

MONTHLY *Business Review*

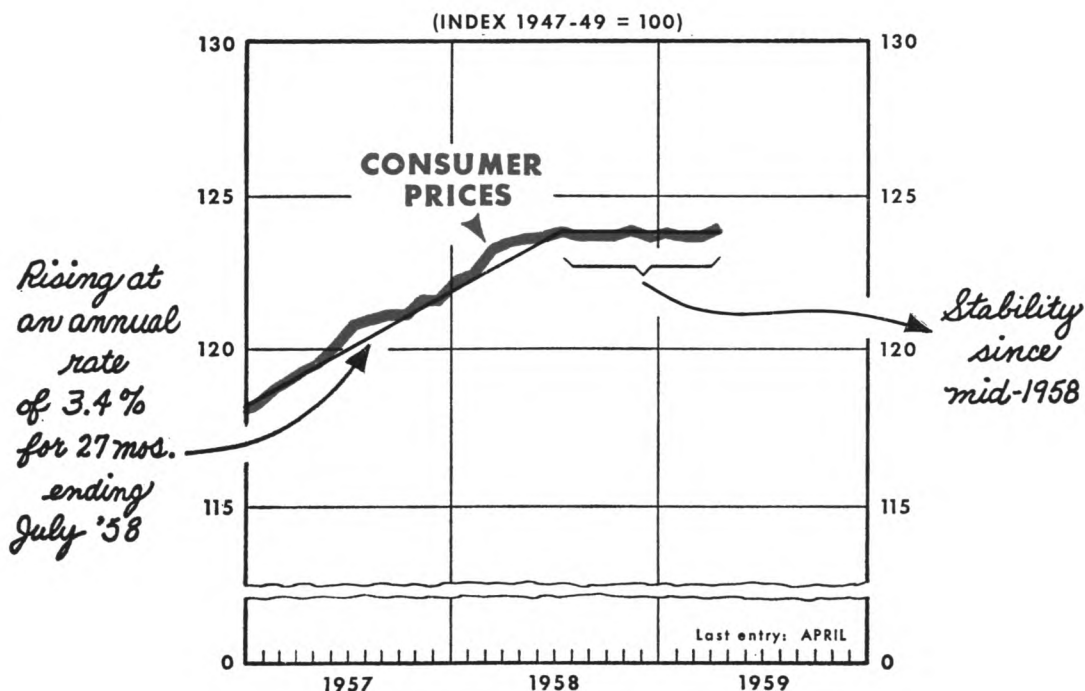
FEDERAL RESERVE BANK of CLEVELAND

June, 1959

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PRICES STABILIZE DURING BUSINESS RECOVERY



New Booklet

Borrowing and lending of a special kind of money known as Federal funds, i.e., deposit balances in the Federal Reserve Banks, have come to be of increasing importance in the short-term money market. Information on the growth and the current structure of the Federal funds market and on the Federal funds rate may be found in a new 111-page booklet entitled:

“THE FEDERAL FUNDS MARKET—A Study by a Federal Reserve System Committee”, published by the Board of Governors of the Federal Reserve System.

(The price of the booklet is \$1.00 each up to 10 copies, and 85 cents each for 10 or more copies in single shipment. Orders should be addressed to the Board of Governors of the Federal Reserve System, Washington 25, D. C.)

Rounding Out A Year Of Price Stability

THE UNITED STATES is now rounding out a year of over-all price stability. This steadiness in the purchasing power of the dollar occurred concurrently with a sharp recovery in economic activity from the recession lows of early 1958, as many business indicators were rising to new record levels.

The recent stability in the general price level offers quite a contrast to the price trends and price expectations of a year ago. From early 1956 through mid-1958, including a recession period, the average price of consumer goods and services had been rising at the alarming rate of nearly 3½ percent per year. Even with the recognition that prices at retail are usually sluggish and rather slow to react to changes in business activity and consumer demand, the continued upward momentum of prices was viewed, not unreasonably, with general apprehension. The question was raised as to how fast prices might rise, once recovery began, since the upward pressures on prices had remained so strong in the face of slackening demand and rapidly falling activity.

