lessen competition "in any line of commerce in any section of the country." These product and geographic areas, or markets, must be empirically delineated to evaluate the competitive impact of particular mergers for enforcement purposes. Prior to empirical delineation, though, markets must be conceptually defined to establish the sought-for performance criteria underlying actual case evaluations.

The socially desirable market performance criteria sought by such legislation includes the lower price and profit levels found in "competitive markets" in contrast to higher price and profit levels expected of "monopolistic markets." Policy actions thus presume certain market definitions and

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accompanying performance levels.

In simplest terms, a market must include buyers and sellers. Interactions between buyers and sellers establish product, price, and geographic dimensions which economists and policymakers use to identify markets.

### Structural Market Definitions

The most common definitions of markets are structural; that is, they are based on the number of buyers and sellers. Structural definitions present problems, however, because the number of participants in a market varies as the market boundaries change, both by product dimension and by geographic delineation. The number of buyers and the product definition are determined simultaneously; the number of sellers and the geographic delineation are determined simultaneously.

### Product Line and Price

Buyers have a market identity only as they commonly demand a specific product. To isolate a group of buyers, a market analyst must first isolate a product. An isolated product is one for which buyers will accept no substitutes. For instance, a buyer might be equally satisfied with orange juice or a soft drink. Increased consumption of one results in a decreased consumption of the other. (This substitutability in consumption is called "cross-elasticity.") In this case, the two forms of refreshment are rather close substitutes. Because they have a high degree of cross-elasticity, they do not make up two completely separate product lines or markets. A more isolated product definition would be a collective term, say, beverages, which, as a group, has a very low degree of cross-elasticity with products like gasoline or ink.

A well-known definition of a product market (or line of commerce) requires that the product "be bounded on all sides by a market gap in the chain of substitutes."<sup>1</sup> Common sense places the buyers of ink and the buyers of orange juice on opposite sides of such a gap. However, in the case of closer substitutes like orange juice, milk, and beer, markets may be outlined only by resorting to a price response measure. Cross-elasticity is actually a measure of substitution in response to price change. If the price of orange juice rose high enough, milk or beer might not appear so remote as substitutes. On the other hand, at no price of orange juice is ink a likely substitute. In this way, product lines can be conceptually isolated and a

group of buyers identified by their reaction to price changes.

Once product and buyers are defined, sellers can be grouped into industries (product line suppliers). "Any such subgroup may be called an industry—strictly a group of sellers of close-substitute outputs who supply a common group of buyers."<sup>2</sup>

### Geographic Area and Price\*

The definitional relation between the number of sellers and a geographic market parallels the interdependence between the group of buyers and the product definition. Again, a price measure is used to focus on the relationship.

Both monopoly and competitive markets, for example, are structurally defined according to the number of sellers. The fewer sellers, the more "concentrated" the pricing and exchange decisions. Economic theory associates higher levels of concentration with higher prices, higher profits, and lower output. Many empirical investigations are conducted to establish this theoretically expected structure-performance link underlying much anti-trust activity.

Obviously, though, the number of sellers and the level of concentration will depend directly on the geographic extent of the market. Regulators may wish to define a market's concentration by the number of participants, but as price theory texts point out, "to know the proper number of individuals to include within the market for a commodity, the market area for the product must be established."<sup>3</sup> It is possible to define arbitrarily a market so specialized and so local that there will be but one seller of a particular product. Contrast the narrow Port St. Joe, Florida, market for auto inventory loans with a broad national market for business credit. The first is geographically small with few sellers; the second is large and includes many sellers. Market structure and extent are interrelated in that definitions of one based on the other appear to be circular or indeterminate.

The mutuality in structural geographic definitions of markets is traditionally overcome by resorting to a price dimension. Alfred Marshall defines a geographic market as the area within which price tends to uniformity. "Thus, the more nearly perfect a market is, the stronger is the tendency for the

<sup>2</sup>Bain, Joe. *Industrial Organization*, New York: Wiley, 1968, p. 6.

\*The synthesis of concepts used to define the theoretical banking market in this study was suggested in conversations with David D. Whitehead, economist at the Federal Reserve Bank of Atlanta, concerning his dissertation in progress.

<sup>3</sup>Stigler, George J. *The Theory of Price*, New York: Macmillan, 1966, p. 92.

<sup>1</sup>Robinson, Joan. *Economics of Imperfect Competition*, New York: St. Martins Press, 1961, p. 5.

Sixty-eight Florida banking markets were examined because their geographic delineation has been established on the service area basis in the course of many actual bank acquisition cases. Only markets having more than one bank were selected, since the investigation centers on comparing price variation within markets with the variation among markets. The markets include a total of 539 banks; the largest market contains 70 banks and the smallest, 2 banks.

Price variables used in previous studies have been limited to passbook savings rates, sampled rates on new automobile loans, and sampled rates on unsecured personal loans. The present analysis uses four actual

savings rates, a calculated rate paid for borrowed funds, and a calculated measure of account service charges for all banks in the respective market areas.

The savings rates for 336 banks are taken from the Federal Reserve System's Quarterly Survey of Time and Savings Deposits for October 1973. Rates for the remaining 203 banks were obtained from FDIC reports of examination conducted during 1973. The other performance variables are taken from the Federal Reserve System's Bank Operating Ratios for 1973. These individual bank ratios are calculated from an average of three Reports of Condition filed during the year.

### The Statistical Test

The statistical test is basically one of significant difference in the mean price prevailing in two areas designated as separate banking markets. The null hypothesis is that there is only a single market—the prices in the subdivided areas are merely the mean prices of two randomly drawn samples from the same population. There should be no difference except by chance variation between these means as estimates of the hypothesized common population mean. However, if the test yields significant differences in the means of the divided areas, the null hypothesis must be rejected; significantly different means must have come from different populations. Then the alternate hypothesis holds: The two areas may be taken as separate banking markets.

Such a test of two means can be extended to test for differences among the means of more than two samples (markets) using analysis of variance and the F-test. (The technique works with variances, though, rather than means.) If a uniform price is characteristic of properly isolated geographic markets, there should be little variation of price within these markets. And if the markets are actually isolated, there should be some variance among their prices because of differing local circumstances. If the markets are indeed separate, the price variation between markets, then, will be greater than the variation within them. The between market variance: within market variance ratio (the F-ratio) will be greater than one.<sup>1</sup>

The null hypothesis is that the areas defined by overlapping bank service areas are not separate markets, that these groupings are merely random samples from a common population. If this is the case, the F-ratio, except for chance variation, will be equal to one. An F-ratio was calculated for each price variable and also for the other performance measures.

F-ratios were also calculated for each performance variable after the banking markets were redefined by using the arbitrary but more commonly used county-line delineation. This tests the accuracy of county lines (in Florida) as a proxy for delineated markets.

Previous studies did not use the F-test because the only price variable used was the passbook savings rate. Since the Federal Reserve Board's Regulation Q sets a maximum rate payable on such accounts, the rate variations among banks would not be normally distributed, even though not all banks pay the ceiling rate. The F-test is limited to samples (markets) drawn from normal populations.

For this reason, Edwards<sup>2</sup> used the following t-test:

$$\frac{\bar{X}_1 - \bar{X}_2}{\sqrt{\frac{S_1^2}{N_1} + \frac{S_2^2}{N_2}}}$$

where  $N_1$  and  $N_2$  are the banks in either market,  $S_1$  and  $S_2$  are the standard deviation, and  $\bar{X}_1$  and  $\bar{X}_2$  are the mean interest rates. Glassman, in a more ambitious study of all banking markets in Pennsylvania, used the chi-square test.<sup>3</sup>

Nonetheless, the analysis of variance was chosen for the present study, since in the fall of 1973 Regulation Q interest rate ceilings did not apply to the four-year and large-denomination CD rates. These, as well as the operating ratios, may be assumed to come from normal populations. Also, Cochran suggests that with nonnormality in the experimental errors, the true probability corresponding to the 1-percent significance level of the F-table may lie between one-half of 1 percent and 2 percent.<sup>4</sup>

<sup>2</sup>Edwards, Frank R. "The Banking Competition Controversy," *National Banking Review*, September 1965, p. 8.

<sup>3</sup>Glassman, Cynthia A. "Banking Markets in Pennsylvania," *Changing Pennsylvania's Branching Laws*, Federal Reserve Bank of Philadelphia, 1973, pp. 19-41.

<sup>4</sup>Cochran, W. G. "Some Consequences When the Assumptions for the Analysis of Variance are not Specified," *Biometrika*, March 1947, pp. 22-38.

<sup>1</sup>The F-ratio is actually a comparison of two independent estimates of the population variance. One is derived from variance within samples and the other from the variance of the sample means. If they are in fact both estimates of the same population, their ratio will equal one. Blalock, Hubert M. *Social Statistics*, New York: McGraw-Hill, 1972.

The F-ratios for the 68 delineated markets are significantly greater than 1 for 7 of the 8 price measures (see table). Five are significant at the .01 level, and two others are significant at the .05 level. The null hypothesis that these geographic areas are not separate banking markets on the basis of uniform price can be rejected.

The F-ratios for the 51 county markets are significantly greater than 1 for six of the eight price measures. Five are significant at the .01 level, and one is significant at the .05 level. The test of the delineated market areas obtained a higher level of significance than the county market test only on the performance variable that included interest received for Federal funds.

Two conclusions seem reasonable: (1) Geographic areas in Florida delineated by clustering bank service areas are separate banking markets and (2) county boundaries are valid proxies for banking markets, at least when concentration or performance studies are carried out with statewide data. This may not be true for studies limited to a small number of counties.

Nine additional performance measures have F-ratios greater than one. All are at the very high .01 level of significance. Various hypotheses and conclusions can be drawn to "fit" these results. In general, the local uniformity of income shares related to pricing, wage measures of efficiency, and portfolio mix seem to coincide with the uniform price delineation of separate banking markets. On the other hand, rates of return and measures of risk, contrary to theoretical expectation, are not uniform within markets delineated either by service area or by county line technique. Bank size and time in operation are likely influences on these variables.

