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MONEY MARKET IN OCTOBER

During October the money and Government security markets continued to reflect the repercussions of the increase in member bank legal reserve requirements, which had become effective in September, and the reactions of investors to intensive and extensive discussion of the support being given the Government security market by the Federal Reserve System. Funds supplied by net Federal Reserve purchases of securities from nonbank investors and by member bank sales of their own Treasury bonds enabled the banks to increase their holdings of short-term Government securities and thus to achieve greater liquidity. The initial result of nonbank investors' transactions in Government obligations and of other transactions affecting member bank reserves was to ease reserve positions materially. The reserve funds thus made available were mopped up by a moderate reduction of Federal Reserve Bank discounts and by a decline in the holdings of short-term Government securities of the Federal Reserve System.

The immediate effect of the raising of legal reserve ratios of member banks in the second half of September had been a heavy liquidation of short-term Treasury securities, especially bills, although the member banks also disposed of moderate amounts of bank-eligible bonds. As a result, for certain banks, particularly those in the larger cities, liquidity—in terms of the proportion of short-term Treasury issues in their portfolios—had been reduced below levels they deemed desirable. In October these banks began to restore, in part at least, the former maturity distribution of their holdings. They acquired substantial amounts of Treasury bills, principally with funds obtained through the deposit, by nonbank investors, of the proceeds of sales of long-term Treasury bonds to the Federal Reserve System, and with funds supplied by country banks rebuilding their balances with city correspondents. These interbank deposits had been drawn down substantially during the period in which the country member banks were adjusting their reserves to the new legal requirements; they were restored in October with the proceeds of the sales of Treasury securities, mainly intermediate and long-term bank-eligible bonds and certificates, some of which, it appears, were taken by nonbank investors. To some extent, the

larger banks bought Treasury bills with funds raised through modest sales from their own bond holdings. Longest-term eligible bonds sold by commercial banks were absorbed principally by savings banks while the Federal Reserve System acquired many of the medium-term issues. In the three weeks ended October 20, Treasury bond portfolios of the weekly reporting member banks in 94 leading cities declined about 200 million dollars, combined certificate and note holdings declined 60 million dollars, and Treasury bills increased 1,115 million dollars (net).

Insurance companies and other institutional investors continued during October to sell long-term ineligible bonds on a large scale, most of these bonds being absorbed by the Federal Reserve System. This selling was related primarily to an increase during October in the volume of alternative investments available for institutional funds, notably new corporate and State and municipal security issues (offered both publicly and privately). However, part of the proceeds of these security issues were reinvested, at least temporarily, in Treasury obligations other than long-term ineligible bonds. The securities so purchased appear to have been acquired in part from country bank portfolios.

The large shifts of Government security holdings (both between types of securities and between classes of investors) that took place during the month did not result in any substantial change in the volume of Reserve credit outstanding; a modest decline in the aggregate volume of Federal Reserve credit in use was effected, as sales and cash redemptions of Treasury bills exceeded purchases of Government bonds by a narrow margin.

An active demand for Treasury bills and other short-term securities developed during the month, not only because member banks were liquidity-conscious, but also because of their easier reserve positions and because many investors sought to decrease the average maturity of their portfolios in order to avoid the consequences of rumored increases in short-term rates. In addition to their purchases of Treasury bills, commercial banks and others were active buyers of the shortest-dated Treasury certificates and notes (those maturing January 1, 1949), and sellers of the longest-dated certifi-

cate issues. A corresponding shift occurred in the Federal Reserve portfolio; longer certificates rose and holdings of the shortest maturities declined.

These and earlier developments reflect the effects of small increases in short-term interest rates, uncertainty as to the future course of such rates, increases in legal reserve ratios, and other measures taken by the Federal Reserve System in cooperation with the Treasury—measures which have succeeded in containing within narrow limits the expansion of bank reserves resulting from a variety of factors, including Reserve System support of the Government bond market.

Actually, despite Federal Reserve Bank purchases of about 10 billion dollars of long-term Treasury issues (net) between November 12, 1947 (when large-scale Federal Reserve purchases of such issues began) and October 27, 1948, total Government security holdings of the System increased only 1.2 billion dollars in this period. (Member banks also obtained reserve funds from a 1.6 billion dollar inflow of gold and a 600 million dollar decrease in currency in circulation.) The explanation of the difference in these figures, of course, lies in the fact that Reserve Bank sales and redemptions of short-term securities, mainly Treasury bills, offset much the larger part of their total bond purchases. (Changes in Federal Reserve System holdings of bonds and other types of Government securities from November 12, 1947 are shown in the accompanying chart.) The experience during the month of October has been generally similar to that of the entire period of about 11½ months. The reserves created during October by System purchases of long-term bonds, from institutional and other nonbank investors, were to a considerable extent eliminated as a result of sales and redemptions of System-held Treasury bills and other short-term obligations.

In addition, it must be remembered that the net increase in Federal Reserve security portfolios during the 11½-month

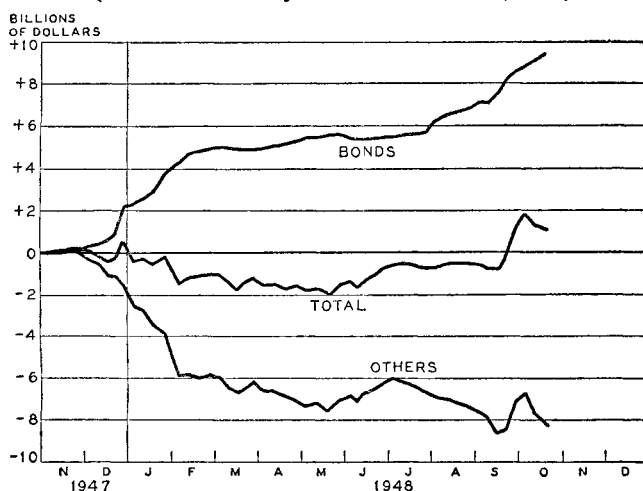
period did not constitute an increase in reserves available for a multiple expansion of bank credit. Legal reserve requirements of the member banks were raised, in three separate instances, by an aggregate of approximately 3 billion dollars, and member institutions sold a like amount of Government securities (chiefly short-term) to the Federal Reserve System to meet these increases. Apart from this rise in the System's security portfolio attributable to increases in legal reserve requirements of member banks, total Government security holdings of the Reserve Banks have declined during the past year. During the same period demand deposits adjusted at the member banks have shown little change, and total loans and investments of these banks have declined moderately.

MEMBER BANK RESERVES

Member banks had no substantial net sources of funds during October other than those supplied as a result of nonbank investor net sales of Government securities to the Federal Reserve System. All other transactions affecting reserve positions tended largely to offset one another. However, this single source of added reserves was sufficiently large to enable the member banks to reduce their borrowings from the Reserve Banks and acquire substantial amounts of Treasury bills—both outstanding issues, principally from the Federal Reserve System, and new bills on subscription from the Treasury. As a result of the increased takings of new bills by the banks, part of the maturing issues, held principally by the Reserve System, was redeemed. The reduction in the member banks' use of Reserve credit was substantial and somewhat larger than their gains of funds, resulting in a small decrease in their excess reserves. The decline in total Reserve credit outstanding was much smaller, however, than the reduction in member banks' use of such credit, owing to the increase in the System's bond holdings.

There was considerable fluctuation in bank reserves during the first two weeks of the month, reflecting chiefly Government security operations of the New York City banks and also an uneven distribution of gains and losses of funds among banks in different parts of the country. Member banks were under some pressure during the week ended October 6 as a result of a sizable holiday demand for currency, a moderate decline in Federal Reserve "float," and a rise in required reserves, which were only partly offset by net Treasury disbursements and net expenditures out of foreign deposit accounts with the Reserve Banks, financed chiefly through sales of gold to the Treasury. The banks nevertheless bought substantial amounts of Treasury bills and reduced their debt to the Reserve Banks, drawing down their excess reserves in the process to 510 million dollars, the lowest level since last May. Most of this decrease occurred among the New York City banks. These institutions, like most other banks, gained substantial amounts of reserves early in the first week of October as a result of nonbank investor sales of Treasury bonds to the Federal Reserve System and redemptions of maturing Treas-

Changes in Government Security Holdings of the
Federal Reserve System*
(Cumulated weekly from November 12, 1947)



* Wednesday dates; latest figures are for October 20, 1948.

ury certificates and notes. Toward the end of the week, the New York City banks purchased large amounts of Treasury bills, incurring a substantial reserve deficiency.

