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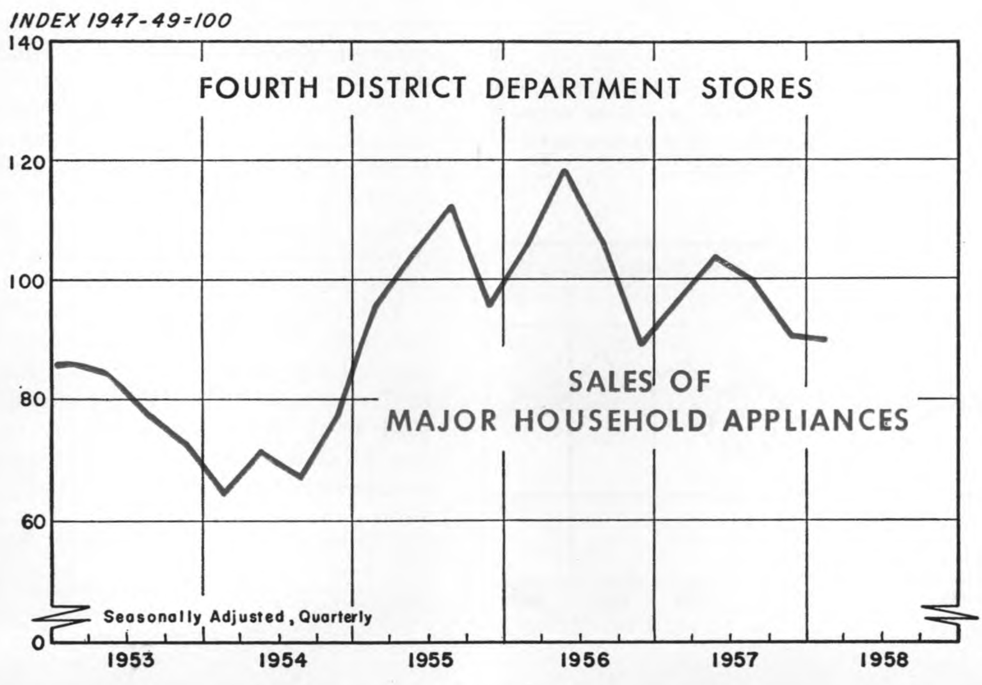
May, 1958

IN THIS ISSUE

Sales of household appliances by department stores leveled off in the first quarter of this year, following previous declines. Sales were appreciably higher than in the recession of 1954 and the physical volume comparison would be more favorable, since appliance prices declined between 1954 and 1958.



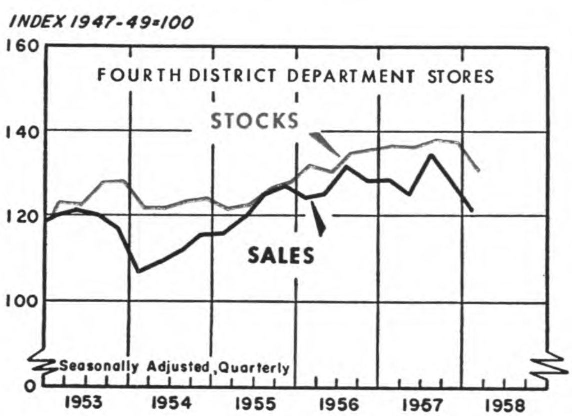
Two Cycles of Department Store Sales

Fourth District

IN VIEW of present attention to rates of consumer spending, it seems timely to take a close view of department store sales during recent months and compare the picture with the trend of sales which prevailed during the previous downturn of the business cycle, that is, during the closing months of 1953 and the first half of 1954. A series of accompanying charts traces the trend of sales and stocks, seasonally adjusted, of Fourth District department stores, as well as the course of sales in several important departments for the period 1953 through the initial quarter of this year.

So far, the decline of department store sales in the Fourth District during the final quarter of 1957 and the first quarter of 1958 has been less than during the same period of the previous recession. April reports indicate that seasonally adjusted sales during the month showed some slight improvement .