The level of significance for interest paid on \$1,000 four-year certificates was disappointingly low, although a somewhat higher level of significance was obtained in delineated markets (.18) than in county markets (.36). These savings certificates are the highly publicized and controversial "wild card" certificates exempted from Regulation Q rate ceilings during the period when the data were reported. As a highly competitive savings instrument, rates on these certificates were expected to provide a particularly accurate test of local banking market delineation.

Two explanations might account for the low level of significance obtained. The certificates, introduced first in the summer of 1973, may have appeared too recently to have established equilibrium market prices by the time of the October survey. Alternatively, many banks may not have been interested in raising funds in this manner and consequently priced their certificates well below the local market rate. For this reason, a 5-percent quoted rate might appear amid several 8-percent quoted rates in the same market. Such great local variance would produce a very low F-ratio.

Finally, an analysis of variance of deposit size by banking market was performed as a loose check for the influence of bank size on the performance measures. Although the test is no substitute for a vigorous two-way analysis of variance to remove the influence of bank size, a large F-value would indicate the need for further testing. The F-ratio was less than one both for delineated markets and county markets, indicating that there is no systematic variation among markets and bank size which would bias the conclusions.

same price to be paid for the same thing at all parts of the market."<sup>4</sup> (This presumes that the product line has been defined.)

Empirical studies have generally followed Marshall's (and Loesch's) means of geographic delineation. Schweiger and McGee first used price uniformity as a tool of identifying banking markets in 1961, utilizing state boundaries as significant market delineators. They found that even when state lines cross through single metropolitan areas, prices differ significantly on either side, indicating separate geographic markets.<sup>5</sup>

Schull and Horwitz used the price approach in 1964 to establish that subsectors of metropolitan areas with branching systems form single banking markets, whereas unit banking metro areas have less price uniformity and, therefore, consist of numerous submarkets.

"Our conception of a 'market' is the traditional economic one. It is a particular place in which goods or services are bought and sold, and in which the relationship between buyers and sellers is such that the prices of the 'same' products tend toward equality. . . . but if a producer can 'separate' his customers so that he can charge different prices for the 'same' product, he is, in effect, selling in more than one 'market.' "<sup>6</sup>

Selling the same article at different prices to different buyers is called price discrimination;<sup>7</sup> a producer is taking advantage of geographic barriers between parts of a product market to charge different prices for the same thing. Different prices are possible only when a producer or several producers do not face a common group of buyers. Buyers must be somehow divided so that goods sold cheaper in one area cannot be bought from the producer and then resold in the higher-price area.

<sup>4</sup>Marshall, Alfred. *Principles of Economics*, London: Macmillan, 1961 ed., p. 324.

<sup>5</sup>Schweiger, Irving, and McGee, John S. "Chicago Banking," *The Journal of Business of the University of Chicago*, July 1961, p. 258.

<sup>6</sup>Schull and Horwitz, "Branch Banking and the Structure of Competition," *National Banking Review*, March 1964, pp. 301-341.

<sup>7</sup>Robinson. *op cit.*, p. 179.

A uniform price for the same commodity, then, is taken as evidence that there is a common group of buyers.

This says that the demand curve for a commodity in each market, if it is truly separate, is independent of the prices charged in other markets. For instance, if a bank lowered its price, other banks serving a common group of buyers would be forced to lower their prices also or lose business. Price discrimination either by one firm or several separate firms would not be possible and a common price would prevail in the geographic market. (A single price would also prevail, of course, if there were only one bank serving an isolated group of customers.)

A bank outside the market, i.e., one serving a different group of buyers in some way isolated from the first group, could maintain a price difference. Difference in price can be used, then, as an indicator of different geographic markets. This says nothing, however, about expected differences in price level and any correlation with the number of sellers.

Frank Edwards also used a uniform price criterion in his 1965 study of the significance of state boundaries as geographic market limits.

"It is obvious that two markets may have identical or nearly identical prices because of a coincidental combination of supply, demand, and structure. However, when a significant difference does exist between the 'mean' prices in two areas, these may be taken as different 'markets.'"<sup>8</sup>

### The Uniform Price Criterion

Price uniformity, then, appears to be a useful tool in empirically establishing geographic markets. This initial delineation is of overriding importance in structural antitrust cases, since it automatically establishes the concentration level.

More accurately stated, the uniform price measure, rather than delineating market limits, verifies a market previously established in the manner described. First, the product line is isolated in terms of a lack of substitutes. Simultaneously, a range of buyers for the product line is established, i.e., those who view the product as unique. A range of sellers, the industry, is next approximated as those firms capable of supplying the product. These are potential buyers and sellers in the product-line sense. The first geographic estimate to include a specific domain<sup>9</sup> of sellers and buyers is judgmentally chosen on the basis of observed exchange patterns, the role of distance between buyers and

sellers, natural obstacles such as mountains and rivers—all usually summed up by an existing political boundary, such as a city, SMSA, or county limit. Such bounds are taken arbitrarily as barriers to buyer mobility and as final delineators of isolated and, therefore, common groups of buyers.

This procedure of arriving at a structural market definition clarifies the importance attached to the initial discussion of banking as a line of commerce. When the Justice Department objected to the merger of the Philadelphia National Bank and the Girard Trust Corn Exchange in 1963, identifying banking's essential product line became crucial. Two line-of-commerce concepts emerged during the case. One, an extension of the standard economic model of a multiple product firm, maintains that banks sell distinct products, such as payment services, loans, fiduciary services, etc., to separate groups of customers.<sup>10</sup> Accordingly, the demand elasticities are different for each product line (i.e., there is a gap in the chain of substitutes), and a bank can practice price discrimination. (Geographic definitions can then be constructed from individually defined product lines.) In this particular case, lower courts viewed credit as the primary product. Commercial credit as a line of commerce permitted geographic delineation of a broad national market which, of course, would be little affected by a local merger.

The alternative line-of-commerce concept viewed banking as a composite service industry.<sup>11</sup> Loan customers are generally deposit customers also, especially when compensating balance requirements are considered. Empirically, long-term customer relationships are observed rather than a constant shifting of customers from bank to bank in response to the pricing of individual services. Following this concept, the Supreme Court found commercial banking to be a single line of commerce in fairly narrow, localized markets. The proposed merger would naturally lead to higher concentration in the market delineated as the local Philadelphia area, and the merger was enjoined.

### The Service Area Concept

In actually delineating geographic markets, though, the two concepts are perhaps not mutually exclusive. Many studies have concluded that the market(s) for the majority of banking services is

<sup>8</sup>Edwards, Frank R. "The Banking Competition Controversy," *National Banking Review*, September 1965, p. 8.

<sup>9</sup>Range and domain are used in the functional sense of mapping a specific subset from all possible market participants.

<sup>10</sup>Schull, Bernard. "Commercial Banks as Multiple-Product Price-Discriminating Firms," *Banking and Monetary Studies*, ed. Deane Carson, Homewood, Illinois: Richard D. Irwin, Inc., 1963, pp. 351-368.

<sup>11</sup>Hodgman, Donald R. *Commercial Bank Loan and Investment Policy*, Bureau of Economic and Business Research, Urbana, Illinois: University of Illinois Press, 1963.

# FLORIDA BANKING MARKET F-RATIOS (1973)

	68 Delineated Markets		51 County Markets	
<b>Prices Paid</b>				
Passbook Savings	2.78+	(.01)*	3.50+	(.01)
1 to 2½-year Certificate	2.25+	(.01)	3.46+	(.01)
\$1,000 4-year Certificate	1.17	(.18)	1.07	(.36)
\$100,000 Certificate	1.33	(.05)	1.52	(.02)
Interest Paid on Deposits/Assets	4.33	(.01)	4.20	(.01)
Interest on Time & Savings Deposits/Total T & S Deposits	1.65	(.01)	1.55	(.01)
<b>Prices Charged</b>				
Interest & Fees on Loans/Average Loans Outstanding	1.81	(.01)	2.08	(.01)
Interest & Fees on Loans & FF/Average Loans Outstanding	1.35	(.04)	1.33	(.07)
<b>Income Shares</b>				
Deposit Account Service Charges/Total Operating Income	2.86	(.01)	4.65	(.01)
Interest & Fees on Loans/Total Operating Income	2.11	(.01)	2.08	(.01)
U. S. Securities Income/Total Operating Income	2.72	(.01)	3.56	(.01)
<b>Portfolio Mix</b>				
Gross Loans/Total Assets	2.56	(.01)	2.56	(.01)
Consumer Loans/Gross Loans	2.06	(.01)	2.64	(.01)
Time & Savings Deposits/Total Deposits	4.78	(.01)	4.95	(.01)
<b>Rates of Return</b>				
After Tax Income/Equity Capital	.80	(.86)	.95	(.57)
After Tax Income/Assets	1.03	(.42)	1.04	(.40)
Net Income/Assets	1.17	(.18)	1.27	(.11)
<b>Efficiency and Risk Measures</b>				
Wages/Assets	2.08	(.01)	2.84	(.01)
Salaries and Wages/Total Operating Income	1.87	(.01)	2.48	(.01)
Interest Paid on Deposits/Total Operating Income	4.29	(.01)	4.25	(.01)
Interest Paid on Borrowed Money/Total Operating Income	.73	(.92)	.73	(.88)
Loan Losses/Average Loans Outstanding	.98	(.52)	1.23	(.14)

Based on data from 539 banks

+ Normality assumption violated

\* Level of significance, i.e., .01 probability, that F-value is by chance

fairly local.<sup>12</sup> Moreover, individual bank service areas for demand deposits, time deposits, business loans, and consumer loans, as determined in numerous merger and holding company acquisition applications, rarely extend beyond local political limits. The service area as a regulatory definition is the contiguous geographic area from which a bank derives approximately 80 percent of its deposits or loans. Loan service areas tend to be somewhat larger than deposit service areas, but their bounds remain local whether measured by narrower product lines or by number or dollar amount of accounts and regardless of account sample size.<sup>13</sup>

With this evidence, the two theoretical concepts might be reconciled. It could well be that there are banking product lines that have different

demand elasticities. However, Joan Robinson added a salient condition for the multiple product argument: Price discrimination is possible, "provided that the elasticities of demand in the separate markets are not equal."<sup>14</sup> So the convenience of "one-stop banking" or the requirement that loan customers maintain compensating balances could make otherwise separate demand elasticities so nearly equal that the observed coincidence of various product line service areas results.

