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MONEY MARKET IN AUGUST

The victorious conclusion of the war in the Pacific may be expected to have a substantial influence on various factors affecting the supply of and demand for funds in the New York money market. As the Treasury's need for funds diminishes and the wartime pattern of production is unwound, a shrinkage in the demand for currency, changes in the flow of funds between New York and other parts of the country, and a possible halt in foreign accumulations of gold in this country, are likely possibilities. These changes may not be substantial for some time, however, and their prospective development had little effect on the money market during August.

The more immediate effects of the end of the war were felt in the market for Government and other securities where the initial reaction was a temporary decline in prices. The recession in prices of Government obligations reflected primarily the withdrawal of purchasers from the market, rather than a substantial increase in selling. Partially tax-exempt Treasury bonds which had been weak for a month before the termination of the conflict fell further in price as the war's end improved the prospects for lower taxes on corporation income which would reduce the value of the exemption. Other sections of the Government security market, which had shown signs of recovering from a decline in July, also turned down temporarily when, after the acceptance by the Japanese of the Allied surrender terms, reports that the Treasury planned to hold a Victory Loan at the earliest possible date became the basis for rumors that the drive might be started in September or early October. As this would have considerably shortened the anticipated period between the seventh and eighth war loans, during which period investors could accumulate funds and make portfolio adjustments, and since it would have made new securities available at an earlier date than had been expected, some slight selling pressure developed.

However, following the official announcement on August 23 that the Victory Loan would begin on October 29 and that subscriptions from investors other than individuals would not be accepted until December 3, prices recovered rapidly. The goal of 11 billion dollars (3 billion less than that of the Seventh War Loan) also suggested smaller supplies of new Government securities in the future. And the absence of a short or intermediate term bond in the "basket" of offerings announced for the Victory Loan, appeared to lend a scarcity value to such securities already outstanding. Prices of intermediate taxable bonds, in particular, turned strong, as banks weighed the possibility that further increases in the amount of Treasury securities available to banks, other than short term issues, might not be anticipated with assurance.

In the corporate security markets a substantial recovery in prices also occurred in the latter part of August, apparently reflecting optimism concerning the prospect for rapid reconversion of industry to a peacetime basis. High grade corporation bonds remained somewhat below their previous highs, but medium grade bonds regained their previous peaks. Industrial stock averages reached new high levels for recent years, but public utilities remained moderately below their 1945 peaks, and railroad stocks regained only part of their losses.

During most of the first weeks of August Treasury certificates of indebtedness and short term Treasury notes were comparatively firm. Toward the end of the third week, however, prices of such securities eased on selling by banks in need of reserves and by a few corporations seeking cash for reconversion purposes, and the Federal Reserve Banks acquired (net) approximately 174 million dollars of certificates and notes during the week in order to supply banks with needed reserves and to maintain an orderly market. Subsequently, the market for these securities became somewhat less active, but there continued to be net sales, chiefly by banks, and Reserve System purchases in the week ended August 29 amounted to 119 million dollars.

Redistribution of Seventh War Loan Securities

The irregularity in Government security prices during the past month has tended to slow down the liquidation of speculative holdings of securities acquired in the Seventh War Loan drive for resale at a profit, although the selling was stimulated in the third week of August by the fear that an early Victory Loan might soon make available a new supply of securities at par. After a decline of about 500 million dollars in loans on Government obligations among weekly reporting member banks in 101 cities in the two weeks ended July 18, it required the next four weeks to effect the liquidation of a like amount of borrowings. Loans on Government securities to borrowers, other than brokers and dealers, showed an accelerated decline in the week ended August 22, but at the end of that time these loans still were higher than at the peak of any preceding War Loan. Borrowings on Treasury securities by brokers and dealers also remained at a high level on August 22.

Not all the liquidation of loans by "other" borrowers, of course, represented the sale of securities for the purposes of realizing speculative profits. A large part undoubtedly reflected repayment of loans out of current income by investing institutions and investors who subscribed for Seventh War Loan securities against future income and financed their purchases with bank loans. Nevertheless, a substantial redistribution of the securities offered in the Seventh War Loan drive from speculative purchasers into more permanent holdings, primarily nonreporting banks and institutional investors, appears to have been effected in the seven weeks ended August 22. This is indicated by the fact that while total Government security loans fell by about 1,100 million dollars, weekly reporting member bank holdings of Treasury obligations other than Treasury bills actually decreased by 150 million dollars and the Federal Reserve Banks added 257 million to their holdings of such securities.

A decrease of 390 million dollars in holdings of Treasury certificates of indebtedness and 134 million in notes in this period was not fully offset by net purchases of 374 million dollars of Treasury bonds. In addition, the reporting banks reduced their holdings of Treasury bills by more than 500 million dollars. During the period of declining Government security prices purchases of Treasury bonds by the banks also tapered off noticeably. The net increase in bond holdings came to 186 million dollars in the five weeks ended August 22, compared with an increase of 188 million in the two weeks ended July 18. On the other hand, the liquidation of bills and other Treasury securities, primarily certificates, took place largely in the last four weeks of this period and was related to the need for reserve funds resulting from higher reserve requirements and increased currency in circulation. Weekly reporting member banks made net purchases of "other" securities in each of the six weeks ended August 22, amounting in the aggregate to 232 million dollars and bringing total holdings to 3.4 billion, highest since November 4, 1942.

