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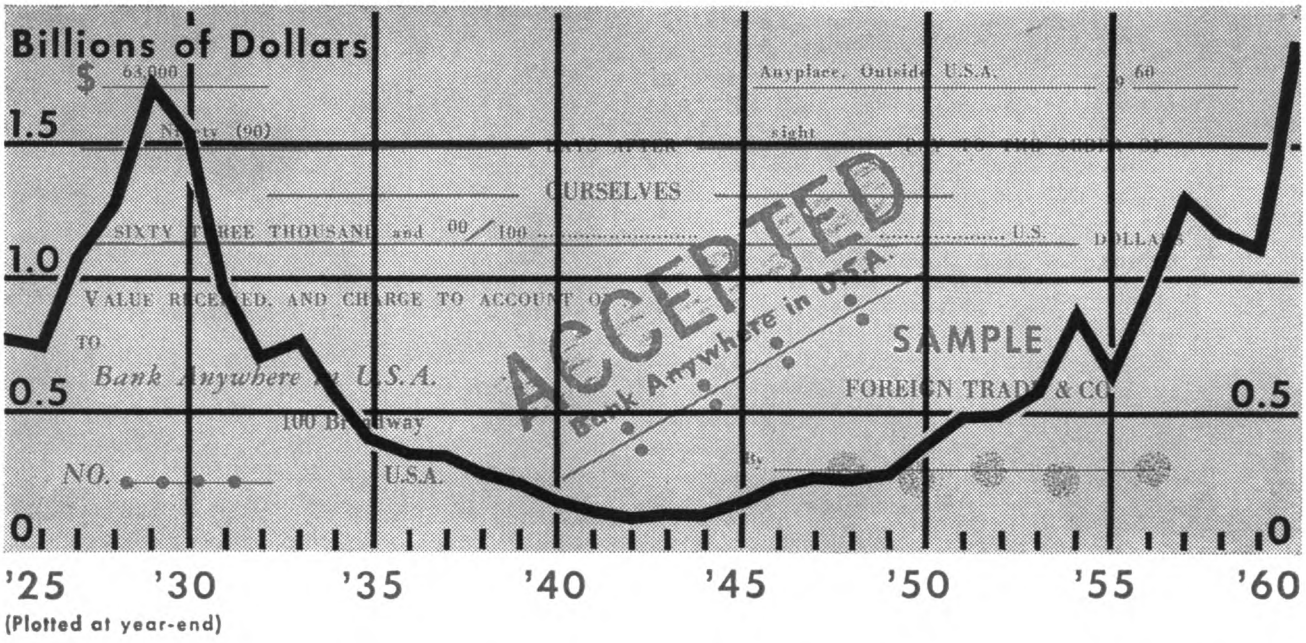
IN THIS ISSUE

Slackening in Heavy Industry.....2
Rebound in Use of Bankers' Acceptances..5
Patterns of State and Local Taxation...11
Notes on Federal Reserve Publications..15
Around the Fourth District.....16

VOLUME OF BANKERS' ACCEPTANCES OUTSTANDING, U.S.



(Plotted at year-end)

The recent sharp expansion in the use of bankers' acceptances as an instrument for financing foreign trade followed a period of relative decline which had lasted for nearly three decades.

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Slackening in Heavy Industry

THE COURSE of industrial production during 1960 can be characterized as a gentle slide. The slide, or sag, during 1960 contrasted with developments in 1959, when the anticipation of the steel strike stimulated industrial activity in the first half of the year, and the strike itself, with the resulting shortages of steel, sharply reduced industrial output during the second half. Thus, from a high point of 110 in June 1959, industrial production dropped to 102 in October, or by about 8 percent. (Figures are seasonally adjusted.)

The effects of the steel strike were not limited to developments in 1959, however; they continued to be felt in 1960. In the first quarter of 1960, inventory accumulation again reached the rate attained in the second quarter of 1959, when steel users had stockpiled as much steel as they could acquire. Strike-depleted inventories of steel were apparently substantially replenished by the end of the first quarter of 1960; if they were not back to pre-strike levels, they were high in relation to what steel consumers wished them to be.

Change in Steel Inventory Policy

It was evidently at about this time that the inventory policies of steel consumers underwent the change which has had such an important effect on industrial developments in 1960, particularly in the Fourth Federal Reserve District. For a variety of reasons, some of which can only be guessed, consumers of steel—primarily in manufacturing and construction—decided that they could get along with smaller inventories than they had previously been carrying, in relation to their current levels of output. Steel-using industries then began to reduce systematically their inventories of steel, with an immediate and drastic effect on steel industry operations, as shown in the accompanying chart.

Thus, steel production dropped from a monthly average of about 11.5 million tons in the first quarter to 7.4 million tons in June. Apart from seasonal drops in July (due to the Independence Day holiday) and in September, steel production showed little change thereafter until November, when it began a further decline, apparently in response to a weakening of activity in steel-consuming industries (as distinct from the inventory reductions of earlier months). Steel production in December was about 5.9 million tons, the lowest monthly total, apart from the months of the steel strike, since April 1958. Output in the year as a whole, although larger than in 1958 and 1959, fell short of the totals produced in 1951, 1955, 1956, and 1957.

With about 40 percent of the nation's basic steel capacity located in the Fourth Federal Reserve District, the impact of the drop in steel industry activity was correspondingly magnified. An impression of the differential effect on the District is shown in the attached chart of manufacturing employment in the United States and the Fourth District.

