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MONEY MARKET IN JANUARY

The contraction of member bank excess reserves which follows War Loan drives, as Treasury deposits built up during the drives are transferred to private accounts, has been much smaller than usual since the close of the Sixth War Loan. Excess reserves of all member banks declined by only 200 million dollars from the peak in December to January 24, 1945. In comparable periods following the three preceding drives, the reduction was 500 million dollars or more.

In large part, this departure from previous patterns may be attributed to Government disbursements from accounts with the Federal Reserve Banks, which have been substantially in excess of receipts. Treasury deposits in the Reserve Banks, which had reached a peak of 1,250 million dollars on December 20, 1944 and had fallen to 900 million in the succeeding week, were further reduced by almost two thirds in the three subsequent weeks ended January 17, 1945. These disbursements placed 565 million dollars of additional reserve funds at the disposal of the banks of the country.

The other important factor responsible for minimizing the decline in excess reserves of member banks was a return flow of currency to the Federal Reserve Banks after Christmas which contributed 160 million dollars to the easing of the banks' reserve positions in the four statement weeks ended January 24. In peacetime years, the flow of currency from the stores to the banks after the Christmas shopping period, together with a seasonal reduction in employment and payrolls, resulted regularly in a substantial retirement of currency, but in war years these seasonal influences have been offset to a large extent by the heavy demand for money for expanding industrial payrolls and for hoarding and other purposes. This year, however, the seasonal return flow of currency apparently has not been fully offset by new demands; furthermore, there was a new factor which contributed to the reduction in outstanding currency in January—cash payments of fourth quarterly instalments of individual income taxes for 1944 which were postponed from December 15, 1944 to January 15, 1945.

Part of the gain in bank reserves from these and other sources was absorbed by an increase in reserve requirements, occasioned by the interdrive shift from War Loan deposits which are reserve free, to private deposit accounts which are subject to reserve requirements. Nevertheless, the banks had enough surplus funds to enable them to retire about 500 million dollars of Federal Reserve credit in the three weeks ended January 17, chiefly through the repurchase of Treasury bills from the Reserve Banks' option accounts, and secondarily through direct subscriptions for Treasury bills in excess of their maturities, as a result of which the Reserve Banks were able to allow some of their bills to mature without replacement. There was a further small decline in Federal Reserve credit outstanding in the week ended January 24.

The easier reserve positions of the banks contributed also to the development of a brisk demand for Government securities. Purchases of Treasury obligations in the New York market by out-of-town banks and other investors brought about a substantial inflow of funds from other sections of the country. Weekly reporting member banks in New York City sold sizable amounts of Treasury bonds, notes, and certificates, and at the same time acquired about 350 million dollars of Treasury bills from the Federal Reserve Bank and from new issues in the three weeks ended January 17. In the week ended January 24, the New York City weekly reporting banks again bought bills and also small amounts of certificates and bonds.

Throughout this four-week period, the New York banks were, in effect, utilizing funds sent in by out-of-town banks to retire Federal Reserve credit. The effect of transfers of funds to New York on the reserve positions of banks in other parts of the country was partly offset by funds gained from other sources, including net Government expenditures and some return flow of currency. Nevertheless, excess reserves of all member banks outside New York City showed a net reduction of close to 200 million dollars.

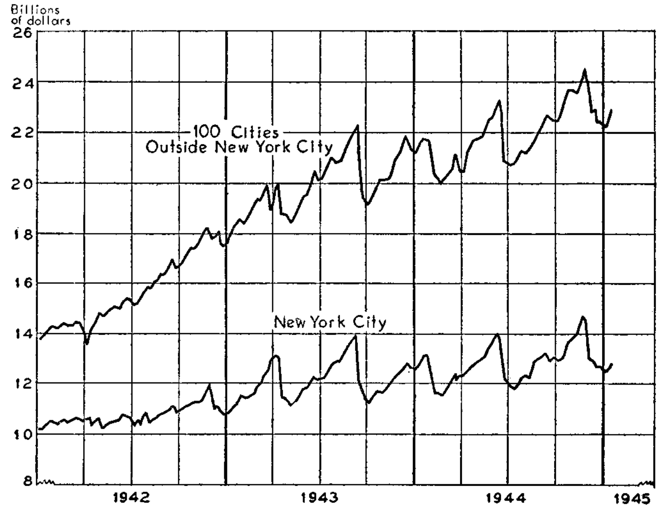
The active demand for Government obligations also afforded dealers and other nonbank investors an opportunity to liquidate securities carried on bank credit from the Sixth War Loan period. In the four weeks ended January 24, loans on Government obligations at New York weekly reporting banks declined by nearly 500 million dollars, divided almost equally between dealers and others. There was a decrease of 183 million in such loans among the reporting member banks in 100 other cities. The latter institutions evidently acquired in the New York market a large part of the Government securities which they added to their portfolios—primarily Treasury bonds (434 million dollars) and some notes.

The market for certificates of indebtedness, which had shown rising yields and declining prices prior to and during the Sixth War Loan drive, improved considerably during January. The Reserve Banks found it necessary to support this market by purchasing large amounts of certificates during December in order to maintain reasonably stable conditions in the market, but Reserve Bank buying during the three weeks ended January 24 was negligible and yields receded to approximately the levels prevailing earlier last fall. All weekly reporting member banks reduced their certificate portfolios by about 60 million dollars between January 3 and 24, indicating the presence of considerable demand from corporations and other nonbank investors.