Member Bank Reserve Positions

Member bank reserves during August were subjected to considerable pressure from a heavy public demand for currency and substantially higher reserve requirements. In the four weeks ended August 22, currency circulation rose 580 million dollars reflecting vacation demands and an unusual increase in the week following the end of the war with Japan. Treasury expenditures continued heavy and resulted in the usual interdrive shift of deposits from reserve-free War Loan to private accounts subject to reserves. Consequently, reserve requirements rose by 400 million dollars. Compelled to seek Federal Reserve Bank credit in order to meet the needs for reserve funds resulting from these and other transactions, notably a loss of reserves through foreign account transactions, member banks increased their borrowings 170 million and made substantial net sales of Treasury bills and certificates which were acquired by the Reserve Banks. In addition, total excess reserves of member banks were reduced moderately. Total Reserve System security holdings rose 726 million in the four weeks ended August 22, and excess reserves of member banks fell 100 million to a total of about 1,050 million.

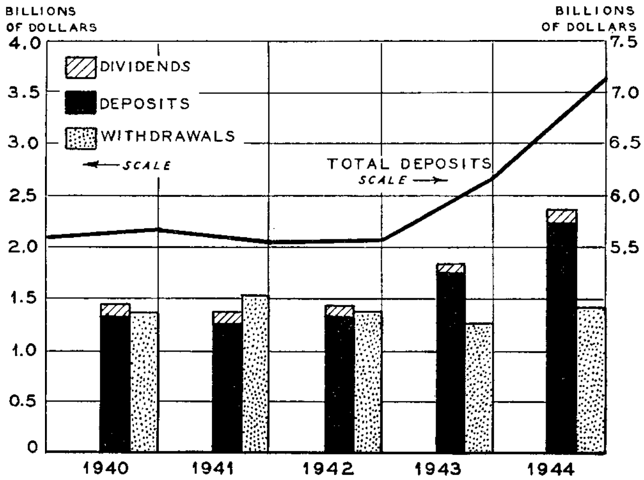
Over the entire four-week period, Treasury receipts from War Loan deposit calls and other sources were just about in balance with expenditures. In New York City, however, Government receipts exceeded disbursements by a wide margin, and the banks lost substantial amounts of reserve funds which the Government evidently spent in other parts of the country. As a result, demand deposits of individuals and businesses in the New York City banks declined 155 million dollars instead of showing the increase usually associated with the disbursement of War Loan deposits. In order to compensate for the loss of reserves resulting from Treasury and other transactions, the New York City banks had to obtain Federal Reserve credit to bring their reserves up to the required levels, largely through the sale of Treasury bills to the Reserve Bank and sales of Treasury certificates in the market (many of which were purchased for the Federal Reserve Open Market Account), and to a much smaller extent through borrowing from the Reserve Bank.

NEW YORK SAVINGS BANKS DURING THE WAR

Deposits in the New York State mutual savings banks are equal to more than half of the deposits in all mutual savings banks in the country. During the war they have risen substantially from 5.6 billion dollars at the end of 1939 to 7.7 billion on June 30, 1945, a gain of 38 per cent, and on the latter date they accounted for nearly a fifth of the total time deposits of individuals, partnerships, and corporations in all banks. The expansion in savings deposits reflected not only a sizable increase in previously established accounts (the size of the average deposit rose from 763 dollars to 943) but also some gain in the number of accounts which increased from 5,974,000 in the beginning of 1940 to 6,333,000 at the beginning of this year.

The wartime growth of savings deposits did not get under way until 1943. For the first three calendar years of war as a whole (1940-42 inclusive), withdrawals from savings accounts exceeded both new funds deposited and dividends accrued, as illustrated in the accompanying chart. Thus there was a small decrease in deposits between the end of 1939 and the end of 1942, as consumers first utilized increased incomes to repay debts and to acquire consumers' durable goods and then drew on their savings accounts to purchase war bonds. But since 1942, as the country became more fully mobilized for war, consumers' durable goods have largely disappeared

Factors Affecting Deposits of New York State Mutual Savings Banks*



* Total deposits, 1939-44, are end-of-year figures; dividends, amounts deposited, and withdrawals, 1940-44, are annual totals.
Source: Savings Banks Trust Company, *Savings Banks Chart Book.*

from the market and many nondurable goods have become scarce. Incomes, however, have continued to grow, and many people have had little alternative but to save in one form or another.

Other forms of savings such as time deposits in commercial banks and in Federal and State savings and loan associations increased more percentagewise between the end of 1942 and 1944 than did mutual savings bank deposits, after exhibiting the same pattern of little or no growth in the first three years of the war. Over the entire period (1939-44) time deposits in New York State commercial banks increased about 40 per cent, and savings and loan association shares nearly 50 per cent. The greater *relative* increase in the other forms of savings may be attributed partly to the fact that their amounts were much smaller in 1939 than mutual savings deposits so that their increases are measured from a much lower base. Over the five-year period commercial bank time deposits increased from 1.9 billion dollars to 2.7 billion and private repurchasable shares in savings and loan associations from 350 million dollars to 520 million. While it is not possible to determine the net amount of United States Savings bonds purchased in the State during these years, at the end of 1944 there were approximately 4 billion dollars of Series E bonds (at current redemption value) outstanding in the Second Federal Reserve District.

The growth of mutual savings bank deposits has been slower for three other important reasons. First, the dividends paid on such deposits are lower than those paid on savings and loan association shares or Savings bonds.[1] Second, in the past one of the great attractions of savings banks was their record of safety. Today deposits up to $5,000 in most commercial banks and shares in savings and loan associations are insured by Federal agencies. Third, mutual savings deposits are much more heavily concentrated in New York City than are other types of time deposits, and neither time nor demand deposits in New York City have risen as rapidly as in the rest of the State.