Sharp Drop in Factory Employment

In mid-November, factory employment in the Fourth District was 9 percent below the point reached in February, the most recent peak. For the U. S. as a whole the decline in manufacturing employment for the corresponding period was only 2 percent. As a result, the total factory workforce in the District in mid-November was only a little above the low point of the 1957-58 recession, while in the U. S. as a whole, manufacturing employment was still much above that level. (The Fourth District accounts for about one-tenth of the total number of persons on manu-

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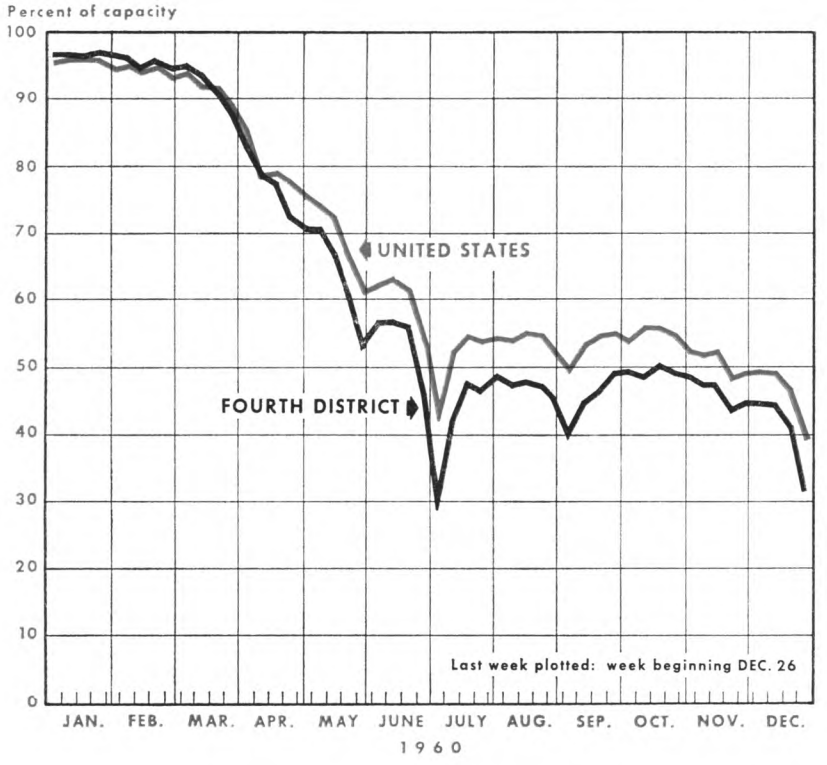
BASIC STEEL PRODUCTION



The desire of steel consumers to hold smaller inventories was primarily responsible for the sharp drop in steel production from January to June, 1960. The decline in output since October, in contrast, was apparently due to some weakening in final demand.

facturing payrolls in the United States.)

As might be expected from the decline in employment, unemployment has also increased in the District. In mid-November insured unemployment in the District was 44 percent above the mid-February total, while unemployment claims in the U. S. as a whole showed a decline over the same period of about 8 percent.

Output of Heavy Industry

The balance of this review will be devoted to a brief discussion of changes in 1960 in the output of the major durable goods industries important in the District. The data for individual industries are drawn from the Federal Reserve Board Index of Industrial Production. The output series to be covered are: iron and steel, coal, fabricated metal products, machinery, autos, and the clay-glass-stone products group. The manufacturing industries to be discussed (which constitute all of the selected series except coal) accounted for about two-thirds of value added by all manufacture in the District in 1957. (The iron and steel group comprehends all of the output of the iron and steel industry, including finished steel products and iron castings, in contrast to the production of ingot steel discussed earlier.)

In considering industrial output in 1960, it needs to be kept in mind that 1960 surpassed 1959 in industrial production, as well as in many other important measures of economic activity, despite the fact that industrial output, particularly in the durable goods industries, declined quite sharply during the year. The two different aspects of industrial production in 1960 are shown in the following table, which compares changes in the output of selected durable goods industries (those

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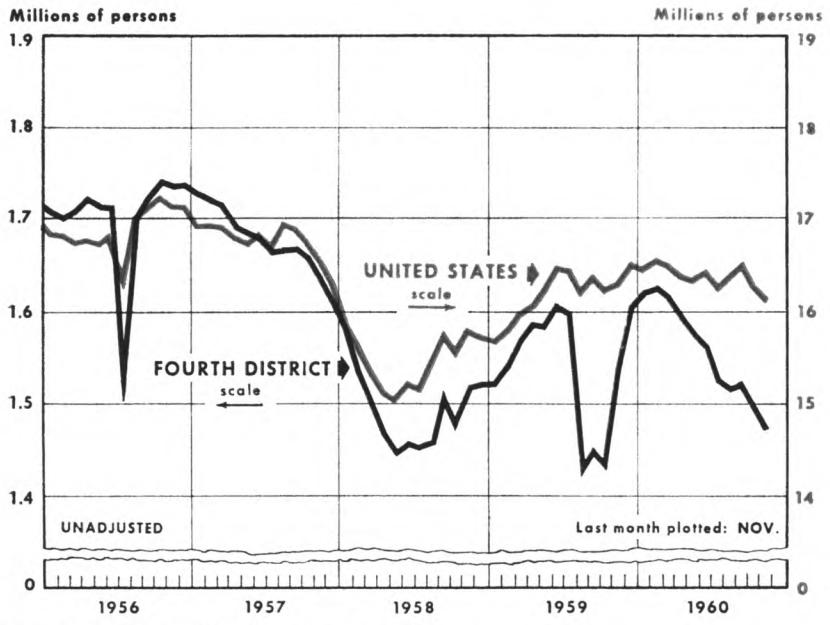
MANUFACTURING EMPLOYMENT



Sources: U. S. data, BLS: Fourth District data, Division of Research and Statistics, Ohio Bureau of Unemployment Compensation

Factory employment in the Fourth District during 1960 dropped more sharply than in the nation, due largely to the fact that 40 percent of the nation's basic steel capacity is located in the District.

which are especially important to the District) between the years 1959 and 1960 as well as changes which took place during 1960.

As the table shows, the change in output of the major District industries between 1959 and 1960 (eleven months) ranged from no gain, in the case of the clay-glass-stone group, as well as coal, to a substantial gain in the case of autos. During the first eleven months of 1960, in contrast, output of all the groups declined, with an especially sharp fall in iron and steel.

The pattern of the decline during 1960 varied considerably from industry to industry, however. As mentioned earlier, most of the reduction in iron and steel production took place in the first half of the year. In the case of autos, the larger part of the downturn took place from October to November, when, instead of the expected seasonal increase, auto production was reduced. Despite that drop, however, indicated production of about 6.7 million cars in 1960 would make it the best year for car production since 1955.