Declines in department store sales during recent quarters, although significant, have been somewhat less than the '53-'54 decline, on a percentage basis. Inventories have also declined.



General Course of Sales

The phase of expansion in sales which had begun during the early months in 1950 came to an end in the second quarter of 1953 and was followed by a year of contraction. Between May 1953 and March 1954, when sales reached bottom, total seasonally adjusted sales by Fourth District department stores declined by nearly 16 percent. Although the second quarter of that year witnessed an upturn, department store sales during the entire year 1954 fell 6 percent short of 1953.

Supported by the rise in general business activity and consequently by the rise of personal income, the upturn in department store sales which began in the spring of 1954 extended for over three years, breaking all previous records. Sales reached a new peak in August of last year, but the decline during the following months almost cancelled the earlier gains for the year. However, a comeback of Fourth District department stores during the 1957 Christmas season brought total sales for the year slightly more than 1 percent above the 1956 volume, in dollar terms. Thus, total sales by Fourth District department stores for the year 1957 were almost 16 percent larger than in 1954 and 9 percent larger than in 1953—the end of the expansion period which had begun in 1950.

The picture would look only slightly less favorable if dollar-volume reports were discounted for the change of prices. For the year 1957, the sales gain of 16 percent from the 1954 level was accompanied by an average rise in department store prices estimated at 3 percent.(1)

(1) Estimate is based on the Department Store Inventory Price Index, issued by the Bureau of Labor Statistics, U. S. Department of Labor. These figures do not necessarily apply to prices charged by Fourth District stores, but they are suggestive of major trends.

Department store trade during the first quarter of 1958 continued considerably below the 1957 average. Seasonally adjusted sales in February were about 10 percent smaller than a year ago and about 15 percent below the peak which was reached in August. There was a slight recovery in March, but total sales by District department stores for the initial quarter of 1958, after adjustment for seasonal variation and the shift in the date of Easter, were off more than 6 percent from a year earlier, and down about 11 percent from the third quarter of last year.

Major Household Appliances

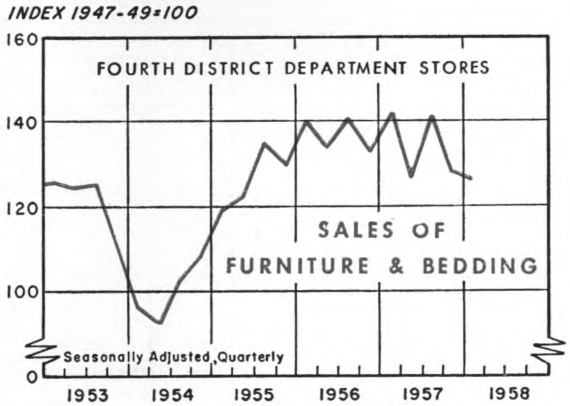
The decline in sales of major household appliances during most of 1953 and the early months of 1954 was followed by a spectacular rise which extended through the first half of 1956.(2) The brisk activity in residential construction which prevailed during the period gave strong support to demand for appliances. Over the period of two years, sales of major appliances by Fourth District department stores increased by some 50 percent. The easing in residential construction in 1956 brought a reversal of trend. Sales during 1957 were down about 9 percent from the previous year. (See cover chart.)

The weak market for appliances has continued into 1958. However, the level of adjusted sales for the first three months of this year was considerably higher than the average for 1954. If adjustments for price changes were made, the picture would appear even more favorable in comparison with 1954, since the prices in this group have, in contrast to the general movement of prices, been declining. It is estimated that prices of major appliances declined by about 10 percent(3) between 1954 (average for the year) and the first quarter of 1958.

Furniture and Bedding

Sales of furniture and bedding declined sharply between the third quarter of 1953 and the second quarter of the following year. As the accompanying chart shows, by the end of 1955 this department not only had recovered the ground lost during the recession, but had exceeded average 1953 figures by nearly 2 percent. For the years 1956 and 1957, sales of this department were approximately 30 percent to 35 percent above the 1954 level.