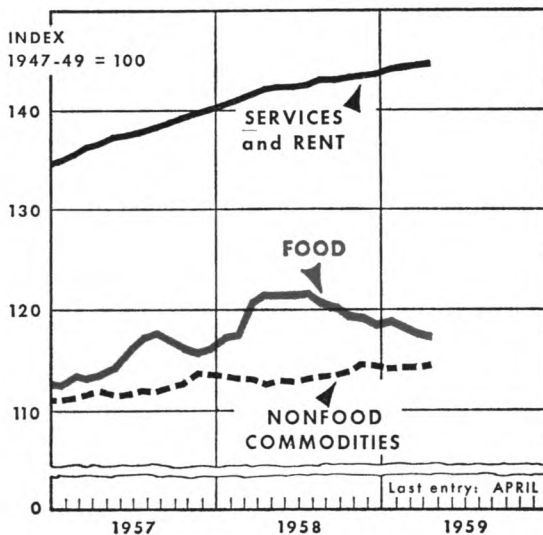
In retrospect, it can be seen that the contraction in business activity was brief and that the recovery was both sharp and vigorous. Spurred by strong consumer demand and an expansion of spending by all levels of government, the physical volume of all goods and services produced in the country reached new record levels in early 1959.

Spending by consumers was one of the major forces, both in limiting the contraction and in stimulating the recovery. Consumer demand and consumer purchasing power have been rising for over a year, after very modest declines during the recession, and both have been at record levels for some months now.

Personal income turned up in March 1958 and is currently running almost 6 percent above prerecession highs. The larger income totals are being supplemented by increased consumer borrowing. Aggregate consumer spending is more than 4 percent above the prerecession peak with expenditures for non-durable goods and for services at record levels while outlays for automobiles and other durable goods have risen substantially.

Against this background of sharp recovery and strong demand, consumer prices on the average have held at or below the level reached in July 1958. (During most of this period, the index has been below the previous peak of July 1958, although in April it returned to that position.) The sideways course of prices during this period is an accomplished fact. A look at some of the factors in-

CONSUMER PRICES



fluencing the general price level helps explain the over-all stability of the past year. Such a look reveals why there is concern as to the durability of the sideways movement and an anxiety about the possibility of a renewal of inflationary trends in the economy.

Falling Food Prices as an Offset

The stability in the average price of consumer goods and services since last summer has been due, in large part, to declines in food prices which offset increases in the prices of nonfood items.

Food items included in the consumer price index declined at an annual rate of 5 percent between July 1958 and April 1959, while prices of nonfood commodities and services increased at an annual rate of almost 2 percent. (Food commodities account for about 29 percent of the total index.) These divergent and offsetting trends provide the simplest, and a nearly but not quite complete, explanation of the stability in the general price average over the past year.

The vagaries of the weather have had a greater impact upon food prices over the past year and a half than is usual. Unusually severe weather in the winter of 1958 restricted the supply of fresh fruits and vegetables at the same time that meat supplies were reduced, forcing prices up sharply in early 1958. Then the weather turned from severe to ideal. It was unusually favorable during the 1958 planting, growing, and harvesting seasons and record crop yields were obtained. Almost concurrently, meat supplies (principally pork) began rising. As a result, food prices, which were unseasonably high at mid-year, dropped faster and further than they might have had the weather been only average.

The prices of services rendered to consumers have risen steadily during the post-war period and have continued to move up during the past year. However, there was some slackening in the rate of increase after the first quarter of 1958.

Of the three major components of the consumer price index, nonfood commodities (which, as distinct from food and services,

account for about 37 percent of the index) were the only group where average prices reacted fairly promptly to the lessening of demand early in the recession; they tilted downward late in 1957. The downward drift amounted to less than one percent, however, and was reversed almost simultaneously with the turnaround of economic activity. This spring, prices of consumer goods (other than foods) averaged nearly one percent higher than in late 1957.