The pattern of decline in coal production in 1960 has followed closely that in iron and steel, to which it is closely related; here also, most of the falling off in production took place in the first half of the year. Coal production in 1960 was evidently about the same as in 1958.

Changes in Output of Selected Durable Goods Industries (Components of the Index of Industrial Production)

	Percent Change (1959 to 1960)*	Percent Change (Jan. 1960-Nov. 1960)**
Iron and steel	+ 9%	−41%
Coal	−0−	−17
Fabricated metal products	+ 3	− 6
Machinery	+ 5	− 7
Autos	+23	−19
Clay, glass, and stone products	−0−	− 3
All durable goods manufacturing	+ 4%	−11%
Total Index of Industrial Production	+ 4%	− 6%

* Based on 11 months of each year
** Seasonally adjusted

(*Continued on Page 10*)

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Rebound in Use of Bankers' Acceptances

THE USE of bankers' acceptances as an instrument for financing foreign trade has recently been in a sharp upswing, after a period of relative decline which had lasted for nearly three decades. During the year just past, the volume of bankers' acceptances outstanding in the United States increased by more than half, so that by year end the total exceeded the previous high which dates as far back as the year 1929.(1)

The use of bankers' acceptances as a short-term credit instrument enables business firms to raise funds for financing foreign trade transactions. A banker's acceptance is a time bill of exchange drawn on a bank by a trader in order to cover the cost of shipment of goods between countries, or storage of goods prior to shipment. When a bank "accepts" such a bill, the time draft becomes, in effect, a predated certified check which is payable to the bearer of the draft at some future date.

Background

The bankers' acceptance market in the U. S. officially began with the passage of the Federal Reserve Act in 1913. The Act authorized member banks of the Federal Reserve System to create acceptances under specified conditions related to foreign trade transactions. Although there had been established markets for bankers' acceptances in other countries for centuries, it was not until the latter part of the 1920's that the use of the acceptance market in the U. S. became relatively widespread. Following a downtrend which began in the early 1930's, the market for bankers' acceptances virtually disappeared during World War II, as shown in the chart on the cover. Beginning in the early postwar period, however, the use of such credit instruments was again stepped up, attaining a new all-time high in 1960.

The market for bankers' acceptances is a segment of the short-term money market. When a bank accepts a time draft drawn on it by a trader, the draft becomes a negotiable instrument which can then be discounted by a bankers' acceptance dealer for resale to investors. To the extent that the accepting bank elects to have the acceptance discounted rather than retain the instrument for its own account, the market for bankers' acceptances is thus an open market source of funds.

Since a bankers' acceptance is created to finance the movement or temporary storage of goods, the maturities of acceptances are tailored to fit the time required to complete the trade transaction. Although maturities can range from one to six months, acceptances usually carry maturities of three months' duration; shipping time is usually considerably longer in foreign trade than in domestic transactions. The use of the bankers' acceptance market allows a seller or exporter of goods to receive immediate payment for a shipment, while the buyer or importer need not make payment until the goods are received.

Due to the complex nature of the dollar acceptance market, accepting banks are relatively large and few in number; they are located principally in the money market center of New York, and have correspondent relations with banks in foreign financial centers.

For a trader, there are a number of advan-

(1) As of December 31, 1929, the total had been $1.7 billion. As of November 30, 1960, the figure was $1.9 billion. The figure for year end, 1960, may be estimated as about the same, or slightly higher than the November 30, 1960, figure, as indicated by the year-end position of the series shown on the cover chart. (Even today, however, the relative role of the bankers' acceptance in the total of foreign trade transactions is not as large as it was in 1929, insofar as total trade volume is now much larger than in 1929.)

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tages in using a bankers' acceptance credit, as compared with other sources of short-term credit. For example, buyers and sellers engaged in foreign trade are generally less well-known to each other than is the case in domestic trade. Insofar as a bank accepts a time bill of exchange, the name and credit of that bank serves as a backstop of the importer's obligation. In addition, any corporation which can qualify with a bank for an acceptance credit can gain access to the acceptance market, unlike the situation in the commercial paper market where only relatively large firms can obtain funds.

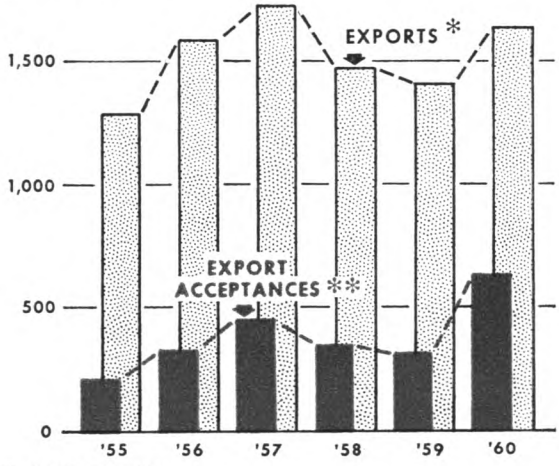
Bankers' acceptances represent for investors a relatively safe and highly liquid short-term investment, comparable in many respects to U. S. Treasury bills. An investor has recourse to the accepting bank, which is liable for payment of the acceptance should a trader default. For some investors, however, the increased amount of paperwork involved with acceptances of odd lot denominations makes them a relatively unattractive investment.

The dollar acceptance market is not employed exclusively by American traders. Lines of credit to foreign traders, particularly European traders, which are granted by accepting banks in this country are established through correspondent relations with foreign banks. In fact, bankers' acceptances have been more popular with European traders and investors than with American traders, since European businessmen have generally had a longer acquaintance and a greater familiarity with the acceptance as a credit instrument. The dollar acceptance market includes both American and foreign traders as well as American and foreign investors.

Types of Bankers' Acceptances

Under the Federal Reserve Act, a member bank can issue a bankers' acceptance under any one of four types of transactions, i.e., exports, imports, domestic or foreign storage of goods prior to shipment between U. S. possessions or between foreign countries, and dollar exchange. The bulk of bankers' acceptances have been created to finance U. S. merchandise exports and imports.