Sales of the furniture and bedding department dipped slightly during the first quarter of this year. During the previous two years, such sales had shown zig-zag quarterly fluctuations at near-record levels.



However, unlike the major appliances group, the advance in sales of furniture and bedding during the three-year period includes the effects of a rise in prices amounting to about 5 percent. If allowance for price changes were made, the level of seasonally adjusted sales in the first quarter of this year would probably not exceed the 1953 average.

Radios, Phonographs, and Television Sets

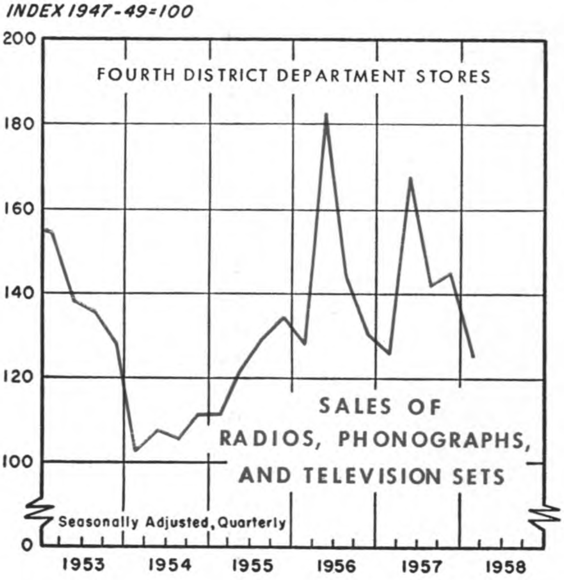
The extent of fluctuation in sales of radios, phonographs, and television sets is shown on an accompanying chart. The ground lost during 1953 and 1954 by this department was not recovered until 1956 when sales exceeded 1953 figures by about 4 percent. Sales increased only moderately in 1957. Seasonally adjusted sales for the first three months of 1958 were about even with a year ago.

It should be noted, however, that the decline in sales by this departmental group dur-

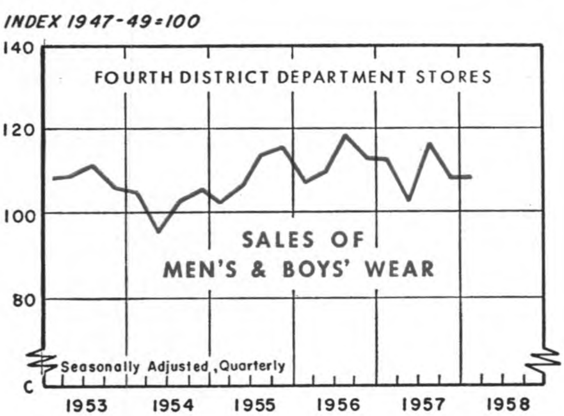
(2) Prior to 1953, sales of major household appliances had lost ground as measured against the base-period years, 1947-49. That is reflected in the chart by a position of the index line below 100.

(3) Based on the Department Store Inventory Price Index, *op. cit.*

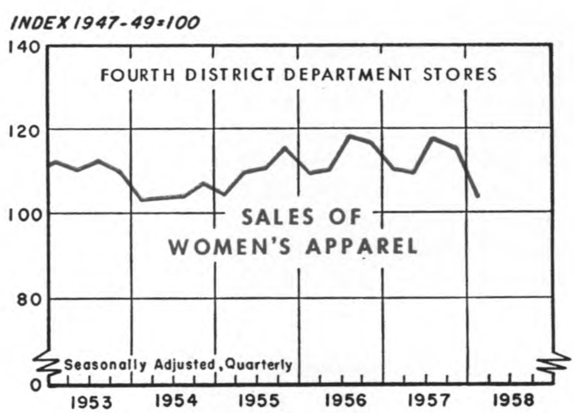
Sales of radios, phonographs, and television sets declined somewhat in the first quarter, but the change was within the range of quarterly fluctuations characteristic of the past two years.



