

MONTHLY *Business Review*

FEDERAL RESERVE BANK of CLEVELAND

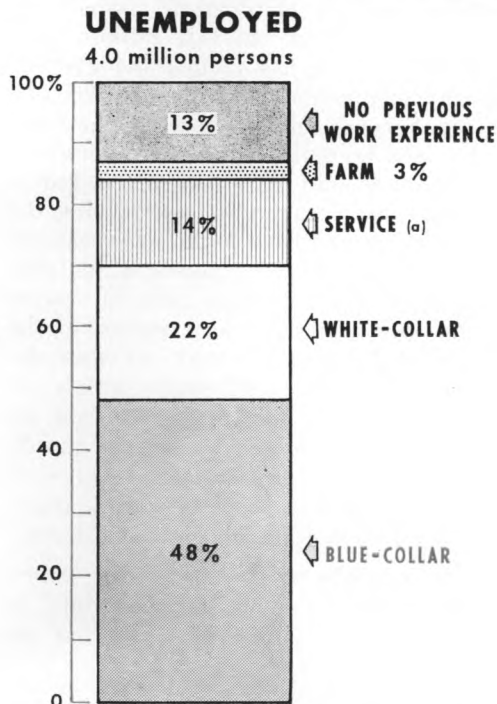
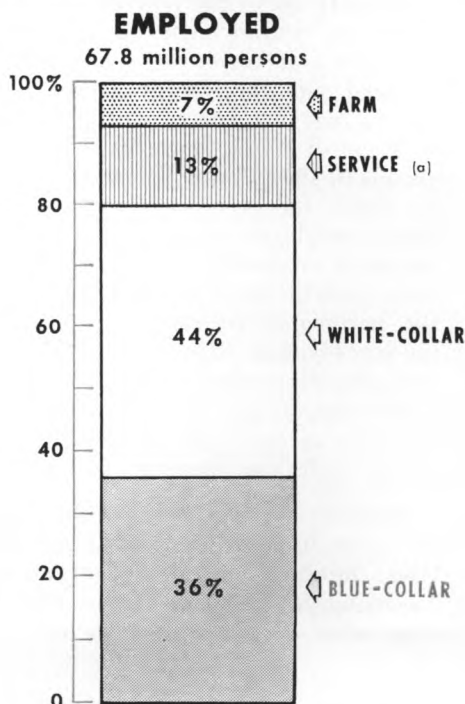
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In 1962, the average number of unemployed persons in blue-collar occupations in the U.S. was more than double the unemployed in white-collar occupations. This was in sharp contrast to the employed portion of the civilian labor force where blue-collar workers were outnumbered by white-collar workers.



(a) Employed in private households and other service occupations.

Source of data: U. S. Department of Labor

Some Aspects of Unemployment

PRESIDENT KENNEDY, in his initial Manpower Report to Congress required under the Manpower Development and Training Act of 1962, emphasized the waste of "an intolerably large proportion of (the nation's) human resources through unemployment and underemployment". He also drew attention to the fact that despite the large supply of unused manpower there exists a serious shortage of qualified workers for essential occupations. There are at present more workers who are experienced in mining coal, making steel or performing heavy manual labor than the economy is able to employ; while at the same time there is a short supply of people capable of working as engineers, computer programmers or appliance repairmen.

This imbalance in manpower utilization is an outgrowth of two factors. First, the net annual increase in employment opportunities—averaging about one-half million over the last five years—has trailed the average net growth in the labor force by over 200,000 each year. Second, the skill level of the work force has not been improved fast enough to meet the rising skill requirements of industries. Hence, the economy is experiencing the existence of specific hard-to-fill job vacancies in the midst of growing surpluses in the labor market. Creating additional jobs—in excess of the number needed to keep abreast of the growth in the labor force—may not cause unemployment to decline sufficiently unless the skills required for the new jobs can be matched by skills available among the supply of jobless workers. One solution, of course, is to develop the missing skills through planned training and retraining of the labor force.

The chart on the cover of this issue, which is supplemented by more detailed data in Table I, shows the imbalance which has de-

veloped between the employed and the unemployed portion of the labor force. A large proportion of the unemployed in 1962 were "blue-collar" workers, particularly semi-skilled operatives from goods-producing industries. Among the employed workers, by contrast, the white-collar group was larger than the blue-collar group, as had been true for several years prior to 1962. This reflects, in part, the increased employment of non-production workers in the manufacturing industries simultaneous with cuts in the number of production workers. Unless the jobless blue-collar workers can be reabsorbed by the industries from which they were displaced, their opportunities for jobs are limited, as it is more difficult for them to meet the requirements of expanding industries outside the goods-producing group.