The volume of export acceptances outstanding has tripled in five years; the direction of year-to-year changes has followed that of merchandise exports.



* Monthly averages
** Outstanding at month end

At the end of World War II, the use of bankers' acceptances based on *exports and imports,* together, represented somewhat over 80 percent of total dollar acceptances. Since 1955, however, due to the increased use of bankers' acceptances to finance other than export and import transactions, these classifications now account for approximately 60 percent of total dollar acceptances. Despite the decline in export and import acceptances as a percentage share of total dollar acceptances, the amount of such acceptances outstanding has expanded by about 125 percent, or $586 million, since the end of 1955.

The pattern of expansion of the export and import types of bankers' acceptances since 1955 is associated with changes in the volume of U. S. merchandise exports and imports, as shown in the accompanying charts. Since 1955, on a year-to-year basis, changes in the amount of outstanding acceptances based on exports

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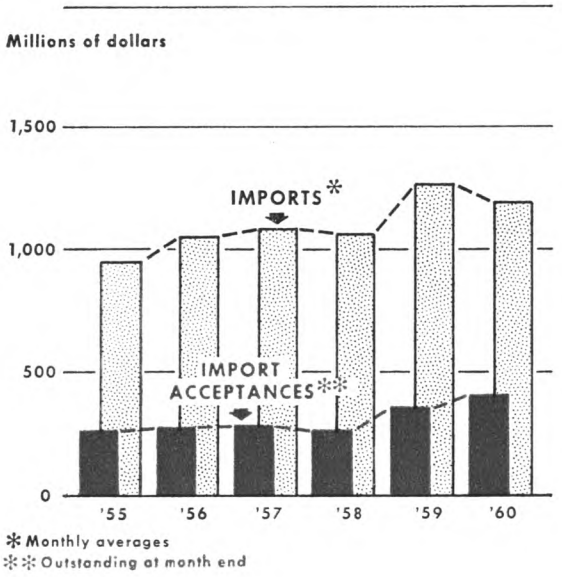
The volume of import acceptances increased by about two-fifths over a five-year interval.



and imports have almost always paralleled changes in the volume of U. S. exports and imports. One exception is that U. S. imports financed by acceptances continued to advance during 1960, although the volume of imports declined from that of the previous year.

The use of bankers' acceptances based on imports has historically been larger than acceptances based on exports. Since 1955, however, the volume of export acceptances has steadily expanded, amounting to $647 million at the end of November, 1960, which was well in excess of the $401 million of import acceptances outstanding. Such a development reflects, in part, greater use of the dollar acceptance market by foreign importers, since the creation of an acceptance is usually undertaken by the buyer or importer of goods. It also indicates the relatively recent and increasing use of the dollar acceptance market by American exporters. An American exporter, for example, in order to get cash immediately, might draw a trade draft on a foreign buyer, submitting the draft and shipping documents to his bank for acceptance.

Accepting banks are also permitted, under the Federal Reserve Act, to finance the *foreign and domestic storage* of specified goods prior to shipment. Goods included in this type of acceptance are usually readily marketable staples, such as cotton, sugar, and other agricultural products. Although the use of this type of acceptance has fluctuated widely since 1955, the amount outstanding at the end of November 1960, amounted to $674 million, or about one-third of total dollar acceptances. The amount of such acceptances outstanding has more than doubled during the postwar period.

A significant portion of the growth in total dollar acceptances has occurred in the amount of time drafts drawn for the purpose of *dollar exchange,* the relatively least important type of acceptance. According to the Federal Reserve Act, "any member bank may accept drafts or bills of exchange drawn upon it . . . , drawn under regulations to be prescribed by the Board of Governors of the Federal Reserve System by banks or bankers in foreign countries . . . for the purpose of furnishing dollar exchange as required by the usages of trade in the respective countries . . ." By creating a dollar exchange credit with an American accepting bank, a foreign bank can provide its customers with dollars to finance imports when the exports of that country to the U. S. are relatively low. The acceptances are repaid with dollars received from relatively larger exports to the United States in later months. Dollar exchange credits have maximum maturities of three months.

It is noteworthy that it has been only in the past three years that the demand for dollar exchange acceptances has widened. At the end of November 1960, acceptances based on dollar exchange amounted to $146 million, or about 8 percent of total dollar acceptances outstanding.

Holders of Bankers' Acceptances

Following a bank's acceptance of a time bill of exchange, the credit instrument can be either discounted through a dealer and then sold to investors, or held by the accepting

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bank for its own account. About 30 percent of total acceptances today are held by accepting banks, and approximately two-thirds of these are based on obligations of their own customers. Acceptances purchased by such banks, which account for the other one-third of their holdings, are held chiefly for the accounts of foreign correspondent banks.

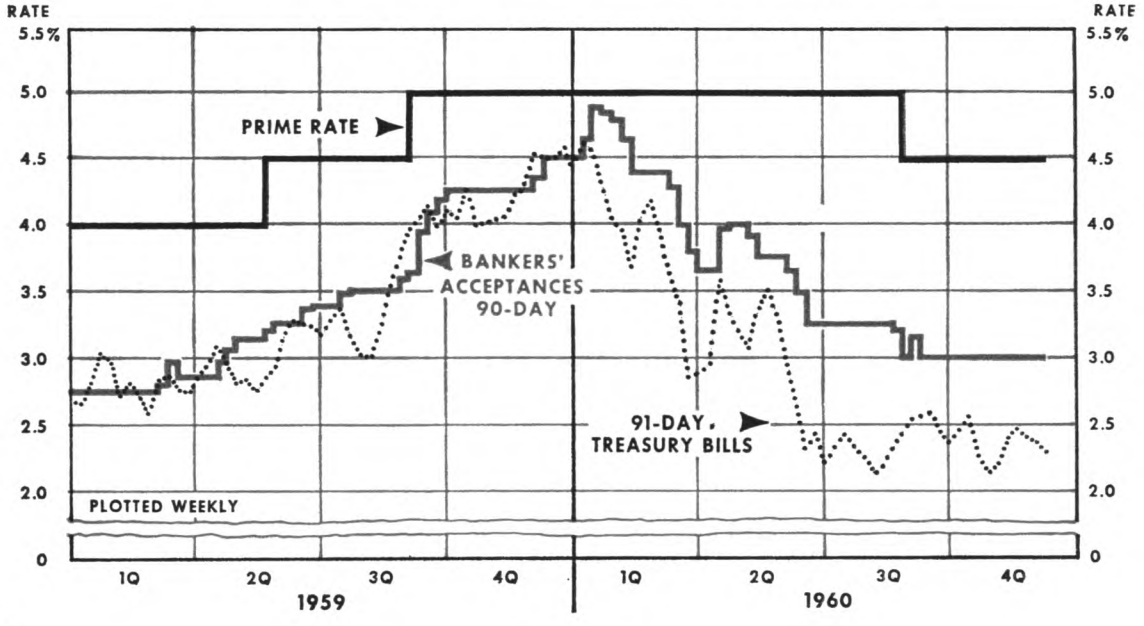
Periodically in the history of the dollar acceptance market, the Federal Reserve System has held bankers' acceptances. Since 1955, the System has held acceptances both for its own account and for the accounts of foreign central banks. The System purchases only three-name acceptances, which have been discounted in the open market and carry maturities of 90 days or less. (The "three names" refer to issuer, accepting bank, and dealer.)

