

MONTHLY *Business Review*

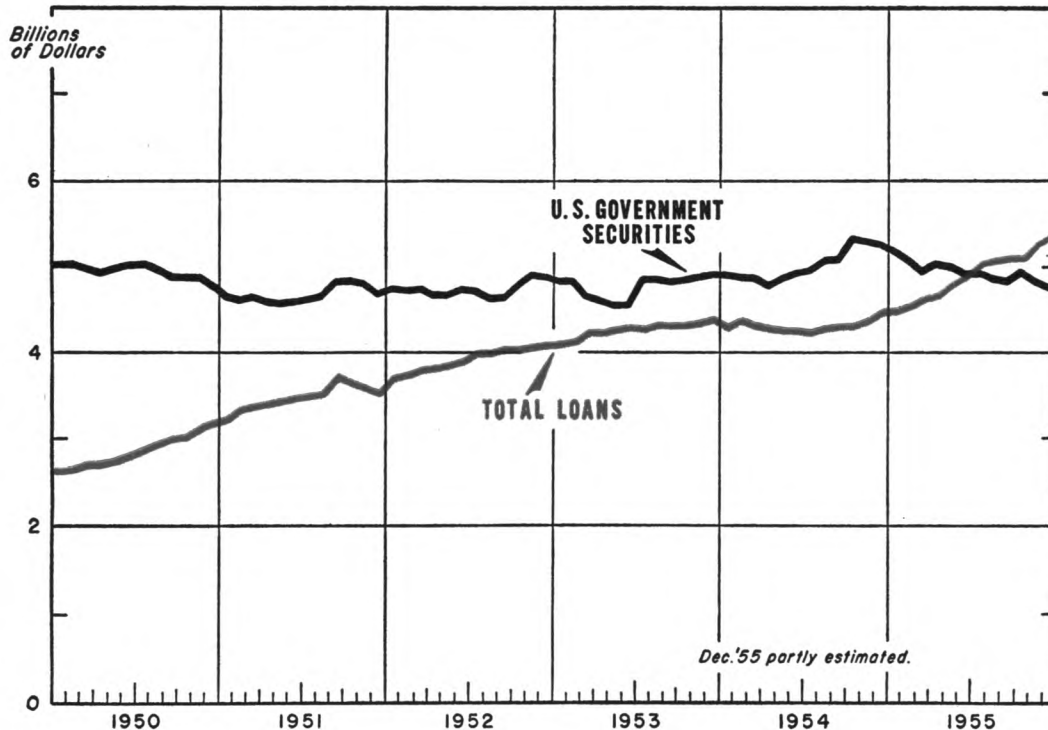
FEDERAL RESERVE BANK of CLEVELAND

January 1956

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LOANS OUTSTANDING AND HOLDINGS OF U.S. GOVERNMENT SECURITIES Fourth District Member Banks



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The Year in Fourth District Banking

THE YEAR OF 1955 opened on a note of confidence and promise with regard to the business outlook. By year end, the new records established by almost every major economic indicator made the previous forecasts seem too conservative.

The broad expansion of expenditures by consumers and business during the year brought heavy credit demands to financial markets. Rising outlays on goods and services were made possible not only by the high levels of income, but by a substantial expansion in credit of all types.

Both in the Fourth Federal Reserve District and in the nation, the resurgence of demand for loans at member banks marked a sharp contrast with the preceding year. It was a profitable year for District banks, even though the rate of expansion in their total of loans and investments was moderated by Federal Reserve policy aimed at promoting sustainable economic growth by restraining inflationary pressures.