Moreover, not only does the service area concept offer an empirical solution to the initial line-of-commerce determination, it helps overcome a further circular argument in the all-important structure-performance relationship. If the uniform price criterion alone were used to establish a geographic market, the structure-performance theorems based on the relation between level of prices and level of concentration (itself derived from price behavior)

<sup>12</sup>Federal Reserve Bank of Chicago, *Bank Loans to Business*, Chicago, 1956; Kaufman, George G. "Bank Market Structure and Performance: The Evidence from Iowa," *Southern Economic Journal*, April 1966, pp. 429-439.

<sup>13</sup>Austin, Douglas V. "Defining the Market Area of a Bank," *The Bankers Magazine*, spring 1969, p. 73.

<sup>14</sup>Robinson. *op. cit.*, p. 181.



## Banking Market Areas

Defined by service area overlap.

Note: The market boundaries shown do not reflect in all cases the current market definitions used by the Board of Governors in bank holding company decisions.

will have no operational content beyond a circular definition.

"To define the market according to the price behavior exhibited destroys any possibility of using the market so defined to say anything about price behavior, and it prejudices the question of which market structure is the relevant one for making predictions."<sup>15</sup>

The measured service concept can break the chain of mutual determination, since it statistically identifies a group of buyers and a supplier. A

market area identified as a cluster of overlapping service areas is in this manner delineated as a common group of buyers together with the sellers, independently of price. Price uniformity can then be used to test if markets so estimated are indeed separate markets. More importantly, markets so defined can be used to produce structure-performance theorems with some predictive content.

### Implications for Case Analysis

The present study not only lends some support to the Glassman (Federal Reserve Bank of Philadelphia) findings on the local nature of banking markets; it also suggests a technique for testing

<sup>15</sup>Steiner, Peter O. "Markets and Industries," *International Encyclopedia of the Social Sciences*, Vol. 9, p. 577.

geographic delineations used to analyze holding company and merger applications (see map).

Market areas are particularly difficult to separate where there are no obvious geographic breaks between population centers. This has been the case in Florida for the coastal area north of Miami and the various cities in Polk, Lake, and Brevard Counties. In the Daytona Beach-New Smyrna Beach area, an actual poll of bank customers had to be used to determine a boundary.

This study suggests a method of delineating

neighboring local markets on the basis of micro-banking data. Banks in contiguous market areas located adjacent to a disputed boundary can be shifted from one side of the boundary to the other until a maximum F-ratio value is attained for the test variables or the highest significance level is achieved.

Such a method is surely easier than polling banks and their customers and may prove valuable when local markets in Georgia, Mississippi, and Louisiana must be determined. ☞

## Bank Announcements

April 1, 1975

### **SOUTH COUNTY BANK**

*South Venice, Florida*

**Opened for business as a member.** Officers: Gilbert N. Parker, chairman; Charles J. Henning, president; Jack G. Shultz, executive vice president; James S. Brown, vice president and cashier; John C. Pinkerton, vice president. Capital, \$500,000; surplus and other funds, \$500,000.

April 4, 1975

### **CITY NATIONAL BANK OF SOUTH DADE**

*Miami, Florida*

**Opened for business as a member.** Officers: Allan T. Abess, Jr., chairman; R. L. Budde, president; Connie Arnaz, vice president and cashier; Florence S. Kmitto, assistant vice president. Capital, \$850,000; surplus and other funds, \$425,000.

April 11, 1975

### **CITRUS PARK BANK**

*Citrus Park, Florida*

**Opened for business as a par-remitting nonmember.** Officers: Robert D. Sellas, president; George G. Lamberson, vice president and cashier. Capital, \$890,000; surplus and other funds, \$311,000.

April 15, 1975

### **THE BANK OF CENTRAL FLORIDA**

*Orlando, Florida*

**Opened for business as a par-remitting nonmember.** Officers: Joseph O. Hutchinson, president; Frank H. Roark, vice president; Keith N. King, cashier. Capital, \$866,790; surplus and other funds, \$433,395.

April 24, 1975

### **DEER CREEK STATE BANK**

*Deerfield Beach, Florida*

**Opened for business as a par-remitting nonmember.**

April 28, 1975

### **JUPITER-TEQUESTA NATIONAL BANK**

*Jupiter, Florida*

**Opened for business as a member.** Officers: Jack T. Williams, chairman; William R. McDonald, president; David N. Devick, cashier. Capital, \$600,000; surplus and other funds, \$400,000.

May 1, 1975

### **CITIZENS BANK**

*Ville Platte, Louisiana*

**Opened for business as a par-remitting nonmember.** Officers: Carl Fontenot, president; J. R. Aucoin, executive vice president; J. B. Veillon, first vice president; Dale Reed, second vice president; Eugene Fontenot, secretary. Capital, \$375,000; surplus and other funds, \$375,000.

May 1, 1975

### **CITIZENS FIRST NATIONAL BANK OF CRYSTAL RIVER**

*Crystal River, Florida*

**Opened for business as a member.** Officers: Thomas J. Tobin, president; Shirley Haynes, vice president and cashier. Capital, \$650,000; surplus and other funds, \$650,000.

May 1, 1975

### **COVINGTON COUNTY BANK**

*Collins, Mississippi*

**Opened for business as a par-remitting nonmember.** Officers: R. E. Blackwell, chairman; Jack D. Triggs, president; Stephen L. Goff, cashier. Capital, \$312,500; surplus and other funds, \$312,500.

May 1, 1975

### **C & L BANK OF BRISTOL**

*Bristol, Florida*

**Opened for business as a par-remitting nonmember.** Officers: J. W. Weaver, Sr., chairman; Jerry M. Smith, president; Butler Read, exec. vice president and cashier.

# The Current Recession in Perspective\*

by Arthur F. Burns, Chairman

Board of Governors of the Federal Reserve System

I am glad to meet with this distinguished group of business and financial journalists in a leisurely setting. As a policymaker, I feel I have much in common with the members of your profession. Both you and I must be alert to every twist and nuance of the changing economic scene. Both you and I must keep busy searching the business skies for some clues to the economic future. I find this aspect of my work exciting and intriguing, as I am sure you do. But it does involve a certain risk for both of us.

Sharing — as we do — the problem of continually meeting deadlines, we are in danger of becoming so preoccupied with the very short run that we fail to see economic events in perspective. For that very reason, I have wanted to take advantage of your invitation, so that we might ponder together the historical developments which have brought our economy to its present condition. This is a large and highly important subject. I cannot hope to do full justice to it on the present occasion. Nevertheless, I shall make a start this evening.

As you are well aware, these past few years have been trying times for the American people. Not only have we lived through the agony of Vietnam and Watergate, but some of us have even begun to wonder whether our dream of full employment, a stable price level, and a rising standard of living for all our people is beyond fulfillment.

Early last year, economic expansion began to falter in our country, as it did in other countries around the world. At the same time, the pace of the inflation that had been building for more than a decade accelerated sharply further. As the year advanced, it became increasingly clear that our economy was moving into a recession.

During the past two quarters, the real gross national product has declined by 5 per cent, and the level of industrial production is now 12 or 13 per cent below last September. The unemployment rate has risen swiftly, and so also has the idle capacity in our major industries. The decline in business activity since last fall has been the steepest of the post-war period, and yet the advance of the price level — while considerably slower than last year — is continuing at a disconcerting pace.

No business-cycle movement can be comprehended solely in terms of the events that occur within that cycle or the one preceding it. The economic

\*An address given before the Society of American Business Writers, Washington, D.C., May 6, 1975.

currents of today are heavily influenced by longer-range developments—such as changes in economic and financial institutions, the course of public policy, and the attitudes and work habits of people. By examining the historical background of recent economic troubles, we should be able to arrive at a better understanding of where we now are.

The current recession is best viewed, and I believe it will be so regarded by historians, as the culminating phase of a long economic cycle.

There have been numerous long cycles in the past — that is, units of experience combining two or more ordinary business cycles. One such long cycle ran its course from 1908 to 1921; another from 1921 to 1933. And if we go back to the nineteenth century, we encounter long cycles from 1879 to 1894 and from 1894 to 1908. These long cycles differ in innumerable ways from one another. But they also have some features in common — in particular, each culminates in an economic decline of more than average intensity.

The beginning of the long cycle that now appears to be approaching its natural end may be dated as early as 1958, but it is perhaps best to date its start in 1961. The upward movement of economic activity which began in that year was checked briefly in 1967 and interrupted more significantly in 1970. Although these interruptions were watched with concern and some anxiety by practicing economists and other interested citizens, they will be passed over lightly by economic historians concerned with large events.

The reason is not hard to see. Putting aside monthly and quarterly data and looking only at annual figures, we find that total employment rose every year from 1961 through 1973. So also did disposable personal income and personal consumption expenditures — both viewed on a per capita basis and in real terms. This sustained upward trend of the economy came to an end in 1974.

The successive phases of the long upswing from 1961 to 1974 provide a useful perspective on our current problems. Some years ago, in my work at the National Bureau of Economic Research, I observed a pattern in past long upswings — an initial stage that may be called the “industrial phase” followed by what is best described as the “speculative phase.” The imbalances that develop in this latter phase lead inevitably to the final downturn. The events of the past 15 years conform rather closely to this pattern.