Since 1955, when the Federal Reserve System re-entered the acceptance market, holdings of acceptances in each year have been less than 15 percent of the total dollar volume of acceptances outstanding. The bulk of its holdings is for the accounts of foreign central banks. Although the Reserve Bank holdings of acceptances for own account represent only about 2 percent of total acceptances outstanding throughout most of the year, such holdings usually increase somewhat toward the end of the year, when private demand for acceptances tends to slacken.

Foreign central banks and other foreign investors usually have held the largest single share of outstanding dollar acceptances. This is attributable in part to the greater familiarity of foreign investors with the credit instrument. In addition, irrespective of any yield advantages of bankers' acceptances relative to other short-term investments, earnings on foreign holdings of dollar acceptances are not subject to the U. S. income tax. On the other hand, the income tax exemption does not apply, except in special cases, to earnings from other short-term investments, such as Treasury bills or time deposits at commercial banks.

Although the income tax exemption is not available to American investors, the roll-call of purchasers of acceptances has included non-financial corporations, savings banks and insurance companies, non-accepting commercial banks, and other private individuals.

SELECTED SHORT-TERM MONEY RATES



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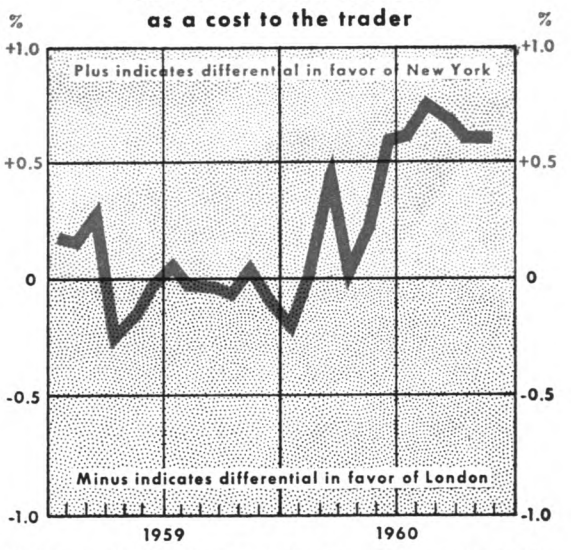
Rates

The open market interest rate on prime bankers' acceptances is a relatively sensitive indicator of the supply and demand for short-term funds. Rates are announced daily by dealers who discount acceptances prior to their sales in the open market. Dealers obtain their commission from the one-eighth percent spread between the bid and offered rates. The average yield on 90-day bankers' acceptances in most recent years prior to 1960 was about the same as the average yield on U. S. Treasury bills. One factor in the growth of bankers' acceptances during 1960 was the increased differential between the acceptance rate and the Treasury bill yield. The average spread between the rates moved from nearly zero in the fourth quarter of 1959 to .80 percent during the third quarter of 1960. It should be recognized, however, that the extent to which borrowers in the acceptance market are able to satisfy their demand for funds depends upon the supply of funds available to the market at any one time.

The exact differential between the bank prime lending rate on bankers' acceptances is rather difficult to determine, although the spread prior to 1960 was usually about one percent. For example, over and above the interest charge, a trader utilizing a bankers' acceptance credit must pay a minimum 1½ percent commission to the accepting bank for the use of the bank's name and credit. In addition, the spread between the acceptance rate (including the commission charge) and the prime bank lending rate tends to overstate somewhat the actual difference in the cost of borrowing. Since commercial banks usually set minimum balance provisions which require some portion of the borrowed funds to be kept on deposit with the bank, the actual cost of bank funds available for use is greater than the stated rate.

As shown in the accompanying chart, whereas the bankers' acceptance rate moved steadily toward the bank rate during 1959, a reverse trend was in evidence throughout most of 1960. The average spread between the bank prime rate and the acceptance rate

RATE DIFFERENTIAL ON BANKERS' ACCEPTANCES
as a cost to the trader



Note: The above differential between acceptance rates in the two centers has been adjusted for the forward premium or discount on sterling.

moved from .57 percent during the first quarter of 1960 to 1.64 percent during the third quarter, before leveling off at 1.50 percent during the months of October and November. If the 1½ percent commission charge is added to the acceptance rate, the cost of acceptance financing was nearly equal to bank financing throughout most of the second half of 1960, without reference to minimum balance requirements.

Rates in New York and London

An important factor in the recent increase of acceptance financing has been the relative attractiveness of such financing in New York, as compared with London. Foreign traders can secure financing in the dollar acceptance market through correspondent relations with American banks, while American traders can secure acceptance financing in the London market through foreign correspondents. Accepting charges of banks in both markets are about the same.

The relative attractiveness of the two centers thus depends on the rate differential between bankers' acceptances in the London and

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New York markets, and on the cost of covering the foreign exchange risk. The possibility of exchange rate fluctuations leads many traders who secure acceptance financing in a foreign currency to contract in advance, in the forward exchange market, for purchase of the needed foreign funds.