Reversing the process in the following week (ended October 13), the New York City banks sold large amounts of Treasury bills and increased their borrowings, turning their deficiency of reserves into an excess. These sales and borrowings were made in part to meet pressure from a transfer of funds to other parts of the country and from Treasury net receipts, but mostly to balance average reserves against requirements. Thus, most of the 465 million dollar increase in excess reserves of all member banks in this week again reflected principally the change in the City banks' position.

The modest shift of funds out of New York City contributed to the easing of reserve positions of the banks in other parts of the country, along with substantially lower required reserves and moderate Treasury net expenditures. Even though in this second week the banks did not have the benefit of additions to reserves from the sales of bonds by non-bank investors to the Federal Reserve System (since those investors reinvested most of the proceeds in short-term Treasury issues), their gains of funds were moderately larger than their losses from other transactions, including a continued reduction in the "float" and a further increase in money in circulation. Nevertheless, the unevenness with which these gains and losses of funds affected different banking institutions was reflected in the fact that many banks outside New York City were compelled to increase their borrowings substantially and to sell moderate amounts of Treasury securities (mainly bonds), while others were able to build up their excess reserves.

In the last two weeks of the month, member bank reserve positions eased. Currency flowed back to the banks after the Columbus Day holiday, Federal Reserve "float" rose, and foreign governments continued to disburse funds on deposit with the Reserve Banks. The banks continued, in addition, to gain funds from Reserve System purchases of long-term restricted Government bonds, and they employed these and other gains of funds not only to meet their needs for reserves but also to reduce their borrowings and increase their Treasury bill holdings.

SECURITY MARKETS

During the past ten months, prices of stocks and bonds have fluctuated irregularly, with mixed trends in evidence toward the close of the period—stock prices rising and bond prices leveling off at almost the low points for the year. On the whole, bond values rose during the first six months of the year and fell subsequently. Rising bond prices during the earlier period were associated partly with the decision of the Treasury in May not to raise the rate on new issues of its short-term securities. The pressure on the bond market in subsequent months may be linked to anti-inflationary measures taken by

the Federal Reserve System and the Treasury, including the raising of the rate on new short-term Treasury issues, and to the renewed fear in some quarters that Federal Reserve support of long-term Treasury bonds at the "pegged" levels might be removed. Of course the continued heavy demand for investment funds in excess of savings has been the basic factor making for lower bond prices (higher yields) in the last four months, as in the last couple of years.

Stock prices also responded to monetary influences, but other factors, such as increased Government expenditures, tax reduction, and apprehension concerning the business outlook were more important. These various factors, however, worked in opposite directions, with the net result that a sizable part of the February-June advance in prices was canceled in the next three months. October witnessed a renewal of the advance as pessimism with regard to the business outlook was replaced by a more optimistic appraisal of near-term business prospects.

In spite of the generally higher level of interest rates and the uncertain course of stock prices, the volume of security flotations for new capital, particularly corporate securities, was considerably larger in the first ten months of this year than in the corresponding period a year ago. The usual summer let-down, and price weakness in the market for outstanding securities, brought about some contraction in the amount of new corporate and municipal issues floated during the third quarter, but in October a marked expansion in the volume of new offerings took place. If securities registered with the SEC or otherwise being readied for sale are offered to the public (or sold privately to large investors) according to schedule, a very sizable volume of new issues may be forthcoming in the remaining months of the year.

BOND MARKET

The first half of 1948 witnessed moderate recovery of bond prices. Large-scale selling of long-term Treasury bonds, primarily to the Federal Reserve System, ceased for a time toward the close of May and the Treasury bond market stabilized at levels above Federal Reserve support prices. In the third quarter, the special offering of Savings bonds to institutional investors, increases in reserve requirements of member banks, and the higher interest rates offered by the Treasury on new short-term security issues brought renewed liquidation of long-term Treasury bonds, and prices declined until they reached support levels for most issues in August, where they remained through October.

Prices of high and medium-grade corporate bonds and of municipal issues in general moved similarly to Treasury bond prices, recovering through early June, falling in the next two months, and leveling off in September and October. The movements of corporate and municipal bonds were, however, wider than those of Treasury bonds, since of course they did not benefit from any official support and their supply was increasing. Municipal bonds in turn were more volatile than corporate issues, for the proceeds of the sale of Government bonds to the

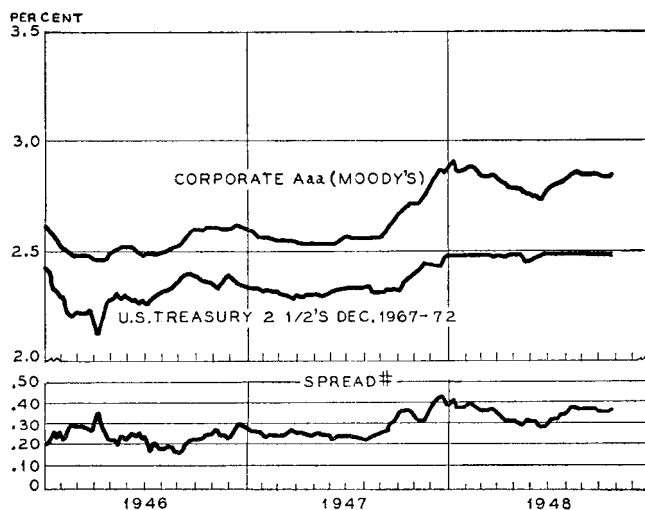
Federal Reserve System (particularly when the sellers were the insurance companies) were reinvested in corporate issues rather than in the lower-yielding municipal obligations. (Insurance companies and some other institutional investors derive no tax benefits from tax-exempt securities.)

Toward the close of October 1948, yields on long-term, taxable Treasury bonds were at levels corresponding to Federal Reserve support prices, yields on highest to medium-grade (Moody's averages of Aaa to Baa) corporate bonds were slightly below the peak reached early in the year, and municipal bond yields showed approximately the same decrease from the 1948 peak.

The period of rising interest rates since the spring of 1946 has been accompanied by a widening of the differential between corporate and Government bond yields, owing to the wider movements in corporate bond yields. Between August and December 1947, when bond yields rose most rapidly, the spread between the average yield on highest-grade long-term corporate issues and that on the longest-term Treasury bond, the 2½'s of December 1967-72, more than doubled. The subsequent decline in bond yields in the first six months of 1948 was accompanied by a shrinkage in this spread, which, however, increased again with the weakness that appeared in the bond market beginning in June. The differential remains substantially above the level that prevailed in 1946 and the first half of 1947, when interest rates were considerably lower.

This tendency of the spread between Government and corporate bonds to widen has had its counterpart in the corporate market in the form of increased spreads between high and medium-grade issues. After many years of narrowing differentials owing to the dearth of new, higher-yielding cor-

Yield on Highest-Grade Corporate Bonds Compared with the Yield on U. S. Treasury 2½'s of December 1967-72
(Weekly, 1946-October 22, 1948*)



* Figures for corporate bond yields are averages of daily figures for weeks ending Friday; Treasury bond yields are Friday figures. The 2½'s of December 1967-72 are ineligible for bank investment.

Difference in yield between corporate Aaa bonds (Moody's) and U. S. Treasury 2½'s of December 1967-72.

Source: Federal Reserve Bank of New York and Moody's Investors Service.

porate issues during the war, the market has begun to evaluate the credit factor in bonds more closely and to demand larger differentials for greater risks.

STOCK PRICES

In the past ten months stock prices have continued to move within a relatively narrow range. The favorable influences on prices of the reduction in Federal income tax rates, the increase in Governmental foreign aid, and the prospects of higher Federal defense expenditures were largely offset by the deflationary influences of increased international tension, further anti-inflationary moves of the monetary authorities, and renewed fears of a business recession. After falling off early in the year, prices rose 20 per cent between February and June and then receded 9 per cent between June and the close of September. A fresh advance in October carried prices 5 per cent above the level prevailing at the end of September to the highest levels since early August. The volume of trading increased during the February-June period of rising prices, reaching an average of almost 2 million shares a day during May. Turnover declined thereafter, reaching the million-share level in July and remaining below that average during most of the subsequent two months. The higher prices in October were accompanied by larger trading volume, which averaged slightly more than one million shares daily.