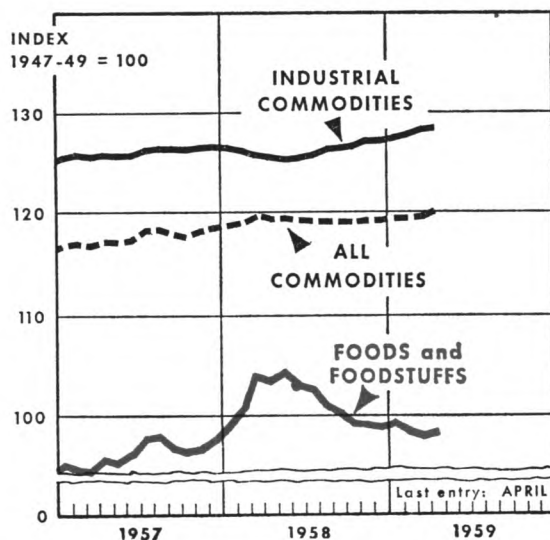
Similar Trends at Wholesale Level

Much the same story—with the total relatively steady, with food down, and with other commodities up—can be told about the course of prices at the wholesale level over the past year.

Average prices of foods and foodstuffs rose in early 1958 and declined fairly steadily thereafter, for the reasons already mentioned. Some slight seasonal increase occurred this spring, but no more than might normally be expected; the general trend should be characterized as downward.

Prices of industrial commodities sagged only slightly during the recession and have been rising markedly during the recovery. Since mid-1958, industrial prices at wholesale

WHOLESALE PRICES



have been rising at an annual rate of 3 percent and have been establishing new record highs each month since last September. The upward climb to new highs occurred in the average prices of finished goods and of materials, components, and supplies for further processing.

The rise of the wholesale price index—after a year of stability—to new record highs this spring was thus the result of a slight seasonal rise in the prices of foods and foodstuffs, combined with a strong upward climb of industrial commodity prices. Whether or not farm prices resume their downward course after this usual spring spurt, thus again offsetting any upward tendencies of industrial prices, remains to be seen. Without attempting to forecast, it may be observed that there are at least some factors in the situation which indicate that some degree of decline in farm prices will be resumed.

Forces Impinging Upon Prices

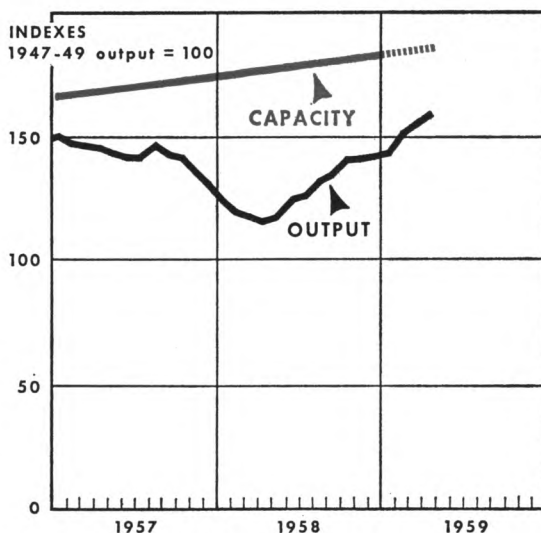
Many forces are at work in the economy that have a bearing upon, or help shape, the course of prices, beyond those which have been specifically mentioned above. Of the many possibilities, at least two should be mentioned, if only because they have changed so markedly and rapidly since 1957. These are the rate of capacity utilization and changes in productivity in manufacturing.⁽¹⁾

Capacity Utilization

The sharp drop in output during a recession results in the underemployment of men and equipment. At such a time, the competition for orders becomes intensified, with a resulting downward pressure upon prices. At the same time, costs are looked at closely and pared wherever possible. But, as demand rises and production picks up, the pressures to hold prices down tend to be dissipated. Then, as capacity rates of operation are approached, the bidding for men, materials, and finished goods tends to bring about renewed upward

⁽¹⁾ Selection of these particular factors for discussion does not imply that financial developments (including monetary and fiscal policies) are unimportant in their impacts upon price trends. This article is limited to the non-financial phases of recent trends.

MAJOR MATERIALS



CAPACITY: estimated for 17 industries as of each January 1.
 OUTPUT: seasonally adjusted monthly figures.

From a production level equivalent to about two-thirds of capacity in early 1958, output of 17 major industrial materials moved up sharply to about 87% of capacity by April 1959.

pressures on prices which may be strong enough to result in another upward movement of the price indexes.