Sales of the men's and boys' wear group of departments showed little change in the first quarter of this year.



The women's apparel departments posted a relatively large sales drop for the first quarter of the year.



ing 1953 and 1954 was accompanied by a substantial reduction of prices at retail. Thus, between July 1953 and January 1955, prices charged by department stores for radios and television sets declined by nearly 10 percent. During the first quarter of 1958, the price level of radios, phonographs, and televisions was about 9 percent below the 1954 average. Consequently, the physical volume of sales of this group at Fourth District department stores was appreciably higher during those years than is shown by the chart curve, which is calculated from the dollar volume of sales.

Men's and Boys' Wear

Men's and boys' wear at Fourth District department stores account for about 10 percent of total dollar volume. As shown by an accompanying chart, sales followed the general decline during the latter part of 1953 and the first half of 1954. In 1954, the decline amounted to about 5 percent. During the following two years, sales followed an upward trend, but gains were smaller than storewide averages. Moreover, they represented, to a considerable extent, an upward adjustment of prices. Sales of men's and boys' wear showed some weakness in 1957 and lost some ground during the year. They eased very slightly in the first quarter of this year. Average sales for the three-month period were the same as in the first quarter of 1956, after seasonal adjustment.

Women's Apparel

Women's apparel includes by far the largest group of departments at department stores, and altogether accounts for over one-third of total sales. As shown by the accompanying chart, sales of women's apparel have, over the years, been more stable than sales in most other departments.

Sales of women's apparel at Fourth District department stores for the first quarter of 1958, seasonally adjusted, declined about 12 percent from the third quarter of last year, while the decline from the high in 1953 to the low in 1954 amounted to only 8 percent.

ANNOUNCEMENT

A new edition of "A Handbook of Department Store Statistics, Fourth Federal Reserve District" is now available upon request to the Research Department of this bank. The revised edition of the Handbook brings up to date the principal tables shown in the three previous editions, those of 1946, 1948, and 1952. The sales and stocks indexes of Fourth District department stores, as well as sales indexes for eleven metropolitan areas of the District, incorporate the major revision of the series which was completed in 1957.

Contract Production in Agriculture

THE PRACTICE of producing agricultural commodities under contract is not new, but it is currently the topic of much discussion. This discussion centers around the use of the contract technique in achieving vertical integration in agriculture, which broadly defined is the coordination of management decisions in two or more different stages in the production, processing, or marketing of agricultural products. Vertical integration may, of course, be accomplished by ownership, or cooperative action, but it is the use of the contract technique to combine activities that are customarily performed on the farm with those normally done by nonfarm business that has stimulated much of the current discussion.

Contract production of agricultural crops takes various forms, but usually it involves an agreement on the part of the producer to deliver to a processor or marketing agency a designated quantity of a commodity meeting certain minimum quality requirements at a previously agreed upon rate of compensation.

The broad acceptance of contract production in the broiler industry—in which over 90 percent of the output is produced under contract—has apparently contributed to the interest in applying this technique to the production of other livestock products such as table eggs, pork, and beef. Since conversion of feed to animal products is the common denominator for all of these enterprises, it is understandable that the results achieved in the production of broilers has had some influence on other livestock enterprises. There are also certain broader economic forces operating within and outside agriculture which may be contributing to the current interest in contract production of agricultural products, as will be noted below.

Contract Production Not New

One of the first industries reported to use the processor-grower contract was the food canning industry. The device was used by this industry as a means of assuring a dependable supply of a known quality of fruits and vegetables for canning. Contract production then became a commonly used technique in the production of sugar beets, sugar cane, popcorn, hatching eggs, and field and garden seeds. The advent of hybrid seeds, which requires the use of controlled pollination seed stocks each year, has broadened the use of contract production in the seed industry.

In recent years contract production has become quite common in one phase of the poultry industry, namely, the production of commercial broilers. Here it met with widespread acceptance on the part of the grower, processor, and the feed supplier as well. In fact, the feed supplier often became the central figure, serving as marketing agency, supplying much of the working capital, taking a great deal of the risk, and sharing the returns with the grower under a variety of plans.

