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Of Credit and Business Conditions

FEDERAL RESERVE BANK OF NEW YORK

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MONEY MARKET IN FEBRUARY

During the past month, the Treasury announced its intention to retire about 2,780 million dollars of its outstanding obligations falling due or called for redemption in March. The issues to be retired consist of 489 million dollars of 3¾ per cent bonds called for redemption on March 15, 1946, 1,291 million 1 per cent Treasury notes maturing on that date, and about one billion dollars of an issue of 4,147 million ⅞ per cent certificates of indebtedness due March 1, 1946. The remaining certificates are to be refunded with a similar issue bearing the same rate and term to maturity as the expiring one. Holders of the maturing issue are to be alloted new certificates on an equal percentage basis (76 per cent), except that holdings of 25 thousand dollars or less will be renewed in full if the investor so elects and that for holdings in excess of that amount the allotment will be not less than 25 thousand.

The scheduled reduction of the public debt is made possible by the very high working balance of the Treasury which resulted from the heavy oversubscription of the Victory Loan. The Treasury raised considerably more funds than it will need to meet current disbursements for many months to come, and its working balance is still close to the peak reached at the end of the Victory Loan. Government expenditures have fallen off more rapidly since the beginning of this year than had been anticipated, and receipts have held up better than expected. Consequently, Treasury withdrawals from War Loan deposit accounts in the banks have been so small that they have been largely offset by new credits to such accounts arising out of payments on deferred subscriptions to Victory Loan issues and payments for current purchases of savings bonds and notes. Near the end of February the Treasury working balance was less than 400 million dollars below the peak of close to 26.2 billion dollars on January 2.

The redemption operation will afford the Treasury an opportunity to reduce its large working balance and the public debt; it will also reduce the potential expansion of private deposits which would occur if all the funds now in War Loan deposit accounts were used to meet ordinary Government disbursements. To the extent that the Government securities to be redeemed are held by the banking system, including the Federal Reserve Banks, no increase in private deposits will result from their redemption. On the whole, it appears unlikely that the operation will have material effects upon the market for Government securities, or upon the money market in general.

The effects of the retirement of public debt on bank reserves and on deposits depend upon the distribution of the securities to be redeemed among bank and nonbank investors, and upon the method of payment adopted by the Treasury. In the case of the March redemptions, about 80 per cent of the total amount involved was held by commercial banks, Federal Reserve Banks, and Government agencies and trust funds as of November 30, 1945, the latest date for which statistics are available. The commercial banks alone owned about two thirds of the total. The Treasury will meet the redemptions largely with funds withdrawn from War Loan deposits in commercial banks, and to a more limited extent with funds on deposit with the Federal Reserve Banks, which on February 20 had reached the unusually high total of 940 million dollars. To provide funds for the redemption of approximately one billion dollars of certificates maturing on March 1, the Treasury has issued a call for the payment from War Loan deposits of a total of 708 million dollars, 472 million dollars on March 1 and 236 million on March 2. The difference will evidently be made up by drawing down the Treasury's balances with the Federal Reserve Banks.

Withdrawals from War Loan deposits to retire securities owned by commercial banks will bring about a net reduction of total deposits, but as the funds withdrawn are immediately returned to the banks in payment for redeemed securities, bank reserves will, in the aggregate, remain unchanged. Thus, the net effect on the commercial banking system will be a simultaneous decline in bank holdings of Government securities and in deposit liabilities.

It is not to be expected, however, that the reserves gained by individual banking institutions from the redemption of securities held by them or their depositors will in all cases approximate the loss of reserves resulting from withdrawals of War Loan deposits. Some banks will receive more funds than they will lose, while others will experience net withdrawals and losses of reserves. Some banks and other holders of securities to be redeemed are reported to have begun adjusting their portfolios shortly after the announcement of the March redemptions by selling part of their holdings of the securities to be retired and purchasing other short term Treasury securities —certificates of indebtedness, notes, and short term taxable bonds.

To the extent that the securities to be retired are held by nonbank investors, their redemption will result in an increase in private deposits and an accompanying rise in bank reserve requirements. If the funds to meet these redemptions are obtained through Treasury withdrawals from War Loan accounts, the banks as a whole will have to adjust their reserve positions to the required levels by drawing upon their excess reserves, disposing of earning assets, or borrowing from the Federal Reserve Banks. Under present conditions, the sale of Treasury obligations in the open market or directly to the Federal Reserve Banks (in the case of Treasury bills), is likely to be the form of reserve adjustment most frequently used. The amount of adjustment required, however, will not be large since holdings of nonbank investors represent a relatively small proportion of the amount of securities to be redeemed.

Redemption of securities held by the Federal Reserve Banks (and Government agencies and trust funds) can apparently be met, at least in the case of the March 1 certificates, by drawing upon Treasury balances in the Federal Reserve Banks, and thus will cause no loss of reserves to member banks. However, it is not possible at this time to foresee whether any net withdrawal of funds from the banks in connection with the March 15 redemptions of securities in Federal Reserve and Government accounts will be necessary, or not.

There has been a relatively heavy demand for short dated Treasury issues in recent weeks which has been in marked contrast to the experience of the past year or more, in which banks tended to purchase largely medium and longer term Treasury bonds with any gain of reserves, or even with funds obtained by the sale of short term securities. There is some evidence that this tendency may have been undergoing a change recently, as a result of the narrowing spread between yields on medium and long term and short term Treasury issues and some uncertainty as to the future course of interest rates, occasioned by frequent discussions in the press of suggested changes in Federal Reserve credit policies and in public debt management policies.