During the war savings banks were forced to make considerable adjustments in their investment policies. Construction activity and hence the number of new mortgages available has been severely curtailed, and the high level of business activity and earnings and correspondingly large tax receipts have enabled many corporations and State and local governments to retire large blocks of bonds. The only outlet, therefore, for the investment of new funds and funds released from other investments has been Government securities. As the accompanying table shows, the mortgage and other real estate

Total Assets of New York State Mutual Savings Banks
(In millions of dollars)

Dec. 31	Total assets	Bonds*	Mortgages and other real estate#	Cash on hand and due from banks	Banking house and other assets
1939	6,385	2,396	3,350	459	180
1940	6,463	2,386	3,361	541	175
1941	6,267	2,417	3,247	431	172
1942	6,264	2,660	3,079	364	161
1943	6,888	3,360	2,913	471	144
1944	7,884	4,604	2,822	315	143
1945†	8,557	5,310	2,773	333	141

*Book value.
#Includes real estate acquired by foreclosure.
† June 30.
Source: Savings Banks Trust Company and Savings Banks Association, State of New York.

holdings of the New York savings banks decreased over a half billion dollars from the end of 1939 to June of this year. Cash and other assets declined by smaller amounts. But the bond portfolio increased nearly 3 billion dollars.

In 1929 about 15 per cent of the savings banks' bond portfolios was invested in Government securities. A decade later this figure had risen to 67 per cent and by the end of last year to 95. At the present time the savings banks hold over 5 billion dollars of such securities which represent about 60 per cent of their total earning assets.

Bond Holdings of New York State Mutual Savings Banks
(Par value; in millions of dollars)

Dec. 31	Total	United States	State and municipal	Railroads	Public utilities	Miscellaneous
1939	2,460	1,637	352	362	95	14
1940	2,474	1,701	326	324	96	27
1941	2,515	1,932	223	261	80	19
1942	2,746	2,336	136	195	66	13
1943	3,417	3,136	75	137	58	11
1944	4,643	4,425	34	115	48	21

Source: Savings Banks Trust Company.

These changes in the composition of the earning assets of the mutual savings banks have been accompanied by a reduction in the average return on their investments and in the

[1] The prevailing dividend rate in the more important New York savings banks is 1½ per cent. The average rate of dividends paid on shares of New York State savings and loan associations for the year ended June 30, 1944 was about 2½ per cent. The yield on Series E Savings bonds, if held to maturity, is about 2.90 per cent per annum.

dividends the banks have been able to pay their depositors. The yield on Government securities is at the lowest point in history, and market conditions have also enabled many corporations to refund their obligations at lower rates. The effect of declining yields on the savings banks' earnings is clearly evidenced by the fact that while the bond portfolio of the savings banks nearly doubled from 1939 to 1944, the amount of interest received increased only 36 per cent. The operating expenses of the savings banks, on the other hand, have shown only a slight increase during the war period in spite of the greatly expanded volume of deposits.

The war, however, has enabled the mutual savings banks to make considerable nonoperating profits from the sale of securities and to liquidate at favorable prices much of the real estate they had acquired through foreclosure in earlier years. For example, partially tax-exempt Government securities are of no special advantage to the savings banks since they are not subject to income taxes. Their holdings of these securities, therefore, have been sold at a premium to commercial banks and other corporations in the excess profits tax brackets or to individuals with large incomes. Profits of this type reached a peak of 124 million dollars in 1943 but declined to 83 million in 1944. Such nonrecurring gains, however, have not been large enough to offset the effects of declining interest rates, and as a result, the average dividend paid by the State's savings banks dropped from the 1929 peak of 4.36 per cent to 1.95 by 1939 and 1.60 by 1944.

Beginning in 1943 additions to surplus and undivided profits have been made for the first time since 1936, partly owing to the high levels of nonoperating profits. The ratio of surplus to deposit liabilities has, nevertheless, been declining steadily since that year. But if cash and United States Government securities are subtracted from deposits, the ratio shows a steadily rising trend and is now about 35 per cent. The need for protection against losses has been reduced during the war by the banks' disposal of much of their holdings of foreclosed real estate, which in 1938 equaled 50 per cent of surplus and undivided profits but which has subsequently fallen to about 6 per cent.

The future trend of savings bank deposits is not readily ascertainable. Withdrawals of funds might be increased, as individuals utilize some of their savings to make good the wartime shortages of consumers' durable goods, or to tide them over periods of unemployment. However, the maintenance of economic activity at comparatively high levels should further generate new savings, offsetting to an unknown extent any unusual withdrawals. In the past, furthermore, deposits in mutual savings banks have not been subject to wide swings. In the depression of the thirties they declined only slightly, compared with a drop of nearly 50 per cent in the time deposits of New York State's commercial banks.

In an effort to build up their real estate and mortgage investments the savings banks are today gearing themselves to enter the field of low cost housing and small home financing instead of concentrating on mortgages on large commercial and residential properties as in the past. F.H.A. insured mortgages on properties in adjoining States, which were authorized in 1943, may prove to be of assistance in maintaining mortgage volume. In the mortgage field though, the savings banks will have to face keen competition from the commercial banks, savings and loan associations, and other institutions. The amount of securities other than Government obligations on the legal list or which may be placed on the legal list for savings bank investment will probably increase some as corporations and local government units seek new funds for expansion, new equipment, and other purposes. How much of the savings banks' earning assets can be shifted into investments with a higher yield than Government securities will, however, depend to a considerable extent on business conditions.