Although stock values, on the whole, as measured by Standard and Poor's broad index of the prices of 416 issues, showed only a nominal increase for the first ten months of the year, several of the industry groups showed substantial improvement. Among these, the most noteworthy were the railroad, aircraft, shipbuilding, electrical equipment, radio, steel, copper, lead and zinc, petroleum, coal, rayon, and brewery stocks. For the most part, shares of industry groups that were strongest during the February-June upswing were, with the exception of the petroleum stocks and a few other groups, among those showing the smallest decreases during the subsequent decline. With the exception of the railroad and rayon shares, furthermore, most of these groups led in the October upswing in prices along with the building material, distillery, shipping, and tire and rubber company shares, which had not been among the outstanding groups in the earlier advance. Steel share prices, which made relatively large gains during October, were also among the groups which did no better than average during the February-June upswing. The better-than-average showing of these groups reflects the particular situations governing specific industries, e.g., larger defense orders, the development of television, and heavy demand for steel, petroleum products, copper, and other nonferrous metals. Prices of only three groups, the petroleum, brewery, and coal stocks, were higher toward the close of October than at the postwar peak of the market as a whole.

Among the stock groups which showed net declines in prices in the first ten months of the year, fertilizer, agricultural machinery, drug and cosmetic, apparel, leather and shoe, soft drink, moving picture, and air transport company shares were weakest,

reflecting prospects for lower farm income in 1949 and lagging demand for nondurable goods and some of the service lines.

NEW ISSUES

The usual summer letdown in new financing and to a lesser extent unsettled conditions in the market for outstanding securities were responsible for a drop of about one fifth in average monthly corporate flotations for new capital purposes to about 400 million dollars (partly estimated) in the four months ended October 31, from 500 million in the first half of the year. However, the July-October total was moderately higher in 1948 than in 1947, and for the first ten months of 1948 corporate new capital flotations were 44 per cent higher than last year.

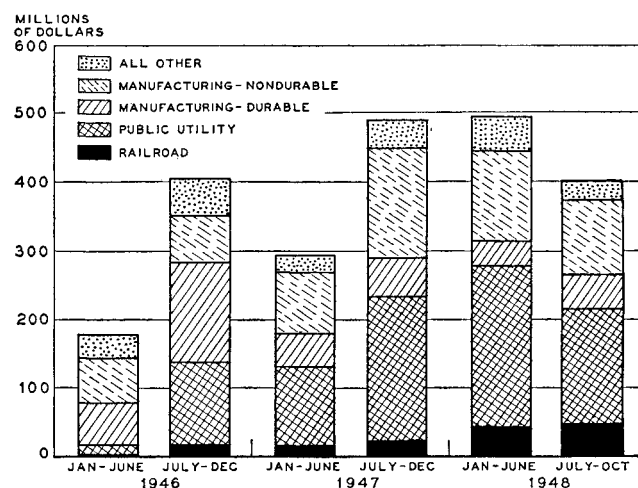
New bond issues during the past four months were generally well received by the market, despite the weakness of bond prices. New offerings were in most cases priced at levels affording higher yields than those on outstanding issues of comparable quality and maturity. However, as a result of the fall in bond prices, the market quotations of many new securities subsequently fell below the issue prices and this did tend to act as a deterrent to the public sale of new bonds. Private sales to insurance companies and other institutions, ungoverned by immediate price developments, remained large, representing about two fifths of all new corporate issues in the ten months ended with October.

The upward movement of stock prices from February to June and again in October failed to stimulate the flotation of common stocks; such issues were practically nominal in amount during July-October. However, there was a considerable spurt in preferred stock issues in the second quarter of the year. Stock issues averaged 20 per cent of all security issues in the first half of the year and fell to about 9 per cent of the total in the succeeding four months.

Despite a sharp drop in volume from the level of the first six months of 1948, utility issues during the next four months were still the most important class of new securities offered in the market and constituted 40 per cent of all new money security flotations. Within the utility group, the electric power corporations have become the most important seekers of capital funds, accounting for about half the utility financing in the first ten months of 1948. Telephone companies, which in the preceding two years had accounted for more than half the utility flotations, fell to 32 per cent this year.

Manufacturing (including mining) enterprises have floated about two fifths of the amounts issued since June 1948, as against one third in the first half of the year and 45 per cent in the entire year 1947. Although new financing by manufacturing companies has been declining since the record high offerings of the last quarter of 1947, the aggregate volume of manufacturing issues in the first ten months of the year was about 14 per cent larger than in the corresponding period a year ago. The petroleum, tobacco, machinery, transportation equipment (other than automobiles), and iron and steel in-

Corporate Security Flotations for New Capital by Industries
(Monthly averages for semiannual periods, 1946-48*)



* Last period shown covers the monthly average for only four months, July through October 1948; September and October 1948 estimated by the Federal Reserve Bank of New York.

Source: *Commercial and Financial Chronicle* data classified by industry by the Board of Governors of the Federal Reserve System.

industries have been the predominant issuers of securities in the manufacturing group in the current year to date.

Railroad security flotations for new capital have increased more than any other group in the first ten months of this year, rising by 150 per cent over the same period in 1947. The sharp increase in railroad financing reflects the greatly enlarged capital expansion program of the common carriers and the ability of rolling stock manufacturers to raise the level of their output substantially. According to the Bureau of Transport Economics of the ICC, the railroads' expenditure on new equipment this year is expected to amount to about 1 billion dollars, or two-thirds more than in 1947. Of this amount, approximately 45 per cent had been spent in the first six months of the year.

In the municipal new issue market, offerings in the four months ended October 31 of this year failed to keep pace with the volume of the first half of the year, largely because of the usual lack of activity during the summer. It is estimated that total offerings of State and local governments averaged about 170 million dollars a month during the last four months, a 20 per cent decline from average monthly offerings of 215 million dollars in the preceding three months, and slightly below the amount offered in the same period of 1947. Despite this decline, the total for the first ten months of the year (2.3 billion dollars) was about 275 million above the total for the corresponding period last year.

The record supply of new municipal issues has not been sold to the public without some difficulties. For the most part, higher rates have had to be offered by municipal governments in order to attract buyers, and there was bound to be some investor resistance to closely priced issues in view of the general trend of rising interest rates. Dealer inventories of unsold issues have been fairly heavy from time to time and have been

disposed of only at concessions from issue prices. Inventories had been substantially reduced by the end of September, although the general feeling among municipal dealers was that they should have been lighter in view of the dearth of new issues during that month. This feeling was substantiated by the difficulties encountered in disposing of part of the very large volume of offerings in October.

The supply of new State and local government bond issues not only grew substantially in October but is likely to grow further. Probably another billion dollars or so of new securities will be added to the backlog when voters make their decisions as to new capital projects and bonus payments at the polls in November. Disposing successfully of the large volume of issues that are likely to be offered will require planning and coordination between municipal bondmen and municipal finance officers to avoid congestion and prevent the development of temporarily oversold conditions in the market from time to time. More attractive yields may also have to be offered in order to attract certain institutional investors interested in high quality of issues rather than in tax exemption.

INTRA-EUROPEAN PAYMENTS PLAN

The Intra-European Payments Plan, proposed by the Organization for European Economic Cooperation and approved in principle by the Economic Cooperation Administration, has been formally adopted by the countries participating in the European Recovery Program, through the OEEC resolution of October 16. Operation of the plan is expected to remove part of the log jam that has increasingly clogged intra-European trade channels.

Before the war, trade among the countries participating in the ERP accounted for 51 per cent of their total exports and 38 per cent of their total imports, and therefore played an essential role in their economic life. When, at the end of the war, efforts were made to resume this trade, it had to be done largely on the basis of bilateral clearing agreements involving reciprocal credits. The bilateral trade pattern was familiar to many countries from prewar days and the reciprocal credit device helped to overcome the shortage of foreign exchange. Underlying the reciprocal credits was the assumption that the balance of trade would fluctuate seasonally, or in any case over short periods. Balances in excess of the agreed credit margins were usually to be paid off in gold. In view of the uncertain trade and supply conditions, the size of the credit margins usually had to be determined arbitrarily rather than on the basis of prospective trade currents and credit needs.