The demand for Treasury bonds was particularly keen and was not confined to reporting member banks outside of New York; nonreporting member and nonmember banks as well as some nonbank investors were also in the market for Treasury bonds. A considerable rise in prices was required to bring out the necessary supplies, and the Federal Reserve Banks sold bonds from time to time in order to help maintain orderly conditions in the market. Bank demand centered chiefly upon the 2 per cent issue floated during the Sixth drive, which carried the smallest premium of the issues bearing this coupon, although there was also continued active demand for partially tax-exempt issues. Among the major suppliers of the new 2 per cent bonds were institutional investors which had acquired them at par during the Sixth drive largely with the proceeds of sales to the banks of earlier issues of Treasury bonds. In disposing of their Sixth War Loan securities, some of these investors repurchased the earlier issues, in effect securing a net profit amounting to a large part of the premium on the Sixth Loan bonds. The undesirable aspects of this procedure were pointed out in the January 1945 issue of this *Review.*

Such practices, by promoting large increases in bank holdings of Government securities, contributed to the ease with which Sixth War Loan quotas were exceeded but may have been a factor in arresting at least temporarily the progress that had previously been made in channeling the liquid cash assets of individuals, corporations, and others into the financing of the war effort. As illustrated in the accompanying chart, it appears that in previous War Loan drives a considerable proportion of the demand deposits accumulated by nonbank investors in the interdrive periods, had been absorbed through sales of War Loan securities. In the Sixth drive, however, the proportion of these accumulated deposits recaptured for war financing fell sharply below that of previous drives, indicating a setback to efforts to finance the war as far as possible with nonbank funds and to limit the amount of bank credit expansion involved.

Adjusted Demand Deposits of Weekly Reporting Member Banks



Source: Board of Governors of the Federal Reserve System.

The growth in deposits between the low point of the Fifth War Loan and the peak of the Sixth was unusually large. This growth may be attributed partly to the fact that only one tax period intervened between the Fifth and Sixth War Loans; consequently corporation and individual withdrawals of deposits for income tax payments were considerably less between July and November than between February and June. And, as Government expenditures continued at much the same rate as in the earlier part of the year, the Treasury was compelled to make much heavier withdrawals from its War Loan deposit accounts between the Fifth and Sixth drives, thus greatly accelerating the growth of private deposit accounts. Unusually large sales of Government securities to banks by other investors in the period preceding the issue date for Sixth War Loan securities also contributed to the growth in individual, corporate, and institutional deposit accounts.

Because of this large growth of bank deposits, there should have been substantially greater amounts of funds available for investment in War Loan securities than ever before, and the amount actually sold in the Sixth Loan was somewhat greater than in any preceding War Loan. The absorption of private deposits, however, while about as great in actual amount as in the previous drives, represented a considerably smaller percentage of the preceding growth than was achieved in other drives. A partial explanation probably lies in the fact that individuals were accumulating funds with which to meet their income tax payments due on January 15 and March 15. But it is questionable whether this factor is sufficient to explain fully the unusually large net increase in deposits between the low point at the close of the Fifth Loan, and the low point at the end of the Sixth.

LOANS TO VETERANS

A new type of partially Government-guaranteed bank loans has arisen out of the passage of the Servicemen's Readjustment Act of 1944, a statute designed to aid the veteran of World War II in his readjustment to civilian life. Under Title III of this act, popularly known as the "G I Bill of Rights," the Veterans' Administration is empowered to issue limited guaranties of loans made to ex-servicemen by private and Governmental lending agencies. Such loans may be extended for the following purposes: (1) the construction, purchase, or repair or improvement of, or payment of delinquent indebtedness, taxes or special assessments on, homes; (2) the purchase of farms and livestock and the purchase, repair or improvement of farm buildings and equipment; and (3) the purchase of a business or business property including buildings, machinery and equipment, tools, and supplies.[1] Farm crop production loans or business working capital loans are not eligible for guaranty by the Administrator of Veterans' Affairs. Loans for refinancing purposes are likewise ineligible for guaranty.

Only veterans in service on or after September 16, 1940 who have been released from the armed services of the United States under conditions other than dishonorable, after active service of 90 days or more, unless released after shorter service because of disability or injury incurred in line of duty, are eligible to apply for guaranteed loans. The veteran may apply within two years after release from service or two years after the war, whichever is later, but in no event later than five years after its termination.

Aside from the fact that only loans extended for the purposes specified above can qualify for the Administrator's guaranty, broadly speaking the following criteria of eligibility have been established:

1. The property securing the loan must be situated in the United States, its territories, and possessions, and must be suitable for the purposes of the loan;
2. The proceeds of the loan will be used only for the purposes specified;
3. The purchase price of the property or construction cost (including the value of the land) may not exceed the reasonable normal value of the property as determined by appraisal;
4. The terms of payment of a home mortgage loan must bear a proper relation to the veteran's present and anticipated income and expenses;
5. The veteran's ability and experience and the conditions under which he proposes to conduct farming or business operations are such as to indicate reasonable likelihood of success in the pursuit of his occupation. In addition, in the case of farm loans, the veteran's financial situation must be such that "he likely will be able to carry on the farming enterprise successfully".[2]

With the exception of "second" loans discussed below, the Administrator's guaranty is limited to 50 per cent of the amount of the loan or two thousand dollars, whichever is less, no matter how large the loan may be. The guaranty may be split among a number of loans for different purposes, but the sum of the guaranties on all loans (including second loans) to one veteran may not exceed two thousand dollars. Subject to certain exceptions contained in the regulations, guaranties of construction loans, although issued before building begins, do not become effective until completion of the project. The guaranty declines or rises pro rata with the decrease or increase in the unpaid amount of the loan. In the event of default, however, the guaranty becomes payable to the lender in the amount current at the time. The right of the Veterans' Administration to recover its loss out of foreclosure and the proceeds of the sale of the security behind the loan becomes effective only after the lending institution's claim has been fully met.