The period from 1961 through 1964 may be regarded as the industrial phase of the long upswing. Productivity grew rapidly — increasing in the private nonfarm sector at an annual rate of 3.6 per cent between the final quarters of 1960 and 1964, or well above the average rate of the preceding decade. Unit labor costs were then remarkably stable, and so too was the general price level. Real wages and profits rose strongly. During this period of sustained

economic expansion, unemployment fell from about 7 per cent of the labor force to 5 per cent, while the rate of use of industrial capacity rose substantially.

The second — or speculative — phase of the long upswing began around 1965 and continued through much of 1974. This ten-year period was marked by a succession of major, interrelated, and partly overlapping speculative waves that in varying degrees gripped other leading industrial countries as well as the United States.

The first speculative movement involved corporate mergers and acquisitions. In the euphoria of what some commentators have called the “go-go” years, rapid growth of earnings per share of common stock became the overriding goal of many business managers. Other yardsticks of corporate performance — such as the rate of return on new investments — were neglected, and so too were the serious risks of increased leveraging of common stock.

The aggregate volume of large corporate acquisitions, which for some years had been running at about \$2 billion per year, jumped to \$3 billion in 1965, to \$8 billion in 1967, to \$12½ billion in 1968, and then tapered off. This was the great era of conglomerates, when a variety of unrelated businesses were brought together under a single corporate management. Entrepreneurs who displayed special skill in such maneuvers were hailed as financial geniuses — until their newly built empires began to crumble. Being preoccupied with corporate acquisitions and their conglomerate image, many businessmen lost sight of the traditional business objective of seeking larger profits through better technology, aggressive marketing, and improved management. The productivity of their businesses suffered, and so too did the nation's productivity.

The spectacular merger movement of the late 1960's was reinforced, and to a degree made possible, by the speculative movement that developed in the market for common stocks. The volume of trading on the New York Stock Exchange doubled between 1966 and 1971, and for a time trading volume on the American Exchange rose even faster. The prices of many stocks shot up with little regard to actual or potential earnings. During the two years 1967 and 1968, the average price of a share of common stock listed on the New York Exchange rose 40 per cent, while earnings per share of the listed companies rose less than 2 per cent. On the American Exchange, the average price per share rose during the same years more than 140 per cent on an earnings base that again was virtually unchanged.

Much of this speculative ardor came from a section of the mutual fund industry. For the new breed of “performance funds,” long-term investment in the shares of established companies with proven earnings became an outmoded concept. In

their quest for quick capital gains, these institutions displayed a penchant for risky investments and aggressive trading. In 1965, a typical mutual fund turned over about one-fifth of its common stock portfolio; by 1969, that fraction had risen to nearly one-half. As Wall Street then had it, the "smart money" went into issues of technologically-oriented firms or into corporate conglomerates — no matter how well or poorly they met the test of profitability.

Speculation in equities was cooled for a time by the stock market decline of 1969-1970, but then it resumed again and took on new forms. Money managers began to channel a preponderant part of their funds into the stocks of large and well-known firms — apparently with the thought that earnings of those companies were impervious to the vicissitudes of economic life. A huge disparity was thereby created between the price-earnings ratios of the "favored fifty" and those of other corporations. Share prices of these "favored" companies were, of course, especially hard hit in the subsequent shakeout of the stock market.

Speculation in common stocks was not confined to the United States. From the late 1960's until about 1973, nearly every major stock exchange in the world experienced a large run-up in share prices, only to be followed by a drastic decline. Indeed, speculation reached a more feverish pace in some countries than in the United States. On the Tokyo stock exchange, for example, both share prices and the trading volume actually doubled in the twelve months between January 1972 and January 1973 and then suffered a sharp reversal.

The third speculative wave that nourished the long upswing of our national economy occurred in the real estate market. Homebuilding fluctuated around a horizontal trend during the 1960's. The vacancy rate in rental housing was at a high level from 1960 to 1965, then fell steadily until the end of the decade, and thus helped pave the way for a new housing boom. Between January of 1970 and January of 1973, the volume of new housing starts doubled. Since then, homebuilding has plunged, and in some sections of the nation it has virtually come to a halt. Failures of construction firms and unemployment among construction workers have reached depression levels. These unhappy developments stem in large measure from the excesses of the housing boom that got under way in 1970.

Inflationary expectations clearly played a substantial role in bolstering the demand for houses. But the boom was fostered also by an array of governmental policies designed to stimulate activity in the housing sector. These governmental measures, however well-intentioned, gave little heed to basic supply conditions in the industry or to the underlying demand for housing.

In response to easy credit and Federal subsidies, merchant builders moved ahead energetically, put up one-family homes well ahead of demand, and

thus permitted the inventory of unsold homes to double between 1970 and 1973. Speculative activity was even more intense in the multi-family sector — that is, in apartments built for renting, and particularly in condominiums and cooperatives, which accounted for a fourth of the completions of multi-family structures by the first half of 1974.

The boom in housing was financed by a huge expansion of mortgage credit and construction loans. Real estate investment trusts played an exceptionally large role in supplying high-risk construction loans for condominiums, recreational developments, and other speculative activities. The growth of real estate trusts was extraordinary by any yardstick. Their assets, amounting to less than \$700 million in 1968, soared to upwards of \$20 billion by 1973. Unsound practices accompanied this rapid growth and, as a result, many real estate trusts now face difficult financial problems.

The speculative boom in real estate was not confined to residential structures. It extended to speculation in land, to widespread building of shopping centers, and to construction of office buildings. By 1972, the vacancy rate in office buildings reached 13 per cent, but this type of construction still kept climbing.

The real estate boom in the United States during the early 1970's had its parallel in other countries. Speculation in land and properties became rampant in the United Kingdom. In 1972 alone, new house prices rose 47 per cent on the average. The amount of credit absorbed in real estate ventures rose so rapidly that the Bank of England felt forced to place special controls on bank lending for such purposes. And in Germany, the boom in residential construction during 1971-73 left an inventory of about a quarter million unsold units—more than a third of a peak year's output—that now overhang the market.

It is in the nature of speculative movements to spread from one country or market to another. Just as the speculative wave in real estate was beginning to taper off in 1973, a new wave of speculation got under way—this time in inventories. That was the fourth and final speculative episode of the long economic upswing from 1961 to 1974. It involved massive stocking up of raw materials, machinery, parts, and other supplies in the United States and in other industrial countries.

The inventory speculation of 1973 and 1974 was the outgrowth of a boom in business activity that had raised its head by 1972 in virtually every industrial country of the world. The synchronism of economic expansion in these countries was partly coincidental, but the expansion that stemmed from ordinary business-cycle developments was reinforced by the adoption of stimulative economic policies almost everywhere. As a result, production increased rapidly around the world and led to a burgeoning demand for raw materials, machine

tools, component parts, and capital equipment—goods for which our country is a major source of supply. The pressure of rising world demand was reinforced in our markets by the devaluation of the dollar, which greatly improved our competitive position in international trade.

By the beginning of 1973, as business firms attempted to meet intense demands from both domestic and foreign customers, serious bottlenecks and shortages had begun to develop in numerous industries—especially those producing steel, non-ferrous metals, paper, chemicals, and other raw materials. In this environment of scarcities, the rise in prices of industrial commodities quickened both here and abroad. The dramatic advance of food prices in 1973, and later in energy prices, greatly compounded the worldwide inflationary problem. In our country, these price pressures were suppressed for a time by price and wage controls, but the general price level exploded when controls were phased out in late 1973 and early 1974.

One of the unfortunate consequences of inflation is that it masks underlying economic realities. As early as the spring of 1973, a perceptible weakening could be detected in the trend of consumer buying in this country. The business community, however, paid little attention to this ominous development. The escalating pace of inflation fostered expectations of still higher prices and persistent shortages in the years ahead, so that intensive stockpiling of commodities continued. Inventories increased out of all proportion to actual or prospective sales. In fact, the ratio of inventories to sales, expressed in physical terms, had risen by the summer of 1974 to the highest figure for any business-cycle expansion since 1957—another year when a severe recession got under way.

In summary, the period from 1965 to 1974 was marked by a succession of interrelated, partly overlapping, speculative waves—first, in buying up of existing businesses; then, in the stock market; next, in markets for real estate; and finally, in markets for industrial materials and other commodities.

A prolonged speculative boom of this kind can seldom be traced to a single causal factor. In this instance, however, a dominant source of the problem appears to have been the lack of discipline in governmental finances.

The industrial phase of the long upswing drew to a close in late 1964 or early 1965. By then, the level of real output was very close to the limits imposed by our nation's physical capacity to produce. By then, the level of wholesale prices was already moving out of its groove of stability. Nevertheless, our Government did nothing to moderate the pace of expansion of aggregate monetary demand. On the contrary, it actually embarked on a much more expansive fiscal policy. The tax reductions of 1964 were followed in 1965 by fresh tax reductions and by a huge wave of spending both

for new social programs and for the war in Vietnam. These misadventures of fiscal policy doomed the economy to serious trouble, but we were slow to recognize this. Indeed, substantial tax reductions occurred again in 1969 and 1971, and they too were followed by massive increases of expenditures.

Deficits therefore mounted, and they persisted year in and year out. Over the last ten complete fiscal years—that is, from 1965 through 1974—the Federal debt held by the public, including obligations of Federal credit agencies, rose by more than 50 per cent. The large and persistent deficits added little to our nation's capacity to produce, but they added substantially to aggregate monetary demand for goods and services. They were thus directly responsible for much of the accelerating inflation of the past decade.

Monetary and credit policies were not without some fault. As every student of economics knows, inflation cannot continue indefinitely without an accommodating increase in supplies of money and credit. It is very difficult, however, for a central bank to maintain good control of money and credit when heavy governmental borrowing drives up interest rates, and when the public is unwilling to face squarely the long-run dangers inherent in excessively stimulative economic policies.

To make matters worse, laxity in our national economic policies spilled over into private markets. The "new economics," of which less is now heard than before, held out the possibility, if not the actual promise, of perpetual prosperity. Many businessmen and financiers came to view the business cycle as dead, and to expect the Federal Government to bail out almost any enterprise that ran into financial trouble. All too frequently, therefore, the canons of financial prudence that had been developed through hard experience were set aside.