BRITISH FINANCIAL AGREEMENTS WITH EGYPT, TURKEY, AND IRAQ

In the August issue of this *Review,* a brief analysis was presented of Great Britain's recent financial agreements with three Western European countries (France, Belgium, and Sweden). In the present article, the scope and nature of the British financial agreements with Egypt, Turkey, and Iraq will be discussed. The Egyptian pact was signed in January of this year, and the other two pacts in May. Since the underlying issues of these three agreements are applicable also to other countries in the Near and Middle East, analysis of the agreements should throw some light on America's commercial problems in this important region. The agreements with Egypt and Iraq, which are of parallel character and are more novel and significant than the agreement with Turkey, are considered first.

The absence of free convertibility of the pound sterling into so-called hard currencies, notably the dollar, and the apparent impossibility of soon reattaining this convertibility in view of the expected aggregate excess of the sterling area's demand for dollars over its dollar supply, are the underlying reasons for the special agreements with Egypt and Iraq. Until this year, no formal agreement limiting the demands upon the sterling area's common pool of scarce foreign exchange was necessary for Egypt and Iraq, because the import licensing practised by the Middle East Supply Center[1], together with prevailing shipping and supply shortages, was sufficiently effective. But with the partial relaxation of MESC controls early this year, and in anticipation of increased purchases of civilian goods by Egypt and Iraq in 1945, it was

[1] The directing body of British and American officials responsible during the war for coordinating the allocation of shipping space and commodity supplies to the widespread Middle Eastern area including Egypt.

felt that special restraints were necessary. The reason why formal agreements were signed only with these two members of the sterling area lies in the fact that the closely controlled import licensing of other sterling area countries, coordinated in London since the outbreak of the war, has acted to hold down the demand for scarce currencies.

The essential feature of the two agreements is the establishment for the calendar year 1945 of a maximum, or target, as the British call it, of allocations of scarce currencies (designated in the agreements as the U. S. dollar, the Canadian dollar, the Swiss franc, the Swedish krona, and the Portuguese escudo) for the payment of imports, services, and investment returns. On the basis of official exchange rates, Egypt is granted a target of the scarce currency equivalent of 10 million Egyptian pounds, equal to about 41.5 million dollars, and Iraq a target of 3,502,500 Iraqi dinars (excluding oil company requirements), equal to about 14 million dollars. The figures are in gross terms, i.e., they do not take account of the scarce currency contributions these countries make to the sterling area pool; such contributions in the case of Iraq, particularly because of its petroleum exports, are usually in excess of its demands upon the pool, and in the case of Egypt, commonly less than its demands, although in certain periods during the war when dollar expenditures by the American military were especially high that was not the case. The target figures do not provide for any liquidation of the blocked sterling balances (mostly accumulated during the war) held by Egypt and Iraq, amounting at the end of 1944 to approximately 300 million and 55 million pounds sterling, respectively.

The agreements stipulate that upward target adjustments are to be made in the event of certain contingencies. In the Egyptian pact, for example, an additional 3 million Egyptian pounds equivalent is provided in case of an Egyptian wheat crop failure, which has since materialized. The agreements also reaffirm the wartime principle of maximum reliance upon the sterling area as a supply source, except that major items now scheduled to come from this area may be obtained from scarce currency areas and paid for out of the pool if there is a saving in cost of over 10 per cent. There is no limitation on Egypt's and Iraq's use of the currencies of countries outside the sterling area whose currencies are not scarce in the pool (the French franc for example), provided such use conforms with exchange control regulations.

The U. S. Department of Commerce has roughly estimated that, under the terms of the Egyptian agreement, American exporters will have a market in Egypt this year (excluding special wheat purchases) of about 5.4 million Egyptian pounds, or about 22.3 million dollars. Except for the lend-lease swollen wartime totals, this would be a record figure and would compare with less than 2.7 million Egyptian pounds in 1939. Though not specified in the agreements, it is believed that sales of surplus American property will be charged against the dollar target. American commercial and financial interests are also expected to benefit, within this year's target, by Egyptian remittances on account of film royalties, interest, dividends, etc., and for traveling and other Egyptian expenditures in the United States, to the equivalent of an estimated 1,075,000 Egyptian pounds.

The agreement with Iraq abolishes the special dollar account that contained that country's dollar earnings and which was earmarked for its eventual free use. Apart from Palestine's dollar receipts for Jewish national institutions and from a small portion of India's dollar earnings, Iraq was alone among sterling area countries in enjoying such an account. The Iraqi Government has favored the continuance of this account in the past on the ground that the retention of its dollar earnings constituted an incentive toward an increase in these earnings. It has been felt on the British side, however, that any important result of this incentive is precluded by the raw material character of Iraqi exports; that, in any event, it would hardly be sufficient to justify special treatment; and that it surely was not to be compared to what Britain itself could gain by expanding the export of its specialties and promoting its tourist attractions, based on a similar incentive. In any case, the abolition of the special Iraqi dollar account, and the more general question of how the sterling area members divide up their available dollar supply, are matters of great interest to the United States, particularly from the viewpoint of their potential influence on the character of American commodity exports, and also from that of the development of direct American connections with the Middle East. A larger target for Iraq and other economically undeveloped countries of the sterling area, for instance, would tend to expand the export of American trucks, machinery, and other manufactured items, whereas a relatively larger supply of dollars for Britain's own use would tend to stimulate American exports of raw cotton and tobacco, for example.

Common to both the Egyptian and Iraqi agreements is the British recommendation that the governments of Egypt and Iraq assume greater responsibilities of exchange control and import licensing so as to keep within their targets. Both governments have accordingly made their exchange control more comprehensive and have also tightened their screening of import license applications. It would therefore appear necessary, at least during the life of these agreements, for American foreign traders in the Middle East to accommodate themselves to a more elaborate structure of commercial controls than before the war; in fact, it is possible that these controls, established for the first time during the war and now expanded somewhat anomalously in the so-called decontrol period, may be maintained even after the agreements lapse. The agreements themselves are to run for the whole of this calendar year and will presumably be subject to renegotiation next year in the light of the circumstances then prevailing.