Table II shows the average annual amount by which employment in major industry divisions and major occupation groups has changed over the last five years, along with the average number of unemployed workers in each of those industry and occupation groups in 1962. Employment changes indicate in which industries and occupations additional employment opportunities might be expected to develop, assuming that employment growth over the short term will follow the pattern of recent changes. By comparing employment changes with the number of unemployed workers in the several groups, a determination can be made as to whether the available supply and the anticipated demand of job skills are likely to match.

Employment has declined during the past five years in all of the goods-producing industries: mining, contract construction, manufacturing, and agriculture, as well as in the blue-collar occupations. (The blue-collar oc-

TABLE I
OCCUPATIONAL COMPOSITION
OF EMPLOYED AND UNEMPLOYED
WORKERS, 1962

(Percentages of Total Employed and
Total Unemployed)

Occupation Group	Employed Workers	Unemployed Workers
Blue-collar workers . . .	35.7%	48.3%
Craftsmen and foremen	12.8	11.4
Operatives	17.7	24.4
Nonfarm laborers . . .	5.2	12.5
White-collar workers . . .	44.1	21.5
Professional and technical	11.9	3.5
Managers, officials, proprietors	10.9	2.8
Clerical workers	14.9	10.5
Sales workers	6.4	4.7
Service workers	13.0	14.2
Private household . . .	3.5	3.0
All other	9.5	11.2
Farm workers	7.2	2.8
Farmers, farm managers	3.9	.2
Laborers	3.3	2.6
No previous work experience		13.2
	100.0%	100.0%

Source of data: U. S. Department of Labor

occupations contribute a large portion of employment in all the goods-producing industries except agriculture.) Considering their performance over the five-year span, it seems unlikely that the goods-producing industries will boost their employment sufficiently to reabsorb a significant portion of the unemployed. Agriculture, which experienced an average annual employment loss of 200,000 even before the latest five-year period, can be written off as a potential source of new employment. The same conclusion applies, in part, to mining where the percentage annual loss has been even larger than in agriculture. Construction employment could conceivably reverse its recent downward trend if the expected increase in family formations should spark an increase in housing demand.

In manufacturing, the largest among the four industry divisions in the goods-produc-

ing sector, the net employment decline over the last five years, although in part reflecting cyclical fluctuations, is the result of a shift toward fewer production and more nonproduction workers. That shift offered few employment opportunities for displaced production workers, as mainly professional, administrative and clerical employees were hired for the nonproduction jobs. A significant improvement in production worker employment appears unlikely as long as the substitution of machines for human labor continues. Therefore, workers in the blue-collar occupations, comprising almost one-half of all the unemployed in 1962, must look primarily outside the goods-producing industries for re-employment.

Employment gains over the five-year span, as Table II indicates, occurred principally in service industries. Within that group, government exceeded all industries in the private sector in both size and percentage of employment growth. Although the increase in all service-producing industries except government was lower during the last five than during the preceding ten years, continued expansion of these industries and of the associated occupations seems certain. Conceivably, such increases in employment could provide berths for the unemployed with suitable skills. It must be remembered, however, that a good portion of the added employment in retail selling, banking, real estate and insurance in recent years represented part-time jobs which met the needs of housewives looking for part-time employment and of employers interested in hiring part-time help for lengthened business hours. With close to 90 percent of the unemployed currently looking for full-time work, the creation of additional part-time positions might attract marginal workers, such as students, but only additional full-time positions could bring down the unemployment level significantly.

A further point should not be overlooked. The employment gains in the field of public administration, especially in state and local government, which accounted for two-thirds of the net increase in wage and salary posi-