Demand for Treasury issues with near term maturities or call dates was reflected in a further decline in Federal Reserve System holdings of certificates of indebtedness and short term Treasury notes of nearly 500 million dollars in the first three weeks of February and a reduction in excess reserves of banks located outside New York City, especially during the week ended February 20. A substantial increase in certificate and note holdings and a decrease in bond holdings of the New York City weekly reporting member banks in that same week suggests some switching out of bonds into short term Treasury issues.

Strength in the Government bond market through the first nine days of February gave way to irregularity subsequently, but after alternate recessions and advances, prices near the close of the month were higher in most cases than at the end of January. Prices of certificates, notes, and short term taxable bonds were generally firm.

Member Bank Reserve Positions

Some reduction in member bank excess reserves has occurred during the past month. In part, this was attributable to Treasury operations and in part to the operations of the member banks themselves. Heavy tax receipts, together with a decline in Federal expenditures for war purposes, were largely responsible for an increase of approximately 360 million dollars in the Treasury's balance with the Reserve Banks during the four weeks ended February 20. Operations of the member banks and of other investors in the Government security market resulted in a substantial reduction in Federal Reserve Bank holdings of Treasury certificates of indebtedness and notes, which more than offset increases in other types of Federal Reserve credit (loans to and Treasury bill purchases from banks losing reserves).

Tax collections and nonbank investor purchases of securities held by the banking system were accompanied by a decline in private deposits, and reserve requirements fell 86 million dollars during the four weeks. A further gain in the monetary gold stock of 98 million dollars, and a small decline in currency in circulation—both additional indications of the reversal of the wartime trends—tended to add to bank reserves. But the aggregate of these and other factors tending to ease member bank reserve positions was far less than the increase in Treasury deposits with the Reserve Banks and the net decline in Federal Reserve credit, and member banks drew down their excess reserves by about 280 million dollars.

For the most part, the same factors affecting the reserves of all member banks were operative in New York City, except that there was a small increase in outstanding currency and that Treasury net receipts were exceptionally large in New York. A substantial movement of business and financial funds to the City, offset in part by a decline in correspondent bank balances kept in New York, tended to ease the pressure on the New York City banks, however.

MEMBER BANK EARNINGS IN 1945

Profits after income taxes, realized by all member banks in this District during 1945 averaged 11.6 per cent of capital funds, compared with 9.5 per cent in 1944 and 7.2 per cent in 1943.* Not all banks, however, shared in the increase; there were over 200 banks in the Second District, or more than 25 per cent of all member banks, which showed a decrease in net profits after income taxes. Most of the banks showing decreases were institutions with less than 20 million dollars of deposits, although a number of the larger banks outside New York City also had smaller profits in 1945 than in 1944.

* These figures represent unweighted averages of the percentages for individual banks; the ratio of aggregate profits to aggregate capital funds, in which the large New York City banks predominate, showed an increase only two-thirds as great in 1945, as those banks had much smaller increases in profit ratios than many medium size banks in the District.

**Selected Average Operating Ratios of All Member Banks
Second Federal Reserve District**

	1943	1944	1945
Number of banks	796	810	805
Percentage of Total Capital Accounts			
Net current earnings	7.3	8.8	9.4
Profits before income taxes	7.9	10.8	14.0
Net profits after income taxes	7.2	9.5	11.6
Cash dividends declared	2.0	2.1	2.1
Percentage of Total Earnings			
Interest on U. S. Gov't securities	$\left.\begin{matrix}\\ \\ \end{matrix}\right\}$ 45.0	$\left.\begin{matrix}\\ \\ \end{matrix}\right\}$ 52.4	49.2
Interest on other securities			8.0
Earnings on loans	39.5	32.3	28.8
Service charges on deposit accounts	7.0	7.2	6.4
All other earnings	8.5	8.1	7.6
Total earnings	100.0	100.0	100.0
Salaries and wages	31.5	29.6	28.4
Interest on time and savings deposits	14.8	15.1	16.4
All other expenses	27.2	25.3	24.8
Total expenses	73.5	70.0	69.6
Net current earnings	26.5	30.0	30.4
Net recoveries	2.9	7.7	15.5
Taxes on net income	2.5	4.2	7.8
Net profits after income taxes	26.9	33.5	38.1
Percentage of Total Assets			
U. S. Government securities	47.0	56.9	61.3
Other securities	9.6	7.2	6.1
Loans	19.4	15.0	13.0
Cash assets	22.0	19.4	18.4

Even though the net profits of nearly three out of four member banks in this District were higher in 1945 than in 1944, bank stockholders obtained little direct benefit in the form of increased dividend payments, as banks generally continued the conservative policy of adding a large part of their net profits (about 80 per cent on the average) to capital accounts, thereby increasing capital funds about 9.5 per cent. The remaining 20 per cent of profits was used for dividends, which for all banks in the District averaged 2.1 per cent of total capital accounts, the same as in 1944.

Operating income increased considerably because of a larger volume of earning assets, mainly in the form of Government securities, although there were also substantial increases in loans to finance the purchase or carrying of Government securities, and, in the case of New York City banks, some increases in industrial and commercial loans. The average rates of return on earning assets were lower than in the previous year. The increase in total current income was more than enough to take care of the increased expenses for salaries, interest on the expanded amount of time deposits, and other increased costs of bank operations, leaving the ratio of net current earnings to total earnings practically unchanged from 1944 for most groups of banks. There were sizable additions to current net earnings from profits on securities sold during the year and from recoveries on loans and securities that had been written down or charged off in previous years, particularly for the medium and larger size banks. However, taxes on net income were much larger than in previous years and for all banks averaged 7.8 per cent of gross earnings and about one fourth of net current earnings. The proportion of earnings used for income taxes increased with the size of banks, and was by far the highest for New York City banks having total deposits of more than one hundred million dollars.