The loan guaranty provisions of the "G I Bill of Rights" may be used to supplement insurance or guaranties of loans which other Governmental bodies are authorized to provide. Where another Federal agency has insured, guaranteed, or made a loan to a veteran for any of the purposes stated in the first paragraph of this article, the Administrator of Veterans' Affairs may guarantee, subject to the limitation of two thousand dollars, the full amount of a second or junior loan to cover the remainder of the purchase price or the cost of construction of the property to be acquired. Such second loans are limited in amount to 20 per cent of the purchase price or cost. For example, a veteran desirous of acquiring a ten thousand dollar home might be able to obtain two loans from a bank, one insured by the FHA for eight thousand dollars and the other guaranteed for two thousand dollars by the Administrator of Veterans' Affairs. In this special type of case the veteran need not invest any of his own funds in the transaction, and the entire credit is insured or guaranteed. It is expected that a great many home loans originating out of the Servicemen's Readjustment Act will be so-called second loans. In the case of loans for the purpose of enabling veterans to go into business, however, this opportunity to obtain second loans is extremely limited inasmuch as very few loans of this type have been made by any other Federal agency.

In general, loans on real estate, equipment, machinery, and tools require first liens in the form of mortgages, conditional

[1] Regulations of the Veterans' Administration covering all three types of veterans' loans have been distributed to all banks and trust companies in the Second Federal Reserve District by this bank. The regulations and forms are now obtainable from local offices of the Veterans' Administration located at Newington, Connecticut; Lyons, New Jersey; Batavia, New York; and 215 West 24th Street, New York 11, New York.

[2] Section 36.4102 (b) (2) of the regulations of the Veterans' Administration on guaranty of farm and farm equipment loans.

sales contracts, chattel mortgages, or security in other forms appropriate to the type of property acquired and to the laws of the various States. The existence of prior tax liens on the property, however, will not necessarily disqualify the loan. Loans not in excess of 500 dollars and those for the purchase of supplies may be unsecured. Loans for repairs or improvements, for payment of delinquent indebtedness, taxes, or special assessments or for initial payment of machinery, equipment, or tools, and second loans to complete purchases are likely to be junior liens secured by second mortgages or unsecured.

For the most part no limit is placed, either in the Servicemen's Readjustment Act or the regulations under it, on the amount of a first mortgage real estate loan so that the laws of the various States and, in the case of national banks the Federal Reserve Act, govern. A number of States have changed their banking laws or regulations to provide that the limitation with respect to the ratio of the amount of the loan to the appraised value of the real estate applies only to the unguaranteed portion of the loan. The Comptroller of the Currency has issued a ruling to the same effect applicable to the national banks.[3]

The amount of a loan for repair, alteration, or improvement of residential or farm property must bear a "proper" relation to the value of the property and in the case of farm real estate to the earning power of such property as well. Second loans, as already noted, may not exceed 20 per cent of the purchase price or cost.

Amounts and maturities of business loans vary with the purpose of the loan. A loan for the entire purchase price of equipment, machinery, or tools (new or used) may not run for more than three years. A loan covering the initial purchase price (down payment) of such items, however, may not exceed one thousand dollars or one third of the purchase price, whichever is lower, and may have an ultimate maturity of no more than two years if the loan exceeds 500 dollars or one year if 500 dollars or less. Loans for the purchase of supplies carry a maximum of one thousand dollars and one year, while loans to acquire businesses must be paid off within five years.

Loans on business and other real estate and all other nonbusiness loans may run as long as 20 years or for shorter periods depending upon the amount of the loan, the amount of amortization payments, the character and condition of the property, and upon other factors. All loans maturing in more than one year are to be amortized at least annually except that payments on the principal of farm real estate loans may be deferred for the first three years and that a "term" loan maturing within five years need not be paid off periodically, if together with any prior liens it does not exceed two thirds of the reasonable normal value of the property.

[3] This ruling has been confined to home loans only.

The maximum interest rate is set at 4 per cent per annum on unpaid balances. The rate on second loans may be 1 per cent higher than that charged on the principal or prior loan but in no event may it exceed 4 per cent. In many instances the rate on the second loan may have to be lower than that on the prior one, inasmuch as the interest rate charged on Government-guaranteed nonwar loans frequently exceeds 4 per cent. The Veterans' Administration is directed by law to pay the first year's interest on the portion of the loan it has guaranteed.

No bonus, commission, or application fee may be charged the veteran in connection with the loan; nor may a premium or penalty be required of the borrower for prepayment of the loan. The customary charges for credit and appraisal reports, title-searching, recording fees, premiums on fire and other hazard insurance required on the property, and other such expenses may be made, however, and may be added to the principal of the loan or paid in any other way agreed upon by the borrower and lender. In addition, the lender may make reasonable charges for any funds advanced on a construction loan during the building period.

Procedures set up for obtaining and approving loans differ somewhat as to details with respect to the various types of loans. In general, the veteran and the lender are required to sign and submit an application for a "Certification of Eligibility" to the regional office of the Veterans' Administration. The certification will be returned to the lender by the loan guaranty office, stating whether or not the serviceman is eligible for a loan and the amount of the guaranty available to him, and listing the name of an approved appraiser who will make an evaluation of the property.