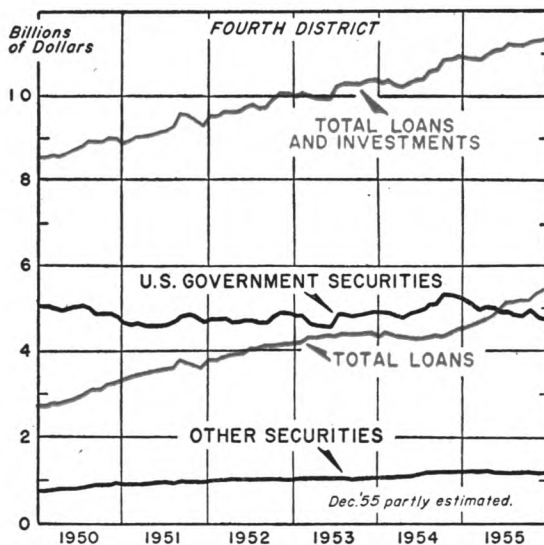
Moderate Rise in Bank Credit

The trend of credit extended by Fourth District member banks in recent years is shown in an accompanying chart. Total loans and investments rose by less than 31½ percent in 1955 — the smallest relative growth of the past five years. By way of contrast, during the recession year of 1954 the rise in total credit extended by District member banks was one of the largest in the postwar period.

The difference between the two years clearly illustrates the impact of the Federal Reserve policy of “leaning against the wind”—that is, promoting credit expansion in periods of downturn and moderating the rise of bank credit in periods of boom. Such a policy is brought to bear by actions that influence the reserve position and hence the credit-granting potential of banks, as discussed at a later point.

The moderate net growth of member bank credit in 1955 resulted from two sharply differing forces, both nationally and in the Fourth District: a vigorous upsurge in loans

The sharp upturn in loans at District member banks during 1955 was offset in part by a decline in their holdings of Government securities.



that was offset in large part by a decline in bank holdings of U. S. Government securities. In order to finance one of the heaviest totals of loan demand of recent years at a time when loanable funds were tight, banks found it necessary to dispose of a large volume of Government securities. (See chart.) For the most part these securities found their way, indirectly, into the hands of pension and trust funds and nonfinancial business corporations. Thus the growth of total bank credit—and deposits—was much less than the expansion in loans.

At Fourth District banks, loans rose by nearly \$900 million, or about 20 percent. One outcome of such a development was that, by mid-1955, total loans of District member banks had risen above their holdings of Treasury securities for the first time in many years.

Reserve City and Country Banks. The trends just noted for all Fourth District member banks conceal important differences between large banks, on the one hand, and medium- and small-size banks, on the other. Cyclical patterns in bank credit are generally more pronounced at large banks—as evidenced by development in 1955.

Loan expansion at member banks in the five *reserve cities* in the District was about 2½ times as large as that of all *country banks*.⁽¹⁾ At the same time, the entire year-to-year reduction in Government security holdings of District member banks, amounting to over \$500 million, occurred at reserve city banks. Country bank holdings of Treasury securities fell somewhat during the first quarter but then rose slowly for the balance of the year—with virtually no change for 1955 as a whole.

Similarly, trends in holdings of corporate and municipal securities differed between the two classes of District member banks. Reserve city banks reduced their holdings of such securities slightly during 1955, in contrast to the large expansion last year.

(1) The reserve cities are Cincinnati, Cleveland, Columbus, Pittsburgh, and Toledo. The 22 reserve city banks hold over half of the total resources of all District member banks.

Country banks, on the contrary, expanded their portfolios of corporate and municipal securities, as compared with a decline in 1954.

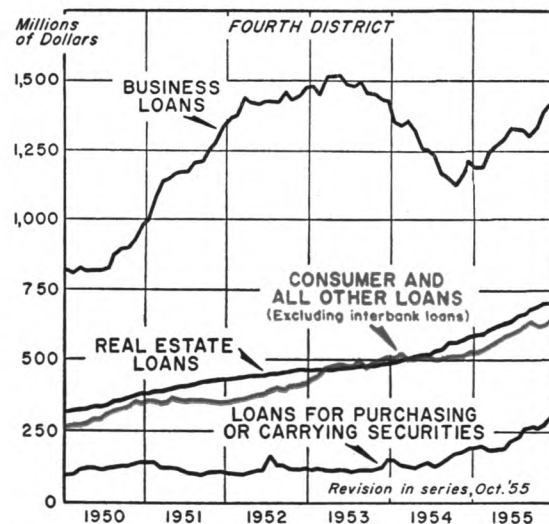
Despite the relatively greater loan expansion at reserve city banks, on net balance, the dollar volume of credit expansion at country banks was over twice as large as that at reserve cities.