While in some instances the expected two-way swings in trade balances materialized, very often the reciprocal credits were utilized only in one direction and therefore tended to become permanent. Pronounced creditor and debtor relations developed, Belgium and Switzerland becoming the chief creditors, France a general debtor. The United Kingdom, which during 1947 and early 1948 was heavily in debt to

many ERP countries, found its position improving rapidly thereafter and is expected to run a large active balance with ERP countries generally during the year ending June 1949. A number of countries, without being large net debtors or creditors, had substantial debits and credits in their various bilateral positions.

As long as credit margins remained available, intra-European trade showed remarkable recovery. During 1947, however, the growing unwillingness of creditors to advance new credits, and the inability or unwillingness of debtors to pay in gold, together with the failure of sterling convertibility, made increasingly necessary the bilateral balancing of trade between each pair of trading countries. Trade in the aggregate began to shrink in terms of physical volume, as the deficit countries were forced to cut their purchases to the level of their sales; and the proportion of trade in nonessential goods grew as surplus countries sought means of converting their outstanding credits into imports.

From a balance of payments viewpoint, this impasse had two aspects. One was the net deficit of individual countries with the other ERP countries as a group, which the debtor countries could meet only by paying out dollars received from other sources. The second was the inconvertibility of European currencies, which prevented a country with equal bilateral deficits and surpluses from using the surpluses to offset the deficits.

The growing paralysis of intra-European trade was a serious threat to recovery. It became clear that European countries, unable to buy all they would like from the Western Hemisphere, must increasingly buy from each other. Furthermore, the most effective distribution and use of resources required that, for a while at least, some of the ERP countries be enabled to incur fairly sizable deficits with the rest of the group. This called for some means of financing the balances.

EARLIER APPROACHES TO THE PROBLEM

Various solutions were tried without success. Sterling convertibility, could it have been sustained, might have solved the problem of compensating bilateral debits and credits by providing a universally acceptable means of payment. Even so, the problem of financing net deficits would have remained. Sterling convertibility having failed, the problem was next attacked through the institution of a clearing scheme conducted by the Bank for International Settlements. This, too, did not produce major results, because the countries that became "permanent members" of the clearing (Belgium and Luxembourg, France, Italy, Netherlands, and the Bizone) did not find enough opportunities for clearing among themselves, while the "occasional members" usually found some motive for rejecting the clearing operations proposed to them by the BIS.

A third line of approach was implicit in the proposal of the Committee of European Economic Cooperation, in September 1947, for stabilization funds aggregating 3 billion

dollars which were to be added to the amount of Marshall Plan aid proposed by the committee. While the proposal was not elaborated in detail and was made primarily for purposes of internal stabilization in the countries to be aided, its effect on intra-European trade might have been to put that trade on a dollar standard. As long as the dollar remains a scarce currency, however, its use as an intra-European means of payment might easily have had restrictive effects. Countries might have endeavored to buy as little from each other as possible, in order to extract dollars from their trade partners that could be spent in the United States, unless the United States were prepared to continue putting up enormous amounts of dollars, or the ERP countries were willing to pursue severely deflationary policies which would mitigate the dollar shortage. From a long-run viewpoint, the universal use of the dollar in world trade would certainly be profitable to the United States, as the similar role of sterling was at one time for Britain. But while the dollar remains a scarce currency, its use as a universal means of payment would almost certainly prove restrictive, and to make dollars sufficiently available at this time to avoid such an outcome would require a disproportionate effort on the part of the United States, or almost impossibly severe deflation on the part of the participating countries.

It was soon realized, however, as the ERP progressed, that American aid could be used to unblock European trade and payments without a special dollar pool and without additional cost to the United States. Two methods, essentially variants of the same principle, were available, the "offshore purchase" method and the "local currency" method. The offshore purchase method, which owes its name to the offshore purchase provisions of the Economic Cooperation Act, consisted in giving intra-European debtors the dollars required to pay for their intra-European deficits. Under this method, which ECA used during the third quarter of 1948, special "supplemental" dollar allotments were made to the debtor countries to meet these deficits, in addition to the "basic" allotments which covered their Western Hemisphere deficits. The supplemental allotments were made on the basis of the bilateral deficits of the recipients with each of the other participating countries, estimated in advance, and were earmarked for expenditure in specific creditor countries. In making its basic allotments to the creditor countries, ECA in turn took into account the dollars they were scheduled to receive in payment of their prospective surpluses with other participating countries. In other words, intra-European debtors were allotted dollars equal to their Western Hemisphere deficits *plus* their intra-European deficits, while creditors were allotted dollars equal to their Western Hemisphere deficits *minus* their intra-European surpluses.

MAIN FEATURES OF THE PAYMENTS PLAN

It is, however, the local currency method which the OEEC has now, for a variety of reasons, decided to use as the basis

of the payments plan. Under this method, the dollars, instead of being given to the debtor as a supplemental allotment, are given directly to the creditor as a "conditional" allotment on the basis of bilateral balances between the ERP countries estimated in advance for one year. The condition for each such allotment is that the creditor must grant the debtor "drawing rights" in the creditor's own currency, equivalent to the conditional dollars received. The debtor then uses the drawing rights to meet his liabilities to the creditor. The aid thus given by ECA is referred to, from the debtor's viewpoint, as "indirect aid." The drawing rights are given on a "gross" basis. In other words, a country that has surpluses with some of its trading partners and deficits with others will grant drawing rights equal to the sum of the surpluses and receive rights equal to the sum of the deficits. This will greatly facilitate the offsetting of its debits against its credits. The creditor will finance the drawing rights he grants out of the "counterpart funds" that he deposits upon receipt of an ECA conditional allotment (or upon receipt of "indirect aid"). The setting up of the drawing rights, however, is not to be delayed until sufficient counterpart funds have been built up. Drawing rights and conditional dollar allotments are rather to be made available simultaneously, although the timing of their actual utilization may differ. If the utilization of conditional dollars and hence the building up of counterpart funds lags behind the utilization of the drawing rights, the creditor is expected to prefinance the drawing rights and later reimburse himself out of the counterpart funds. The debtor, upon using the drawing rights, is to establish a counterpart fund in his own currency, just as if he had received a direct grant from ECA.

In addition to the drawing rights, funds to cover intra-European deficits are being made available through the release of existing balances. These are mostly sterling balances, aggregating the equivalent of 209 million dollars, which the United Kingdom will release for financing that part of its surplus with the Continental countries that is not covered by drawing rights. It should be noted that the United Kingdom surplus includes that of the entire sterling area.

Both the drawing rights and the existing balances will be used, not for direct payments to creditors, but via a clearing mechanism that is to be an extension of the present BIS clearing. All ERP countries will participate in this clearing, Switzerland and Portugal entering it on a special footing. The balances that accumulate in the payments-agreements accounts as a result of current trade will be cleared monthly. With some qualifications, only currently arising balances will enter into this clearing, old balances being consolidated, except those which are released for the purpose of covering deficits. At the outset the clearing will be limited to situations where, with the aid of the drawing rights, closed chains of indebtedness can be established in which each country in the chain holds the currency of the preceding country while its currency in turn is held

by the following country ("first order clearing"). In such a chain, all debits and credits, if they are equal, can be wiped out and no new debtor-creditor relationship arises. Clearings in which new credit relationships would arise ("second order clearing") may be proposed by the agent (the BIS) but can be vetoed by countries that feel themselves adversely affected. It is planned to broaden the scope of the clearing and reduce the veto right later on. For the time being, however, the clearing aspect seems likely to play only a minor role within the payments plan.