No really satisfactory measure of capacity utilization is available for our economy in general. The employment rate—proportion of labor force at work—is one measurement which is relevant. In these terms, it would be noted that the rate dropped to about 92.5 percent during the worst of the recession and is currently running around 94.7 percent, indicating that there is still room for improvement before optimum rates of use are reached. In assessing the price outlook, and aside from social implications, the current employment rate may be taken as suggesting that output can rise still further without the supply of labor becoming restrictive.

The accompanying chart shows another measure of capacity utilization in terms of 17 major materials which comprise about 10

percent of the nation's industrial output.⁽²⁾ From an operating level equivalent to about two-thirds of capacity at the bottom of the recession, output in these 17 major industries moved up to about 87 percent of capacity by April 1958. Insofar as the price outlook is concerned, this figure suggests the possibility that further increases in demand can be satisfied without undue pressures upon prices.

It should be noted, however, that the production rates of these 17 major materials are quite sensitive to changes in activity and demand; they fluctuate over a much wider range than the rate of over-all industrial output. Consequently, the changes in capacity utilization of the major industrial materials overstate the magnitude of the fluctuations that have occurred in general industrial activity since 1957.

The sharp "V" effect of the production curve of the 17 major materials reflects, in exaggerated form, the swing that occurred in over-all economic activity during the recent recession. Prior recessions have often taken a "U" shape, with production bouncing along on the bottom for some months before turning up. Thus, in many past recessions, the downward pressures on prices coming from the under-utilization of capacity had a longer time to produce their effects than was the case in the '57-'58 period.

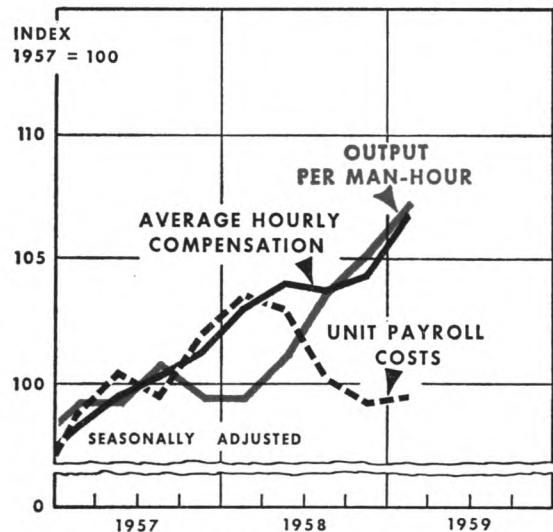
Productivity and Labor Costs

Trends in productivity, especially as they compare with hourly pay, thus affecting unit payroll costs, have also shown some trends favorable to price stability during the recovery period.

Measuring productivity changes—particularly in the short run—is known to be a controversial undertaking. The simplest approach that can be made with regularly available statistics is to relate physical output in manufacturing to total man-hour input (both pro-

(2) Compiled by the Board of Governors of the Federal Reserve System. Steel, petroleum products, cotton yarn, synthetic fibers and yarn, pulp, paper, and paperboard are weighted most heavily in the index.

PRODUCTIVITY and EARNINGS All employees in manufacturing



Output per man-hour in manufacturing has risen sharply since early 1958, as is characteristic of recovery periods. Even with the continued rise in labor compensation, the net result, at least for this recent period, has been a decline in unit payroll costs.

duction and non-production workers⁽³⁾ and to total compensation paid. This will give a rough approximation of trends in productivity and unit payroll costs (excluding fringes) in manufacturing, as shown by the accompanying chart.

Output per man-hour of all employees in manufacturing rose sharply during the recovery period, increasing by 8 percent between early 1958 and early 1959. Similar rapid gains in productivity had marked the recovery periods of the two previous postwar recessions.

Judging from corresponding productivity trends in the previous two recessions, however, it would appear that this relief of pressure on prices from the labor-cost side is now about over. The sharp rise in output per man-hour in the '49-'50 and '54-'55 recoveries

(3) In the absence of any monthly figures, it is assumed that non-production workers had a standard 40-hour week throughout the period under consideration.

Basic data for this chart are from U. S. Department of Commerce, U. S. Department of Labor, and Federal Reserve Board.

lasted only for four or five calendar quarters and then productivity leveled off for at least six months. Since average hourly compensation has shown a consistent upward trend, unit payroll costs will likely start to rise as soon as the rate of increase in productivity slackens. Such a slackening in productivity gains may, in fact, be occurring at the present time, to be reflected in future statistical reports.