Despite the additions to capital funds, as previously mentioned, the average ratio of capital accounts to total deposits declined from over 9 per cent to 8 per cent, but the ratio of capital to all assets other than cash and Government securities rose to 43 per cent from 40 in 1944 and 34 in 1943.

BACKGROUND AND AIMS OF THE ANGLO-AMERICAN FINANCIAL AGREEMENT

At the end of January joint resolutions were introduced in the Senate and the House of Representatives designed to give legislative effect to the Anglo-American Financial Agreement of December 1945 (the main provisions of which were summarized in the January issue of this *Review*), and it is anticipated that hearings will soon be held before the appropriate Congressional committees. The agreement has already been approved by the British Parliament. Because of the size of the credit provided for in the agreement, and because of the wide scope and complex nature of the other provisions of the agreement, it may be useful to review the character of the British balance of payments difficulties which have given rise to the need for financial assistance, the contribution which the proposed 3,750 million dollar line of credit would make toward the solution of those problems, and the benefits which this country may expect to derive from the agreement.

In the years immediately preceding the war the British balance of payments was in a state of reasonable equilibrium. For example, in 1936-38 the United Kingdom experienced an annual average deficit on current account of only 43 million pounds, the net result of an average deficit of 389 million on merchandise trade account, and of net receipts of 203 million from overseas investments, 105 million from shipping, and 38 million from all other services, such as insurance, commissions, and tourist trade.

This balance of payments pattern was sharply upset by the war, and the external financial position of the United Kingdom underwent a severe deterioration. Primarily as a result of huge overseas military expenditures, the British deficit on current account rose to an annual average of 731 million in the years 1940-44, and aggregated 4,189 million pounds from September 1939 to June 1945 (apart from goods and services acquired under lend-lease and Canadian mutual aid). In order to finance this cash deficit, it was necessary for the United Kingdom to increase its external debt (chiefly in the form of sterling balances held by foreign monetary authorities) by 2,879 million pounds, to sell 1,118 million pounds of its overseas investments, and to reduce its official gold and dollar holdings by 152 million pounds. By June 30, 1945 the United Kingdom, long the world's leading creditor nation, had become a net debtor, with external debts of 3,355 million pounds (of which about 80 per cent was owed to sterling area countries), while its overseas investments had been reduced to substantially under 3,000 million pounds (in nominal values).

The serious condition of disequilibrium in which the war has left the British balance of payments will inevitably persist, although on a diminishing scale, for several years. Sales of overseas investments and increases in foreign debt have reduced net investment income receipts by about 50 per cent, compared with the 1936-38 annual average. Reductions in net shipping earnings may be anticipated for several years as a result of a net wartime decline of about 25 per cent in British shipping tonnage. Earnings from insurance and other financial services are also likely to be smaller. Moreover, continuing large overseas military expenditures may be expected for another year or two, in view of the time required to bring British troops home. Above all, imports will tend to be much larger than before the war because of the need for reconstruction and repair of war-damaged factories and homes, reequipment and replacement of peacetime plant (which was seriously undermaintained during the war), replenishment of depleted inventories, and expansion and modernization of the prewar plant generally. Import prices will also be considerably higher than before the war, probably by at least 50 per cent.

In order to offset this disequilibrium in its current balance of payments and also to pay off its external debts over a period of years, the United Kingdom will have to increase the volume of its exports, according to official estimates, to about 175 per cent of the 1938 level. For several years, however, no such increase is possible, despite active foreign demand. For one thing, since British exports had to be sacrificed during the war, and declined in volume by 70 per cent between 1938 and 1944, it will inevitably take time, even from a purely technical point of view, for the United Kingdom to switch over again to a full exporting basis. More important, however, its available domestic resources will be relatively scarce over the next few years in the face of pressing internal requirements, and, despite continued rationing and priorities, the amount that can be released for export purposes will of necessity be limited.

The United Kingdom will therefore face an unavoidably large deficit on current account during the transition period when it is reconverting and restoring its industries to peacetime production and struggling to expand its export trade. It is officially estimated that this deficit, even on the assumption of continuing close control over expenditures abroad, will aggregate about 1,250 million pounds in 1946-48, of which 750 million will be incurred in 1946 alone. The British anticipate more modest deficits in 1949 and 1950, and expect that exports will have risen sufficiently by 1951 to wipe out the deficit. Over the 6-year period to 1951 the aggregate deficit may thus be estimated at about 1,500 million pounds (of which probably between 35 and 40 per cent will be incurred vis-a-vis the United States). The exchange requirements of the United Kingdom will be further increased to the extent that it is found necessary to pay off some portion of the existing external debts during this period.

Available British resources are insufficient to meet these requirements. Net official gold and dollar holdings had declined by October 1945 to 453 million pounds, of which a part must necessarily be held as a minimum working balance. Little reliance can be placed upon further sales of overseas investments, since the most marketable ones have already been disposed of. Any additional sales, moreover, would further increase the British balance of payments deficit by reducing interest and dividend receipts. Finally, the maximum amount of net aid that the United Kingdom might obtain from the International Monetary Fund would be limited to the amount of its quota, or 325 million pounds.