Loan Trends

A more detailed picture of District loans trends is presented in an accompanying chart, dealing with leading-city banks which accounted for about 70 percent of the expansion of member bank loans in 1955.⁽²⁾

All types of loans expanded rapidly during the year—reflecting the broad base of the upturn in general business. The recovery that began late in 1954 was highlighted initially

All types of loans expanded rapidly at weekly reporting member banks during 1955—reflecting the broad base of the upturn in general business.



(2) The chart on loans applies to 17 weekly-reporting member banks, located in 6 cities, and holding over half of the resources of all District member banks. Business loans, as charted, include commercial, industrial, and agricultural loans. During October, 1955, a revision in loan classification by reporting banks produced the following changes: business loans, +\$34 million; loans for purchasing or carrying securities, -\$1 million; real estate loans, -\$1 million; and consumer and all other loans, -\$32 million.

by expansion of credit demands arising from growing consumer purchases of houses, autos, and household durables, as well as from a shift from liquidation to accumulation of business inventories. At a later point, credit demands were augmented by business outlays on construction and producers' durable equipment.

Business loans accounted for about 40 percent of total loan growth at weekly reporting banks in the Fourth District during the year. Mainly because of the importance of heavy industry in the District, the previous year's decline in business loans had started earlier, had lasted longer, and had gone further than in the nation as a whole. By the end of 1955, however, about three-fourths of the lost ground had been recovered.

In the manufacturing and mining category, loans to firms in petroleum, coal, chemicals, and rubber showed the largest dollar gain, followed by loans to firms producing metal and metal products. Borrowings by makers of textiles, apparel, and leather constituted the only category in manufacturing and mining to show a declining trend.

During the second half of 1955, the swelling demand for business loans was augmented by the usual seasonal rise in borrowings by food, liquor, and tobacco firms, by commodity dealers, and by concerns engaged in wholesale and retail trade.

As a reflection of the high level of building activity, business loans to construction firms rose steadily throughout the year. In addition, *real estate loans* showed a strong trend at District banks, rising even more sharply than the large expansion last year. Consumers have been buying houses—both old and new—at a record rate, with a greatly enlarged volume of mortgage credit.

The rise in consumer expenditures during 1955 on durable goods other than houses was also financed by heavy borrowing. Such credit demands were reflected in a record extension of business loans to sales finance companies by District member banks, and also in a sharp

growth of other loans to individuals (largely consumer loans).

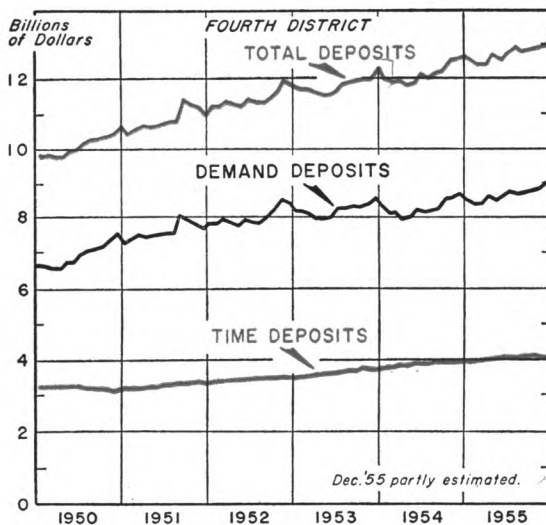
Deposits

The volume of commercial bank deposits varies largely with changes in bank loans and security holdings. A net increase in loans and investments of the banking system as a whole produces newly-created deposits, while deposits are reduced by a net decline in bank credit.

For any given region of the country, however, the direction of the inter-district flow of funds is a basic determinant of the ability of banks to expand credit. In periods of prosperity, the Fourth District tends to be on the receiving end of a net inflow of funds from other districts. The growth of deposits at District member banks during 1955 probably was attributable mainly to the above source, particularly at country banks. The inflow of funds from other districts permitted a large part of the growth of loans and investments discussed earlier.