Upon determination that the veteran is eligible the required papers must be duly prepared, executed, and submitted to an agency designated by the Veterans' Administration for recommendation—in the case of business loans, the RFC or the SWPC, in the case of farm loans, the Farm Security Administration through local veterans' loan certifying committees,[4] and for second loans on residential property, the FHA. The Veterans' Administration has as yet designated no such agency to review and make recommendations on other types of home loans and is performing these functions itself through its regional offices. The following papers are specified for most types of loans:

1. Certification of eligibility.
2. Loan Guaranty Certificate evidencing the Administrator's obligation under the loan.
3. Original application for guaranty.

[4] Where the ex-serviceman is unfamiliar with farming conditions or the available farm land in the community in which he is desirous of settling, he is required to seek the advice of a local veteran's advisory committee operating in conjunction with county agent's office in the Agricultural Extension Service; thus some protection against unwise investment is provided. The veteran's application may then be submitted by the lending institution to the certifying committee for recommendation.

4. Credit report with respect to the borrower[5] (in case of farm loans required only upon request of the Administrator).
5. Appraisal report.[6]
6. Copy of conditional sales contract if this form of security is used; also a copy of any option or loan agreement.
7. Loan closing statement giving the estimated amounts to be disbursed by the creditor for the borrower.
8. A statement of the kinds and amounts of insurance required for the protection of all three parties against loss from fire and other hazards, and the estimated premium cost.[5]

If the loan is recommended by the agency it goes to the regional office of the Veterans' Administration for approval. All papers except the original application and in appropriate cases the appraisal and credit reports go back to the lender, together with an executed contract of guaranty in the form of a Loan Guaranty Certificate (in the case of second loans on homes, the papers are returned to the FHA which in turn sends them back to the lender). The loan is then "closed" by the lender by securing a certificate of title, necessary signatures, etc., and a report of the loan closing is furnished the Administrator within two months of the closing. If the loan is disapproved, the papers are returned to the lender, together with a letter stating the reasons for disapproval. A copy of the letter is sent to the veteran. The lender or veteran may appeal to the Administrator in Washington for a review of the decision within a month after the receipt of notice of denial.

In view of these complicated procedures, the handling of veterans' loans may involve considerable expense to lending institutions. The profitableness of such loans may therefore be subordinate to the main consideration which will probably be whether or not the loans can reasonably be expected to assist ex-servicemen to reestablish themselves successfully in civilian life.

Care Required in Making Loans

It has been made quite clear that the loan provisions of the Servicemen's Readjustment Act do not confer on the veteran the right to obtain a guaranteed loan more or less automatically. Officials of the Veterans' Administration have emphasized the distinction between a loan and a bonus or grant. It should also be made clear that the lending institution shares with the Government the risks involved in such loans, and is not relieved by the Government's partial guarantee from exercising ordinary business prudence. Because the loan must eventually be paid back, both the lending agency and the Veterans' Administration will have to exercise considerable care in appraising the prospects for repayment and will have to make reasonably certain that the loan is practicable with respect to the relationship of the amount of the loan and the schedule of payments to the veteran's prospective income.

In connection with farm and business loans, the chief test of practicability is the veteran's ability and experience in his particular field of endeavor which may be counted upon to improve his chance of achieving success in his venture. It is evident that a great many applicants for loans may not be able to meet these tests. Representing primarily the younger element in the population, ex-servicemen in large part had not yet begun to make their way in the economic world at the time they were called to the colors, and so may be lacking in training and experience. The risks involved in the extension of credits to veterans appear to be greatest for business loans—the Administrator of Veterans' Affairs has termed the business loan as "probably one of the most hazardous provisions" of the Act. Least risk appears to be attached to the home loans.

The provision of the Act authorizing partially guaranteed loans to enable veterans to go into business for themselves may constitute an innovation in Federal loan legislation, in that it is probably the first attempt to provide loans for the specific purpose of enabling individuals either to launch new businesses or to acquire interests (whole or part) in existing enterprises. The substantial risks involved in such loans are indicated by the heavy mortality among small businesses. The best interests of the veterans as well as the Government and the lending institutions will be served by encouraging veterans to embark only upon ventures in which they may have a reasonable prospect of success.

BUDGET MESSAGE OF THE PRESIDENT OF JANUARY 9, 1945

Owing to uncertainties relating to the end of the war, one must regard as highly tentative the fiscal year 1946 budget estimates of Federal receipts and expenditures contained in the President's Budget Message transmitted to the Congress on January 9, 1945. Avoiding any prediction concerning the length of the war on either front, the President stated that for the fiscal year 1946 he was using a tentative estimate of 70 billion dollars for war expenditures, although the figure might range from less than 60 billion to more than 80 billion depending upon assumptions which might be made with respect to the course of the war. Receipts, from income taxes in particular, would also be affected to some extent by deviations in actual expenditures from the estimates, because of the effects on industrial production and the national income.

Based upon the projected receipts and expenditures of the

[5] Not required where the loan does not exceed 500 dollars.

[6] Not required where the loan does not exceed 500 dollars. In the case of farm loans of 500 dollars or less for repairs, alterations, or improvements, an abbreviated appraisal report must be submitted by the agency recommending the loan. The opinion of such agency as to the value of livestock, farm machinery, or equipment based on inspection or evidence or review of the application for such a loan of over 500 dollars, may constitute the appraisal report. No appraisal report is ordinarily required for business loans on new machinery, equipment, tools, or supplies.