It is clear, then, that if the British are to be enabled to finance overseas expenditures in the volume necessary to carry them safely through the transition period, resort will have to be had to substantial borrowings abroad. The British deficit vis-a-vis Canada is likely to be met by means of Canadian credits. Credits might also be expected for another year or two from sterling area and other countries in the form of continued foreign accumulations of sterling balances. In general, however, the external financing problem of the United Kingdom over the next five years is primarily one of obtaining dollars needed to meet the deficit with the United States, as well as with other countries to the extent that they are unwilling to accept further sterling.

If the proposed American credit to the United Kingdom is not forthcoming, that country will inevitably be forced to reduce its expenditures on American goods and services in keeping with the limited amount of dollars at its disposal, thereby retarding necessary domestic reconstruction, restoration of exports, and alleviation of its austere wartime standard of living. Instead, the United Kingdom would have to try as far as possible to obtain needed imports from the sterling area, and other countries closely allied to it economically, by tightening the financial and trading links with these countries, by continuing and even intensifying its restrictive external wartime controls and arrangements, and by pursuing bilateral arrangements designed to exploit its strong bargaining position as an importer. The United States would find its exports increasingly discriminated against in foreign markets or even excluded in some cases. The world as a whole would tend to drift into State-directed, bilateral, and discriminatory trade and exchange practices, organized on bloc lines, thereby contributing to economic warfare and political instability. The Bretton Woods organizations, now about to be set up, would have no place within such a framework. The British authorities have already announced, in fact, that they would have to withdraw from these organizations if the credit agreement fails to pass Congress.

The proposed American line of credit of 3,750 million dollars is specifically designed to meet the minimum net dollar requirements of the United Kingdom and thereby to assist that country over its difficult transition period without the need for recourse to restrictive external controls and policies. The size of the credit has been so adjusted that, in conjunction with its other external resources, the United Kingdom will be enabled to finance its over-all dollar shortage during this period, including the dollars needed in connection with certain of the commitments imposed upon that country under the terms of the agreement. These commitments, which will remove wartime arrangements which have operated in a restrictive and discriminatory fashion against American and other non-sterling area countries' exports, include: (1) the restoration of free convertibility into dollars or other currencies of sterling obtained through current transactions by sterling area countries; (2) the removal of exchange controls with regard to current transactions with the United States; (3) the removal of restrictions on payments or transfers for current international transactions in general; (4) the abolition of the so-called dollar pool (i.e., permitting sterling area countries to dispose freely of any dollars they acquire); and (5) free convertibility of some part of the accumulated sterling balances now held by sterling area countries. Except for (2) and (5), which are to become operative from the effective date of the agreement and at an "early" date, respectively, these commitments are to come into operation no later than one year from the effective date of the agreement. These commitments may be expected to improve considerably the prospects for the foreign trade of the United States, not only with the United Kingdom, but also with many other countries.

The United Kingdom will also be committed to the completion at an early date of arrangements to settle its huge accumulated external debts. These arrangements (in addition to making part of the debts freely convertible into dollars or other currencies at once) are to involve a scaling down in the principal of the debts and the repayment of the remainder in freely convertible currency over a period of years beginning in 1951. Furthermore, the United Kingdom agrees not to use quantitative import restrictions in such a way as to discriminate against imports from any country. Above all, the British authorities have agreed to support the American proposals for an International Trade Organization at the forthcoming International Conference on Trade and Employment. These proposals look forward, among other things, to international cooperation in the reduction of tariffs, elimination of preferential duties, limitations upon the use of quantitative import restrictions and export subsidies, establishment of equality of treatment in international trade, curbing of restrictive business practices, supervision of inter-governmental commodity agreements, and the achievement of high levels of employment and income.

By enabling the United Kingdom to speed the restoration of its industries and the recovery of its export trade, and by calling for the early dismantling of its discriminatory external controls, the Anglo-American agreement constitutes an essential condition for the reestablishment of multilateral, nondiscriminatory policies in international trade, a high over-all level of American exports, and an expansion of international trade in general. These wider international benefits will result from the strategic position of the United Kingdom in the world economy and of the pound sterling in the network of international settlements, and from the traditional role of that country as the world's largest importer (and our greatest single customer). Unless, therefore, there is a rehabilitation of Britain's external finances (to which the American credit will make an important contribution), there can be no hope of a removal of restrictive and discriminatory practices which interfere seriously with international trade, are obstacles to the achievement of international economic well-being, and even threaten the maintenance of world peace.

While the agreement will enable the United Kingdom to permit free convertibility of sterling at an early date and to remove discriminatory exchange and trade arrangements, there can, of course, be no absolute assurance that that country will be able to continue such policies into the more distant future and gradually to remove quantitative import restrictions and State-directed trading. The crucial problem is whether British exports of goods and services will have risen by the end of 1951 (when repayments on the proposed American credit and other external debts will commence) to a level sufficient to enable the United Kingdom to finance debt repayments as well as current overseas expenditures (which will continue at a high level) within the multilateral framework envisaged in the agreement. For, clearly, the United Kingdom could not countenance foreign borrowing indefinitely.

The ability of the United Kingdom to expand its exports to the required level by 1951 and to maintain them at a high and reasonably stable level thereafter will depend essentially upon deliberate action by that country, as well as upon a favorable international economic environment in general.

From the specifically British side, export expansion will depend, for one thing, upon the ability of British producers to adapt the character of their exports to the changing requirements of the world market resulting from industrialization of other countries and technological change. For example, since former leading exports such as coal and cotton textiles will probably continue their prewar declines, increasing attention will have to be directed to machinery, vehicles, and other capital goods, and to higher grade consumers' goods which require unusual skill in their production. It will also be necessary for the United Kingdom to modernize and expand its capital plant and to raise its over-all national productivity in order to improve its competitive position in world markets.