The expansion in total deposits at Fourth

In contrast to the previous year, demand deposits of District member banks expanded substantially during 1955, while the growth of time deposits slowed down.



District member banks amounted to about 4 percent, somewhat better than last year. The pattern of demand and time deposits differed from that of last year, however. As might be expected in a period of high-level business activity, about four-fifths of the deposit growth occurred in demand deposits. In 1954, by way of contrast, most of the expansion took place in time deposits—which are relatively inactive funds.

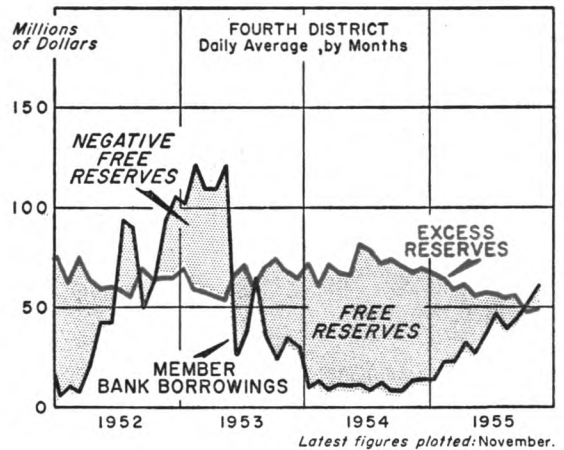
As in the case of total loans and investments, *country banks* accounted for over two-thirds of the expansion in total deposit accounts. Their share of the demand deposit growth was even larger.

Deposit Turnover. Not only did the volume of demand deposits at District member banks rise substantially more than last year, but the rate of spending of such accounts also increased. For the three months ended in November 1955, for example, the volume of checks written against privately-held demand deposits was 17 percent larger than in the year-ago period.

Since about 90 percent of all expenditures are made by means of checking accounts, the combination of larger demand deposits and a higher rate of turnover was a significant factor in the rising volume of consumer and business expenditures during the year. Both nationally and in the Fourth District, idle funds were transferred to spenders, and the available money supply was more fully utilized.

In large part, the activation of idle funds during 1955 was an outgrowth of the change in the composition of bank assets. As non-bank investors exchanged deposits for the U. S. securities sold to them in large volume by the banking system, the banks lent such funds to business and consumers who were borrowing in order to increase their outlays. Deposits created through loan expansion at banks thus tend to be more active, at least initially, than those created by the bank acquisition of Government securities.

With the decline in excess reserves and rise in member bank borrowings, the free reserves of District member banks declined steadily throughout 1955 and became negative in the late months of the year.



Reserve Position

Sales of Government securities by member banks in order to meet part of the heavy loan demand in 1955 were an outgrowth of their tighter reserve position. An accompanying chart portrays one aspect of that developing tightness for District member banks — the downward trend of excess reserves and the rise in member bank borrowing. Consequently, the volume of free reserves—excess reserves less member bank borrowing—dwindled steadily throughout 1955 and became negative in the late months of the year.

The broad purpose of Federal Reserve policy during 1955 was to promote conditions conducive to sustainable non-inflationary growth in the economy. Thus policy actions were such as to moderate the growth of member bank reserves to a point consistent with the flow of goods and services. If total bank credit and deposits had risen as rapidly as bank loans during the year, the result would have been clearly inflationary.

Consequently, with restraint being exercised over the growth of member bank reserves, member banks had to adopt a number of

measures to meet the heavy loan demand; such steps tended to raise the cost and tighten the availability of bank credit.

Large-scale sales of Government securities by banks, both in the District and the nation, tended to lower the prices of such securities and raise their yields. The lower the prices of Governments, the more reluctant banks become to sell additional securities in order to make more loans.

At the same time, it became necessary to use existing reserves more fully. Excess reserves of District member banks (which are held mainly by country banks) declined steadily throughout the year. The continuation of this trend, which had begun with economic recovery in the second half of 1954, further reduced the liquidity and latent lending power of member banks.