Treasury and Government corporations, net borrowing from the public would amount to 44 billion dollars for the fiscal year ending June 30, 1945 (of which approximately 27 billion had been consummated by December 31, 1944) compared with 57 billion for the fiscal year 1944, while the corresponding figure for the fiscal year 1946 would be 34 billion. At present levels of savings it is expected that nonbank investors would provide about 30 billion dollars of the annual requirements; the remainder would have to be raised through the banking system. An earlier end of the war than was assumed would, of course, imply an even more rapid decline in the amount to be borrowed from the public, as expenditures would tend to drop faster than receipts.

Net receipts of the Treasury are estimated at 41 billion dollars for the fiscal year ending June 30, 1946, or 4.5 billion below the revised estimate for the current year and 3 billion below the year ended June 30, 1944. A little over 3 billion of the decline from 1945 to 1946 is in direct taxes on individuals (of which the completion this year of the payment of "unforgiven" 1942 or 1943 taxes accounts for about 900 million), while taxes on corporations are expected to be approximately 800 million lower. The President cited the anticipated decline in Federal expenditures as an influence toward lower incomes and tax receipts. Direct taxes on individuals and corporations together will account for approximately three fourths of the total revenues for the fiscal year 1946.

Total expenditures, including the net outlays of Government corporations, exclusive of those for debt retirement, are estimated at 83 billion dollars for the year ending June 30, 1946, or 17 billion lower than for the fiscal year 1945 and 12 billion below actual expenditures for fiscal 1944. The anticipated decline from 1945 to 1946 is accounted for by a decrease of war expenditures from 89 billion to 70 billion and a rise of 2 billion in other expenditures. The war expenditure estimate for 1946 assumes that the Lend-Lease Act, which expires June 30, 1945, will be extended, but the message stated that lend-lease "will be liquidated with the end of the war."

During the first half of the current fiscal year war expenditures were made at an annual rate of 88 billion dollars; the revised estimate indicates that an annual level of 90 billion is expected to prevail during the six months ending June 30, 1945. It was estimated that the total war program, measured by appropriations, unliquidated contract authorizations, and net commitments of Government agencies, would reach 450 billion dollars by June 30, 1946 of which about 91 billion would remain unexpended on that date.

Of the 13 billion of estimated 1946 expenditures for other than war purposes, nearly 10 billion was placed in the "aftermath-of-war" category which covers veterans' pensions and benefits (2.6 billion), refunds of taxes (2.7 billion), and interest on the public debt (4.5 billion—of which, however, nearly 1 billion represents the interest charge on debt incurred prior to the start of our defense program). The total of these three items is larger than the whole Federal budget for any year prior to 1941, with the exception of the years 1918 and 1919.

Assuming declines in the Treasury's cash balance of 5 billion during the fiscal year 1945 (to 15 billion on June 30) and 2 billion during the next year (to 13 billion), borrowing requirements of the Treasury are estimated to amount to 51 billion and 41 billion, respectively, compared with 64 billion in 1944. This would allow for the net retirement of nearly 1.9 billion dollars of Government corporations' obligations during the entire fiscal year 1945 (leaving about 1.6 billion for the period January 1-June 30, 1945) and 660 million during the following fiscal year. The gross public debt (231 billion on December 30, 1944) would rise to 252 billion by June 30, 1945 and to 292 billion a year later. The present statutory debt limit of 260 billion (face amount) would therefore be sufficient to carry the Treasury only to next June 30, after allowing for the unearned discount on Savings bonds. As a matter of fact, the Seventh War Loan drive, predicted for next May or June by the Secretary of the Treasury, may carry the debt above the present limit. Trust account and other net cash receipts—Social Security taxes in the main—will reduce the amount to be borrowed from the public.

The President's message called attention to the fact that no change in tax legislation was proposed at this time and stated that "wartime taxes must be maintained as long as large-scale war expenditures are necessary." On the other hand, it was stated that minor tax adjustments will become possible and desirable "when a favorable development of the war allows a major decline in war expenditures." Looking to the postwar period, it was suggested that "we must overhaul the wartime tax structure to stimulate consumers' demand and to promote business investment" and it was recommended that the elements of such a program be developed now so that it can be put into effect after victory.

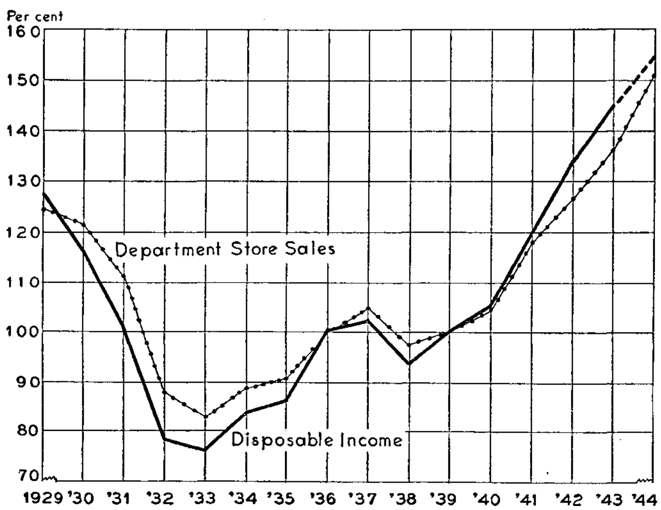
The Budget Message contained a number of proposals designed to aid domestic reconversion and the attainment of full employment and a greater measure of economic security, and also the reconstruction and rehabilitation of foreign countries. If carried out, most of the proposals would lead to substantial expenditures by the Federal Government in the transitional and postwar periods. A departure from past practice was the inclusion in the message of a table showing the "nation's budget"—a breakdown of the gross national product for the calendar years 1939 and 1944. In referring to this table, the President pointed out that if full employment is to be provided by private enterprise in peacetime, consumers' expenditures and business investments must increase by about 50 per cent, measured in constant prices, above the level of the year 1939. His discussion of the subject implied that if consumers' expenditures and business investments are not sufficient to provide full employment and a high level of gross national product, it will be the policy of the Government to provide jobs and sufficient purchasing power in the hands of the public to assure sustained markets and employment.