TABLE II
UNEMPLOYMENT AND
CHANGES IN EMPLOYMENT
By Industries and Occupations

	Average Annual Change in Employment 1957-1962 (a) (000's)	Average Unemploy- ment 1962 (b) (000's)
INDUSTRY DIVISIONS		
Goods-producing industries		
Agriculture	— 206	128
Manufacturing	— 85	1055
Contract construction	— 45	473
Mining	— 36	56
Service-producing industries		
Transportation & public utilities	— 63	176
Finance, insurance, real estate	+ 63	88
Trade	+ 137	685
Services and miscellaneous	+ 202	616
Government	+ 312	80
MAJOR OCCUPATION GROUPS		
Farmers & farm laborers	— 239	112
Operatives	— 98	972
Industrial laborers	— 24	502
Craftsmen, foremen	+ 3	457
Sales workers	+ 44	187
Clerical workers	+ 191	420
Professional, technical workers	+ 314	140
Private household workers	+ 49	121
Other service workers	+ 185	447
Managers, officials, proprietors (excluding farm)	+ 141	112

(a) The industry breakdown of employment changes reflects only wage and salary employees (except for agriculture), while the occupational breakdown includes all employed persons.

(b) Persons without previous work experience are excluded; the industry breakdown also excludes unpaid family workers.

Source of data: U. S. Department of Labor

tions over the past five years, were sparked by the rapid expansion in the areas of public education and public health. Demand for teachers and other professional workers will remain strong. Again, however, new job openings in those fields will do more to brighten employment prospects for new labor force entrants with the necessary credentials than to enhance the fortunes of the present unemployed who do not possess the required skills.

In the formulation of manpower policies it would seem appropriate to assume that employment growth will be largest in government, private service-producing industries, and nonproduction functions of manufacturing. With respect to new labor force entrants, particularly those who will reach working age during this decade, the immediate task is to evaluate our educational facilities at all levels to assure that they are equipped for training adequate numbers of qualified persons to keep industries staffed and prevent occupational shortages, and to minimize the number of inadequately prepared entrants.

A more immediate and perhaps more difficult task is to provide the present unemployed, many of whom are permanently displaced due to inadequate or obsolete skills, with employment opportunities. This calls for an extensive program of vocational training to improve the skills of unemployed persons with a white-collar background, and to replace or provide skills for a much larger number of those whose work experience has been in manual or blue-collar occupations.

Occupational retraining of workers permanently displaced from their jobs has been carried out for several years under individual state programs and, more recently, under federal auspices. To a considerable extent, the training has been in the area of white-collar and service occupations. The results, though encouraging in some aspects, have been less than sensational. For example, through the middle of 1962, some 6,000 persons in 147 projects had started training under the provisions of the Area Rehabilitation Act of 1961, while about 6,300 persons were enrolled at the end of 1962 in about 300 courses authorized under the more broadly designed and more generously endowed Manpower Development and Training Act of 1962 (MDTA). More recent figures indicate that the number of trainees is growing.⁽¹⁾

The requirement that training courses under MDTA can be approved only if specific local occupational shortages have been certi-

(1) Over 800 MDTA projects with over 22,000 trainees had been started as of June 1, 1963.

fied, acts as a brake on the speed at which training can reach the high volume envisaged by its sponsors. A large expansion of training activities should not be expected unless the economy expands first and creates more jobs. If, at that point, qualified workers are neither on hand nor available through upgrading and on-the-job training of present employees, retraining of unemployed persons could swing into high gear.

Vocational retraining is a logical approach to the task of upgrading the skill level of the labor force. The success of the training program, however, depends not only on the development of enough job vacancies to justify training but also on the presence of enough workers who possess both the desire and the ability to be fitted with a new vocational skill.

A recently published survey of over 2700 recipients of unemployment compensation in the Detroit labor market area offers some quantitative information as to the degree of interest in retraining among jobless workers.⁽²⁾ Four persons out of five in the sample group expressed willingness to go to school for occupational retraining.⁽³⁾ Interest was found to be lower among older than among younger people, declining sharply from about 85 percent for the age groups below 45 years to a low of 20 percent among persons 65 years and older. Previous educational attainment did not significantly affect the degree of interest except among the few college graduates in the sample, most of whom declined to seek training in a new skill.

The study did not cite reasons why 20 percent of the persons questioned expressed no interest in retraining. Unwillingness to shift to lower-paying occupations or to leave the community, usually included among possible objections to retraining, should not have influenced the replies substantially since the survey question omitted any references to

specific occupations or job locations. Fear of "going back to school" among older persons or those with poor schooling, fear of losing seniority rights by transferring to another line of work, or simply a feeling of resignation, could have prompted negative votes.