The most important consideration affecting the longevity of the agreements concerns the development of Britain's international economic position after the war, including its progress in the orderly liquidation of war debts and in meeting postwar current account deficits. Elimination of the bilateral and discriminatory features of these agreements after the transition years will undoubtedly depend heavily upon the degree of success achieved through appropriate international action (which would be greatly aided by a vigorous and orderly American economy) in establishing an expanding and stable level of international trade and investment. The proposed International Monetary Fund is intended to exert an influence toward that end, since one of the Fund's purposes will be to restore a multilateral system of international payments for current transactions and to eliminate foreign exchange restrictions which hamper world trade. On the other hand, the Fund cannot, during the first five years (or even more) of its operations, prevent the retention of restrictions on current account transactions such as are incorporated in the agreements here reviewed, so long as the national authorities concerned consider the restrictions necessary.

The Anglo-Turkish Agreement, following the lines of the bilateral trade and payments arrangements established between Britain and Turkey in the past, notably in the agreement of February 3, 1940 (superseded by the present document), aims to facilitate the resumption on a peacetime basis of orderly commercial and financial relations between the two countries. The new agreement mainly provides that all payments between Turkey and the sterling area will be made in their respective currencies through special, supervised accounts, which are not convertible into third currencies except that up to 20 per cent of Turkish holdings of sterling may be used, at the discretion of the British authorities, for payments in other currencies, including the dollar. Though no limit is placed upon either country's holdings of the other's currency, it is not expected that sizable balances will accumulate on either side, because of the limited convertibility of the pound sterling and the long-frozen Turkish balances of the past. The agreement, as a matter of fact, includes special incentives to Turkish exportation so as to help British creditors use their frozen Turkish balances.

Unlike the British agreements with Western European countries, the Anglo-Turkish agreement lacks any monetary stabilization feature, that is, neither government obligates itself to help support the other's currency at an agreed-upon exchange rate. The only reference to exchange rates is in the responsibility placed upon the Turkish Government not to reduce the premium which it pays for the proceeds of exports to the sterling area, though it is free to raise the premium. Under the agreement, Britain, in the event of its formal readoption of agricultural import quotas, promises to give Turkey equitable treatment, a provision that has been interpreted in British trade circles as possibly foreshadowing the reintroduction of such restrictions. The agreement is to remain in force until April 30, 1946 and for successive periods of twelve months, unless proper termination notice is given no later than three months before the end of any such period. It is also provided that the terms of the agreement will be reviewed and necessary amendments made in case either signatory becomes a party to an international monetary agreement. Under the terms of the International Monetary Fund plan, this would mean the eventual abolition of the limited and discretionary convertibility of the currencies involved, as embodied in all three agreements under review, in favor of free and unlimited convertibility, at least so far as currently accruing balances resulting from trade and service transactions (as distinct from capital transactions) are concerned.

CORPORATE CAPITAL FINANCING DURING THE WAR

The volume of new corporate security issues rose sharply during July to a total of almost one billion dollars, the greatest volume in any month since September 1929. In part, the heavy July financing represented the accumulation of offerings that might have been made in May and June but for the Seventh War Loan drive. About 15 per cent of the month's flotations were offered by domestic corporations for the purpose of financing the expansion of plant and equipment and meeting additional working capital requirements. The estimated total of "new money" issues of about 150 million dollars was, nevertheless, highest since August 1941. Securities issued for the purpose of retiring outstanding issues, repaying bank indebtedness, and for other purposes dominated the month's offerings, amounting to more than 800 million dollars, an all-time record. (Data are based on compilations of the Securities and Exchange Commission.)

An unusually large volume of corporate financing was achieved in July in spite of the tendency toward lower prices that developed in the security markets during the month, which retarded to some extent the smooth distribution of new securities to investors in several instances. In a few cases trading in new issues took place at prices lower than those at which the securities were initially offered by underwriters. It appeared, nevertheless, that most of the new securities were eventually placed with investors.

Irregular price tendencies continued into the following month and were a factor in curtailing the volume of flotations in August, which according to preliminary indications fell to about 40 per cent of the July total. However, this was in part a natural drop from the very high volume of the preceding month.

For the first seven months of 1945, corporate financing in the capital market approximated the three billion dollars of new issues offered to investors in the whole of 1944. The total volume for the current year will undoubtedly be the greatest since 1936. As in 1944, refunding issues so far this year have accounted for about 80 per cent of the total.

During the war the volume of corporate financing in the capital market was subject to wide fluctuations. The outbreak of war in 1939 was not followed by any sharp expansion in the volume of new corporate issues; despite a substantial increase in industrial activity stimulated by defense preparations, the volume of capital financing increased only about 25 per cent from 1939 to 1940 and remained unchanged in 1941. The entrance of the United States into the war was followed by a decline in new issues in 1942 to a level 60 per cent below that of the preceding two years, as Government financing expanded and the sale of corporate issues for expansion of peacetime activities and refunding purposes contracted. A gradual rise in corporate security offerings ensued in 1943 and gathered momentum in 1944 and 1945.

In the three years, 1942-44, the volume of railroad and public utility financing for improvements and expansion declined by about 65 per cent from the volume of the preceding three years, while that of industrial corporations increased more than 50 per cent. Wartime restrictions on the availability of materials and labor reduced the expenditures of railroad and utility companies for such purposes to a point where they could be met in large part from high current earnings, whereas restrictions on construction and equipment fell less heavily upon industrial concerns which were directly engaged in the war effort. Nevertheless, the major part of the increase in new capital raised by industrial companies went to meet added working capital needs rather than new plant and equipment.