Many of our business corporations courted trouble by permitting sharp reductions in their equity cushions or their liquidity. In the manufacturing sector, the ratio of debt to equity—which had been stable in the previous decade—began rising in 1964 and nearly doubled by the end of 1974. Moreover, a large part of the indebtedness piled up by business firms was in the form of short-term obligations, and these in turn grew much more rapidly than holdings of current assets.

Similar trends developed in some segments of commercial banking. Large money-market banks came to rely more heavily on volatile short-term funds to finance their business customers, and at times they increased their loan commitments to businesses beyond prudent limits. A few bank managers, too, began to concern themselves excessively with maximizing short-run profits, so that the prices quoted for their common stock would move higher. Capital ratios of many banks deteriorated; questionable loans were extended at home and

abroad; insufficient attention was given here and there to the risks of dealing in foreign exchange markets; and too much bank credit went into the financing of speculative real estate ventures.

A variety of loose practices also crept into State and local government finance. Faced with rapidly expanding demands for services and limited sources of revenue, some governmental units resorted to extensive short-term borrowing and employed dubious accounting devices to conceal their budget deficits. Statutory debt limits were circumvented through the creation of special public authorities to finance the construction of housing, schools, and health facilities. Some of these authorities issued so-called "moral obligation" bonds, which investors in many instances regarded as the equivalent of "full faith and credit" obligations. The novel financial devices seemed innocuous at the time, but they have recently become a source of serious concern to investors in municipal securities.

A nation cannot realistically expect prosperous economic conditions to continue very long when the Federal Government fails to heed the warning signs of accelerating inflation, when many of its business leaders spend their finest hours arranging financial maneuvers, and when aggressive trade unions push up wage rates far beyond productivity gains. After 1965, the strength of the American economy was gradually sapped by these ominous trends. Productivity in the private nonfarm sector, which had grown at an annual rate of 3.6 per cent from 1961 through 1964, slowed to a 2.2 per cent rate of advance from 1964 to 1969, then to 1.5 per cent from 1969 to 1974. Expansion in the physical volume of national output likewise declined during successive quinquennia. The rate of inflation, meanwhile, kept accelerating.

With the pace of inflation quickening, seeds of the current recession were thus sown across the economy. Rising prices eroded the purchasing power of workers' incomes and savings. Corporate profits diminished—a fact that businessmen were slow to recognize because of faulty accounting techniques. New dwellings were built on a scale that greatly exceeded the underlying demand. Inventories of commodities piled up, often at a fantastic pace, as businessmen reacted to gathering fears of shortages. Credit demands, both public and private, soared and interest rates rose to unprecedented heights.

These basic maladjustments are now being worked out of the economic system by recession—a process that entails enormous human and financial costs. Our country has gone a considerable distance in developing policies to alleviate economic hardships, and these policies have been strengthened recently. Nevertheless, the recession has wrought great damage to the lives and fortunes of many of our people.

This recession has cut deeply into economic

activities. It must not, however, be viewed as being merely a pathological phenomenon. Since we permitted inflation to get out of control, the recession is now performing a painful—but also an unavoidable—function.

First, it is correcting the imbalances that developed between the production and sales of many items, also between orders and inventories, between capital investment and consumer spending, and between the trend of costs and prices.

Second, business managers are responding to the recession by moving energetically to improve efficiency—by concentrating production in more modern and efficient installations, by eliminating wasteful expenditures, by stimulating employees to work more diligently, and by working harder themselves.

Third, the recession is improving the condition of financial markets. Interest rates have moved to lower levels as a result of declining credit demands and of the Federal Reserve's efforts to bolster the growth of money and credit. Commercial banks have taken advantage of the reduced demand for loans to repay their borrowings from Federal Reserve Banks, to reduce reliance on volatile sources of funds, and to rebuild liquid assets. The rapidly rising inflow of deposits to thrift institutions has likewise permitted a reduction of indebtedness and addition to their liquid assets.

Fourth, the recession is wringing inflation out of the economic system. Wholesale prices of late have moved down, and the rise of consumer prices has also slowed. Although general price stability is not yet in sight, a welcome element of price competition has at long last been restored to our markets.

These and related business developments are paving the way for recovery in economic activity. No one can foresee with confidence when the recovery will begin. The history of our country indicates clearly, however, that the culminating downward phase of a long cycle need not be of protracted duration.

Signs are multiplying, in fact, that an upturn in economic activity may not be far away. For example, employment rose in April after six successive months of decline. The length of the workweek also stabilized last month. The rate of layoffs in manufacturing is now turning down, and some firms have been recalling workers who formerly lost their jobs. Sales of goods at retail—apart from autos—have risen further. Business and consumer confidence has been improving. And prospects for an early upturn in economic activity have been strengthened by passage of the Tax Reduction Act of 1975.

Our nation stands at present at a crossroads in its history. With the long and costly cycle in business activity apparently approaching its end, the critical task now is to build a solid foundation for our nation's economic future. We will accomplish that

only if we understand and benefit from the lessons of recent experience.

Since World War II, a consensus has been building in this country that the primary task of economic policy is to maintain full employment and promote maximum economic growth. We have pursued these goals by being ever ready to stimulate the economy through increased Federal spending, lower taxes, or monetary ease. Neglect of inflation and of longer-run economic and financial problems, has thus crept insidiously into public policy making. Our Government has become accustomed to respond with alacrity to any hint of weakness in economic activity, but to react sluggishly, and sometimes not at all, to signs of excess demand and developing inflationary pressures.

The thinking of many of our prominent economists has encouraged this bias in our economic policies. During the 1950's and 1960's, they frequently argued that "creeping inflation" was a small price to pay for full employment. Some even suggested that a little inflation was a good thing—that it energized the economic system and thus promoted rapid economic growth.

This is a dangerous doctrine. While inflation may begin slowly in an economy operating at high pressure, it inevitably gathers momentum. A state of euphoria then tends to develop, economic decision-making becomes distorted, managerial and financial practices deteriorate, speculation becomes rampant, industrial and financial imbalances pile up, and the strength of the national economy is slowly but surely sapped. That is the harsh truth that the history of business cycles teaches.

To emphasize this truth, I should now like to offer this distinguished group of journalists a bit of professional advice. Since few of you are reluctant to pass along hints as to how I should do my job, I have decided to suggest to you what the really big economic news story of 1975 is likely to be.

The story has to do with the drama now unfolding on Capitol Hill in the implementation of the Budget Control Act adopted last year. If I am right in thinking that our present economic difficulties are largely traceable to the chronic bias of the Federal budget toward deficits, there can be no doubt about the importance of what is now being attempted.

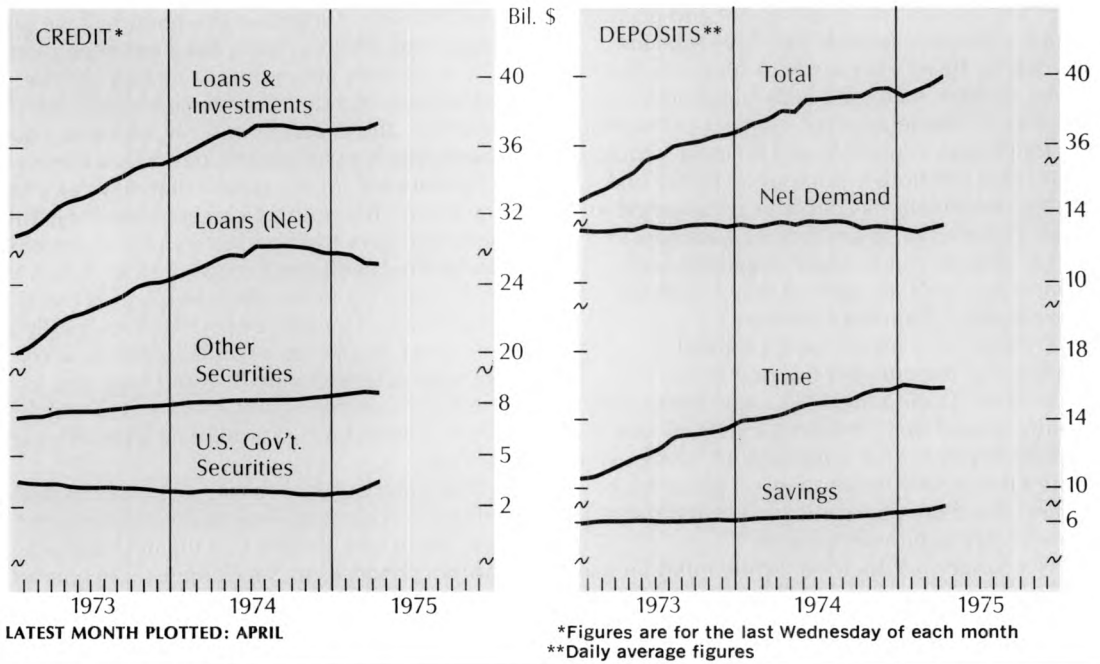
No major democracy that I know of has a more deficient legislative budget process than the United States—with revenue decisions separated from spending decisions and the latter handled in piecemeal fashion. Budgets in this country have just happened. They certainly have not been planned.

We are now attempting to change that by adopting integrated Congressional decisions on revenues and expenditures. My advice to you journalists is to follow this new effort closely. It has a significance for our nation that may carry far into the future. But nothing can be taken for granted here. We have tried budgetary reform once before under the Legislative Reorganization Act of 1946, and it failed. It failed partly because of the challenge to cherished Committee prerogatives, partly also because Congress as a whole balked at accepting so much self-discipline. I would urge you to study the history of that earlier effort and to watch the present undertaking for tell-tale signs of similar faltering.