In the Broiler Industry

The significant role of the feed dealer in broiler production is illustrated by the results of a survey conducted by the United States Department of Agriculture and the Delaware Agricultural Experiment Station in the Delaware broiler area in 1955. This survey revealed that two-thirds of the broilers were produced under contract with feed dealers and 28 percent by feed dealers themselves, while only 6 percent were produced by independent growers. The five different types of contracts in use in that area indicate the manner in which contract production in the broiler industry varies from that common to the production of farm crops under contract where the producer normally assumes a greater share of the risk. The contracts used in the Delaware broiler area include:

1. A Share system whereby returns are split on a predetermined basis of 75-25, 80-20 or 2/3-1/3, with the grower receiving the larger share of the split.

2. Guaranteed-Share system in which the grower is guaranteed $40 to $50 per thousand birds started and one half of the net return, if any, over the guarantee.

3. Flat Fee plan in which the grower is paid $50 to $75 per thousand birds started, regardless of the prices or total return.

4. A Feed Conversion payment plan based on the ratio between feed used and broiler meat produced. (A figure of 2.5-2.8 lbs. of feed per pound of gain is not uncommon in broiler production.)

5. The Salary plan in which the grower is paid a specified amount for raising broilers; the salary is frequently stated on a monthly basis.

Under all of these types of contract, the grower usually provides the house, equipment, and labor required to raise the flock. The dealer in turn furnishes the feed, medicine, vaccine, and other supplies and also arranges and pays for the chicks, the fuel and the litter. Title to the broilers remains with the dealer until the products are marketed. The dealer absorbs any deficits, if the flock fails to sell for an amount equal to the sum of the items charged against it. The contractual agreements covering more than 70 percent of the broilers produced under contract (according to the 1955 survey) provide for some return for labor and investment.

Slightly over half of the broiler growers included in the survey were full-time farmers. The remainder were part-time farmers, retired persons, and nonfarmers. Generally the contract growers produced broilers on a somewhat smaller scale than the independent growers, who for the most part were full-time farmers. Those in charge of the survey report that most of the growers preferred to grow broilers under contract. Growers indicated a willingness to invest funds, labor and material in houses and equipment, but few were willing to accept all of the risks associated with investing in the chicks, feed and supplies required.

The survey reported no evidence that the methods and policies of lending institutions had an appreciable influence on the extent of contract production. Small growers were financed on terms which appeared to be about as favorable as those extended to large growers.

The contract plans used in the Delaware broiler area, which are similar in principle in many respects to those used in the other major broiler-growing areas, offer the following incentives to the grower:

1. The contractor shares the risk with the grower, and in the case of the flat fee and salary plan he virtually assumes all of the risk.

2. The contractor assures a market outlet for the broilers when they reach market weights.

3. A considerable amount of the capital required is furnished by the contractor.

4. The contractor assists in management and frequently provides technical information and assistance.

The fact that 6 percent of the broilers in the Delaware area and probably no more than 10 percent of the national output are produced independently suggests that growers are willing to relinquish some management decisions (including opportunities to sell for the top price in periods of shortage) in favor of reducing their risk and being assured of a market outlet. As soon as broilers have reached market weights, the financial losses tend to mount rapidly if the products are not moved to market promptly.

Contract Production of Other Agricultural Products

Will the factors which contributed to the broad acceptance of contract production in the broiler industry ultimately lead to its use

(Continued on Page 9)

The 1958 Survey of Demand Deposit Ownership

Fourth District

Despite the decline in privately-held demand deposits during the twelve months ended January 1958, the distribution of such deposits *by type of owner* has remained generally unchanged. The change in the general business scene, from expansion to decline, has had a negligible effect upon the ownership distribution of demand balances, as revealed by a comparison of the 1958 Survey with previous annual surveys of Ownership of Demand Deposits of Individuals, Partnerships, and Corporations. For the Fourth Federal Reserve District, business firms continue to hold about three fifths of the total dollar vol-