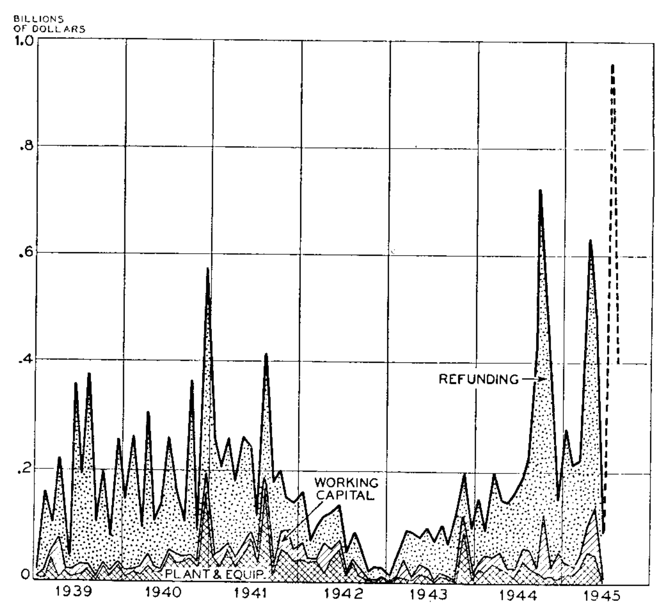
In spite of the unprecedented expansion in industrial capacity and business activity during the war, the volume of security issues to finance plant expansion and to supply working capital showed no such increase as occurred during the first World War, and in no year equaled the last peacetime peak of about one billion dollars reached in 1937.

The reason for this seeming anomaly is the direct financing by the Federal Government of a large part of the war industrial facilities built (or building) between July 1, 1940 and the end of the war. Private enterprise, nevertheless, invested substantial amounts of its own funds in war (and war-supporting) facilities. Offerings of new corporate securities for the purpose of adding to plant and equipment, however, amounted to only 2 billion dollars. The major part of the expansion, together with enlarged working capital needs, was evidently financed from other sources, including depreciation allowances, Government-guaranteed war production loans, Government progress payments and advances on war contracts, and the temporary use of funds accumulated for tax payments.

An entirely different policy was pursued in financing industrial expansion during World War I when the bulk of the capital expenditures were made with private funds obtained in large part from the capital market. Thus, in order to satisfy the requirements of a far smaller program, domestic corporations floated an average of 1.6 billion dollars of new securities each year from 1914 through 1918 (according to figures compiled by the New York Journal of Commerce), as compared with an average of about 1.5 billion a year from 1939 through 1944, and the proportion for new capital investment was probably much greater in the earlier period. Although information concerning the distribution of the new issues between new capital and refunding is not available for the World War I period, in view of the rising trend of interest rates during those years it is probable that a major part of the new issues represented new capital in the strict sense. On the other hand, about three quarters of the value of new corporate securities issued from 1939 through 1944 were refunding issues.

The predominance of refunding issues during the war points to an even more striking anomaly, declining interest rates in wartime. Unprecedentedly heavy Government demands upon the capital market were financed at record low interest rates and yields on corporate obligations declined further. As a result corporate issuers were able to achieve substantial savings in fixed charges by refunding outstanding securities with new issues bearing lower coupons, a tendency which spread into preferred stocks on a growing scale in recent years. In many instances, corporations supplemented the proceeds of the sales of new securities with their own cash resources (which were augmented by increased earnings and conservative dividend payments) to pay off outstanding issues. Redemptions of security issues in excess of new offerings, together with open market purchases of outstanding obligations, resulted in a net reduction of about 2 billion dollars, or 5 per cent, in corporate long term debt between the end of 1939 and 1944.

New Corporate Security Issues*



* Net proceeds of the sale of new issues after underwriting and other expenses, and purposes for which proceeds are used.

Source: Securities and Exchange Commission; July and August 1945 totals estimated by Federal Reserve Bank of New York.

At the same time, declining interest rates, together with the Government's financing of the major portion of the expansion of industrial facilities and of working capital needs, precluded the necessity for active supervision of new corporate security flotations such as existed during World War I, when issuing of new securities without the approval of the Capital Issues Committee was practically prohibited. In this war, cooperation between investment bankers and the Treasury has been substituted for control. New corporate and other non-Federal issues since 1943 have been timed by bankers so as to reach the market in the months between War Loans, with virtually no such offerings made while drives were in progress. The concentration of corporate security marketings in the months between drives is evident from the sharp peaks and troughs shown in the accompanying chart for the period beginning in 1944 when the sale of new issues reached high levels.

DEPARTMENT STORE TRADE

Department store sales in this District during August were approximately 10 per cent above those of a year earlier. Considerably larger increases were reported in the early part of the month, but the gain for the month was affected by the rather general closing of stores for two days after the Japanese capitulation and by somewhat smaller increases in the latter part of the month. The seasonally adjusted index declined slightly from the July peak and was close to the average for the first seven months.

During the period January through July sales have averaged 14 per cent above the corresponding 1944 period and more than 65 per cent above 1939. Among the individual cities, Binghamton has shown one of the largest gains for any city of the District over last year and also the war period as a whole; sales in that city have increased almost 150 per cent since 1939. Although Albany ranks first in its gain over 1944, comparison with 1939 shows sales only 30 per cent higher, the smallest increase for any city. Syracuse and Newark both show increases a little above average for the year, but for the war period Syracuse experienced an increase of over 100 per cent while Newark gained only 50 per cent. Sales in New York and Rochester were about average, and the gain since 1939 was approximately 70 per cent for both cities. Niagara Falls, Buffalo, and Bridgeport fell considerably below average in their gains this year; during the war period Niagara Falls experienced one of the largest gains, 150 per cent, while Buffalo and Bridgeport experienced increases of 90 and 50 per cent, respectively. Sales in the latter city recovered this year to the 1942 peak, while all other cities reached new highs for the war period.