The potential gain for our nation from budget reform is enormous even in this first year of "dry run." If, in fact, the work of the new budget committees produces in the Congress a deeper understanding of the impossibility of safely undertaking all the ventures being urged by individual legislators, a constructive beginning toward a healthier economic environment will have been made. On the other hand, if the new budget procedures are scuttled, or if they are used with little regard to curbing the bias toward large-sized Federal deficits, there ultimately may be little anyone can do to prevent galloping inflation and social upheaval.

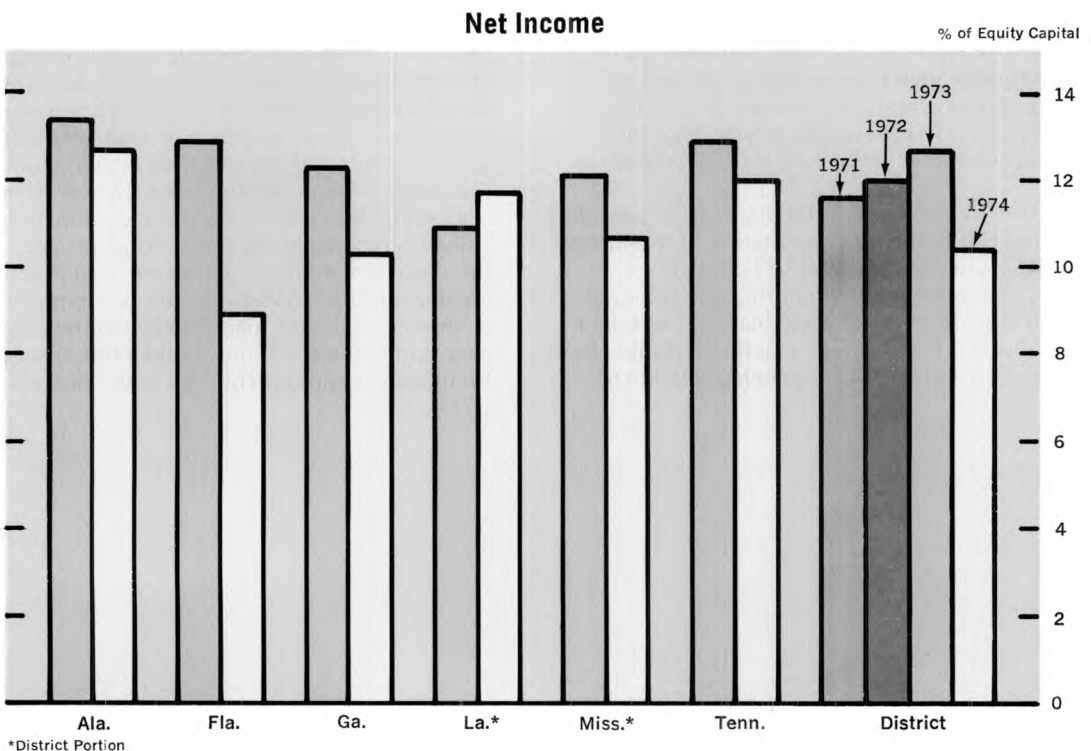
I am inclined to be optimistic about the outcome. More and more of our people are becoming concerned about the longer-range consequences of Federal financial policies. Perspective on our nation's economic problems is gradually being gained by our citizens and their Congressional representatives. A healthy impatience with inflation is growing. You journalists are becoming more actively involved in the educational process. I therefore remain hopeful that we shall practice greater foresight in dealing with our nation's economic problems than we have in the recent past, and that we will thus build a better future for ourselves and our children in the process.

# BANKING STATISTICS



## SIXTH DISTRICT BANKING NOTES

# 1974: Lower Bank Earnings



District banks experienced strong demands for credit and rising interest rates during 1974. Though record interest rates on loans pushed operating income to new highs, banks were also forced to pay record interest rates for funds. As a result, operating expenses rose more than income and profitability declined. Net income, as a percentage of equity capital, for District member banks declined from 12.7 percent in 1973 to 10.4 percent last year. Even though earnings were down, banks tended to maintain their cash dividends by paying out a larger portion of net income.

Earnings declined in five District states; the largest drop was in Florida. Alabama banks posted the smallest decline and continued with the highest earnings rate in the District. After declining in 1973, Louisiana banks again bucked the District trend by exhibiting higher earnings in 1974.

Increased income usually leads to higher earnings, but this is not always the case. While banks collected more income in interest from loans and investments, they also had to pay much higher interest rates for deposits and borrowed funds. These crosscurrents worked to the disadvantage of many banks.

Because of a strong loan demand, District banks increased their portfolios, at the same time cutting back on securities relative to total assets. Larger relative volumes and a higher return on loans (9.35 percent in 1974 compared to 8.52 percent in 1973) increased the proportion of total income derived from lending. Part of the higher loan interest, however, was offset by increased losses on loans and additional provisions for such losses. Real estate

#### SOURCES AND USES OF BANK INCOME\*

INCOME	1973 (percent)	1974
Loans	65.9	68.8
Treasury securities	8.9	7.1
State and municipal obligations	9.6	9.3
<b>EXPENSES</b>		
Interest on deposits	36.7	40.4
Interest on borrowed money	1.7	2.3
Employee expenses	20.6	20.0
Provision for loan losses	2.4	3.6
Taxes	4.1	2.5

\*Expressed as a percentage of total operating income

loans, though they grew the most, seem to have caused much of the problem.

The major factor accounting for last year's sharply higher expenses was higher interest costs. The average rate of interest paid on time deposits rose

Note: Data based on "1974 Operating Ratios, Sixth District Member Banks," now available upon request (max. 10 copies).

#### RATES OF RETURN ON ASSETS AND INTEREST ON DEPOSITS

	1973 (percent)	1974
Loans (including Federal funds)	9.52	10.67
Loans (excluding Federal funds)	8.52	9.35
Treasury securities	6.01	6.72
State and municipal obligations	4.36	4.70
Interest on all time deposits	5.38	6.25

from 5.38 percent to 6.25 percent; such payments equal 40 percent of total income. Interest on borrowed funds such as Federal funds purchased, a major expense for most large banks, was also much higher. And at times last year banks had to pay more for Federal funds than the interest rates they charged their prime customers for loans. One large expense, employee wages and salaries, declined in relation to total costs.

The earnings decline affected every size of bank, though in different ways. The smallest banks (deposits of less than \$10 million) tended to have the lowest earnings level. These banks have relatively higher salary and occupancy expenses. They also experienced a large increase in interest payments on

#### DISTRIBUTION OF ASSETS\* AND LIABILITIES

	1973 (percent)	1974
Loans	52.7	54.8
Treasury securities	9.8	7.7
State and municipal obligations	14.1	14.3
Gross loans	52.7	54.8
Cash assets	13.1	12.9
Time deposits to total deposits	53.8	56.5

\*as a percent of total assets

time deposits. And since these banks tend to concentrate on loans with relatively constant rates of return (real estate and consumer instalment lending), they were less able to take advantage of the increasing returns on other loans available throughout most of last year.

The very largest District banks, in contrast, were able to spread salary and occupancy expenses over a large asset base; also, they tended to make more business loans, which allow quicker adjustment to other borrowing costs. These banks' earnings suffered most from much higher interest payments on deposits and borrowed funds, expenses that amounted to three-fifths of total operating expenses.

JOHN M. GODFREY

# Sixth District Statistics

## Seasonally Adjusted

(All data are indexes, unless indicated otherwise.)