Although an unemployed worker may be interested in receiving vocational retraining, his ability to benefit from it might be limited by such obstacles as an inadequate education or discriminatory employment practices in his community with reference to age, sex or race. While these limitations are not directly measurable, their potential effect may be suggested by data on age, sex, race and education of job seekers. Statistics on the 4 million unemployed in 1962 reveal that 62 percent were men, that two out of every ten were teenagers and three were at least 45 years old, and that one out of five was a Negro. The annual data do not include information on educational attainment.

A special survey of the unemployed 18 years and older, for March 1962, showed that 37 percent had completed their high school education and almost the same percentage had had only 8 years of schooling or less, including 8 percent "functional illiterates" with less than 5 years of grade school. Corresponding figures for the civilian labor force 18 years and older show that 54 percent held high school diplomas, and 27 percent reported not more than 8 years of elementary school, including close to 5 percent with less than 5 years.⁽⁴⁾

As a high school education becomes an essential requirement for a growing number of jobs, it also becomes a prerequisite for en-

(2) Wickersham, Edward D., *Detroit's Insured Unemployed and Employable Welfare Recipients*, Kalamazoo, Mich. (E. W. Upjohn Institute for Employment Research) 1963.

(3) The sample was comprised of 80 percent males; two-thirds of the persons were under 45 years of age and 20 percent were Negroes. In terms of their occupations, 20 percent were unskilled, twice that number semiskilled, and 22 percent skilled.

(4) Data available for individual states or localities corroborate the national figures. For example, information published quarterly by the Pennsylvania Bureau of Employment Security for the state's insured unemployed show that barely one-third of their number in 1962 possessed a high school diploma while two-fifths had no high school education at all. Among older age groups and blue-collar occupations the deficiency in schooling was even more pronounced. Only one-sixth of the insured unemployed over 44 years of age were high school graduates while three-fifths had had only 8 years of schooling or less.

Of the more than 2700 insured unemployed in Detroit (see footnote 2) one-third had attended only elementary school (for 8 years or less) while slightly fewer had completed high school. Nonwhites in the Detroit group included 21 percent high school graduates and 44 percent with only elementary school.

rollment in training classes. As a result, inadequate schooling may turn out to be a serious obstacle for many potential trainees.

There are no statistics to show how many eligible persons do not receive training on the grounds that they lack a basic education or that due to their age or race there would be little opportunity for them to be employed after completion of the course. The mortality rate in the procedure by which suitable trainees for specific courses are selected from the vast pool of eligibles is surprisingly high. It may be a clue to what appears to be a wide gap between intention and feasibility of the program. The 6300 people actually enrolled in training classes by the end of December 1962 came from a group of less than 9000, the final survivors of an initial group of over 107,000 "prospects" whose number had been successively reduced through screening interviews and testing.⁽⁵⁾

Those 6300 trainees do not appear to represent a cross-section of the unemployed. They included over 60 percent of persons in the prime age group between 22 and 44 years. Only 10 percent of these selected were over

(5) More recent reports show 269,000 "prospects" and 27,000 "finalists" through April of this year.

44 years of age.⁽⁶⁾ Over 60 percent were men and women who had completed their high school education, and only 10 percent of the trainees had gone to school for only eight years or less. More recent data, through April of this year, show the same preponderance of trainees from the "preferred" age and education groups.

Obviously, the present manpower training program cannot train persons with minimum qualifications unless jobs that cannot be filled and are within their range of ability are available. Perhaps a different approach is called for in their behalf. Instead of training workers to enable them to meet requirements of existing or anticipated jobs, efforts might be made to develop jobs suited to the abilities of available workers whose educational deficiencies preclude effective skill improvement. As an example, it has been suggested that an "intensive study of the job structure in hospitals, restaurants, hotels, motels, laundries and other service industries" might result in additional employment of unskilled workers.⁽⁷⁾

(6) MDTA data for Ohio, as published by the Division of Research and Statistics of the Ohio Bureau of Unemployment Compensation, show an even lower percentage of trainees over 44 years.

(7) Professor William Haber, in his preface to Wickersham's study of unemployed workers in Detroit (see note 2).

Patterns In Bank Deposits and Earnings

(Fourth District)

RECENT YEARS have witnessed some interesting developments in commercial banking. Of particular significance is the pattern of deposits at commercial banks and the subsequent impact on bank resources and income. The emerging pattern in banking is a nation-wide phenomenon, but this study is confined to developments at member banks in the Fourth District. The importance of the changes can be more clearly documented by a review of the trend that has emerged in the period from the close of 1957 through 1962.⁽¹⁾

In the subject period, the total resources of all member banks in the Fourth District increased by \$3.9 billion, or 25.6 percent. More than two-thirds of this growth was provided by a \$2.6 billion increase in time deposits. Time deposits expanded steadily by nearly 60 percent during the five year period, while demand deposits increased by only 5 percent. As a result, the ratio of time and savings deposits to total deposits rose from 43 percent in 1957 to an average of nearly one-half of total deposits of all Fourth District member banks in 1962.