DEMAND DEPOSIT ACCOUNTS OF INDIVIDUALS, PARTNERSHIPS, AND CORPORATIONS BY TYPE OF OWNER

(Estimates for insured commercial banks, Fourth Federal Reserve District)

TYPE OF OWNER	January 30, 1957				January 29, 1958			
	Number (thousands)	Amount (millions of dollars)	Percentage Distribution		Number (thousands)	Amount (millions of dollars)	Percentage Distribution	
			Number	Amount			Number	Amount
Business:	**402**	**$5,453**	**10.3%**	**61.8%**	**403**	**$5,004**	**10.2%**	**61.2%**
Nonfinancial	381	4,754	9.8	53.9	385	4,379	9.8	53.5
Financial	21	699	0.5	7.9	18	625	0.4	7.7
Corporate	*132*	*4,424*	*3.4*	*50.1*	*135*	*4,164*	*3.4*	*50.9*
Noncorporate	*270*	*1,029*	*6.9*	*11.7*	*268*	*840*	*6.8*	*10.3*
Personal	**3,096**	**2,568**	**79.2**	**29.1**	**3,124**	**2,396**	**79.6**	**29.3**
Nonprofit Organizations	**235**	**371**	**6.0**	**4.2**	**236**	**363**	**6.0**	**4.4**
Trust Funds of Banks and Deposits of Foreign Residents and Firms	**2**	**240**	**0.1**	**2.7**	**2**	**241**	**0.1**	**3.0**
Farmers, Noncorporate	**173**	**192**	**4.4**	**2.2**	**160**	**171**	**4.1**	**2.1**
TOTAL	**3,908**	**$8,824**	**100.0%**	**100.0%**	**3,925**	**$8,175**	**100.0%**	**100.0%**

ume of privately-owned demand deposits and only one tenth of the number of such deposits. On the other hand, personal accounts continue to comprise almost four fifths of the number of deposits and less than three tenths of the dollar volume.

As shown in the accompanying table, the dollar volume of demand deposits (IPC) declined about 7 percent during the year ended January 1958, while the number of accounts rose slightly. The resulting decline in the average size of demand deposit accounts probably reflects some diversion of funds from demand to time deposits. Evidence from other sources indicates that funds have been attracted from demand deposits by higher interest rates paid on time deposits.

Most of the ownership groups classified separately in the Survey experienced a decline in dollar volume between January 1957 and January 1958 commensurate with the total reduction in deposits. The exception was a slight increase in the deposit volume of the ownership group that includes trust funds of banks and deposits of foreign residents and firms. Declines in demand balances of other ownership groups during 1958 ranged from 2 percent for nonprofit organizations to 18 percent for noncorporate business.

The data reported here are estimates of the dollar volume and the number of demand deposit accounts held at all Fourth District insured commercial banks. (Information of the type shown in the accompanying table, but further classified by size of bank, is available upon request.) The sample of banking offices for the 1958 Survey was the same as the sample for 1957 with minor adjustments for changes in banking structure. In the Fourth District, 105 insured commercial banks provided sample data on ownership of demand deposits held at 153 of their banking offices as of January 29, 1958. These offices, representing 9 percent of the total number of insured banking offices in the Fourth District, held 36 percent of the total dollar volume of demand deposits of individuals, partnerships, and corporations.

Contract Production in Agriculture

(Continued from Page 7)

in the production of livestock and other agricultural products currently produced by independent producers? Much discussion during recent months has centered about that question and its implications.

Some individuals and firms obviously believe that contract production can be applied to other farm products, since they have already made substantial investments in such plans for the production of pork, beef, and table eggs.

Contract production of table eggs is reportedly receiving considerable attention in the Great Plains and the South where feed dealers and egg-marketing agencies are offering contracts to farmers in an effort to encourage a quality egg production program. One plan reported in a recent Department of Agriculture study was originated by a feed manufacturer in cooperation with an egg-marketing firm. Under this plan, the producer constructs a laying house according to specifications, with or without outside assistance in financing, depending on the circumstances. He agrees to maintain a specified number of layers of approved types, to use the feeds specified, and to follow a quality egg production program. The eggs are marketed under a brand name at a premium over the regular market price.