With a view to obtaining reserve funds to help meet the persistent demand for credit, member banks borrowed increasingly larger amounts from the Federal Reserve Banks during the year. In light of this increased borrowing and the further growth of inflationary pressures, the Federal Reserve Banks raised their discount rates in several steps in April,

August, September and November. By year end, the cost of borrowing by member banks was $2\frac{1}{2}$ percent, compared with the rate of $1\frac{1}{2}$ percent which prevailed prior to April. In view of the higher cost, as well as the general reluctance of member banks to remain in debt for an extended period, the necessity to borrow reserve funds tended to reduce the availability and raise the cost of bank credit in general.

Free reserves of District member banks became negative in the fourth quarter of the year, while for all member banks in the nation, that situation had developed as early as August. With total member bank borrowing exceeding excess reserves, the present volume of member bank deposits is being supported by net borrowed reserves funds, which is the main significance of "negative free reserves". Such a situation tends to militate against overly-rapid further expansion in bank credit at a time when the demand for goods and services is pushing hard against the productive capacity of the economy. The augmenting of consumer and business incomes with borrowed purchasing power must be moderated, if rising prices are to be avoided and sustainable economic growth maintained.

ANNOUNCEMENT

Stock in the Federal Reserve Bank of Cleveland has been issued to the Society National Bank of Cleveland, Cleveland, Ohio. Upon the opening of the bank on January 16, 1956, it becomes a member of the Federal Reserve System.

The new bank will operate eight branches. Its capital structure is: Capital \$2,000,000, surplus \$2,500,000 and undivided profits \$500,000. Henry S. Sherman is chairman of the board of directors and Mervin B. France, president.

Department Store Trade in 1955

DEPARTMENT STORE TRADE in the Fourth Federal Reserve District surpassed all previous records during 1955. The sales total by the end of the year was 10 percent above 1954 and more than two percent greater than the previous all-time record set in 1953.

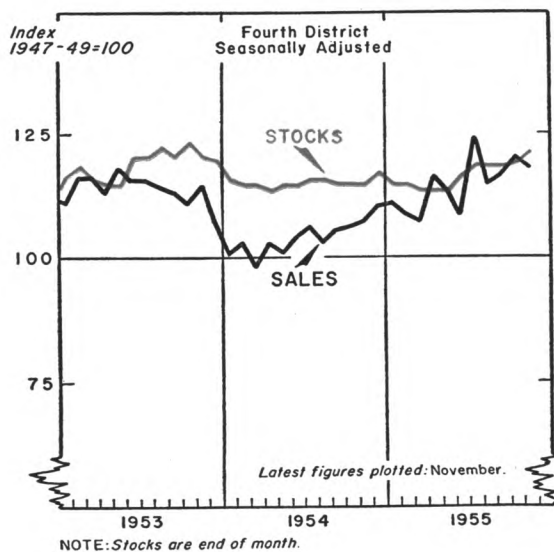
At the beginning of the year, the sales pace was more than seasonally strong, and adjusted sales for January were above December 1954 levels by a small margin. Such a brisk pace, however, was not maintained, and by March, the seasonally adjusted sales index had dropped back to 107 percent of the 1947-49

average. Part of the decline in March can probably be attributed to the bad weather of the final weeks of the month, at the time of early Easter shopping. Unusually strong Easter trade in April, however, raised adjusted sales to the highest levels in nearly two years, and, in addition, marked a full year during which sales of Fourth District department stores had been on an upward trend.

April sales remained as the high-water mark for the year until the exceptionally heavy volume of summer trade during July resulted in a higher level of adjusted sales. At an index level of 124, July sales not only marked the peak for the year, but also the highest position for seasonally adjusted sales in any month since the hectic "scare-buying" days in January, 1951.

Sales in the following months fell below the high July levels, but an upward trend was clearly discernible again in October and November. For the month of December, it is estimated that adjusted sales were within a few percentage points of the July peak, with the result that the annual average for 1955 was about 10 percent above 1954 and two percent above the previous record in 1953.