A British importer who secures a 90-day acceptance from a bank in New York to finance a purchase of goods from the United States would thus be likely to buy dollars for delivery in three months. In this way he would fix his obligation to the American bank in terms of sterling, thereby protecting himself against the possibility of paying more sterling to discharge his dollar obligation when the acceptance matures. Consequently, the cost of forward exchange is an integral part of the cost of financing between the two money market centers.

As shown in the accompanying chart, the difference between acceptance rates in New York and London, including adjustment for the forward discount (or premium) on sterling, fluctuated between the two centers during 1959. Throughout most of 1960, however, the differential between financing in the two money market centers was clearly in favor of New York. As a result, it was advantageous for both American and foreign traders to utilize the acceptance market in the United States, particularly since midyear of 1960.

Slackening in Heavy Industry

(*Continued from Page 4*)

In the cases of machinery and of fabricated metal products (an industry group which turns out such diverse products as stampings, fasteners, and furnaces) all of the decline took place in the second half of the year. The same is true of the clay-glass-stone group, where output was actually larger in midsummer than at the beginning of the year.

As the year 1960 was coming to a close, a number of spokesmen for heavy industry, including especially the somewhat buffeted steel industry, were seeing on the horizon at least some signs of a renewal in the pace of business orders. Few, however, were willing to commit themselves to a forecast of a very strong first quarter for 1961.

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Patterns of State and Local Taxation

(Fourth District)

WITHIN the Fourth Federal Reserve District there are more than 4,000 different governmental units (states, cities, townships, counties, school districts) which have the power to levy taxes in one form or another. This multiplicity of taxing units operates under legal powers that vary considerably from one state to another and from one community to the next. As a result, the tax pattern—i.e., the types of revenues collected and the sources from which they are derived—is necessarily not consistent throughout the District.

Before examining some of the major points of variation in taxing practices within the Fourth District, however, it may be noted that the over-all uptrend of statewide tax revenues in the area during the past decade has been broadly similar to that of the nation as a whole. Thus, in the fiscal year 1960,[1] the four states lying wholly or partly within the Fourth District (Ohio, Pennsylvania, Kentucky, and West Virginia) collected a total of more than $2.3 billion in tax revenues, a sum that was twice as large as corresponding revenues in 1951. During the same period, tax collections of all states in the nation increased 102 percent.

(1) State governments usually conduct their business on a "fiscal year" basis rather than by the calendar year, with the fiscal year normally running from July 1 through June 30. Pennsylvania, however, is an exception, with its fiscal year running from June 1 through May 31.

Nevertheless, according to the latest figures available, state and local tax burdens in the Fourth District states are below the national average. As shown in the accompanying table, in fiscal year 1958,[2] all four states in the District had combined state and local tax burdens which were below the national average, expressed as a percentage of personal income. In addition, the per capita state and local tax burden in the individual states within the Fourth District in fiscal year 1958, expressed in dollars, was in each case clearly less than the average burden of all states in the United States.

In the four states of the Fourth District, tax revenues, from a variety of sources, accounted in the aggregate for 66 percent of total state revenues in fiscal year 1959. The remaining revenues consisted of Federal grants, fees, fines, profits of state enterprise, etc.

Ohio

In Ohio, the only state completely within the Fourth District, state tax revenues between fiscal years 1951 and 1960 rose 108 percent, or slightly more than the national average. The largest single source of tax revenue

(2) Local taxation data are usually not available until at least two years after the end of the fiscal year.

TAX BURDENS OF FOURTH DISTRICT STATES

	Total State and Local Taxes as a Percent of Personal Income	Total State and Local Taxes Per Capita
Kentucky	7.7%	$107.18
Ohio	7.3%	$159.27
Pennsylvania	7.2%	$153.03
West Virginia	7.9%	$119.15
UNITED STATES	8.5%	$175.34

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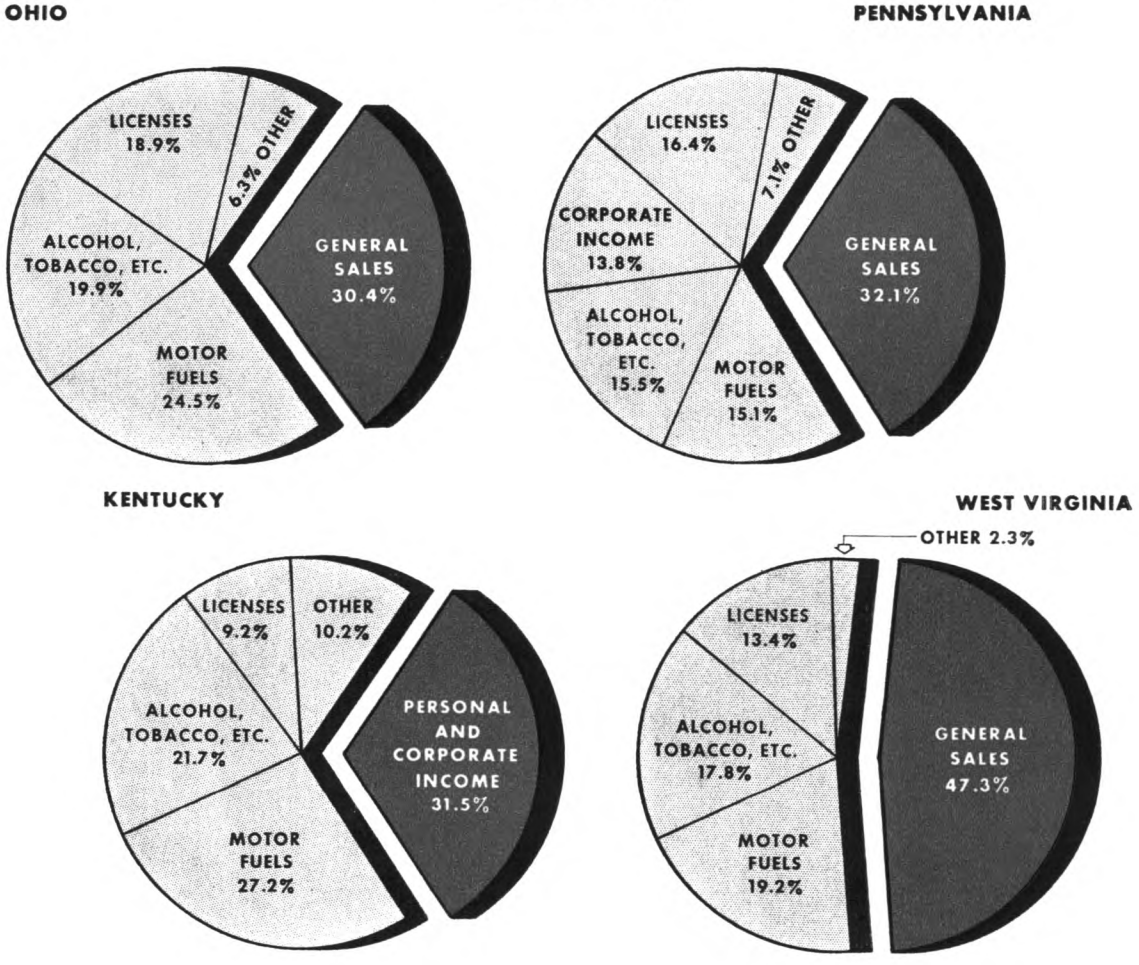
SOURCES OF STATE TAX REVENUES