The essence of the payments plan, in simplest terms, is to make ERP dollars do double duty: once to move goods within Europe, and again to move goods to Europe from overseas. At the same time, the plan effectively implements the "net aid" concept, which is the most rational criterion of the need of each country for foreign aid. The magnitude of the net aid that is required depends, not only on the country's Western Hemisphere deficit, but also on its intra-European deficit or surplus, i. e., on the net deficit in its over-all balance of payments, disregarding possible balances with other nonparticipating countries. A country that has an intra-European deficit on top of its Western Hemisphere deficit needs aid to cover both. A country with an intra-European surplus, on the other hand, can use this surplus to reduce its dollar aid requirements, provided the surplus can be converted into dollars. This is what the payments plan does. The "conditional allotment" of dollars, though it has the appearance of a grant, is no gift at all. It is payment for goods that the surplus country is to deliver to its debtors. All that the conditional allotment does for the creditor—and it is still a good deal—is to make the surplus convertible into dollars so it can be used to cover part of the Western Hemisphere deficit. The debtor country receiving "indirect aid" is the main beneficiary of the operation. Likewise, of course, the drawing rights granted by the creditors are not gifts, but simply export surpluses for which the creditors receive dollars. This is not to deny that some of the ERP countries may be making a very valuable contribution to the recovery of their fellow-participants. But this depends primarily, not upon whether they are intra-European creditors or debtors, but upon the amount of net aid that they demand relative to a fair appraisal of their needs.

TRANSFERABILITY OF DRAWING RIGHTS

To ensure the effective working of the payments plan, an element of flexibility has been added through the limited transferability of drawing rights. The transfer of drawing rights means that the obligation of the creditor who originally granted the rights is assumed by some other creditor, which implies that the conditional dollar allotment on which the rights are based is taken from the original creditor and given to the new one. Without this device, the plan might easily create intolerable rigidities, and might also fail to protect the legitimate needs of the debtors. As to the danger of rigidity, it is to be noted

that the advance estimates of trade balances on which drawing rights and conditional allotments are based cover a one-year period. The original estimates presented by debtors and creditors, respectively, for the year ending June 1949 differed remarkably, and their reconciliation by OEEC necessarily must have been based upon estimates of a type subject to a high margin of error. A really effective clearing mechanism would give relief from rigidity if sufficient reciprocal credit margins or existing balances were available, but there is no information to indicate that they will be. Thus, the plan would put trade into a strait-jacket which would be none the less irksome because it was multilateral. This danger has been overcome, to some extent, by making the drawing rights transferable.

The protection of debtors is another aim sought by injecting flexibility into the plan. The debtor countries have pointed out that their drawing rights will not be worth what they seem unless they are as effective as dollars in securing goods. They feared that if they were placed on a local-currency basis instead of on the dollar basis used under the offshore-purchase system, the creditor countries would gain a considerable bargaining advantage. Upon receiving the "conditional dollars" directly from ECA after setting up the drawing rights, the creditor countries, it was feared, might feel tempted to go slow on supplying desirable goods against the latter, through use of export licenses or by excessive price demands. To make sure that the drawing rights would be as effective as dollars in bargaining for goods, it has therefore been agreed that under certain conditions debtors should be allowed to seek some other creditor who would be willing to grant them drawing rights, on condition of course that the conditional dollar allotment be transferred from the original to the new creditor. The danger for the creditor of losing dollars is likely to make him willing to honor his drawing right obligations as if the debtor were in fact buying with dollars.

The transferability of drawing rights has the general effect of injecting an incentive to export into the payments plan because it offers countries an opportunity to earn extra dollars. Debtors too have this incentive, since (with the exception of Greece) even those countries that are debtors on balance have bilateral surpluses with some trade partners and therefore extend some drawing rights. Without transferability, incentives would be largely lacking.

There are various factors, however, that counsel moderation in the actual operation of the transfer of drawing rights. One is that very sizable changes in dollar allotments to creditors cannot be made without severely disturbing the planning of their imports and eventually the working of their entire economy. The total of ERP dollars relative to recovery needs is so limited that their allocation must be made with the utmost deliberation and cannot be left in any major degree to the free play of intra-European trade balances. A second point is that easy transferability of drawing rights, at the debtor's option,

Distribution of Drawing Rights, Existing Resources, and ERP Aid, July 1948—June 1949
(In millions of dollars)

Aid to be granted (+) or received (-) by (1)	Drawing rights to be received (+) or granted (-) by													Drawing rights and existing resources utilized					Position including United States aid			
	Austria (2)	Belgium (3)	Denmark (4)	France (5)	Greece (6)	Italy (7)	Netherlands (8)	Norway (9)	Sweden (10)	Turkey (11)	United Kingdom (12)	Bizone (13)	French Zone (14)	Gross drawing rights granted (15)	Gross drawing rights received (16)	Net drawing rights granted or received (15+16) (17)	Existing resources to be utilized* (18)	Total intra-European position (17+18) (19)	United States dollar allotments# (20)	Net aid (20-17) (21)	Net aid plus existing resources (21-18) (22)	
	Austria.....	..	- 4.5	- 0.1	- 2	+ 0.4	+ 2	- 1	- 1.5	+ 0.7	..	- 25	- 32	- 0.5	+ 3.1	- 66.6	- 63.5	..	- 63.5	217.0	280.5	280.5
Belgium**.....	+ 4.5	..	+ 6.5	+ 40	+ 13	- 11	+ 72.5	+ 23	+ 6	+ 2	+ 30	+ 17	+ 4	+ 218.5	- 11	+ 207.5	..	+ 207.5	250.0	42.5	42.5	
Denmark.....	+ 0.1	- 6.5	..	- 2.7	+ 2	..	..	..	+ 3	- 1.5	..	- 1	- 0.2	+ 5.1	- 11.9	- 6.8	..	- 6.8	110.0	116.8	116.8
France.....	+ 2	- 40	+ 2.7	..	+ 5	- 11	..	- 5	..	..	- 200	- 63	- 14	+ 9.7	- 333	- 323.3	+ 10	- 313.3	989.0	1,312.3	1,302.3
Greece.....	- 0.4	- 13	- 2	..	..	- 5	..	- 5	..	..	- 10	- 4	- 3	..	- 66.8	- 66.8	- 20	- 86.8	146.0	212.8	232.8
Italy.....	- 2	+ 11	..	+ 11	+ 7	..	..	+ 0.5	+ 0.1	+ 5	- 25	+ 10.1	+ 2.6	+ 47.3	- 27	+ 20.3	- 45	- 24.7	601.0	580.7	625.7
Netherlands.....	+ 1	- 72.5	..	..	+ 5	..	..	- 2	- 2	+ 0.8	..	- 8.5	+ 2	+ 11.3	- 83	- 71.7	- 65	- 136.7	496.0†	567.7‡	632.7‡
Norway.....	+ 1.5	- 23	..	+ 5	+ 2	- 0.5	- 2.5	..	- 21.8	- 0.5	..	..	..	+ 16.5	- 48.3	- 31.8	..	- 31.8	84.0	115.8	115.8
Sweden.....	- 0.7	- 6	- 3	..	+ 5	- 0.1	+ 2	+ 21.8	..	+ 1	..	+ 5	..	+ 34.8	- 9.8	+ 25	- 60.2‡	- 35.2	47.0	22.0	82.2	
Turkey.....	..	- 2	+ 1.5	..	+ 13	- 5	- 0.8	+ 0.5	- 1	+ 12	+ 1.5	- 28.5	- 8.8	+ 19.7	..	- 19	+ 0.7	50.0	30.3	49.3
United Kingdom.....	+ 25	- 30	..	+ 200	+ 10	+ 25	..	..	..	..	..	+ 46.5	+ 5.5	+ 312	- 30	+ 282	+ 209	+ 491	1,263.0	981.0	772.0
Bizone.....	+ 32	- 17	+ 1	+ 63	+ 4.3	- 10.1	+ 8.5	..	- 5	- 12	- 46.5	..	..	+ 108.8	- 98.6	+ 10.2	- 9.8	+ 0.4	414.0	403.8	413.6
French Zone.....	+ 0.5	- 4	+ 0.2	+ 14	+ 0.1	- 2.6	- 2	..	..	- 1.5	- 5.5	..	..	+ 14.8	- 15.6	- 0.8	..	- 0.8	100.0	100.8	100.8
Total.....	+ 63.5	- 207.5	+ 6.8	+ 323.3	+ 66.8	- 20.3	+ 71.7	+ 31.8	- 25	- 19.7	- 282	- 10.2	+ 0.8	+ 810.4	- 810.4	+ 564.7	+ 228.8	+ 699.6	4,875.0\$	4,875.0\$	4,875.0\$	

* Release of balances indicated by (+), right to their use by (-).