The dollar value of department store stocks at the close of July was 16 per cent above a year earlier and 75 per cent larger than 1939. Outstanding orders approximately equaled the dollar value of stock on hand. They were 8 per cent above those on July 31, 1944 and about 5 times the 1939 level.

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

Locality	Net sales July 1945	Net sales Jan. through July 1945	Stocks on hand July 31, 1945
Department stores, Second District	+18	+14	+16
New York City	+19	+15	+16
Northern New Jersey	+20	+15	+22
Newark	+23	+16	+24
Westchester and Fairfield Counties	+ 8	+10	+27
Bridgeport	+ 4	+ 5	+21
Lower Hudson River Valley	+22	+17	+ 6
Poughkeepsie	+24	+16	—
Upper Hudson River Valley	+24	+15	+14
Albany	+33	+19	—
Schenectady	+18	+12	+ 7
Central New York State	+17	+13	+10
Mohawk River Valley	+ 6	+ 6	+ 2
Utica	+ 6	+ 5	0
Syracuse	+24	+16	+14
Northern New York State	+ 8	+18	—
Southern New York State	+19	+15	+13
Binghamton	+22	+18	+16
Elmira	+14	+ 9	+ 9
Western New York State	+15	+11	+13
Buffalo	+14	+ 9	+ 9
Niagara Falls	+ 8	+10	−13
Rochester	+18	+14	+25
Apparel stores (chiefly New York City)	+36	+22	+16

Indexes of Department Store Sales and Stocks Second Federal Reserve District (1935-39 average=100 per cent)

Item	1944 July	1945 May	1945 June	1945 July
Sales (average daily), unadjusted	100	148	156	118
Sales (average daily), seasonally adjusted	149	156	169	176
Stocks, unadjusted	138	167	165	161
Stocks, seasonally adjusted	152	165	172	175

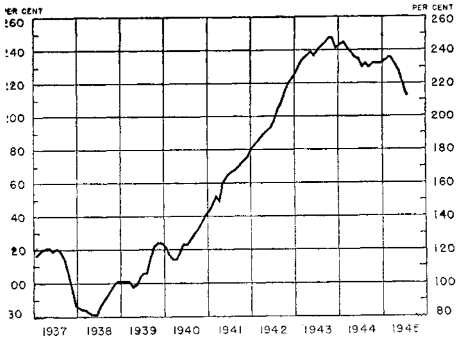
Indexes of Business

Index	1944 July	1945 May	1945 June	1945 July
Industrial production*, 1935-39 = 100 (*Board of Governors, Federal Reserve System*)	230	225r	220	212p
Electric power output*, 1935-39 = 100 (*Federal Reserve Bank of New York*)	201	208r	205	203p
Ton-miles of railway freight*, 1935-39 = 100 (*Federal Reserve Bank of New York*)	231	235	239	
Sales of all retail stores*, 1935-39 = 100 (*Department of Commerce*)	179	177	182p	
Factory Employment				
United States, 1939 = 100 (*Bureau of Labor Statistics*)	165	151	148	144p
New York State, 1935-39 = 100 (*New York State Dept. of Labor*)	145	138	134	128p
Factory Payrolls				
United States, 1939 = 100 (*Bureau of Labor Statistics*)	311	303	298	
New York State, 1935-39 = 100 (*New York State Dept. of Labor*)	274	268	263	249p
Income payments*, 1935-39 = 100 (*Department of Commerce*)	233	242	244p	
Wage rates, 1926 = 100 (*Federal Reserve Bank of New York*)	165	170	170p	
Cost of living, 1935-39 = 100 (*Bureau of Labor Statistics*)	126	128	129	129p
Velocity of demand deposits*, 1935-39 = 100 (*Federal Reserve Bank of New York*)				
New York City	90	81	106	94
Outside New York City	85	73	92	76

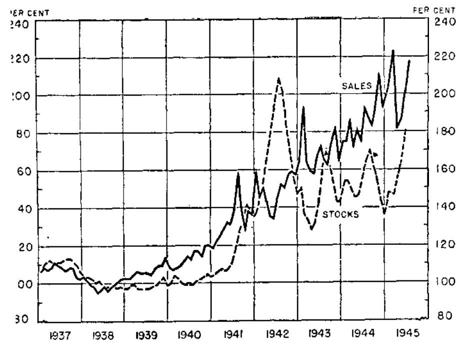
* Adjusted for seasonal variation. *p* Preliminary. *r* Revised.