THE RELATIONSHIP OF DEPARTMENT STORE SALES AND DISPOSABLE INCOME IN NEW YORK STATE

Among the various factors which determine the annual volume of department store trade, the amount of income after taxes, or disposable income, is the most important. An analysis of past relationships between disposable income and department store sales may be of help in evaluating the performance of individual stores or groups of stores and also in appraising the postwar outlook for department store trade.

The accompanying chart compares department store sales and disposable income in New York State for the period 1929-44. Estimates of year-to-year changes in department store sales in New York State are based on reports obtained by this bank from a representative group of department stores.[1] Disposable income of individuals in New York State

Indexes of Department Store Sales and Disposable Income in New York State, 1929-44 (1939 average=100 per cent)



Source: Federal Reserve Bank of New York; disposable income estimate for 1944 preliminary.

was computed by deducting from total income payments in the State (as estimated by the United States Department of Commerce) all direct personal taxes collected in the State. The principal direct taxes paid by individuals in New York are Federal and State personal income taxes and Federal and State estate and gift taxes; it was also assumed that 25 per cent of all local property taxes are paid by individuals, the rest by business. In addition, income received by nonresidents was excluded from the estimate of disposable income for New York State.

It appears from the chart that fluctuations in department store trade correspond closely to changes in disposable income. In 1939 disposable income in New York State amounted to 10,360 million dollars and department store sales to 444 million. During the 16-year period the portion of consumer income spent in department stores showed very little variation, reaching 4.8 per cent in 1932 but declining to 4.0 per cent in 1943. In depression years department store sales decline somewhat less than the disposable income of individuals, since many consumers spend out of savings or reduce their current savings. In 1942 and 1943, owing to shortages of many durable goods and to increased saving, department store sales in New York State failed to reach the volume which might have been expected on the basis of peacetime relationships and of wartime income levels. In 1944, however, department store sales appear to have shown a relatively greater increase than the disposable income of individuals in the State.

During the period 1929-44, an increase or decrease of 10 per cent in disposable income in the State has been accompanied by an average change of 8 per cent in department store sales. A change of 1 billion dollars in disposable income has in the average raised or lowered department store sales by 34 or 35 million dollars.[2]

[1] Federal excise taxes and New York City sales tax not included in sales figures.

[2] A report including estimates of disposable income and department store sales for New York State, 1929-44, and a more detailed description of the technique used to obtain the data which appear in this article may be obtained upon request.

Indexes of Business

Index	1943 Dec.	1944 Oct.	1944 Nov.	1944 Dec.
Industrial production*, 1935-39=100 (*Board of Governors, Federal Reserve System*)	241	232	232	232*p*
Munitions output, 1943=100 *r* (*War Production Board*)	117	112	109	110*p*
Electric power output*, 1935-39=100 (*Federal Reserve Bank of New York*)	197	193	196	198*p*
Ton-miles of railway freight*, 1935-39=100 (*Federal Reserve Bank of New York*)	228	224	215*p*	
Sales of all retail stores*, 1935-39=100 (*Department of Commerce*)	172	180	187*p*	
Factory employment				
United States, 1939=100 (*Bureau of Labor Statistics*)	169	155	153	154*p*
New York State, 1935-39=100 (*New York State Dept. of Labor*)	160	146	145	145*p*
Factory payrolls				
United States, 1939=100 (*Bureau of Labor Statistics*)	328	314	312*p*	
New York State, 1935-39=100 (*New York State Dept. of Labor*)	297	287	286	283*p*
Income payments*, 1935-39=100 (*Department of Commerce*)	223	236	238*p*	
Wage rates, 1926=100 (*Federal Reserve Bank of New York*)	160	167	168*p*	
Cost of living, 1935-39=100 (*Bureau of Labor Statistics*)	124	127*r*	127	127*p*
Velocity of demand deposits*, 1935-39=100 (*Federal Reserve Bank of New York*)				
New York City	65	76	76	87
Outside New York City	74	73	76	84

* Adjusted for seasonal variation. *p* Preliminary. *r* Revised.