Fiscal Year 1960



for the state is the general sales tax, which in fiscal year 1960 provided over 30 percent of total tax revenues. This tax has quadrupled its revenue yield since its inception in 1935. Like similar taxes in effect in 34 other states, Ohio's tax, levied at the rate of 3 percent, falls on general retail sales.

The second largest source of tax revenue in Ohio in fiscal year 1960 was the tax on motor fuels, which, levied at the rate of 7¢ per gallon, accounted for more than 24 percent of total tax revenues. Producing 19 percent of total Ohio tax revenues in fiscal year 1960, license taxes ranked third among the various sources of revenues. The remaining 27 percent of total tax revenues was derived from a number of excise taxes, such as the tobacco and beer taxes, the inheritance tax, and the gift tax. According to the sources of state tax revenues, most of the tax burden in Ohio rests clearly on either consumption or use, while business tax burdens are relatively light.

Pennsylvania

The state of Pennsylvania (in which 19 of the counties and some 33 percent of the popu-

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lation fall within the Fourth District) has a tax system with many features similar to that of Ohio. Like Ohio, Pennsylvania's total tax revenues have risen more than the national average, increasing 106 percent between fiscal years 1951 and 1960. The main tax-system similarity to Ohio lies in the significance for Pennsylvania of the sales tax. Although Pennsylvania did not introduce the Selective Sales and Use Tax until 1956, in fiscal year 1960, on the basis of a 4 percent levy, it accounted for more than 32 percent of total tax revenues. The sales tax on consumers was Pennsylvania's answer to the problem of finding a tax source, not already covered by Federal taxation, in order to meet growing state expenditures.

License taxes and motor fuel taxes which ranked second and third among Pennsylvania state tax revenues in fiscal year 1960, brought in 16 percent and 15 percent, respectively, of total tax revenues. Pennsylvania levies a tax of 5¢ per gallon on gasoline. Unlike Ohio, the state of Pennsylvania taxes the income of business corporations; this levy produced more than 13 percent of total tax revenues in fiscal year 1960.

Kentucky

Until July 1960, Kentucky, in which 56 of the counties and 43 percent of the population fall within the Fourth District, was unique among states of the District in that it did not levy a general sales tax, but did levy a tax on personal and corporate incomes. In July 1960, however, Kentucky joined the majority of the states in the nation by levying a 3 percent state sales tax. Prior to the introduction of the sales tax, taxes on both personal and corporate income had been the only sources of tax revenue responding significantly to increases in Kentucky's economic activity. In fact, the combined revenues of the personal and corporate income taxes in fiscal year 1960 made up more than 31 percent of total state tax revenues. Income tax revenues more than doubled between 1946 and 1960, while other tax revenues remained virtually the same. The rise in revenue from income taxes, however, was not sufficient to bring Kentucky's rate of increase in total tax revenue up to the national average. Thus, Kentucky's total tax revenues increased about 86 percent from 1951 through 1960, as constrasted with the national average rise of 102 percent.

The second largest source of tax revenue in Kentucky was the motor fuel tax which produced 27 percent of total revenue in fiscal year 1960 by means of a levy of 7¢ per gallon. The remaining 42 percent of the total tax revenues in fiscal year 1960 was collected through various excise taxes, license taxes, gift taxes, and property taxes, which were individually relatively unimportant.

West Virginia

The state tax situation in West Virginia, in which six of the counties and 11 percent of the population lie within the Fourth District, is unusual in a number of ways. For example, West Virginia's total tax revenues have increased only 68 percent in the last nine years, the smallest increase of the four states in the District and considerably below the national average. Moreover, West Virginia derives most of its tax revenues from one tax source, thereby creating an unusual tax structure. A gross sales tax, called the Business and Occupation Tax, combined with a consumer's sales tax, provided more than 47 percent of total state tax revenues in fiscal year 1960. Such heavy reliance upon sales taxation as the major source of revenue is somewhat at variance with the tax systems of the other states in the District. The motor fuel tax of 7¢ per gallon, which brought in 19 percent of total tax revenues in fiscal year 1960, and license taxes which contributed 13 percent in the same year, lagged far behind the sales tax as sources of revenue.

Considering the District as a whole, the taxation by the various states has resulted in steadily increasing tax revenues. As the states have sought new and additional revenues to pay for constantly increasing expenditures, there has been greater emphasis placed on sales and income taxes. It is noteworthy that state property taxes, which once constituted the main source of state tax revenues, are now

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virtually nonexistent, averaging only 3.2 percent of total tax revenues of all states in the Fourth District in fiscal year 1960. Taxes on motor fuel are important in all the states and are usually earmarked specifically for highway programs.