External conditions will also be of great importance, since a large expansion of British exports will require a high level of foreign demand. This will depend upon the maintenance of high levels of national income, notably in the United States, as well as upon the removal of barriers to international trade.

MEETINGS OF THE BRETTON WOODS INSTITUTIONS

On March 8 the first meetings of the Boards of Governors of the International Monetary Fund and of the International Bank for Reconstruction and Development will be held at Wilmington Island, near Savannah, Georgia, for the purpose of organizing the two institutions. In keeping with the provisions of the Articles of Agreement, the meetings have been called by the United States in its capacity as the member having the largest quota in the Fund and the largest number of shares in the Bank. In attendance will be the governors of each institution appointed by each of the 35 charter members of the Fund and of the 34 charter members of the Bank. (Colombia has officially adhered to the Fund, but not to the Bank.) The American governor of both institutions is Secretary of the Treasury Fred M. Vinson.

Countries which attended the United Nations Monetary and Financial Conference at Bretton Woods, New Hampshire, in July 1944, but did not sign the Articles of Agreement by December 31, 1945, have been invited to send observers to the meetings. These countries (whose quotas and subscriptions aggregate somewhat less than 20 per cent of the total quotas and subscriptions of the Fund and the Bank, respectively), include: the Soviet Union, Australia, New Zealand, Venezuela, Panama, Nicaragua, El Salvador, Haiti, and Liberia. Observers have also been invited from Denmark, which may become a member, according to the Articles of Agreement, when a Fund quota and a Bank subscription have been officially assigned to it.

Although few details have been released concerning the nature of the agenda, it may be presumed that the two meetings will be concerned primarily with drawing up by-laws and other organizational details.

Each of the five members having the largest quotas in the Fund and the largest number of shares in the Bank is entitled to appoint an executive director of each institution. At the present time the "Big Five" of each institution consist of the United States, Great Britain, China, France, and India (the latter country being included because of the failure of the Soviet Union to ratify the agreements before December 31, 1945). The remaining directors must be elected, and these elections are likely to take place at the forthcoming meetings. In the case of the Fund, two directors are to be elected by the Latin American countries and five by the other members (excluding the "Big Five"). In the case of the Bank, seven directors will be elected by members other than the "Big Five." Once the executive directorates are constituted, they are to choose the managing director of the Fund and the president of the Bank.

It is probable that the two meetings will also discuss the terms and conditions on which new members will be admitted to the Fund and the Bank, including countries which attended the Bretton Woods conference but which did not sign the Articles of Agreement by December 31, 1945, and countries which did not attend that conference. The size of the quota and subscription for Denmark and the admission of that country to the Fund and the Bank may be decided, and any applications for membership which may have been made will presumably be considered at the meetings.

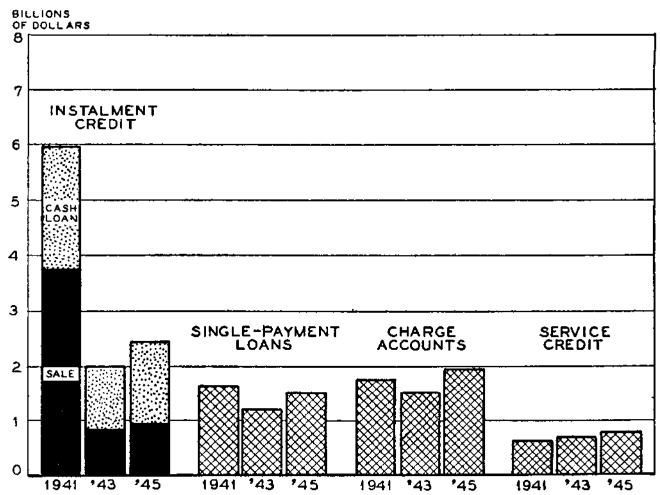
The location of the head offices of the Fund and the Bank may also be decided upon. The Articles of Agreement specify that the head office of each institution shall be established in the United States. According to newspaper reports, Washington and New York are the two cities most actively being considered.

While the date on which the two institutions will commence active operations is not known, it is generally believed that the Fund and the Bank should be functioning within about six months.

CONSUMER CREDIT IN 1945

The total amount of consumer credit outstanding increased approximately 800 million dollars between the end of 1944 and 1945, or nearly twice as much as in the preceding year, according to the latest estimates of the Board of Governors of the Federal Reserve System. The total outstanding at the end of December, 6.6 billion dollars, was, nevertheless, still nearly a third under the 1941 peak. Resumption of the manufacture of limited amounts of consumers' durable goods and further price increases were among the more important factors tending to enlarge the demands for consumer accommodation, although with the large backlog of wartime savings many individuals who formerly might have borrowed or purchased durable goods on the instalment plan now are in a position to pay cash.

Consumer Credit by Principal Types
(Estimated amount outstanding at end of year*)



* December 31, 1945 preliminary.

Most of the increase in consumer credit was in the volume of instalment and single-payment loans, particularly those extended by the commercial banks. In addition, instalment cash loans of small loan companies were up a little over 50 million dollars, and there were also smaller increases in loans made by credit unions and in the instalment credits of automobile dealers, furniture, department, jewelry, and other retail stores. Instalment accounts of household appliance stores showed no net change over the year. Automobile paper, however, which is ordinarily the largest single type of instalment paper, and outstanding credits of household appliance companies were only small fractions of their prewar volume. Department stores, furniture stores, and other retail outlets were not affected to the same extent by wartime production restrictions, but even their instalment sales at the end of December were more than 50 per cent below 1941 levels. Before the war instalment credit was the most important type of consumer credit, usually accounting for 50 to 60 per cent of the total amount outstanding, and an expansion in total consumer credit to anything like prewar levels will probably be dependent upon expansion of this type of credit, once consumers' durables again become available in quantity.