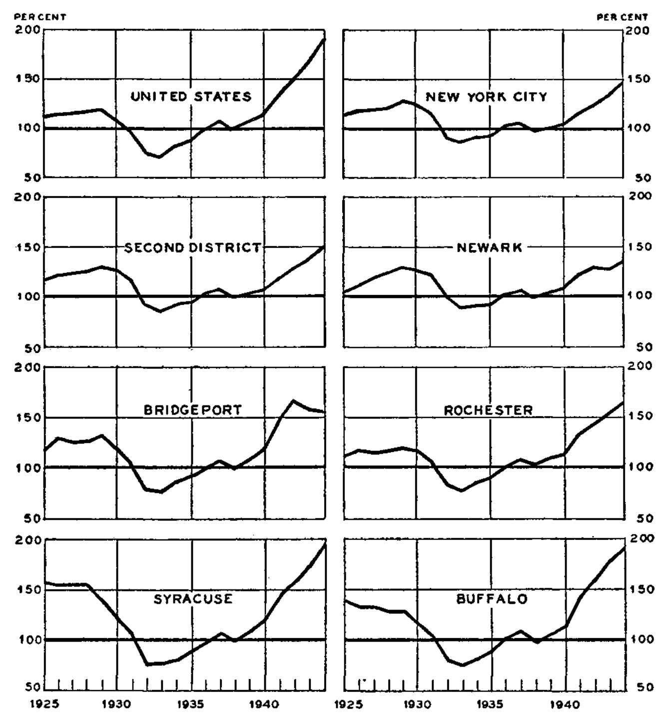
DEPARTMENT STORE TRADE

Unusual weather conditions, particularly in Upstate New York, together with a merchandise inventory depleted by the greatest Christmas buying on record, adversely affected January trade in this District. The dollar volume of department store sales last month, after adjustment for seasonal fluctuations, was about 7 per cent below the average for the final quarter of 1944 and the lowest since last June. At the beginning of January, the seasonally adjusted index of department store stocks had declined almost 20 per cent from last August's peak and was the lowest since the middle of 1943. Merchandise on order at the close of the year equaled the dollar volume of stocks on hand. Outstanding commitments were 15 per cent above those of one year earlier and three times the dollar amount on order at the close of 1942. Trade sources indicate that a substantial portion of these orders are overdue.

Department store sales in this District last year amounted to roughly 800 million dollars, or 13 per cent of the United States total. New York City sold 425 million dollars worth of department store merchandise; Newark, 75 million; Buffalo, 65 million; Rochester, 40 million; Syracuse, 20 million; and Bridgeport, 13 million. The accompanying chart shows the trend of sales in these cities from 1925 to date. During the war period sales in the District have lagged behind those in the country as a whole, because of the relatively small increases in New York City and Newark. Buffalo and Syracuse have shown gains greater than the United States average. The annual increase during the past few years has been fairly constant for New York City, Buffalo, Rochester, and Syracuse. During 1944, Newark showed a gain following a slight decline in 1943, while sales in Bridgeport were lower for the second consecutive year, following an unusually rapid expansion in 1941 and 1942.

The trend of sales among the various cities is related to the changes in the amount of income available for spending, which are occasioned largely by the expansion and contraction in manufacturing activity and hence in payrolls (see the discussion of sales and disposable income included in this issue). It will be noted that department store sales have substantially exceeded the predepression peaks in most cities. These indexes, however, are based on the dollar volume of sales; changes in the price and quality of department store merchandise have varied considerably during the past two decades. In addition, the trend during the war period has been influenced by the preference for, and in some cases the greater availability of, higher priced items.

Indexes of Department Store Sales in the United States, Second District, and Selected Cities within the District, 1925-44 (1935-39 average=100 per cent)



Source: Board of Governors of the Federal Reserve System and Federal Reserve Bank of New York.

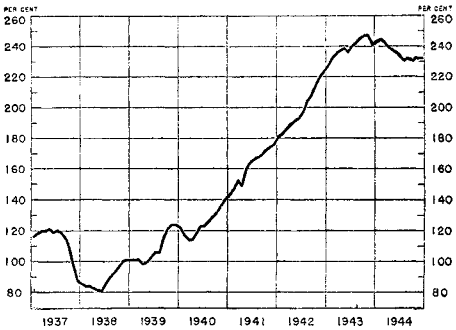
Department and Apparel Store Sales and Stocks, Second Federal Reserve District, Percentage Change from the Preceding Year

Locality	Net Sales		Stocks on hand
	Dec. 1944	Jan. through Dec. 1944	Dec. 31, 1944
Department stores, Second District	+13	+10	− 7
New York City	+15	+12	− 8
Northern New Jersey	+13	+ 7	− 6
Newark	+12	+ 6	− 5
Westchester and Fairfield Counties	+13	+ 3	−17
Bridgeport	+ 7	− 1	−26
Lower Hudson River Valley	+22	+17	+12
Poughkeepsie	+21	+15	—
Upper Hudson River Valley	+10	+ 3	− 1
Albany	+15	+ 6	—
Schenectady	+ 6	0	+ 2
Central New York State	+13	+10	+ 2
Mohawk River Valley	+ 8	+ 4	− 6
Utica	+ 7	+ 5	—
Syracuse	+16	+13	+ 6
Northern New York State	+24	+14	—
Southern New York State	+18	+11	− 7
Binghamton	+20	+12	—
Elmira	+22	+12	—
Western New York State	+ 7	+ 7	0
Buffalo	+ 6	+ 6	0
Niagara Falls	+10	+ 4	+ 5
Rochester	+ 8	+ 9	0
Apparel stores (chiefly New York City)	+21	+12	+ 3

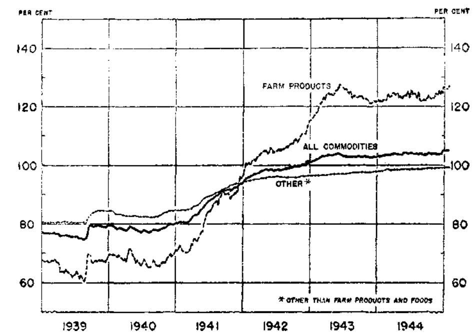
Indexes of Department Store Sales and Stocks Second Federal Reserve District