Local Taxation

The various local tax systems in all four states of the District have some noteworthy features. One of the most critical problems facing many local governments in the Fourth District, as well as others in the nation, is that of finding adequate income to carry on growing public services. Since World War II, for example, numerous efforts have been made to broaden local tax bases by inducing state legislatures to allow local governments to levy new types of nonproperty taxes. In only a few cases, however, have such changes been made. Thus, Ohio, Pennsylvania, and Kentucky are three of the only four states in the nation in which local units of government actually undertake to levy a tax on income. The other state (Missouri) has only one unit which utilizes such a tax. Thus, the municipal income tax is, by and large, a Fourth District phenomenon.

In *Ohio,* a 1919 ruling by the Ohio Supreme Court allowed local governments to tax that which is not taxed by the state. It was not until after World War II, however, that any local governmental unit utilized this ruling. At the present time there are over 50 local units in Ohio which tax personal and corporate income. Of the 41 cities of the United States having a population over 250,000, eight of them use the municipal income tax as a source of revenue. Three of the eight—Cincinnati, Columbus, and Toledo—are in Ohio. Although in these individual units, the income tax revenues average more than 35 percent of the total tax revenues, for the state of Ohio as a whole local income taxes make up less than 8 percent of the total tax revenues of all local governments.

The main tax utilized by local governments in Ohio is still the property tax, which provided more than 60 percent of the tax revenues of Ohio's cities, counties and school districts in fiscal year 1958. Other taxes such as sales and use taxes, motor fuel taxes, and other excise taxes accounted for the remainder of total tax revenues. In fiscal year 1958, in Ohio, local and state taxes combined took 7.3 percent of personal income.

Pennsylvania set the basis for its rather unusual local tax structure much more recently. In 1947, Pennsylvania Statute No. 481 allowed local governments to tax that which the state did not. Since corporate income was already taxed, such a tax was excluded from use by local governments, but local governments all over the state began to tax personal income. Although the Pennsylvania statute of 1947 was intended to relieve the tax burden of the property owner, property taxes still are the major source of tax revenue for the various local governments. The main difference is that since the inception of the local income taxes, property tax rates have remained essentially static. The combined state and local tax burden in Pennsylvania in fiscal year 1958 amounted to 7.2 percent of personal income.

Kentucky is another of the four states in the United States which, in effect, uses a local income tax. Taxes levied on earned income by some local units in Kentucky are legally identified as occupational license taxes.[3] A tax on income, however, is used by relatively few local units in Kentucky as compared with local governments in Ohio and Pennsylvania. In the part of Kentucky falling within the Fourth District, the cities of Lexington, Covington, and Newport levy such a tax.

Local tax revenues in Kentucky are derived mainly from the general property tax. None of the three larger Kentucky cities located within the Fourth District (Ashland, Covington, and Lexington) has a general sales or gross receipts tax. In fiscal year 1958, more than 57 percent of the tax revenues of these cities came from property levies. The total

(3) Although providing for payment of a percentage of any type of earned income, the occupational license tax was held to be a tax upon the privilege of working and conducting a business, with the amount of tax paid constituting merely a monetary measure of this privilege. (308 Ky 420 (1948)).

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state and local tax burden in Kentucky in fiscal year 1958 was 7.8 percent of personal income.

West Virginia is not included in the states of the nation which permit local income taxes, but its tax structure has its own unusual features. While the major portion of local taxes levied by cities, counties, and school districts is on property, the various cities, taken as a group, present a different picture. Whereas the national average in fiscal year 1958 showed 49 percent of the total revenues of all cities coming from property taxes, only 29 percent of the revenues of the cities in West Virginia were so derived. A relatively large percentage of the total revenues of the cities comes from municipal sales taxes which are patterned after the state sales tax. The combination of state and municipal sales taxes thus tends to emphasize the regressive character of West Virginia's total tax picture. The total state and local tax burden in West Virginia in fiscal year 1958 was 7.9 percent of personal income, the highest of the four states in the District.

NOTES ON FEDERAL RESERVE PUBLICATIONS

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

"Farm Prices and Consumer Food Prices", Federal Reserve Bank of San Francisco, November 1960.

"America's Capacity to Produce", Federal Reserve Bank of Chicago, November 1960.

"Why Has Money Become Easier?", Federal Reserve Bank of Atlanta, December 1960.

"Gold in the American Economy", Federal Reserve Bank of Chicago, December 1960.

"Corporate Participation in the Government Securities Market", Federal Reserve Bank of Kansas City, December 1960.

(*Copies may be obtained without charge by writing to the Federal Reserve Bank named in each case.*)

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Around the Fourth District—

Department Store Sales

	Nov. '60 % change from year ago	Jan. - Nov. '60 % change from year ago
Toledo	+ 7%	+ 2%
Portsmouth	+ 4	− 1
Columbus	+ 2	+ 2
Cleveland	− 1	+ 2
Pittsburgh	− 1	+ 4
Cincinnati	− 2	+ 1
Youngstown	− 3	+ 1
Akron	− 3	+ 1
Canton	− 4	− 1
Wheeling	− 4	−0−
Lexington	− 6	− 4
Erie	− 9	− 3
Springfield	−12	− 8
FOURTH DISTRICT TOTAL	−0−	+ 2

* * *

Aggregate Fourth District *department store sales* during the year 1960 were about 2 percent above those of 1959.

* * *

Electric power output in northeastern Ohio averaged 6 percent below a year earlier during November and December. A 6 percent increase had previously been registered during September and October.

* * *

As the new year got under way, commercial and industrial *loans* at 26 weekly reporting banks in the Fourth District were nearly 5 percent above the year-ago level.

* * *

During the week ended January 4, *reserves* of 26 reporting banks with the Federal Reserve Bank increased while *borrowings* declined. For the second consecutive week, reporting banks were not in debt to the Federal Reserve bank.

* * *

The number of claims filed in Cleveland for *unemployment* compensation increased by 2,500 during the Christmas holiday week to a total of nearly 44,000, more than twice as many as in the corresponding year-ago period. The week's increase climaxed a net rise of approximately 8,000 during the month of December.

(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.)

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