Charge account sales also rose substantially during 1945, and at the end of December accounts payable were estimated to be approximately 9 per cent above the end of 1941. This modest expansion in charge account credit, however, reflects the tremendous increase in the volume of retail store sales and the general rise in the price level rather than a growth in the proportion of charge account to total sales. For the last two years roughly 30 per cent of total department store sales have been charge account transactions, while before the war this figure was usually closer to 45 per cent. Credit arising out of the services of doctors, hospitals, cleaning and laundry establishments, and other service organizations continued its steady rise during the past year. Service expenditures have risen considerably with higher levels of income, but the increase in service credit outstanding has been comparatively small.

Consumer Instalment Loans of Commercial Banks

Consumer instalment loans of commercial banks expanded somewhat more rapidly during 1945 than those made by any other type of financing institutions in the consumer credit field, and at the end of December they represented a little over 11 per cent of the total amount of consumer credit outstanding. In large measure this above average increase was the result of a conscious effort on the part of many banks to expand their activities in this field. The initial results of this policy can be seen in the fact that while before the war the larger part of the banks' retail automobile paper was purchased from dealers or other financing agencies, most of the increase in bank holdings of automotive paper today represents direct loans made by banks to consumers for the purchase of automobiles. Bank holdings of purchased automobile paper have shown little net change since 1943, while direct loans rose nearly 50 million dollars between the end of 1944 and 1945, accounting for nearly a third of the total increase in the consumer instalment paper of the commercial banks in this period. Personal instalment cash loans also accounted for a substantial part of the rise in this type of bank credit during the past year, and repair and modernization loans showed a net increase for the first time since 1940, reflecting both the easing of building restrictions following the end of hostilities and the tremendous demand for housing.

Percentage Change in Consumer Instalment Credit Outstanding of Commercial Banks in 1944 and 1945

Type of credit	Dec. 31, 1943 to Dec. 31, 1944		Dec. 31, 1944 to Dec. 31, 1945†	
	All commercial banks*	37 banks in Second District	All commercial banks*	37 banks in Second District
Retail instalment credit	+13r	+ 8	+33	+15
Automobile	+15	+24	+35	+73
Other	+10	+ 6	+29	+ 8
Repair and modernization loans	− 7	−18r	+46	+74
Personal instalment cash loans	+11r	+ 2r	+22	+22
Total	+ 9r	− 1r	+30	+27

* Estimated by Board of Governors of the Federal Reserve System.
† December 31, 1945 preliminary.
r Revised.

In the Second District, reports from 37 member banks indicate that the largest dollar increases in their consumer loans in 1945 were in personal instalment and repair and modernization loans. Automobile loans, as the accompanying table shows, increased very sharply percentagewise during the year, but at the end of December they represented only about 5 per cent of the total outstanding amount of consumer instalment credits of this group of banks. For the past several years, however, banks in the District have not held as large a proportion of automobile paper in their consumer instalment loan portfolios as banks in other sections of the country.

WARTIME CHANGES IN FURNITURE STORE TRADE

Noticeable improvement in furniture store sales in this District began in the fourth quarter of 1945, but the dollar volume of sales for the full year was still slightly below that of the peak year 1941, whereas in all other districts combined, furniture store sales were above 1941. Furniture production was curtailed sharply in 1942 and retail stores in this District reported a decline in sales volume of 12 per cent from the preceding year's peak. Only slight declines were registered in the two following years. During the first nine months of 1945 sales increased 7 per cent over the corresponding 1944 period, and a gain of 20 per cent in the fourth quarter raised the increase for the full year to 12 per cent. Among the five principal cities of the District, percentage comparisons with 1944 and 1941 sales were as follows:

City	1945 compared with	
	1944	1941
New York City	+10	+ 2
Newark	+23	−17
Buffalo	+10	− 4
Rochester	+18	+ 6
Syracuse	+15	−15

Furniture is sold predominantly on the instalment basis, but the proportion sold for cash has been increasing during the past four years. In 1941 Second District stores sold approximately 12 per cent on a cash basis. This proportion increased to 17 per cent in 1942, and by 1945 cash sales accounted for almost one quarter of the total.

With the advent of Regulation W, accounts receivable of the furniture stores declined sharply. Receivables have shown little change during the past year, and they are currently 50 per cent below the 1941 high. The collection ratio (collections, exclusive of down payments, as a percentage of first-of-the-month receivables) has increased from 10 per cent in 1941 to 16 per cent in 1945.

At the close of last year stocks on hand in the furniture stores of this District were 11 per cent higher than at the close of the preceding year, but 35 per cent below the 1942 peak.

DEPARTMENT STORE TRADE

Retail merchants in this District are marketing an unprecedented dollar volume of merchandise, and they are planning for a still larger consumer demand during the coming months. Using department store reports as a barometer of trade activity, sales in February were again more than 25 per cent above those of a year earlier, and the seasonally adjusted index exceeded last March's peak by about 10 per cent. This index is now more than double the 1935-39 average.

Variations in the departmental buying trends are becoming more pronounced. During the war years department stores depended on the high dollar volume of women's wear sales, and they supported peak operating activity by promoting these lines to the fullest extent. With the shift to a peacetime economy, the most important factor in the further rise in sales is the pent-up demand for homefurnishings and men's wear. The outlook for the coming months is based on the anticipated market for this type of merchandise.