Industrial Prices Rise Early

In the '49-'50 and '54-'55 recovery periods, the average prices of industrial commodities did not show any significant upward push until industrial production had topped its previous peak. In the latest recovery, however, industrial prices started rising almost concurrently with the increases in industrial activity. Perhaps one factor, among others, was the very brevity of the recession, which meant that the pressures to hold down prices

were at work in the economy for too short a period to take hold.

Another factor should be mentioned, i.e., a rather general expectation that inflationary pressures will continue. While no proof exists that such an inflationary psychology enters into the consideration of what price to charge, it is fairly evident that a large portion of the nation's consumers expect prices to rise,⁽⁴⁾ while pressures in the stock and bond markets seem to be partly motivated by investor hedging against inflation. It seems a valid inference that some of this inflationary expectation is being carried over into price-making decisions. To that extent, the outlook for a continuation of the relative stability of the price indexes is dimmed. Psychological factors of this type, however, have a way of changing—often after a considerable lag behind the changes in the underlying objective factors.

(4) See "1959 Survey of Consumer Finances, Preliminary Findings", *Federal Reserve Bulletin*, March 1959.

NOTES ON FEDERAL RESERVE PUBLICATIONS

Recent statements on Federal Reserve policy and related matters include:

"Economic Growth without Inflation", by C. CANBY BALDERSTON, Vice Chairman, Board of Governors of the Federal Reserve System. (Address before the Economics Club of Pittsburgh, Pennsylvania, May 14, 1959.)

"Progress and Economic Stability", by J. L. ROBERTSON, Member, Board of Governors of the Federal Reserve System. (Remarks before the Annual Convention of the Ohio Bankers Association, Cleveland, Ohio, April 28, 1959.)

"Strategic Factors in Current Business Outlook", by WOODLIEF THOMAS, Economic Adviser to the Board of Governors of the Federal Reserve System. (Address at the Helen Slade Memorial Conference on Forecasting sponsored by American Statistical Association, New York, N. Y., April 23, 1959.)

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

Around the Fourth District—

Department Store Sales, April and Year-to-Date

	April '59 % change from year ago	Jan.-April '59 % change from year ago
Youngstown	+14%	+ 7%
Pittsburgh	+11	+ 8
Cleveland	+10	+ 7
Portsmouth	+10	+15
Columbus	+ 9	+ 9
Wheeling-Steubenville	+ 7	+10
Springfield	+ 5	+ 7
Canton	+ 5	+ 7
Lexington	+ 4	+ 9
Erie	+ 2	+ 6
Cincinnati	+ 1	+ 5
FOURTH DISTRICT TOTAL	+ 9	+ 7

* * *

During April, *bank debits* in 32 Fourth District centers exceeded the year-ago month by 16 percent, pointing up the improved business conditions since April 1958, the low point in the recession. Three of the reporting centers, Franklin, Pennsylvania, and Springfield and Hamilton in Ohio, posted new record highs. Franklin scored the largest relative increase with a 30 percent gain over April 1958 while in Springfield and Hamilton, bank debits were up 26 and 24 percent, respectively, from a year earlier.

* * *

Total sales by Fourth District department stores in April were up 9 percent from April of last year, as shown in the table above. Especially large gains were reported by the homefurnishings departments. Thus, *sales of radios, phonographs, and television sets* were up 31 percent from a year earlier, *furniture and bedding* up 22 percent, *domestic floor coverings* up 21 percent, and *major household appliances* up 14 percent.

* * *

Savings deposits of individuals at 48 reporting banks in the Fourth District amounted to a new high of \$2,815 million late in April, an increase of about \$4 million from a month earlier. However, the average weekly increase of \$741 thousand was the smallest since last September.

* * *

In Cleveland, the May total of 7,700 *new automobile sales* marked a 24-month peak, only 35 units below the same month two years ago. Since the April total had already set a four-year high for that month, new car sales in the second quarter of 1959 are exceeding those of the corresponding quarter of every other other year except record 1955.

(The above items are based on various series of District or local data, which are assembled by this bank and distributed upon request in the form of mimeographed releases.)