The growing importance of time and savings deposits as a source of funds is principally the result of higher interest rates available on savings deposits and the introduction of negotiable time certificates of deposit.

Commercial banks have been successful in attracting larger proportions of individual savings, as well as an increasing share of liquid assets of corporations and state and local governments. In recent years, corpora-

tions and state and local governments have been placing increased emphasis on the profitable utilization of idle funds. The results of a survey of negotiable time certificates of deposit conducted in the Fourth District by the Federal Reserve Bank of Cleveland reflect this trend.⁽²⁾ As of December 5, 1962, the volume of negotiable time certificates outstanding at 26 weekly reporting Fourth District member banks was over \$500 million. The volume was double the amount outstanding one year earlier and over ten times the amount outstanding as of December 31, 1960.⁽³⁾

Corporations, states and political subdivisions hold the bulk of the certificates. An important part of the recent increase in time deposits may have represented a shift from demand deposits, on which banks are not permitted to pay interest. In addition, banks are now able to compete with other short-term interest bearing obligations, e.g., U. S. Treasury bills and commercial paper, which have, in recent years, served as an investment media for corporate cash surpluses.

Earning Asset Patterns

While time deposits have provided Fourth District member banks with the principal source of funds during the past five years, the attempt to maintain the rate of profitability on these costlier resources has served as the principal factor in changing the composition of earning assets.

(2) The survey was part of a nation-wide study conducted by the Board of Governors of the Federal Reserve System.

(3) While the ten-fold increase in negotiable time certificates since 1960 is distorted by the size of the base, the trend is, nevertheless, important.

(1) This period was characterized by a more rapid growth in time deposits than had prevailed earlier in the postwar period.

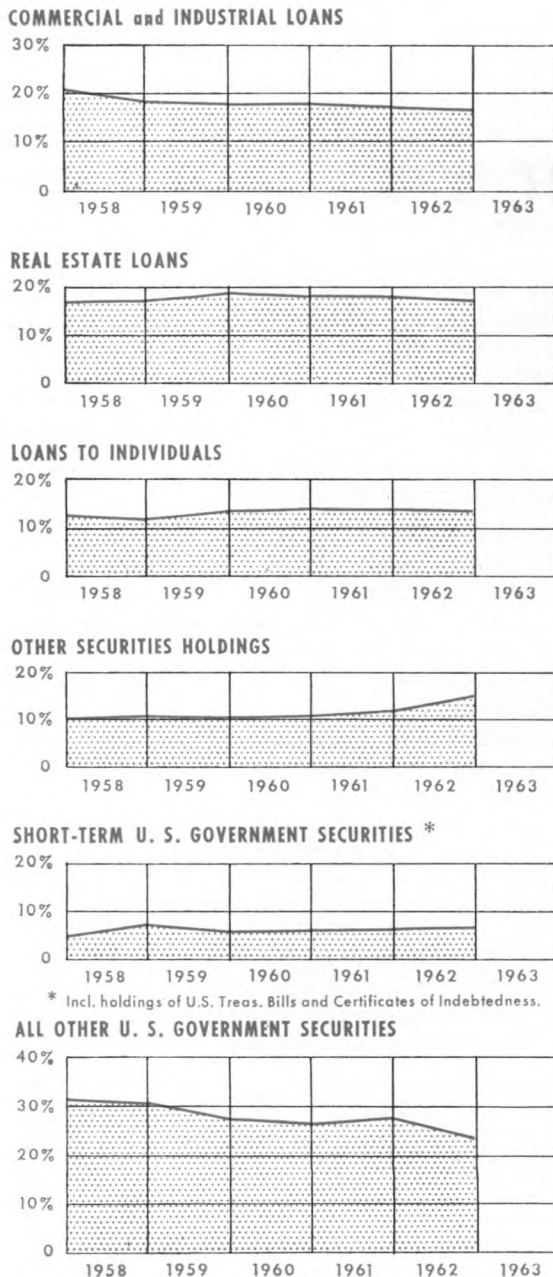
Lending patterns have changed as new outlets have been sought to offset the slack in business loan demand. Commercial and industrial loans have become a less significant portion of the earning assets of commercial banks as both financial and non-financial corporations have become less dependent upon the banks for working capital requirements. Many firms have been able to satisfy capital requirements from internally-generated funds resulting from retained earnings and more liberal depreciation allowances. In addition, an increasing number of corporations have resorted to the commercial paper market as a convenient and less costly method of acquiring short-term capital.⁽⁴⁾ Corporations have also become important suppliers of funds to the money market, e.g., by investing in short-term paper. The growing importance of self-financing techniques such as these has contributed to the declining importance of commercial and industrial lending by commercial banks. In view of the decline, banks have had to find other uses for loanable funds.