FEDERAL RESERVE BANK OF NEW YORK

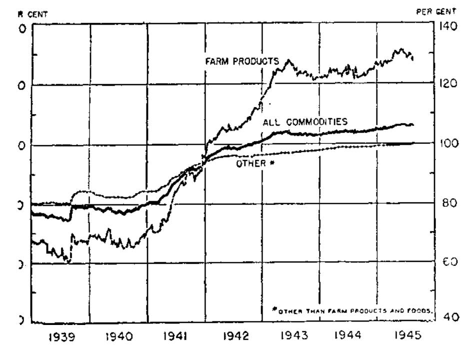
MONTHLY REVIEW, SEPTEMBER 1945



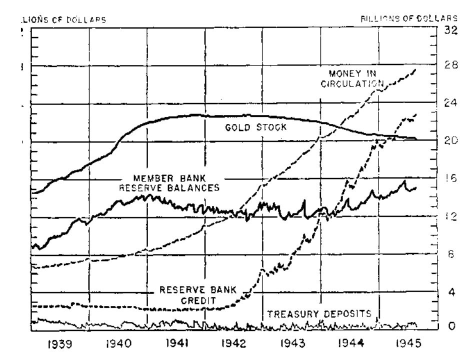
.dex of Physical Volume of Industrial Production, Adjusted for Seasonal Variation (1935-39 average=100 per cent)



dexes of Value of Department Store Sales and Stocks, Adjusted for Seasonal Variation (1935-39 average=100 per cent)



lexes of Wholesale Prices Compiled by Bureau of Labor Statistics (1926 average=100 per cent; latest figures are for week ended August 18)



mber Bank Reserves and Related Items (Latest figures are for August 15)

General Business and Financial Conditions

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

INDUSTRIAL activity declined further in July and the early part of August and was sharply curtailed in the latter part of the month as munitions cutbacks were greatly accelerated. Retail trade was maintained in July and early August at a high level for this season of the year.

Industrial Production

Industrial production in July, the last full month of high level production for war, was 212 per cent of the 1935-39 average, according to the Board's seasonally adjusted index, as compared with 220 in June. Following the surrender of Japan most munitions contracts were canceled, and as a result it is expected that munitions output and industrial production will show much larger declines in August.

Production of aircraft declined about 20 per cent in July and operations at shipyards and in other munitions industries were reduced considerably from the June rate. Steel production in July and the early part of August was about 5 per cent below the June level. In the week following Japan's surrender activity at steel mills decreased sharply to a rate of 70 per cent of capacity. Production of nonferrous metals continued to decline in July, while output of lumber and stone, clay, and glass products was maintained.

Production of most nondurable goods declined somewhat in July, but, as a group, output of these products was slightly above a year ago. Cotton consumption was 14 per cent below the preceding month and was 11 per cent below last July. Activity in the meatpacking, canning, and baking industries, after allowance for seasonal changes, was down somewhat from June. Production of alcoholic beverages rose sharply as distilleries were released from industrial alcohol production. Activity in chemical, rubber, and other nondurable goods industries declined slightly.

Coal production declined about 5 per cent in July and the first part of August from the June rate, while output of crude petroleum continued to increase and was in record volume.

Contracts awarded for private construction continued to rise sharply in July and were more than three times the low level prevailing last summer, according to F. W. Dodge Corporation data. Contracts for privately-owned nonresidential building showed the largest increase. On August 21, all restrictions over the construction of industrial plants were removed.

Distribution

Department store sales declined much less than is usual from June to July, and the Board's seasonally adjusted index rose from 201 to 218 per cent of the 1935-39 average. Sales in July were 15 per cent larger than in the corresponding period last year. During the first two weeks of August sales were about 20 per cent larger than a year ago.

Carloadings of most classes of railroad freight declined somewhat in July and the early part of August and were below the volume shipped during the same period last year. Shipments of l.c.l. merchandise, however, were at about the same rate as prevailed during the same period last year.

Commodity Prices

Wholesale commodity prices generally showed little change from the early part of July to the early part of August. Following the announcement of peace negotiations prices of cotton and grains declined somewhat—especially contracts for delivery next year—while prices of most other basic commodities continued unchanged.

Retail prices advanced somewhat further in June. Food prices rose 2 per cent and retail prices of clothing, housefurnishings, and miscellaneous items continued to show slight advances.

Agriculture

Crop prospects improved during July and, according to indications on August 1, total output this year will be only slightly smaller than the record volumes of 1942 and 1944. Of the major crops only production of cotton, corn, and apples is expected to be less than a year ago. Marketings this summer of most livestock products except hogs have been about as large as, or larger than, the high levels of recent summers.

Bank Credit

Loans and investments at reporting banks in 101 leading cities declined by 1.2 billion dollars between the close of the Seventh War Loan and mid-August. Reflecting repayments on advances made during the drive, loans for purchasing or carrying Government securities declined by a billion dollars. Loans both to brokers and dealers and to other bank customers decreased by approximately 500 million dollars each, compared to drive and immediate pre-drive increases of 1.1 billion and 1.8 billion dollars, respectively. While bank holdings of Treasury bonds continued their steady week-to-week increase, holdings of bills and certificates, which had increased during the drive, began to decline again in late July and August. On balance, the total portfolio of Government securities declined by 350 million dollars. Holdings of other securities showed a small increase over the six-week period.

Following the close of the Seventh Drive, deposits of businesses and individuals began to increase again as Treasury expenditures transferred funds from war loan to private accounts. The average level of required reserves accordingly rose by about 500 million dollars between the drive-end low point and mid-August. Reserve balances increased by about 300 million dollars and excess reserves dropped by about 200 million to around 1.2 billion outstanding; this was still somewhat above the generally prevailing interdrive level of slightly less than a billion dollars.

Member bank borrowing from the Federal Reserve Banks, which had declined to a minimum by the close of the Seventh Drive, increased by 275 million dollars in the subsequent six-week period ended August 15. Reserve funds were also supplied to member banks through an increase of 125 million dollars in Government security holdings at the Reserve Banks, as well as by temporary fluctuations in other Federal Reserve Bank credit and in Treasury deposits at the Reserve Banks. Only partially offsetting increases in such funds were a currency outflow of 520 million dollars and a small decline in gold stock. The currency outflow during July, 360 million dollars, was the largest in the past few months; early August increases were also substantial.