		Latest Month 1975	One Month Ago	Two Months Ago	One Year Ago		Latest Month 1975	One Month Ago	Two Months Ago	One Year Ago
<b>SIXTH DISTRICT</b>						Unemployment Rate (Percent of Work Force)	Apr.	9.8	10.2	9.5
<b>INCOME AND SPENDING</b>						Avg. Weekly Hrs. in Mfg. (Hrs.)	Apr.	38.0	38.4	40.4
Manufacturing Payrolls	Apr.	170.6	168.2	170.2	172.3	<b>FINANCE AND BANKING</b>				
Farm Cash Receipts	Mar.	224	214	254	203	Member Bank Loans	Apr.	265	267	249
Crops	Mar.	391	308	354	218	Member Bank Deposits	Apr.	216	214	202
Livestock	Mar.	177	188	194	203	Bank Debits**	Apr.	310	294	280
Instalment Credit at Banks* (Mil.\$)						<b>FLORIDA</b>				
New Loans	Apr.	568	522	628	687	<b>INCOME</b>				
Repayments	Apr.	613	604	714	643	Manufacturing Payrolls	Apr.	178.7	180.7	179.4
<b>EMPLOYMENT AND PRODUCTION</b>						Farm Cash Receipts	Mar.	309	249	229
Nonfarm Employment	Apr.	129.9	130.3	131.1	134.5	<b>EMPLOYMENT</b>				
Manufacturing	Apr.	107.8	107.5	109.1	119.7	Nonfarm Employment	Apr.	149.6	149.8	150.1
Nondurable Goods	Apr.	106.7	105.9	108.0	116.7	Manufacturing	Apr.	117.6	117.2	118.5
Food	Apr.	104.5	104.5	104.0	106.4	Nonmanufacturing	Apr.	155.8	156.1	156.2
Textiles	Apr.	96.4	95.2	96.5	114.2	Construction	Apr.	158.3	162.1	167.4
Apparel	Apr.	102.0	101.1	104.3	115.8	Farm Employment	Mar.	80.8	75.3	77.2
Paper	Apr.	104.9	105.0	107.5	114.2	Unemployment Rate				
Printing and Publishing	Apr.	123.7	125.0	126.0	131.0	(Percent of Work Force)	Apr.	12.3	10.7	9.5
Chemicals	Apr.	105.4	105.7	107.9	110.4	Avg. Weekly Hrs. in Mfg. (Hrs.)	Apr.	39.2	39.9	39.5
Durable Goods	Apr.	109.2	109.5	110.5	123.4	<b>FINANCE AND BANKING</b>				
Lbr., Wood Prods., Furn. & Fix.	Apr.	94.5	94.0	95.9	111.2	Member Bank Loans	Apr.	288	301	308
Stone, Clay, and Glass	Apr.	116.8	116.6	119.1	130.9	Member Bank Deposits	Apr.	240	242	241
Primary Metals	Apr.	102.9	103.9	106.6	114.6	Bank Debits**	Apr.	303	309r	296
Fabricated Metals	Apr.	121.2	121.8	122.8	134.5	<b>GEORGIA</b>				
Machinery	Apr.	149.8	150.4	151.4	164.7	<b>INCOME</b>				
Transportation Equipment	Apr.	97.5	97.5	96.5	110.3	Manufacturing Payrolls	Apr.	150.0	149.1	151.5
Nonmanufacturing	Apr.	137.7	138.4	138.9	139.8	Farm Cash Receipts	Mar.	202	218	244
Construction	Apr.	133.1	136.4	141.0	160.3	<b>EMPLOYMENT</b>				
Transportation	Apr.	123.4	123.6	124.8	127.7	Nonfarm Employment	Apr.	124.5	125.1	125.9
Trade	Apr.	134.3	135.1	135.6	138.2	Manufacturing	Apr.	98.8	97.8	98.2
Fin., ins., and real est.	Apr.	149.9	150.3	151.1	153.2	Nonmanufacturing	Apr.	136.3	137.6	138.3
Services	Apr.	153.9	154.3	154.7	151.7	Construction	Apr.	124.0	128.2	133.2
Federal Government	Apr.	105.0	106.0	106.2	104.0	Farm Employment	Mar.	104.0r	104.6r	99.0r
State and Local Government	Apr.	143.7	143.5	142.8	137.1	Unemployment Rate				
Farm Employment	Mar.	94.1r	93.8r	92.2r	98.5r	(Percent of Work Force)	Apr.	10.3	11.5	11.2
Unemployment Rate	Apr.	10.2	10.1	9.3	5.1	Avg. Weekly Hrs. in Mfg. (Hrs.)	Apr.	38.7	37.9	38.3
Insured Unemployment						<b>FINANCE AND BANKING</b>				
(Percent of Gov. Emp.)	Apr.	6.9	6.7	6.1	2.2	Member Bank Loans	Apr.	248	250	256
Avg. Weekly Hrs. in Mfg. (Hrs.)	Apr.	38.8	38.6	38.9	39.7	Member Bank Deposits	Apr.	195	191	190
Construction Contracts*	Apr.	163	224	153	228	Bank Debits**	Apr.	381	353	326
Residential	Apr.	133	131	110	247	<b>LOUISIANA</b>				
All other	Apr.	191	316	195	210	<b>INCOME</b>				
Cotton Consumption**	Mar.	56	54	53	86	Manufacturing Payrolls	Apr.	167.0	169.4	166.3
Manufacturing Production	Mar.	139.8	141.4	142.6	147.7	Farm Cash Receipts	Mar.	239	181	346
Nondurable Goods	Mar.	142.6	144.6	144.4	146.8	<b>EMPLOYMENT</b>				
Food	Mar.	135.9	135.6	135.0	131.1	Nonfarm Employment	Apr.	120.2	120.9	121.2
Textiles	Mar.	136.5	136.9	137.0	148.2	Manufacturing	Apr.	107.2	107.4	108.0
Apparel	Mar.	117.9	120.9	125.1	137.3	Nonmanufacturing	Apr.	122.9	123.7	124.0
Paper	Mar.	132.4	133.7	135.5	135.4	Construction	Apr.	105.5	107.6	109.2
Printing and Publishing	Mar.	126.3	127.3	127.9	133.3	Farm Employment	Mar.	102.5	102.7	64.5
Chemicals	Mar.	160.4	159.7	156.7	155.4	Unemployment Rate				
Durable Goods	Mar.	135.5	136.6	139.7	149.6	(Percent of Work Force)	Apr.	8.1	8.4	8.8
Lumber and Wood	Mar.	129.3	126.2	120.2	149.5	Avg. Weekly Hrs. in Mfg. (Hrs.)	Apr.	38.6	39.5	38.8
Furniture and Fixtures	Mar.	115.2	117.1	121.4	152.0	<b>FINANCE AND BANKING</b>				
Stone, Clay, and Glass	Mar.	135.5	142.3	144.8	157.5	Member Bank Loans*	Apr.	253	261	253
Primary Metals	Mar.	101.4	102.7	105.2	109.2	Member Bank Deposits*	Apr.	207	207	201
Fabricated Metals	Mar.	111.3	112.6	116.1	131.3	Bank Debits*/**	Apr.	261	259	253
Nonelectrical Machinery	Mar.	151.3	153.8	156.7	147.6	<b>MISSISSIPPI</b>				
Electrical Machinery	Mar.	226.7	227.8	232.4	250.7	<b>INCOME</b>				
Transportation Equipment	Mar.	122.4	121.8	128.1	127.1	Manufacturing Payrolls	Apr.	195.9	193.0	195.4
<b>FINANCE AND BANKING</b>						Farm Cash Receipts	Mar.	230	215	329
Loans*						<b>EMPLOYMENT</b>				
All Member Banks	Apr.	267	276	278	272	Nonfarm Employment	Apr.	126.5	127.5	128.3
Large Banks	Apr.	250	255	261	254	Manufacturing	Apr.	118.6	119.5	121.3
Deposits*						Nonmanufacturing	Apr.	130.2	131.2	131.5
All Member Banks	Apr.	219	219	217	210	Construction	Apr.	125.9	135.0	140.5
Large Banks	Apr.	192	193	188	181	Farm Employment	Mar.	86.2	85.2	84.6
Bank Debits*/**	Apr.	308	303r	287	293	<b>ALABAMA</b>				
<b>ALABAMA</b>						<b>INCOME</b>				
<b>INCOME</b>						Manufacturing Payrolls	Apr.	172.2	170.6	176.4
Manufacturing Payrolls	Apr.	172.2	170.6	176.4	181.8	Farm Cash Receipts	Mar.	204	233	300
Farm Cash Receipts	Mar.	204	233	300	217	<b>EMPLOYMENT</b>				
<b>EMPLOYMENT</b>						Nonfarm Employment	Apr.	118.3	118.5	120.1
Nonfarm Employment	Apr.	118.3	118.5	120.1	121.9	Manufacturing	Apr.	106.1	105.8	109.3
Manufacturing	Apr.	106.1	105.8	109.3	118.4	Nonmanufacturing	Apr.	123.8	124.3	125.0
Nonmanufacturing	Apr.	123.8	124.3	125.0	123.4	Construction	Apr.	131.4	131.2	134.3
Construction	Apr.	131.4	131.2	134.3	141.2	Farm Employment	Mar.	113.6	112.7	115.6
Farm Employment	Mar.	113.6	112.7	115.6	125.0r	<b>JUNE 1975, MONTHLY REVIEW</b>				

		Latest Month	One Month Ago	Two Months Ago	One Year Ago
Unemployment Rate (Percent of Work Force)	Apr.	8.4	8.5	7.6	3.7
Avg. Weekly Hrs. in Mfg. (Hrs.)	Apr.	38.8	38.1	38.5	39.2

#### FINANCE AND BANKING

Member Bank Loans*	Apr.	248	266	263	257
Member Bank Deposits*	Apr.	217	217	215	216
Bank Debits**	Apr.	259	255r	237	260

#### TENNESSEE

##### INCOME

Manufacturing Payrolls	Apr.	172.1	167.0	171.1	174.5
Farm Cash Receipts	Mar.	197	244	184	205

\*For Sixth District area only; other totals for entire six states

\*\*Daily average basis

†Preliminary data

r-Revised

N.A. Not available

Note: All indexes: 1967=100.

Sources: Manufacturing production estimated by this Bank; nonfarm, mfg. and nonmfg. emp., mfg. payrolls and hours, and unemp., U.S. Dept. of Labor and cooperating state agencies; cotton consumption, U.S. Bureau of Census; construction contracts, F. W. Dodge Div., McGraw-Hill Information Systems Co.; farm cash receipts and farm emp., U.S.D.A. Other indexes based on data collected by this Bank. All indexes calculated by this Bank.

†Data benchmarked to June 1971 Report of Condition.

#### EMPLOYMENT

Nonfarm Employment	Apr.	125.1	125.5	126.9	129.4
Manufacturing	Apr.	107.5	107.5	109.4	119.9
Nonmanufacturing	Apr.	134.9	135.5	136.6	134.7
Construction	Apr.	135.8	138.4	146.0	139.8
Farm Employment					
Unemployment Rate (Percent of Work Force)	Apr.	9.0	9.6	7.8	4.3
Avg. Weekly Hrs. in Mfg. (Hrs.)	Mar.	89.8	93.6	94.0	91.4r

#### FINANCE AND BANKING

Member Bank Loans*	Apr.	274	291	287	258
Member Bank Deposits*	Apr.	220	224	220	203
Bank Debits**	Apr.	258	276	260	265