As an alternative, banks have resorted to aggressive expansion of loans to individuals and to additions to their investment portfolios. Since 1957, loans to individuals provided 16 percent of the \$3.9-billion increase in Fourth District member bank assets. Investment in tax-exempt state and local government securities accounted for 29 percent of the expansion, while mortgage loans accounted for a large part of the remaining advance in bank credit.⁽⁵⁾ As a result, holdings of municipal securities doubled and loans to individuals expanded by 43 percent in the 1957-1962 period. Real estate lending grew by 37 percent, despite intense competition from savings and loan associations. In contrast, commercial and industrial loans and holdings of U. S. Government securities advanced only 5 percent and 8 percent, respectively.

(4) Financial corporations sell sizeable amounts of short-term, negotiable paper directly to investors. Currently, the stated rate of interest on this paper is at least one percent less than the "prime rate" at commercial banks.

(5) In this article, municipal securities holdings or revenue from municipal securities refers to the asset item "other securities" holdings, since municipal obligations account for about 90 percent of all other securities.

Chart 1.
SELECTED EARNING ASSETS
AS A PERCENT OF
TOTAL EARNING ASSETS
Fourth District Member Banks
as of December 31



Source of data: Federal Reserve Bank of Cleveland.

As alternative uses for funds have been exploited more fully, the asset mix of Fourth District banks has been noticeably changed, as shown in Chart 1. Of particular interest is the increasing representation of risk assets and the declining importance of investment in U. S. Government securities.⁽⁶⁾ As the growth in time deposits accelerated in 1961 and 1962, the banks intensified their efforts to acquire higher-yielding risk assets to offset rising time deposit expense. Growing willingness among many banks to reduce downpayment requirements and extend maturities on real estate and consumer loans allowed them to compete more aggressively. The volume of loans of this type has been successfully expanded but not without some sacrifice of liquidity.⁽⁷⁾

total loans to total deposits for all Fourth District member banks rose, although irregularly, throughout the 1957-1962 period. Second, the ratio of risk assets (defined as total loans and all securities other than U. S. Government securities) to total assets, which is a more revealing measure, likewise rose during the period. The decline in liquidity of Fourth District member banks is the natural result of the reallocation of earning assets which was undertaken to justify the acceptance of larger proportions of costlier time deposits. Declining liquidity is probably considered by banks as more desirable than the prospect of sharply eroding profits. Part of the rationale of this approach reflects the fact that in the past there has been less volatility associated with time deposits as compared with demand

LIQUIDITY MEASURES of FOURTH DISTRICT MEMBER BANKS

Ratios from Balance Sheets as of December 31

RATIO	1957	1958	1959	1960	1961	1962
TOTAL LOANS to TOTAL DEPOSITS	46.9	45.9	50.5	51.7	49.9	51.5
RISK ASSETS* to TOTAL ASSETS	50.3	49.6	53.6	54.6	53.7	57.7

* Total loans and investments, excluding U. S. Government Securities holdings

Source of data: Federal Reserve Bank of Cleveland

There are indications that most of the growth in holdings of municipal bonds occurred in the longer-maturities where higher yields are available. While the increased yield was believed essential, the extension of the average maturity of these securities resulted in a reduction of liquidity.

The accompanying table illustrates the recent change in liquidity through the use of two conventional measures. First, the ratio of

deposits. Thus, many bankers reason that there is less need for secondary reserves.

On the other hand, as indicated in Chart 1, the banks have maintained the liquidity of their non-risk assets by concentrating a constant proportion of their increasing earning assets in short-term U. S. Government securities.⁽⁸⁾

Operating Results

The combination of an increasing proportion of time deposits and the shifting empha-

(6) Risk assets, for purposes of this article, are defined as total loans and all investments other than U. S. Government securities.