At the present time sales in the men's wear group are being hampered by the shortage of suits and coats. The men's furnishing departments report exceptionally large gains in spite of the inadequate supply of shirts. Within the homefurnishings group, many items are moving into stock rapidly, and the increased sales are not being supported out of inventory. Exceptionally large increases are being reported for housewares, and stocks are well above the year earlier level. In the furniture department the supply is becoming more adequate to meet the demand, and sales are considerably higher than last year. In the coming months the ready market for major household appliances and radios will contribute to a high sales volume for this group.

Sales of women's wear as a whole continue to maintain a substantial increase over last year's record volume, although wide variations appear within the departments. Fur sales continue below last year's level, although stocks are adequate. Hosiery and lingerie sales show declines because of the merchandise shortages. The shoe department has been reporting better-than-average sales gains, although stocks are relatively low. Ready-to-wear sales and stocks show increases about equal to the total store average.

Anticipating a high level of sales during the coming months, department stores in this District at the close of January had a record dollar volume of outstanding orders on their books. During the past year these orders have increased 15 per cent and are now about three times the amount outstanding at the beginning of 1943. The dollar volume of stocks at the close of January was also at a record high for that date, 8 per cent above the January 31, 1945 level and 5 per cent higher than on the corresponding 1943 date. Since the close of September, however, the ratio of stocks to sales has declined. Currently the dollar volume of stocks is only two thirds of outstanding orders, as compared with twice the orders at the beginning of 1943.

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

Locality	Net sales		Stocks on hand Jan. 31, 1946
	Jan. 1946	Jan. through Dec. 1945	
Department stores, Second District....	+26	+13	+ 8
New York City	+25	+14	+ 7
Northern New Jersey	+27	+13	+16
Newark	+26	+14	+12
Westchester and Fairfield Counties	+15	+ 8	+14
Bridgeport	+ 9	+ 4	+14
Lower Hudson River Valley	+32	+14	+10
Poughkeepsie	+31	+14	+ 5
Upper Hudson River Valley	+34	+15	+11
Albany	+60	+23	+16
Schenectady	+ 9	+ 8	+ 5
Central New York State	+31	+11	— 3
Mohawk River Valley	+17	+ 5	0
Utica	+12	+ 4	+ 6
Syracuse	+38	+14	— 7
Northern New York State	+46	+17	—
Southern New York State	+22	+13	+ 7
Binghamton	+26	+15	+ 4
Elmira	+15	+ 9	+10
Western New York State	+27	+ 9	+ 6
Buffalo	+32	+ 8	+10
Niagara Falls	+ 6	+ 8	— 2
Rochester	+21	+12	0
Apparel stores (chiefly New York City)	+23	+21	0

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

Item	1945			1946
	Jan.	Nov.	Dec.	Jan.
Sales (average daily), unadjusted	123r	235	307	155
Sales (average daily), seasonally adjusted	149r	182	181	187
Stocks, unadjusted	133	173	136	144
Stocks, seasonally adjusted	150	152	150	162

r Revised.

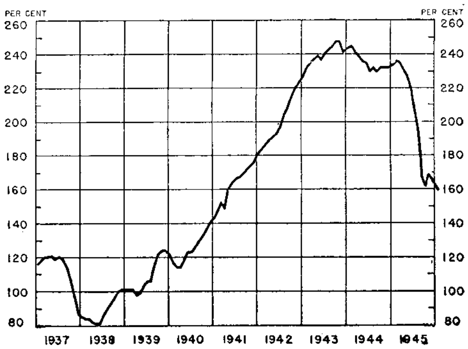
Indexes of Business

Index	1945			1946
	Jan.	Nov.	Dec.	Jan.
Industrial production*, 1935-39 = 100 (*Board of Governors, Federal Reserve System*)	234	168	164	159p
Electric power output*, 1935-39 = 100 (*Federal Reserve Bank of New York*)	206	187	187	187p
Ton-miles of railway freight*, 1935-39 = 100 (*Federal Reserve Bank of New York*)	212	179	182p	
Sales of all retail stores*, 1935-39 = 100 (*Department of Commerce*)	193	216	211p	
Factory employment				
United States, 1939 = 100 (*Bureau of Labor Statistics*)	163	122	122	122p
New York State, 1935-39 = 100 (*New York State Dept. of Labor*)	144	117	118	119p
Factory payrolls				
United States, 1939 = 100 (*Bureau of Labor Statistics*)	335	213	216p	
New York State, 1935-39 = 100 (*New York State Dept. of Labor*)	290	220	224	227p
Income payments*, 1935-39 = 100 (*Department of Commerce*)	242	236	234p	
Wage rates, 1926 = 100 (*Federal Reserve Bank of New York*)	169	168	168p	
Consumers' prices, 1935-39 = 100 (*Bureau of Labor Statistics*)	127	129	130p	
Velocity of demand deposits*, 1935-39 = 100 (*Federal Reserve Bank of New York*)				
New York City	94	82	99	101
Outside New York City	78	73	84	79

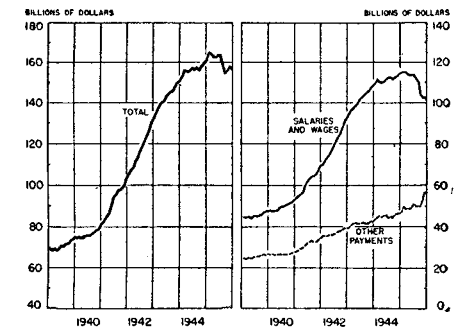
* Adjusted for seasonal variation. p Preliminary.