Ownership Of Demand Deposits

Fourth District

PRIVATELY-HELD demand deposits at insured commercial banks in the Fourth Federal Reserve District amounted to an estimated \$8,489 million on January 28, 1959. Deposit growth during the preceding twelve months, amounting to \$314 million, contrasted sharply with the \$649-million decline which had been experienced in the year ended January 29, 1958. The changing business scene, from decline to recovery, was a principal factor, but continued strength in personal income and the effects of a relaxation of monetary policy during the recession period also contributed to the renewal of deposit growth.

Along with the increase in deposit volume, the annual Survey of Ownership of Demand Deposits⁽¹⁾ reveals some small changes in the distribution of deposits by type of holder — changes which apply both to number of accounts and to dollar balances. The total number of accounts increased less than 3 percent in contrast to a 4 percent increase in dollar volume. As a result, the average size of deposit balance increased slightly.

Business Accounts

As indicated in the accompanying table, business deposits continue to account for a large share of the total volume of privately-held demand deposits, amounting to three-fifths of the total in early 1959, while personal deposits continue to account for the bulk of the number of such accounts, four-fifths in early 1959.

(1) The Survey of Ownership of Demand Deposits of Individuals, Partnerships, and Corporations, conducted on January 28, 1959, was the third annual survey of the same sample of insured commercial banking offices, except for minor adjustments for changes in the banking structure. These reporting offices, representing 9 percent of all insured banking offices in the Fourth District, held 36 percent of the total dollar volume of privately-held demand deposits on December 31, 1958.

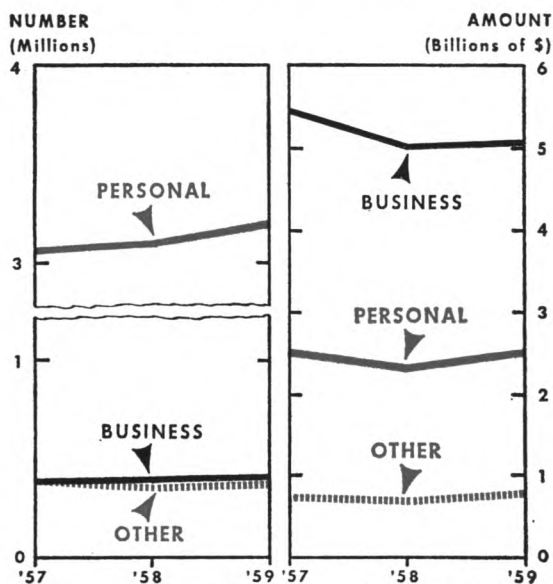
When business accounts are separated according to type of business, firms in non-financial lines, such as manufacturing and trade, held about 51 percent of the dollar volume of privately-held demand deposits in early 1959. Such firms lost ground during 1958 in the volume of deposits held as well as in the relative share of all such deposits. Apparently, the business recovery, which was substantial between January 1958 and January 1959, was less marked in the Fourth District than for the nation as a whole, as demand balances of nonfinancial firms at the nation's insured commercial banks rose an estimated 5 percent.

On the other hand, financial businesses, which refer to credit agencies other than banks,⁽²⁾ experienced a 14-percent increase in their deposit balances and a slight improvement in their relative position when compared with other types of depositors. Despite the fact that financial business firms held less than one-tenth of all privately-held demand deposits in the Fourth District, the \$88-million increase during the year ended January 28, 1959, was more than one-fourth of the total increase for all depositors. A 17-percent increase in the number of accounts held by financial firms suggests an expansion of this type of business in the Fourth District. However, the gain in dollar balances may also reflect a preference for demand deposits over other types of holdings during 1958.

Business accounts may also be separated according to legal form of organization. Demand balances of corporate business, which amount to more than four times demand bal-

(2) Financial business as defined for the Survey of Ownership of Demand Deposits includes sales finance companies, savings and loan associations, credit unions and mortgage companies; security and commodity brokers and dealers; insurance carriers; and investment trusts, investment companies, holding companies and mutual funds.