(7) Real estate and consumer loans of commercial banks are usually extended to individual borrowers and for extended periods of time, which increases the risk of default and limits the banks' ability to liquidate these assets. Loans to commercial and industrial customers are usually considered less risky and more liquid.

(8) Short-term U. S. Government securities, as used in this article, are defined as holdings of U. S. Treasury bills and certificates of indebtedness. They do not include holdings of Treasury notes and bonds scheduled to mature in 12 months or less.

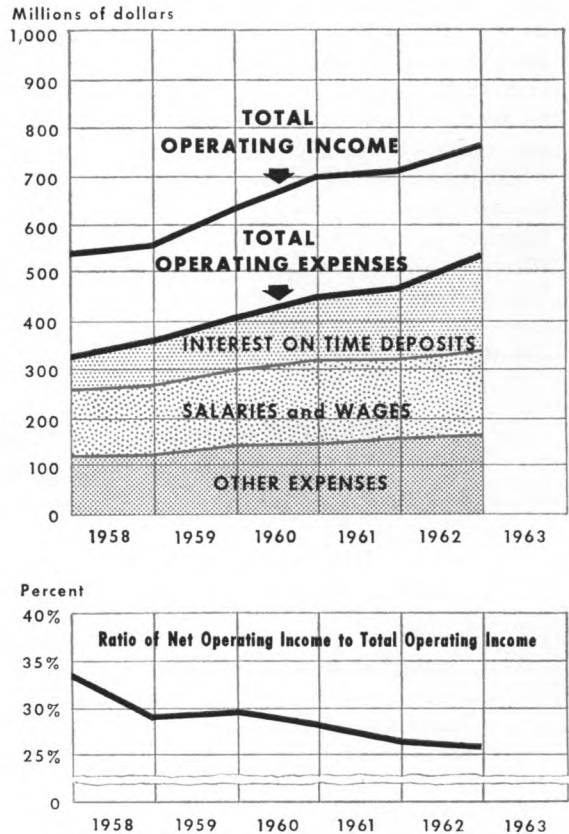
sis in their employment has changed the pattern of both revenue and expenses of Fourth District member banks. One of the principal objectives of bank management in recent years has been to find more profitable uses for funds that would offset the increasing costs associated with higher proportions of time deposits. Reflecting these efforts, total operating income of Fourth District member banks increased by nearly 42 percent in the 1957-1962 period. Loan income accounted for over one-half of the expansion, and the average return on loan accounts advanced from 5.72 percent to 6.11 percent. Income from municipal securities holdings nearly doubled in the five year period, with a particularly strong upsurge coming in 1962.⁽⁹⁾ Rising tax-exempt income accounted for about 13 percent of the total increase in revenue. The average rate of return on municipal holdings increased during each of the past five years; during 1962, the average tax-exempt return on municipal accounts was 3.16 percent, up from 2.69 percent in 1957.⁽¹⁰⁾ Income from U. S. Government securities also advanced as rising yields offset both the declining importance of these holdings in bank portfolios and the trend toward a shorter maturity structure. Income from Government portfolios contributed almost 20 percent to the growth in revenue in the 1957-1962 period. The remainder of the gain in operating income was provided by rising service charges and trust department fees.

Despite the favorable trend in operating income during the past five years, operating expenses at Fourth District banks have moved upward even more sharply causing a troublesome profit squeeze. Operating expenses increased by 63 percent in the 1957-1962 period, with interest expense being responsible for nearly three-fifths of the increase. Interest payments on time deposits

(9) Municipal securities holdings were expanded especially rapidly in 1962, as banks sought to bolster their tax-exempt income to offset the higher rate of interest that many banks began paying on savings deposits during the year.

(10) While interest rates on state and local government securities have been in a declining trend during most of the past three years, the lengthening of the average maturity of these holdings has enabled the banks to increase the average yield on portfolios of other securities.