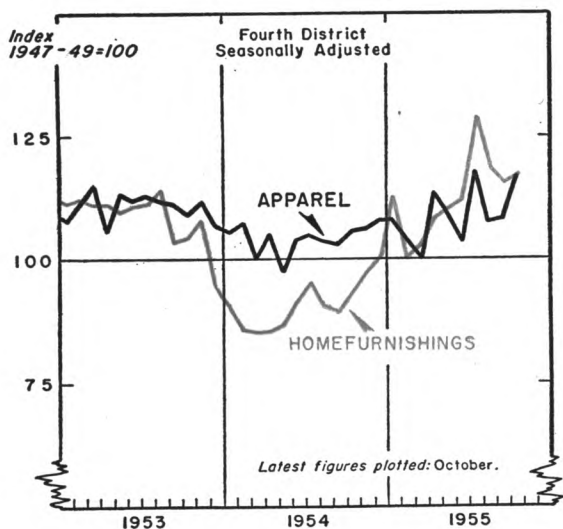
By the end of the year, Fourth District department store sales were 20% above the low position reached in 1954. Stocks rose more moderately.



Inventories

Inventories held by Fourth District department stores throughout 1955 followed an orderly and conservative pattern, with no wide swings caused either by heavy buying or by

Sales of homefurnishings rose sharply from last year's reduced volume. Apparel sales also rose.



liquidation of stocks. The range from the low to the high positions for the year amounted to only five percent on a seasonally adjusted basis, in spite of fluctuations in sales which were three times as great. The general trend of inventories through the year, however, was moderately upward. The average level for the year was approximately two percent below 1953 levels. A conservative handling of stocks during the year was apparent in most of the individual departments, both in the apparel and the homefurnishings lines.

Apparel and Homefurnishings

The rise in sales during 1955 was shared by both the apparel and homefurnishings lines which constitute the major divisions of department store offerings. The larger sector, as represented by apparel sales, showed a more moderate rate of gain than was the case for homefurnishings; the apparel sales pattern closely resembles that of total sales. Sales of apparel were exceptionally strong in July and October, after allowance for season-

al variation, and again during the Christmas trade season, according to preliminary reports.

The spectacular rise in sales of homefurnishings during 1955 brought such sales to a position only slightly below the peaks of 1950 and 1951. By July of 1955, when sales were apparently stimulated by demand for air conditioners and other appliances, seasonally adjusted sales of the entire homefurnishings group were 53 percent above the low point to which they had fallen in March 1954. For the year, sales of homefurnishings are estimated at 25 percent above 1954 and only 3 percent below the all-time record of 1951.

The revival of homefurnishings sales is also apparent when the sales performances of the individual departments are ranked according to the percentage change from 1954 to 1955. The five departments showing the greatest percentage change from the previous year are all in the homefurnishings sector, with sales of major household appliances showing the largest gain of all departments. (See table.)

SALES BY DEPARTMENTS, 1955

Percent Increase or Decrease from 1954⁽¹⁾
Fourth District Department Stores

Department	% Change from 1954
Major Household Appliances.....	+49
Rugs and Carpets.....	+39
Upholstered and Other Furniture.....	+30
Mattresses, Springs, Studio Beds.....	+25
Housewares.....	+24
.....	
.....	
.....	
Cotton Yard Goods.....	- 2
Silks, Velvets, Synthetic Yard Goods.....	- 4
Woolen Yard Goods.....	- 7
Laces, Trimmings, Embroideries, and Ribbons.....	- 7
Women's and Misses' Suits.....	- 9

(1) Figures are for January through November

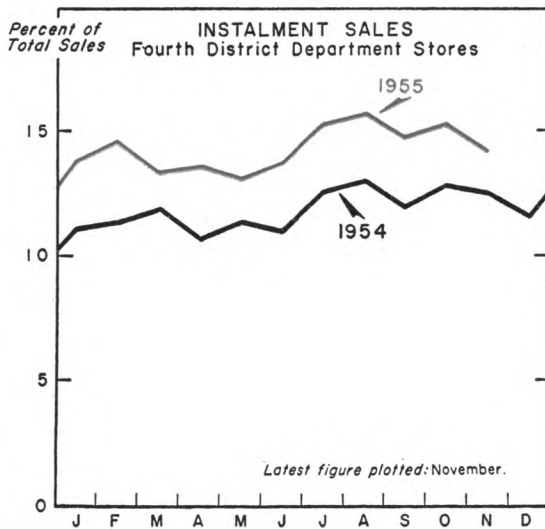
Sales by the piece goods and household textiles departments, on the other hand, showed year-to-year declines. Sales of women's and misses' coats and suits showed the largest drop from a year ago, with sales off by 9 percent.