**PRIVATELY-HELD DEMAND DEPOSITS
BY TYPE OF HOLDER**
Fourth Federal Reserve District



NOTE: Figures plotted as of January 30, 1957; January 29, 1958; and January 28, 1959. The miscellaneous type of holder, "Other", includes accounts held by unincorporated farmers, nonprofit organizations, foreign individuals and firms, and trust funds of banks.

ances of noncorporate business, declined slightly between early 1958 and 1959 while noncorporate business firms registered a 16-percent increase. In dollar terms, corporate business balances declined \$77 million while noncorporate balances increased \$135 million.

The deposit data just cited do not necessarily mean that smaller businesses, which of course are more generally represented by the noncorporate than by the corporate form of organization, fared better during the recovery in 1958. Differences in practices between large and small firms in the management of temporarily idle balances may be a significant factor in explaining why the noncorporate business group showed a substantial rate of increase in bank deposits. For example, corporate business throughout the nation added \$4 billion to its holdings of Treasury securities during the last half of 1958. Comparable data are not directly available on holdings of Treasury issues for noncorporate business. However, holdings of Treasury issues by

"miscellaneous investors", the group in which noncorporate business is classified by the Treasury Survey of Ownership of the Federal Debt, were unchanged in 1958.

Demand balances for all business firms in the Fourth District increased a slight 1 percent between January 29, 1958, and January 28, 1959, reflecting the dominant weight of corporate nonfinancial figures in the total volume of privately-held demand deposits. Business deposits, amounting to \$5,064 million on January 28, 1959, were about 7 percent below the prerecession level of January 30, 1957. (See accompanying chart.)

Individual Accounts

Of all types of deposit holders, individuals posted the largest gain in demand balances at insured commercial banks in the Fourth District. Personal accounts rose \$186 million between early 1958 and early 1959, to account for about six-tenths of the increase for all types of depositors. Balances of individuals by early 1959 had more than recovered the ground lost during 1957. Growth in disposable income as the recovery progressed and the protection which had been afforded to accumulated deposits by unemployment compensation and other transfer payments during the recession were major factors in the expansion of personal demand balances. In addition, an increase in the number of personal accounts during 1958 was accompanied by a moderate increase in the average size of account.

Demand deposits of unincorporated farmers was the single class of ownership that declined in both number of accounts and dollar volume between the 1958 and 1959 survey dates. This occurred at the same time that farm income was improving. The larger decline in number of accounts (5 percent) than in dollar volume (less than 1 percent) indicates that forces other than farm income and general business improvement were at work. For example, consolidation of farm units and the switching of farm land to other uses such as highways and residential and industrial construction, has resulted in a reduction of the number of farms and farm operators. During 1958, the number of farms in the four

DEMAND DEPOSITS OF INDIVIDUALS, PARTNERSHIPS, AND CORPORATIONS
BY TYPE OF HOLDER
January 28, 1959

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

TYPE OF OWNER	Number (Thousands)	Amount (Millions)	Percentage Distribution		Percent Change From January 29, 1958	
			Number	Amount	Number	Amount
Business:	409	\$5,064	10.2%	59.7%	+ 1.4%	+ 1.1%
Nonfinancial.....	387	4,351	9.6	51.3	+ 0.5	- 0.6
Financial.....	22	713	0.5	8.4	+16.9	+14.0
<i>Corporate</i>	137	4,087	3.4	48.2	+ 0.7	- 1.8
<i>Noncorporate</i>	272	977	6.8	11.5	+ 1.5	+16.3
Personal	3,220	2,582	79.9	30.4	+ 3.1	+ 7.8
Farmers, Noncorporate	152	170	3.8	2.0	- 5.0	- 0.6
All Other ⁽¹⁾	249	673	6.1	8.0	+ 4.8	+11.3
TOTAL	4,030	\$8,489	100.0%	100.0%	+ 2.7%	+ 3.8%

NOTE: Details may not add to totals due to rounding.

(1) Includes nonprofit organizations, trust funds of banks, and foreign residents and firms.

states included, entirely or in part, in the Fourth District declined about 3 percent.

Nonprofit organizations account for about seven-tenths of the \$69-million increase between the 1958 and 1959 survey dates in the miscellaneous category labeled "All Other" in the accompanying table. Deposit balances

of foreign residents and firms declined by more than one-half, while trust funds of banks increased 12 percent.

(Information similar to that on the accompanying table, but further classified by size of bank and including average size of account, is available upon request.)



FOURTH FEDERAL RESERVE DISTRICT