Other instances of contract production of livestock products include contracts between feed-dealers and producers for the production of hogs. While most of the interest in contract hog feeding is said to center in the southern fringes of the Corn Belt and the upper South, there are also reports of contract plans in the main part of the Corn Belt. One in the central

Corn Belt reportedly places major emphasis on the leasing of breeding stock of a high quality (meat-type) hog.

The feeding of cattle and lambs under contract is also said to be increasing. A common arrangement is for the rancher to contract with a feedlot operator to fatten livestock at an agreed upon rate per pound of gain, or a share of the profit. Since these contracts are frequently between farmers, they do not contribute to vertical integration in the production of agricultural products to the same extent as feed dealer-producer contracts for hogs, or processor-grower contracts for canning crops.

Vertical Integration Fostered by Economic Forces

The increasing tempo of technical change in agriculture has been accompanied by a steady dispersion of functions from the farm to off-farm businesses. Farmers buy more of the items used in production today than formerly. Moreover, most of the resources of the farm business tend to be concentrated on the production of a few major products.

A generation ago, entrepreneurial risk was spread over several products; farms customarily performed more of the production and processing functions than are commonly performed today. Under those conditions, if one product failed to yield a profit, the gain from another frequently compensated for the deficiency. Moreover, the net returns from a given crop often could be enhanced by performing more of the processing or marketing functions incident to the sale of the product to the ultimate consumer. Under the high degree of specialization which characterizes much of American agriculture today, that is virtually impossible.

This transfer of functions from the farm places the present day commercial farmer in the position of being increasingly dependent upon the specialized operation of growing crops and raising livestock for market. Moreover, with fewer products to sell, it becomes increasingly important that there be a market for those products which will yield a profitable return. This may in part account for the willingness of farm operators to enter into production contracts to produce agricultural products for a specific market.

There are a number of other developments within agriculture which may conceivably influence farm operators to look with favor on producing for specific markets. One of these is the relatively high capital requirements involved in establishing and maintaining a farm business. The average investment per farm today is virtually two and one half times what it was in the mid-forties. Another factor which has presumably exerted an influence is that net farm income over the past five years has represented the smallest percent of the gross farm income for any similar period of record going back to 1910.

One of the developments outside of agriculture which has tended to foster contractual relations between producer and processor is the rapid growth of food super markets. Over the past five years, the number of super markets is reported to have increased by 63 percent. Moreover, super markets now reportedly account for over 60 percent of the total volume of sales as compared with less than 50 percent, five years ago.

Due to the large volume of products required to service such markets, growers and processors (both private and cooperative) have made extensive use of production contracts to serve the super market outlet with a dependable volume of a specified quality of agricultural products.

NOTES

Among the articles recently published in monthly business reviews of other Federal Reserve banks are:

"The Swing to Services", Federal Reserve Bank of Chicago, April 1958.

"Financing the Expansion in Farm Debt", Federal Reserve Bank of Kansas City, April 1958.

"The Treasury's Deposit Balances and the Banking System", Federal Reserve Bank of New York, April 1958.

(Copies may be obtained by writing to the Federal Reserve Bank named in each case.)

* * *

Recent statements on Federal Reserve policy include:

"Sputnik and Monetary Policy." Remarks by J. L. Robertson, member of the Board of Governors of the Federal System, before the Nineteenth Annual Pacific Northwest Conference on Banking. State College of Washington, Pullman, Washington. April 10, 1958.

"Dollar ($) Design." Address by M. S. Szymczak before the Chicago Association of Commerce and Industry and the Chicago Chapter, American Institute of Architects. Chicago, Illinois. April 10, 1958.

(Copies of these addresses are available at the Board of Governors of the Federal Reserve System, Washington 25, D. C.)

FOURTH FEDERAL RESERVE DISTRICT