Instalment Sales

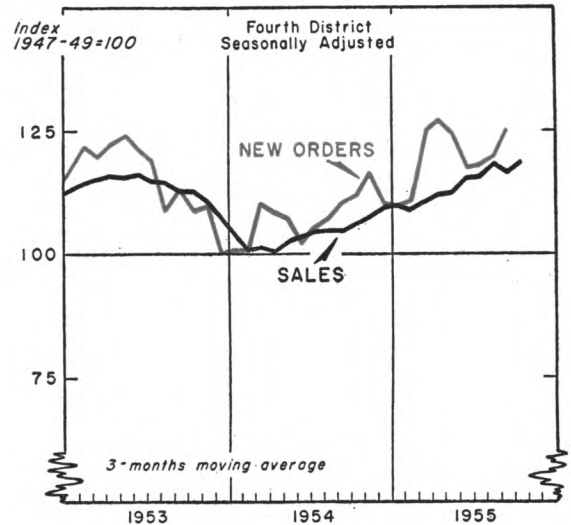
A substantial rise in instalment buying accompanied and supported the great gain in sales of furniture, appliances, and other "big-ticket" items of the homefurnishings departments. During 1955, instalment sales accounted for an increasingly large proportion of total sales. For the year as a whole, instalment sales' share of total sales rose nearly one-fifth above 1954 levels, as shown by an accompanying chart.

Instalment-account outstandings during 1955 reflected the rising use of instalment credit, showing a slow but nearly constant increase throughout the year. At the end of

Instalment sales made up a larger proportion of total sales during 1955 than in any previous year on record.



New orders placed by District department stores rose sharply in the spring of the year. Generally, they have followed the pattern of sales since 1953.



October, instalment-account outstandings were 18 percent above the average for 1953 and represented a new high for the past few years.

New Orders

New orders placed by department stores increased sharply in the first half of the year, after adjustment for seasonal variation. By April, the volume was 25 percent above the 1947-49 average, and slightly above the levels reached in the spring of 1953. During the summer months, the total was reduced somewhat, but in the last month for which data were available, new orders were approaching new high positions.⁽¹⁾

(1) The "new order" series shown in the chart is derived by combining information on outstanding orders, inventories and sales as supplied each month by a substantial group of co-operating department stores. The sales index depicted in the same chart is based on a somewhat larger sample of reporting stores. Both series in this particular chart are seasonally adjusted and are smoothed by use of three-month's moving averages.

Metropolitan Areas

Department store sales in all the major centers of the Fourth District were above the previous year's totals. The centers which showed the greatest year-to-year gains were *Pittsburgh* and *Youngstown*, where sales were up by 19 percent and 15 percent, respectively.⁽²⁾ At the lower end of the range, sales in *Portsmouth* were 3 percent above the 1954 volume, and department store trade in *Lexington* was up only 2 percent from a year ago. The year-to-year percentage changes for each major center in the District are shown by an accompanying table.

(2) The especially large year-to-year gain in Pittsburgh is associated in part with the strike conditions of the previous year. All figures here are based on 11 months' data for both years.

DEPARTMENT STORE SALES BY CITIES

Percentage Change from 1954 to 1955⁽¹⁾

Metropolitan Area	Percent Change
FOURTH DISTRICT	+10
Akron.....	+ 7
Canton.....	+ 4
Cincinnati.....	+ 6
Cleveland.....	+ 8
Columbus.....	+ 8
Erie.....	+ 5
Lexington.....	+ 2
Pittsburgh.....	+19
Portsmouth.....	+ 3
Springfield.....	+12
Toledo.....	+ 9
Wheeling-Steubenville.....	+ 6
Youngstown.....	+15

(1) Figures are for January through November

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FOURTH FEDERAL RESERVE DISTRICT