# Debits to Demand Deposit Accounts

## Insured Commercial Banks in the Sixth District (In Thousands of Dollars)

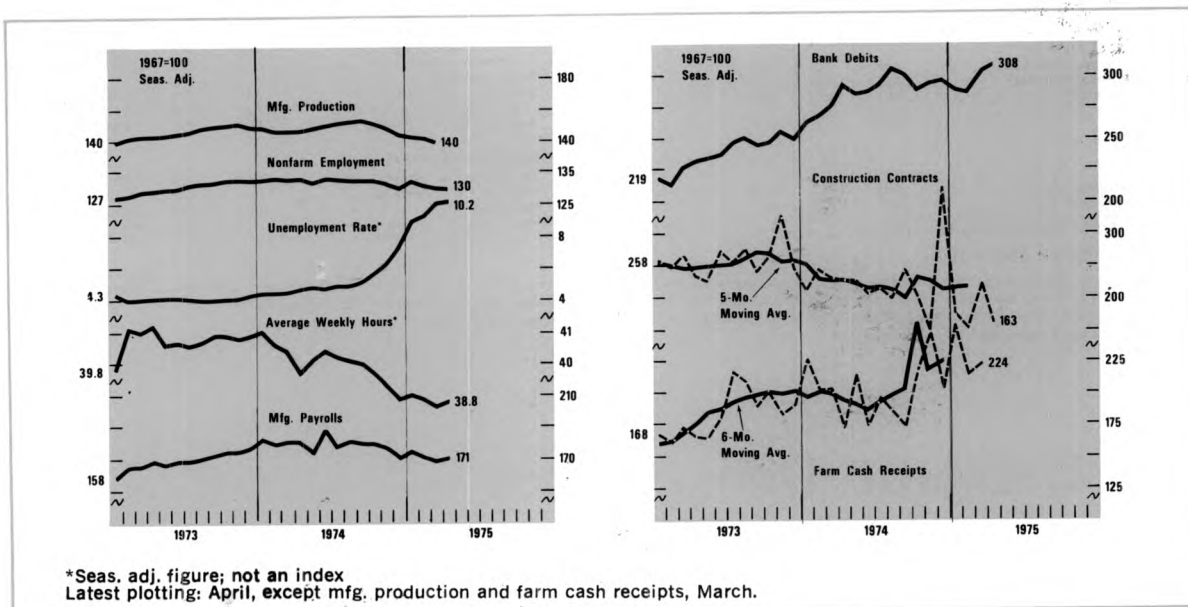
Percent Change							Percent Change												
			Year to date 4 mos. from 1975					Year to date 4 mos. from 1975											
	April 1975	March 1975	April 1974	Mar. 1975	Apr. 1974	from 1974		April 1975	March 1975	April 1974	Mar. 1975	Apr. 1974	from 1974						
STANDARD METROPOLITAN STATISTICAL AREAS <sup>1</sup>																			
Birmingham	5,815,746	5,213,832	4,393,125	+12	+32	+24	Bradenton	214,283	201,863	220,293	+6	-3	+3						
Gadsden	107,292	99,576	108,759	+8	-1	+2	Monroe County	125,398	142,448	119,789	-12	+5	+9						
Huntsville	402,409	398,694	359,123	-1	+12	+21	Ocala	251,772	225,667	219,551	+12	+15	+6						
Mobile	1,510,229	1,396,602	1,228,559	+8	+23	+26	St. Augustine	46,296	49,474	64,938	-6	-29	-23						
Montgomery	860,170	738,199	684,067	+17	+26	+17	St. Petersburg	1,106,088	962,494	1,133,289	+15	-2	-2						
Tuscaloosa	274,789	257,096	252,197	+7	+9	+7	Tampa	2,456,866	2,197,768	2,196,051	+12	+12	+9						
Bartow-Lakeland-Winter Haven																			
Daytona Beach	909,589	860,623	803,434	+6	+13	+9	Athens	169,488	165,782	184,552	+2	-8	+1						
Ft. Lauderdale-Hollywood	543,237	483,914	496,244	+12	-9	+15	Brunswick	124,973	116,003	118,863	+8	+5	+20						
Ft. Myers	2,197,921	1,878,105	2,331,826	+17	-6	-4	Dalton	180,924	157,850	196,240	+15	-8	-14						
Gainesville	477,695	445,890	415,941	+7	-15	+8	Elberton	28,500	25,982	30,043	+10	-5	+5						
Jacksonville	285,117	286,469	286,585	-0	-1	+6	Gainesville	176,855	163,605	165,431	+8	+7	+9						
Melbourne	5,061,661	4,921,194	5,023,580	+3	-1	-1	Griffin	77,538	69,260	95,290	+12	-19	-10						
Titusville-Cocoa	478,973	456,796	514,659	+5	-7	+5	LaGrange	38,345	39,876	52,736	-4	-27	-15						
Miami	7,756,151	7,302,095	7,888,835	+6	-2	-1	Newnan	50,241	43,477	59,617	+16	-16	-14						
Orlando	1,729,627	1,564,279	1,687,774	+11	+2	-2	Rome	165,620	157,446	165,521	+5	+0	+3						
Pensacola	511,659	516,670	477,061	-1	-7	+16	Valdosta	118,224	109,106	114,728	+8	+3	+8						
Sarasota	610,162	545,104	621,469	+12	-2	+2	Abbeville	19,449	18,915	18,507	+3	+5	+11						
Tallahassee	1,014,988	1,170,233	933,039	-13	+9	+2	Bunkie	17,708	17,401	12,327	+2	+44	+34						
Tampa-St. Pete	4,670,570	4,245,402	4,486,879	+10	+4	+1	Hammond	117,847	111,708	96,669	+5	+22	+34						
W. Palm Beach	1,268,676	1,298,338	1,484,807	+2	-15	-4	New Iberia	88,381	88,379	72,165	+0	+22	+33						
Albany																			
Atlanta	191,476	185,396	224,815	+3	-15	-4	Plaquemine	29,411	32,115	24,355	-8	+21	+30						
Augusta	23,191,372	19,494,214	21,831,289	-19	+6	+6	Thibodaux	74,271	68,809	41,221	+8	+80	+71						
Columbus	660,043	630,502	664,350	-5	-1	+8	Hattiesburg	149,210	151,160	143,964	-1	+4	+15						
Macon	503,324	455,134	492,807	+11	+2	+2	Laurel	85,663	77,280	88,056	+11	-3	+1						
Savannah	862,580	818,046	796,033	+5	+8	+13	Meridian	136,488	120,054	141,043	-14	-3	+2						
Alexandria	1,022,588	969,055	597,159	+6	+71	+68	Natchez	62,988	54,233	60,559	+16	+4	+7						
Baton Rouge	316,682	331,531	289,221	-4	+9	+10	Pascagoula												
Lafayette	1,995,526	1,903,051	1,593,069	+5	+25	+38	Moss Point	152,626	181,599	156,059	-16	-2	+4						
Lake Charles	421,327	376,154	309,814	+12	+36	+33	Vicksburg	80,579	75,768	91,175	+6	-12	-11						
New Orleans	291,050	271,125	281,607	+7	+3	+12	Yazoo City	54,650	52,429	53,457	+4	+2	+4						
Biloxi-Gulport	5,769,502	5,476,521	5,147,463	+5	+12	+13	Bristol	148,181	149,755	147,035	-1	+1	+17						
Jackson	312,768	284,203r	254,769	+10	+23	+18	Johnson City	181,929	173,483	196,011	+5	-7	-0						
Chattanooga	1,710,050	1,656,263	1,787,249	+3	-4	+9	Kingsport	326,636	356,381	308,353	-8	+6	+9						
Knoxville	1,283,410	1,300,110	1,386,500	-1	-7	-8	DISTRICT TOTAL							98,324,031	91,001,602r	93,405,524	+8	+5	+8
Nashville	1,577,568	1,669,234	2,001,952	-5	-21	-2	Alabama	12,429,289	11,194,767	9,825,146	+11	+27	+21						
OTHER CENTERS	4,703,678	4,638,890	4,240,712	+1	+11	+18	Florida	30,028,461	28,360,143r	30,572,896	+6	-2	-0						
Anniston	121,924	121,614r	122,399	+0	-0	+10	Georgia	30,671,954	26,830,394	28,973,013	+14	+6	+8						
							Louisiana	10,576,305	10,058,772	9,133,325	+5	+16	+19						
							Mississippi	3,594,940	3,430,534r	3,601,171	+5	-0	+6						
							Tennessee	11,023,082	11,126,992	11,299,973	-1	-2	+8						

<sup>1</sup>Conforms to SMSA definitions as of December 31, 1972.

r-Revised

Figures for some areas differ slightly from preliminary figures published in "Bank Debits and Deposit Turnover" by Board of Governors of the Federal Reserve System.

# District Business Conditions



Some encouraging signs were intermingled with lingering weakness in the Southeastern economy. Job gains in manufacturing tempered April's rise in unemployment. Consumer instalment credit declined at a more moderate rate. Agriculture benefited from rising livestock prices, improved planting weather, and strong farm cash receipts. District banks received increasing amounts of consumer savings deposits, but construction sagged as the nonresidential sector weakened.

Despite an upturn in manufacturing jobs, total nonfarm employment declined in April. The unemployment rate rose only moderately, however, because some workers stopped seeking jobs. Workers were recalled in several manufacturing industries; in others, job losses were halted. Textiles and apparel both showed significant job gains at the same time that the average workweek and hourly earnings increased. The employment slide in nonmanufacturing and construction continued, with only state and local government showing gains.

Consumers' instalment indebtedness to commercial banks, buffeted by conflicting currents, continued to ebb during April. Automobile and non-automotive consumer goods credit receded further. Home repair and modernization credit was essentially unchanged, while personal loans outstanding rose for the second consecutive month, primarily as a result of increased loan extensions. New auto registrations for March sank 16 percent below the year-ago level, documenting the prolonged weakness of auto sales. Department store sales in March were buoyed by an early Easter.

Following five consecutive months of decline, prices of farm products stabilized in April and may have turned upward in May, owing to rising cotton

and livestock prices. Hog prices, in particular, have moved sharply above year-ago levels, reflecting a severe curtailment in pork production. Broiler placements have also increased but remain under the comparable 1974 level. Crop planting progressed rapidly, following earlier delays from heavy rainfall. Cash farm receipts, boosted by crop sales in Florida and Louisiana, continued strong through the first quarter of the year.

District member banks continued to experience sizable deposit gains during May. Inflows of pass-book savings deposits have accounted for over one-half of the increase. The larger banks reported that business loan demand remained weak; the businesses paying off loans are mostly service firms, wholesale and retail trade establishments, food products industries, and the textile and apparel industries.

The value of construction contracts declined in April. The nonresidential sector accounted for all of the drop as it failed to maintain March's unusually high level. The value of residential contracts remained at the same level recorded in March because reductions in Florida were offset by gains in other states. Large deposit inflows continued at savings and loan associations, but residential mortgage rates crept upward.

Note: Data on which statements are based have been adjusted whenever possible to eliminate seasonal influences.