Including both conditional and unconditional allotments.

** Includes Luxembourg.

† Includes 84 million of United States aid for Netherlands East Indies.

‡ Net of 9.8 million in balances to be released, and 70 million in rights to balances that are to be utilized.

§ Includes United States aid to Eire, 79 million; to Iceland, 11 million; and to Trieste, 18 million.

Source: Columns 2 to 19 from *Records & Statistics*, Supplement to *The Economist*, Vol. IV, No. 92 (October 16, 1948), p. 352; columns 20 to 22 based on OEEC data.

would give the debtor free rein to "shop around" with dollars. This might have the same restrictive effects as dollar trading, already discussed. It might become a motive for cutting imports, particularly on the part of the creditor from whom drawing rights were being transferred. Finally, it seems clear that a creditor should not be penalized severely for having made too liberal estimates of his prospective surplus, if at the time that aid was being divided this liberality had earned him only moderate concessions in added dollars.

The issue of the transferability of drawing rights caused some delay in the final approval of the plan by OEEC, because of objections by the British. Britain and Belgium are the only countries that have scheduled substantial net surpluses. Britain, as appears in the table, has undertaken to supply a net surplus equivalent to 491 million dollars (of which 282 million is accounted for by net drawing rights, and 209 million by the release of existing sterling balances). A large part of the goods in question will come from the independent sterling area, which may cause Britain's indebtedness to that part of the sterling area to go up. This British undertaking was an important factor in getting the other countries to accept the distribution of aid proposed by OEEC, because it increased the amount of net aid available to them. The British themselves, however, have expressed some doubt as to their ability to meet this commitment. On the other hand, it is believed in some quarters that Belgium will have little trouble in meeting the commitment it has made of 207.5 million dollars, and could even increase its exports if it received payment in dollars. There is, consequently, a chance that drawing rights and conditional dollars may be transferred away from Britain. Belgium, on

the other hand, is the creditor most likely to gain from transferability, and has been a warm supporter of the device. The Belgian point of view has also appealed to the traditional American preference for multilateralism, with which concept transferability has come to be identified, although in the context of the payments plan it really should be looked upon as an element simply of flexibility.

A satisfactory compromise appears now to have been found under which a modification of drawing rights may be recommended by OEEC only in three cases: (1) *force majeure*; (2) proof by the debtor that despite every reasonable effort he is unable to use his rights against the original creditor; and (3) proof by the creditor that rights granted by him are no longer needed. In the last case, the drawing rights presumably would be canceled and the net aid to the creditor would go up correspondingly. In all other cases unused drawing rights are to remain in force after the end of the year for which they have been granted. Since decisions affecting drawing rights also affect the allotment of conditional dollars, they will in any case be subject to the approval of ECA.

USEFULNESS OF THE PLAN

The payments plan may be expected to produce a number of valuable results. It will probably increase the volume of trade and make this trade more effective because it will remove the compulsion to balance accounts bilaterally. Trade can now be made as multilateral as is desired, within reasonable limits. Nevertheless, one may doubt whether the plan offers a lasting solution to the problem of European payments. This is by no means a condemnation of the plan. It will perform an extremely valuable function by breaking the present

financial impasse in intra-European trade. Its contribution, in terms of additional goods moved, should be at least of the order of half a billion dollars, and indirectly perhaps much more. But the present limitations of the plan clearly mean that continued thought and work must be directed toward strengthening it, as well as toward the development of a more fundamental solution of the intra-European payments problem.

BUSINESS CONDITIONS IN THE SECOND FEDERAL RESERVE DISTRICT

Business activity in the Second Federal Reserve District continued at high levels during the first ten months of 1948. Many of the principal business indicators have shown increases over 1947, but in general such gains have been smaller than in the rest of the country. This represents a continuation of the tendency which has prevailed for the past two years. In the first year following the end of the war, the dominating influence in this District of the apparel and other nondurable goods industries minimized reconversion problems and helped to maintain relatively high levels of employment, production, and income to a greater extent than in the rest of the country. But once the initial postwar period of reconversion and labor difficulties had passed, the further gains in this District were relatively more moderate than elsewhere in the nation.

In appraising business conditions in a limited area, about the only detailed indicators that are promptly and readily available for nonagricultural activity are the statistics of employment in various industries. Factory employment, as estimated for the Second Federal Reserve District, showed a slight decline in the first nine months of 1948 compared with the same period last year, whereas in the country as a whole there was a gain of 3 per cent. However, other Second District nonagricultural industries, except construction, showed increases in employment that more than offset the reduction in factory employment, even though the gain was smaller than that for the same industries in the country as a whole.

In New York State¹ the year-to-year declines in factory employment appeared to be centered in the durable goods lines, reflecting in part a readjustment to more normal peacetime demand, such as the nondurable goods industries underwent in 1947. Employment in durable goods manufacturing in September 1948 was slightly below that for the same month in both 1947 and 1946. Machinery and electrical apparatus showed the greatest declines from last year, while the number of workers in shipyards and airplane factories, which dropped sharply between 1946 and 1947, has risen somewhat in recent months. Nondurable goods industries had about the same number of employees in September 1948 as in September 1947, although fewer than in September 1946. The number of workers in apparel firms in September was only slightly less than in Sep-

¹ Estimates of New York State employment are furnished by the Bureau of Research and Statistics, Division of Placement and Unemployment Insurance, New York State Department of Labor.

tember 1947 and about 6 per cent less than two years earlier. Food processing plants and textile mills have added workers, but there has been a decline in miscellaneous manufacturing.

The trends in factory employment in the various industrial areas of the Second District have largely reflected differences in types of manufacturing industries. The employment picture in New York City has been dominated in the past two years by the sharp seasonal fluctuations of the apparel industry, a pattern which had largely disappeared in the war and reconversion periods. From April through September of this year, New York City factory employment was lower each month than in the corresponding month of 1946 and 1947, and at the seasonal low point in July 1948 employment reached the lowest mark in eight years. The women's outerwear industry in the New York area reported that the value of shipments in the first half of 1948 was 9.5 per cent above the first half of 1947. Allowing for price changes, this indicates a well-sustained rate of production; in the rest of the country, however, shipments rose 16 per cent in the same period.

The New York City printing and publishing industry employed slightly fewer workers than a year earlier but somewhat more than in 1946, while employment in most metalworking concerns was below that in the corresponding period last year.

In Upstate New York, business conditions following reconversion proved to be more stable than in New York City, with factory employment in all areas well above prewar levels. During the spring and summer of 1948, however, there were declines in employment in the Elmira and Utica areas and to a lesser extent in Buffalo. Claimants for unemployment insurance in mid-September were fewer than on the corresponding 1947 date in the Albany, Binghamton, and Poughkeepsie regions (and also in New York City and the suburban areas), but were substantially more numerous in Elmira, Utica, Syracuse, Rochester, and Buffalo. In New Jersey, factory employment has been running above last year's figures, and, as in New York State, the gain has been largely in nondurable goods lines. In the Connecticut portion of the Second District, employment appears to have fallen below 1947 levels.

Besides manufacturing, the only other major industry group in the Second District to show a drop in activity has been construction. Employment in New York State construction firms during the first eight months of 1948 averaged 4 per cent below the year-earlier level, although in New Jersey there appeared to be some year-to-year gain. The country as a whole showed an average increase of over 8 per cent in construction employment during the same period. Likewise, both residential and nonresidential construction contracts awarded in the Second Federal Reserve District during the first three quarters of this year have shown smaller gains than those in the rest of the area (37 States) covered by the F. W. Dodge Corporation data.

These declines in manufacturing and construction employment have been more than offset by increases in the other nonagricultural industries. The trade and service industries in

particular have hired more workers, although here too the gains have generally been smaller than in the rest of the country. Wholesale and retail establishments in New York State increased their working forces by an average of 2½ per cent in the first eight months of 1948. Employment also increased in finance, insurance, and real estate firms, in Federal, State, and local government offices and establishments, and in communications and other public utilities. This last increase partly reflected an advance in electric power output of 7 per cent in New York State (compared with a national average of 10 per cent), which is in itself an important indicator of the increase in over-all business activity.