FEDERAL RESERVE BANK OF NEW YORK

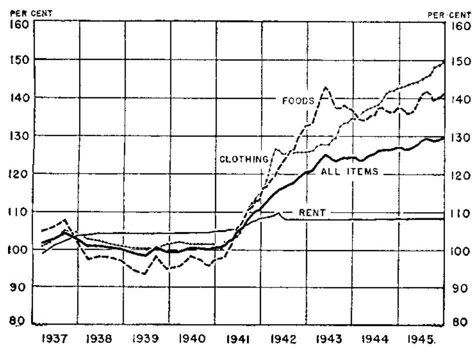
MONTHLY REVIEW, MARCH 1946



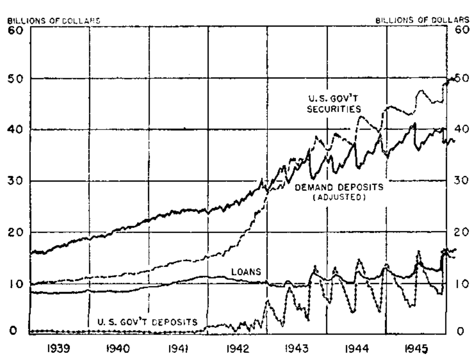
Index of Physical Volume of Industrial Production, Adjusted for Seasonal Variation (1935-39 average=100 per cent)



Income Payments to Individuals, Based on Department of Commerce Estimates. Wages and Salaries Include Military Pay. Monthly Figures Raised to Annual Rates



Indexes of the Cost of Living as Compiled by Bureau of Labor Statistics. Last Month in Each Calendar Quarter through September 1940, Monthly Thereafter (1935-39 average=100 per cent)



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 February 20)

General Business and Financial Conditions

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

OUTPUT at factories declined further in January and the early part of February owing to work stoppages. Production and employment in most nonmanufacturing lines, however, continued to advance and the value of retail trade was maintained considerably above last year's level.

Industrial Production

Wage disputes sharply reduced output in the iron and steel and electrical machinery industries during January and the early part of February. These decreases were offset in part by increased output in most other manufacturing lines and in mining. The Board's index of total industrial production was at a level of 159 per cent of the 1935-39 average in January, as compared with 164 in December.

Steel mill operations, which averaged 83 per cent of capacity in the first three weeks of January, dropped to around 6 per cent during the succeeding four weeks. Since settlement of the wage dispute in the steel industry, output has recovered sharply and during the last week of February operations were scheduled at 59 per cent of capacity.

Activity in machinery industries declined about 5 per cent in January, mainly because of work stoppages in plants of leading electrical equipment producers after January 15. Output of most other types of machinery continued to increase. Activity in the automobile industry rose in January, even though plants of the leading producer remained closed by a labor-management dispute. About twice as many automobiles and trucks were assembled in January as in December. Passenger car assemblies were at an annual rate of 700,000 cars which, however, was only about one fifth of the 1941 rate.

Lumber production rose considerably in January and there were substantial increases in output of most other building materials from previous low levels. Production gains were also recorded in January at textile and paper mills, at printing and publishing establishments, and in the furniture, tobacco, chemical, and rubber products industries.

Output of minerals rose 5 per cent in January, reflecting large increases in output of anthracite and bituminous coal and a small gain in production of crude petroleum. Coal production in January and the first part of February was at a rate about 8 per cent above a year ago.

Employment

Employment at trade establishments in January showed a much smaller decline than is usual after the Christmas season and employment in most other industries continued to advance. Construction employment in January was double the level in the same month last year, and, following large increases since last autumn, employment in the trade, finance, service, and miscellaneous industries was substantially larger than a year ago. Employment at factories was about one-fifth lower than at the beginning of 1945 as reductions in munitions employment were only partly offset by increases in other employment. Unemployment rose somewhat further by the middle of January to a level of 2,300,000 persons.

Distribution

Value of department store sales in January was 15 per cent above last year and in the first half of February the increase was larger. Retail sales at stores selling furniture, building materials, and other durable goods were from 25 to 40 per cent above a year ago in January and the total value of retail trade since the first of the year has been about one-fifth higher than during the same period last year.

Railroad freight traffic was reduced from the middle of January to the middle of February owing mainly to the work stoppage in the steel industry. Shipments of agricultural commodities, coal, and general merchandise, however, remained at high levels.

Commodity Prices

Federal price policies were modified in the middle of February to permit increases in ceilings made necessary by Federally approved wage-rate advances and sellers now may ask for immediate price relief rather than waiting six months. Accompanying this action steel prices were raised by 8 to 9 per cent. Ceiling prices for a number of other manufactured products, including certain foods, cotton goods, paper, and lumber, have also been increased in recent weeks.

Bank Credit

Treasury deposits increased by more than one billion dollars in the five weeks ended February 20, reflecting large Treasury tax receipts, reduced expenditures, and sales of savings bonds and tax savings notes in excess of securities redeemed. Deposits, other than Government and interbank, showed little change during this period, in contrast to developments in former post-drive periods when funds were shifted rapidly from Treasury balances to accounts of businesses and individuals. Bank loans made for purchasing and carrying Government securities were further reduced, while commercial, industrial, and agricultural loans continued to increase.

Banks continued to increase their holdings of Government securities, purchasing bonds in the market and Treasury certificates from the Federal Reserve Banks. Nonreporting banks drew upon their balances with city correspondents to increase their loans and investments. City banks met this and other drains in part by selling bills to the Reserve Banks.