Item	1943	1944		
	Dec.	Oct.	Nov.	Dec.
1935-39 average = 100				
Sales (average daily), unadjusted	228r	173	207	269
Sales (average daily), seasonally adjusted	131r	152	164	155
1923-25 average = 100				
Stocks, unadjusted	112	132	131	104
Stocks, seasonally adjusted	115	120	114	106

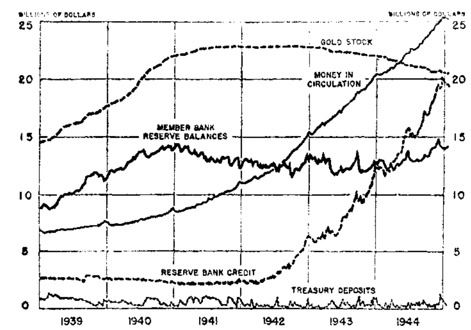
r Revised



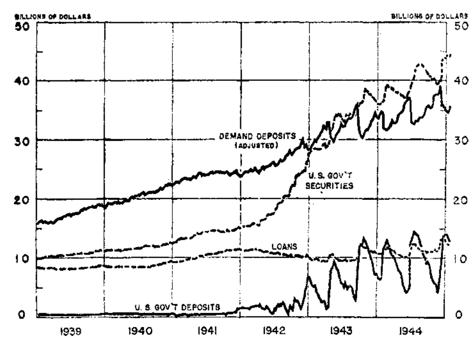
Index of Physical Volume of Industrial Production, Adjusted for Seasonal Variation (1935-39 average=100 per cent)



Indexes of Wholesale Prices Compiled by Bureau of Labor Statistics (1926 average=100 per cent; latest figures are for week ended January 20)



Member Bank Reserves and Related Items (Latest figures are for January 17)



Member Banks in Leading Cities. Demand Deposits (Adjusted) Exclude U. S. Government and Interbank Deposits and Collection Items. Government Securities Include Direct and Guaranteed Issues (Latest figures are for January 17)

General Business and Financial Conditions in the United States

(Summarized by the Board of Governors of the Federal Reserve System)

PRODUCTION and employment at factories increased somewhat in December. Retail buying was exceptionally active in December and the first half of January and wholesale commodity prices advanced.

Industrial Production

Total industrial production was maintained in December at the level of the preceding month, which was 232 per cent of the 1935-39 average, according to the Board's index. Manufacturing output showed a slight rise because of increased output of war products, while minerals production declined, reflecting a sharp drop in coal production.

Gains over the November levels of activity in the machinery, transportation equipment, chemicals, petroleum refining, and rubber industries followed a renewed drive to expand output of critical munitions. Military events in December resulted in higher production schedules for munitions and in additional Federal measures to assure manpower for war output and to increase inductions into the armed services. Stringent limits were placed on the use of metals in civilian products under the programs initiated last fall.

Output of metals decreased somewhat further in December. In the first three weeks of January steel production continued to decline, partly because of severe weather conditions. Output of aluminum has been held at a level of about 90 million pounds per month since last autumn. The curtailment of aluminum sheet production during 1944 was reported in January to have led to a critical supply situation for this product in the light of the recently raised aircraft schedule.

Lumber production showed the usual seasonal decline in December. Output for the year 1944 was about 5 per cent below 1943, and a further decline is expected in 1945 owing to continued shortages of manpower and equipment.

Cotton consumption and output of manufactured foods were maintained in December at the level of the preceding month. There were declines in shoe production and in activity at paper mills.

Output of coal in December was about 12 per cent below average production in the preceding 11 months. In order to assure supplies to meet the most essential needs, restrictions on less essential civilian uses of coal were instituted in January. Crude petroleum production was maintained in December in large volume, while output of iron ore showed the large seasonal decline customary in this month.

Distribution

During the November-December Christmas shopping season department store sales rose to new high levels and were 15 per cent larger than in the corresponding period a year ago. The high level of sales was maintained in the first half of January, taking into account usual seasonal changes in trade.

Carloadings of railroad freight declined more than usual in December. During the first two weeks of January loadings were 5 per cent less than during the same period a year ago, owing to decreases in all classes of freight except miscellaneous shipments.

Commodity Prices

The general level of wholesale commodity prices advanced somewhat from the early part of December to the middle of January. Prices of most farm products were higher. After the middle of January grains and cotton declined but were still above early December levels. Steel scrap, which had been considerably below ceiling levels in the autumn, showed a sharp price rise. Prices of nonferrous metal scrap, cement, and various other industrial materials also increased in December and the early part of January.

Bank Credit

In the four weeks ended January 17, Government security holdings at weekly reporting member banks increased further. Loans for purchasing and carrying Government securities declined from the level reached during the Sixth War Loan drive; most of the decline was in the loans to customers, but loans to brokers and dealers also were reduced moderately. The Government securities added to reporting member bank holdings in this period consisted mainly of bonds and bills.

Excess reserves held by member banks declined relatively little from the peak reached during the Sixth War Loan drive. Reserve requirements increased, but member bank reserve balances also increased by approximately the same amount. Spending of Treasury balances and a reduction of nonmember deposits at Reserve Banks more than offset a decline in holdings of Government securities by the Federal Reserve Banks. Currency in circulation declined 130 million dollars during the three weeks following the Christmas peak, the largest decline for any corresponding period since early 1942.

Following the Sixth War Loan drive, adjusted demand deposits renewed their increase, and time deposits increased at a more rapid rate than demand deposits. Between War Loan drives, time deposits in all banks have been increasing at the rate of almost three quarters of a billion dollars a month.