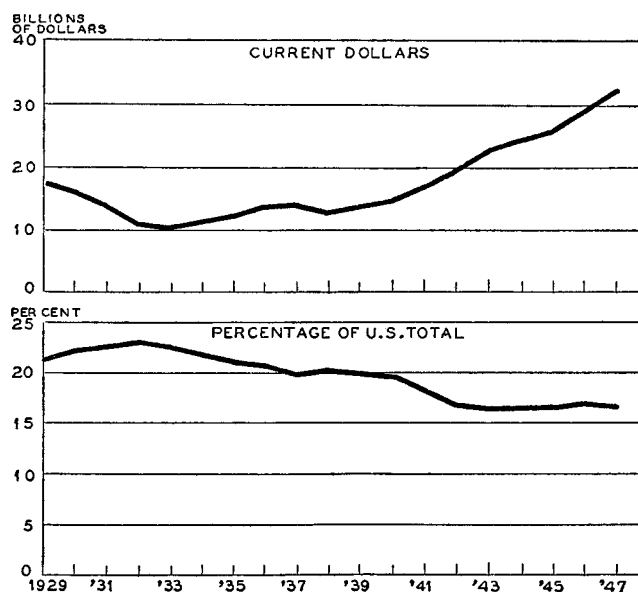
Cash receipts from farm marketings in New York State in January-August 1948 were 14 per cent above the same period in 1947, whereas for the country as a whole the average increase was only 6 per cent. Milk, poultry, and dairy products—the mainstay of this District's agriculture—continued to sell at high prices during 1948, while the price declines in grains and other crops which adversely affected farm incomes in other sections of the country were reflected here chiefly in the form of lower feed costs and higher net incomes.

The dollar volume of department store sales in the Second District in January-September 1948 was 6 per cent above the corresponding months of 1947, compared with 8 per cent for the country as a whole. Year-to-year increases in sales at all types of independent retail stores in New York City and Northern New Jersey during the first eight months of 1948 were on the whole smaller than the nation-wide average of 8 per cent, but in Upstate New York the gains were generally larger than the national gain.

One of the best and most comprehensive indicators of the economic activity in a region is the amount of income which is produced there and which is received by its inhabitants in the form of wages, profits, and property income. The trends in a region's income payments reflect its growth compared with the rest of the nation, the relative well-being of its population, and its position as a market, both for its own products and those of other regions. Estimates of income payments in the Second Federal Reserve District, based on U. S. Department of Commerce data by States, are shown in the accompanying chart for the period 1929-47.

It is undeniably true, as the chart indicates, that the Second District accounted for a smaller proportion of the national total in 1947 than it did in 1929 or in the prewar years, but this movement cannot be attributed to a decline in activity within this District. In fact, there has been a very sizable and steady increase in the dollar volume of income payments in this District since 1938. The relative increases in income have been much greater in other areas of the nation, it is true, but in almost every case these advances have occurred in newer and less developed areas. It would be well-nigh impossible for a highly industrialized and heavily populated region like the Second

Income Payments in the Second Federal Reserve District: Current Dollars and Percentage of the United States Total



Source: Computed by Federal Reserve Bank of New York from U. S. Department of Commerce data.

District to match the rate of expansion which the South, the Southwest, or the Pacific Coast States have been experiencing since the beginning of the war.

In a larger sense, the chart depicts the relative stability of the Second Federal Reserve District's economy. There is a distinct inverse relationship between the level of income and the Second District's share of the national total. When the dollar volume of income payments declined between 1929 and 1932 and between 1937 and 1938, the percentage received in the Second District rose, because the cut in dollar payments in other sections of the country was much sharper. Conversely, the rate of increase in this District has ordinarily been exceeded elsewhere, resulting in a decline in the Second District's portion. The reason for this area's relative stability of income, of course, lies in the industrial composition of the area. Manufacture of consumers' nondurable goods plays an extremely large part in the Second District economy, whereas areas where the durable goods industries predominate are subject to much wider cyclical swings, both upwards and downwards. Large portions of this area's industry were not readily adaptable to output of military goods during the war, and consequently industrial expansion took place to a much larger extent elsewhere.

Agriculture is much less important in this District than in any other Federal Reserve District, accounting for less than 2 per cent of income payments in 1947, compared with a nation-wide average of 10 per cent and between 25 and 60 per cent in 10 States. Thus, the abrupt changes in output because of crop failures and the extreme cyclical fluctuations

in farm prices have little effect on this area's income. The fact that this District has been relatively little affected by the post-war farm prosperity has depressed its share of total income payments during the past few years, but by the same token this area was relatively better off during the long years of depressed farm prices. A further stabilizing factor has been the much larger proportion of property income in total income payments in this District than in the rest of the country.

DEPARTMENT STORE TRADE

During October, Second District department store sales expanded in line with seasonal expectations, according to preliminary estimates. Even though there was an additional shopping day last October, the year-to-year increase compares very favorably with that of recent months. On a daily average basis the gain was clearly the best in about a year. It should be noted, however, that during last October unusually warm weather had some adverse effect on sales. On the average, dollar sales during the first three quarters of 1948 have run

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

Locality	Net sales		Stocks on hand Sept. 30, 1948
	Sept. 1948	Jan. through Sept. 1948	
Department stores, Second District.	+ 6	+ 6	+12
New York City.	+ 4	+ 5	+10
Northern New Jersey.	+ 6	+ 6	+15
Newark.	+ 5	+ 5	+11
Westchester County.	- 1	+ 2	+ 9
Fairfield County.	+12	+ 2	+16
Bridgeport.	+12	+ 1	+14
Lower Hudson River Valley.	+ 5	+ 8	+18
Poughkeepsie.	+ 9	+11	+21
Upper Hudson River Valley.	+ 9	+ 9	+17
Albany.	+ 9	+ 8	+13
Schenectady.	+11	+10	+20
Central New York State.	+ 4	+ 6	+17
Mohawk River Valley.	+ 5	+ 8	+26
Utica.	+ 6	+ 8	+22
Syracuse.	+ 3	+ 5	+13
Northern New York State.	0	+14	-
Southern New York State.	+10	+11	+18
Binghamton.	+14	+13	+15
Elmira.	+ 4	+11	+39
Western New York State.	+12	+11	+12
Buffalo.	+14	+11	+ 5
Niagara Falls.	+18	+ 7	+19
Rochester.	+10	+11	+25
Apparel stores (chiefly New York City).	+ 1	0	+ 8

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

Item	1947	1948		
	Sept.	July	August	Sept.
Sales (average daily), unadjusted.	243r	181	187	257
Sales (average daily), seasonally adjusted.	238r	266	256	252
Stocks, unadjusted.	228r	215	242	256
Stocks, seasonally adjusted*.	216	242	242	243

r Revised.

* Seasonal adjustment factors for 1946-48 revised; available upon request from Research Department, Domestic Research Division.

about 6 per cent better than last year. Trade circles expect this gain to be maintained through the rest of 1948.

The accompanying table shows that the retail value of District stocks on September 30 was 12 per cent greater than a year previously, when they were particularly low. The increase partly represents a normal response of inventory to the year-to-year improvement of sales and perhaps some inadvertent accumulations, as in men's clothing. The table also shows that the largest relative increases in stocks took place in the smaller stores outside New York City. The most important characteristic in the movement of stocks during this year has been that month-to-month changes reflected little more than the usual seasonal influences.

Outstanding orders on the books of a group of the larger District stores at the end of September were fully one-fifth below the level of a year ago and thus showed a radically different change as compared with stocks. Likewise, new orders placed during September were considerably below last year's and failed to show the usual seasonal increase from August. The combination of a reduced volume of outstanding orders and an increase in sales resulted in a considerably lower ratio of outstanding orders to sales than for September 1947 (1.4 as against 1.8). This sharp retrenchment of order positions reflects increased caution on the part of department stores.