Chart 2.
OPERATING INCOME AND EXPENSES
Fourth District Member Banks
as of December 31

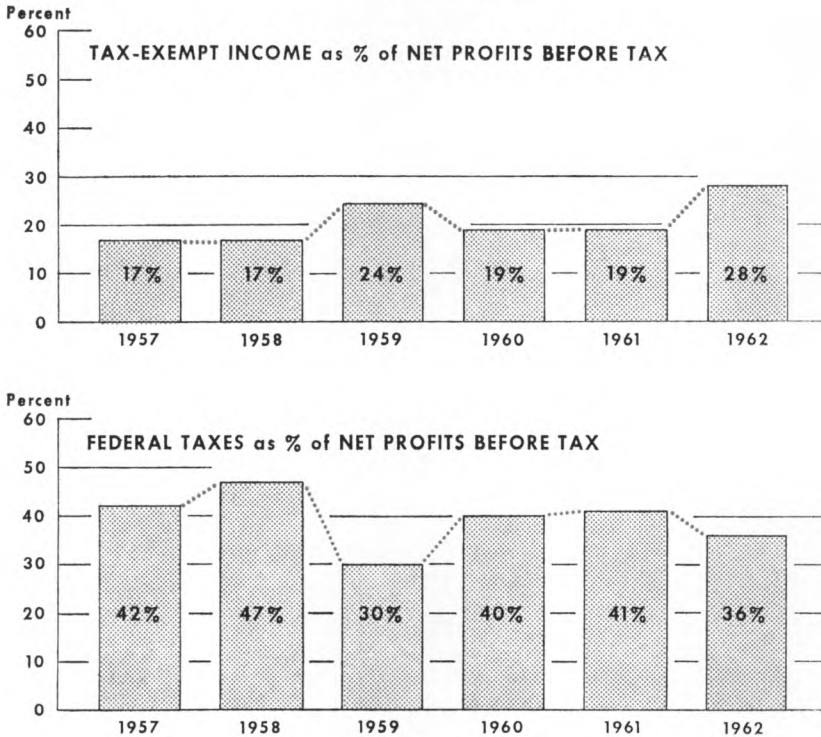


Source of data: Federal Reserve Bank of Cleveland.

expanded by 162 percent as the volume of time deposits rose persistently and as the average rate of interest paid on these deposits moved progressively higher from 1.60 percent in 1957 to 2.63 percent in 1962. Despite tighter control of all other operating expenses, net current operating income as a percentage of total operating income declined almost uninterruptedly.

Chart 2 points up the divergent trends in selected income and expense items. The operating profit ratio declined from 33.6 percent

Chart 3.
EFFECT OF TAX-EXEMPT INCOME ON NET PROFITS
Fourth District Member Banks
as of December 31



The increasing proportion of tax-exempt income has contributed to a declining trend in the rate at which the net profits of Fourth District member banks have been taxed.

Source of data: Federal Reserve Bank of Cleveland.

in 1957 to 26.1 percent in 1962.⁽¹¹⁾ Time deposits expense gradually replaced salaries and wages as the largest single expense item of Fourth District member banks. The factor most directly responsible for the deterioration in the operating profit ratio is the divergent trend which has developed between the cost of deposits and the yield on earning assets. In the 1957-1962 period, the average rate of interest paid on time deposits rose by one percent while the average return on earning assets rose by slightly less than one-half percent. As a result, the spread between the average return on earning assets and the average interest cost on time deposits nar-

rowed from 2.07 percent in 1957 to 1.52 percent in 1962. In addition, time deposits accounted for an increasing share of total deposits, thereby intensifying the profit squeeze.

Profitability

Non-operating sources of income contributed nothing on balance to net profits during the 1957-1962 period. In only two years, 1958 and 1961, did recoveries and profits on securities and loans exceed losses and charge-offs on these items. In all other years, profits before income taxes were reduced by net losses and charge-offs which reflect the losses incurred through changes in the composition of securities holdings and transfers to re-

(11) The operating profit ratio is defined as the ratio of net operating income to total operating income.

serves against losses on loans. As a result, profits before income taxes in 1962 were only 20 percent larger than the 1957 figure, having increased at about one-half the rate of increase in total income during the period.

To counteract the declining profit margin, banks have acquired increasing amounts of municipal securities. A successively larger proportion of bank earnings has come from tax-exempt interest on these securities and the annual income tax liability has been ab-

sorbing a smaller proportion of earnings. Chart 3 shows rising tax-exempt income and the resulting decline in the effective rate of taxation of District member bank earnings in the 1957-1962 period. Income from other securities increased from a low of 17 percent of pre-tax profits in 1958 to a high of 28 percent in 1962. In contrast, Federal income tax payments declined from a high of 46.6 percent of pre-tax profits in 1958 to 36.0 percent in 1962.

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