Indexes of Business

Index	1947	1948		
	Sept.	July	August	Sept.
Industrial production*, 1935-39 = 100. (Board of Governors, Federal Reserve System)	186	186	191	191p
Electric power output*, 1935-39 = 100. (Federal Reserve Bank of New York)	238	247	253	252p
Ton-miles of railway freight*, 1935-39 = 100. (Federal Reserve Bank of New York)	203	201	208p	
Sales of all retail stores*, 1935-39 = 100. (Department of Commerce)	318r	337	337	338p
Factory employment United States, 1939 = 100. (Bureau of Labor Statistics)	160	158	162	164p
New York State, 1935-39 = 100. (N. Y. S. Div. of Place. and Unemp. Ins.)	130	122	126	128p
Factory payrolls United States, 1939 = 100. (Bureau of Labor Statistics)	345	360	375p	
New York State, 1935-39 = 100. (N. Y. S. Div. of Place. and Unemp. Ins.)	288	284	297	306p
Personal income*, 1935-39 = 100. (Department of Commerce)	301	310	314p	
Composite index of wages and salaries*†, 1939 = 100. (Federal Reserve Bank of New York)	180r	191	193p	
Consumers' prices, 1935-39 = 100. (Bureau of Labor Statistics)	164	174	175	175
Velocity of demand deposits*, 1935-39 = 100 (Federal Reserve Bank of New York)				
New York City.	88	97	103	104
Outside New York City.	86	91	96	93

* Adjusted for seasonal variation.

p Preliminary.

r Revised.

† A monthly release showing the 15 component indexes of hourly and weekly earnings in nonagricultural industries computed by this bank will be sent upon request. Tabulations of the monthly indexes, 1938 to date, may also be procured from the Research Department, Domestic Research Division.

FEDERAL RESERVE BANK OF NEW YORK

MONTHLY REVIEW, NOVEMBER 1948

National Summary of Business Conditions

(Summarized by the Board of Governors of the Federal Reserve System, October 23, 1948)

INDUSTRIAL output and employment were maintained in September at August levels. Value of department store sales in September and the early part of October showed about the usual seasonal increase. Prices of foods declined from earlier record levels, while prices of most other commodities showed little change.

INDUSTRIAL PRODUCTION

The Board's seasonally adjusted index of industrial production was maintained in September at 191 per cent of the 1935-39 average. Manufacturing output showed a small gain, while minerals production declined 3 per cent.

Steel mill activity in September was at a rate of 96 per cent of capacity as compared with 93 per cent in August. Output of electric steel reached a new record level. In the third week of October total steel production was scheduled at a rate of 99 per cent of capacity. Activity at most metal fabricating plants showed little change in September. Automobile production was curtailed further but increased sharply in the last week of September, reflecting mainly settlement of strikes at suppliers' plants. Output of lumber and stone, clay and glass products declined somewhat in September.

Production of nondurable goods rose slightly in September and was at a level close to the June rate. Cotton consumption and production of paperboard and rubber products showed small further gains from the reduced summer levels. Food production was in larger volume in September, reflecting increased meat production and a recovery in canning operations from the sharply curtailed rate in August. Output of petroleum products was reduced somewhat in September mainly because of labor disputes at refineries in California.

Production of minerals declined in September, reflecting chiefly the reduced output of crude petroleum on the West Coast. In the early part of October petroleum output recovered to the August rate. Coal production declined somewhat in September and the first half of October and was below year-ago levels, reflecting some reduction in demand, mainly for export.

CONSTRUCTION

Contracts awarded for construction, reported by the F. W. Dodge Corporation, declined further in September reflecting mainly seasonal decreases in most types of awards. The number of new houses started, according to Department of Labor preliminary estimates, declined from 83,000 in August to 81,000 in September. Last year the number of new units started was 86,000 in August and 94,000 in September.

DISTRIBUTION

Value of department store sales in September and the early part of October was maintained close to the advanced level prevailing since last May, after allowance is made for the usual seasonal changes.

Railroad freight carloadings showed less than the usual seasonal rise in September and the early part of October, and shipments of most classes of freight during this period were in smaller volume than in the same period a year ago.

COMMODITY PRICES

The general level of wholesale commodity prices declined 3 per cent from the middle of September to the first week of October, reflecting chiefly sharp decreases in prices of livestock products. During the subsequent two weeks prices of these products increased somewhat. Spot prices for corn dropped sharply in September and the first three weeks of October and were moderately below the support level for the new crop. Wholesale prices of textiles, leather, lumber, and coal declined somewhat, while further marked advances were reported in prices of various metal products.

Retail food prices in mid-October were estimated to be about 5 per cent below the record high reached in July, while consumer prices of most other groups of items advanced somewhat further in this period.

BANK CREDIT

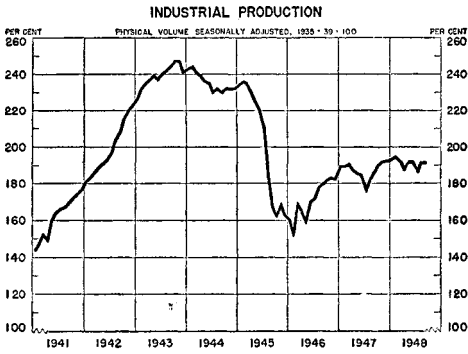
Required reserves of all member banks were increased by about 2 billion dollars in the latter part of September as a result of the action of the Board of Governors in increasing reserve requirements against net demand and time deposits. The increase in required reserves necessitated substantial sales of Government securities by banks to the Federal Reserve in the latter part of September, but the increase was about equal to the volume of reserve funds that had been supplied to banks in the period June through September by gold inflow and net sales of Government securities to the Federal Reserve Banks by nonbank investors.

Federal Reserve support purchases of long-term Government securities from insurance companies and other nonbank investors continued large during the first three weeks of October. Banks used the reserve funds supplied them by Federal Reserve transactions with nonbank investors to purchase short-term securities from the Reserve Banks. Total holdings of Government securities at the Reserve Banks declined somewhat.

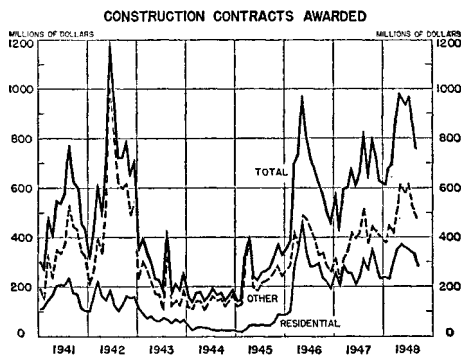
Business loans showed further rapid growth at banks in leading cities during September and the first half of October. Real estate and consumer loans also continued to rise. During the first half of October, banks in leading cities added somewhat to their holdings of Government securities, following reductions in late September to meet higher reserve requirements.

INTEREST RATES AND SECURITY MARKETS

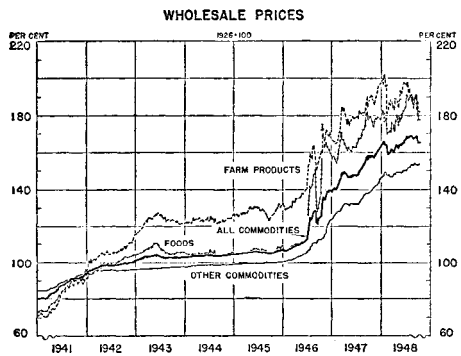
Yields on short-term Government securities rose slightly in late September and early October. Prices of high-grade corporate and municipal bonds were relatively stable during the first three weeks of October, and common stock prices rose somewhat, following moderate declines in September.



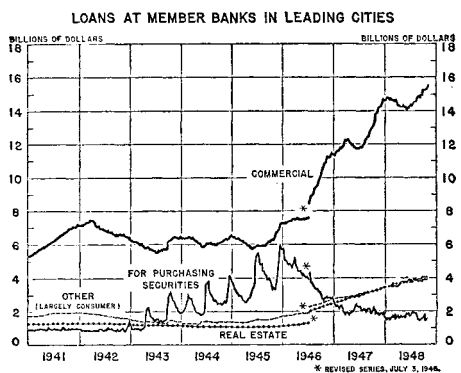
Federal Reserve index. Monthly figures; latest figure shown is for September.



F. W. Dodge Corporation data for 37 Eastern States. Other includes nonresidential buildings and public works and utilities. Monthly figures; latest shown are for September.



Bureau of Labor Statistics' indexes. Weekly figures; latest shown are for week ended October 16.



Excludes loans to banks. Wednesday figures; latest shown are for October 13.