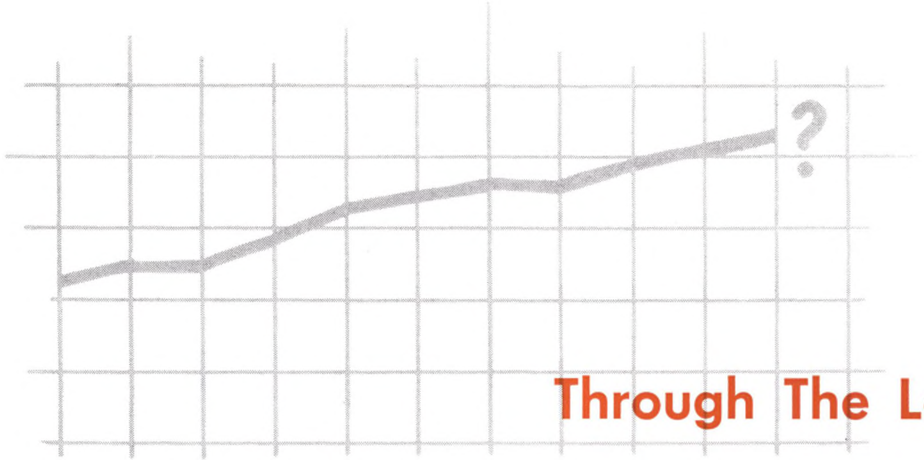
MONTHLY REVIEW

Missiles: Military symbol of economic strength

FEDERAL RESERVE BANK OF RICHMOND FEBRUARY 1958



Through The Looking Glass

Through the medium of their published forecasts, "interviews" have been held with 62 analysts in order to obtain a comprehensive view of expert opinion on the outlook for economic activity this year. The following article is a report on "the other fellow's" thinking; no views or opinions of this Bank are implied or expressed. In view of the wide range of opinions given and the opposing interpretations of current developments, it would appear that the universal motto of forecasters might be "Frequently wrong but never in doubt."

While there is definitely a majority opinion, holding that the current downturn will be of moderate proportions, the divergencies of views are more pronounced than they have been for some time. Standing together at the same point in time and circumstance, a number of leading economists find themselves poles apart in their forecasts.

There is also an unusually large amount of "iffiness" in this year's batch of forecasts, and the sheer weight of number in agreement is not particularly persuasive that the 1958 outlook is an open book.

MERELY A BREATHER? The majority opinion is that the present downturn will be a moderate one in both duration and intensity. The earlier forecasts of temperate decline, made in November and early December, generally referred to mid-1958 as the turning point. Since mid-December the approximate transition date has been advanced to Labor Day. After that date most of the economic indicators are expected to veer upward again to produce a moderate advance in aggregate business activity.

One of the terms used frequently to describe the nature of the downtrend forecast by the moderates is "breathing spell." It is explained that the economy is taking a breather while excessive inventories are worked down and until an expanded national security program begins to swell the income stream. It is generally assumed that expenditures for new plant and equipment are not likely to turn upward soon. However, the depressing influence of curtailed business investment will be countered by increasing government outlays—Federal, state, and local—gradually increasing consumer spending, and the cessation of inventory liquidation. Residential building is also seen on the plus side this year, but there does not seem to be too much strength of conviction on this point. Finally, many of those in the camp of the moderates feel that a check to the first-half decline and an assist to the second-half recovery will come from greater availability of funds and lower borrowing costs this year.

In brief, this group of forecasts—the majority group—finds the seeds for a second-half recovery in both major areas of the economy, private and public. Anti-recession programs of the Federal government will not have to turn the tide unassisted.

NO GUARANTY There are those, of course, who are not looking through such rose-colored glasses as are the moderates. This minority group does not subscribe to the opinion that sometime during the first six months of 1958 business will cease living off its stocks and switch to inventory accumulation. Its members point out that in the 1953-54 recession inventory liquidation was a protracted process, dragging on through four consecutive quarters before it was again necessary to step up production in order to build up inventories. With virtually nothing in short supply and with an easing demand in general, this very small group reasons, business is more likely than not to continue working down its inventories well beyond the mid-point of this year.

Nor does this group find strength in Federal spending to the extent that the moderates and optimists do. Undoubtedly, it is admitted, anti-recession programs initiated by the Federal government will do the trick—but not overnight. At least six months, maybe longer, will be required before business and personal incomes will begin to reflect significantly the gradual increase in Federal outlays.

One forecast in this group questions the economic efficacy of the expanding national security program. There is "little chance that we can get rid of burdensome inventories or find productive use for excess capacity by merely increasing government spending for things which we, as consumers, don't want and which we, as producers, can't pay for. We can't live on missiles!"

Estimates derived from government and business surveys of a 7% or slightly greater decline in expenditures on new plant and equipment are taken with a grain of salt by the pessimists. They point to the tremendous sums invested in production facilities in recent years and contend that industry in general has excess capacity. This they argue will take many more than just a few months to correct. The depressing influence of declining outlays for expansion and modernization of productive facilities will be neither short-lived nor moderate in severity.

THIS TIME? So arguing, the pessimists (They would choose the term "realists.") take issue with the opinion that present difficulties will be ironed out by mid-year or so and the stage set for the resumption of general economic expansion. They do not set a date themselves; the very nature of their forecast precludes a definite terminal date. Their fear is that this time the decline may develop the cumulative downward forces that in the past have produced the whirlpool of depression. Few go so far as to say they definitely expect the onslaught of a depression. Only one forecast has been noted—there may be others—that minces no words in projecting a continuous decline well beyond 1958. "Every postwar boom has been followed," this particular analyst points out, "by a major depression and there is no reason to think that this one will have a different ending."

Other forecasters in this group carry their arguments only to the brink of depression. They do not plunge into the abyss. They are convinced, however, that the economy this year will be subjected to "greater strains and stresses than anything experienced since World War II."

"FLATLY DISAGREE" "Balderdash" (or its economic equivalent)retorts another minority group;

The specter of unemployment, on the increase at the opening of 1958, holds no fears for most forecasters. In general, total consumer spending is seen as being well maintained or rising this year.

"the corrective forces are already at work, and 1958 will be another year of economic expansion." The optimist group, including those who forecast an upturn in the first quarter of this year or well before mid-year, is small in numbers but imposing in individual reputations. In the proverbial nutshell, this group views the downturn under way at the beginning of this year as merely "a sharp bump" on the road to further expansion.

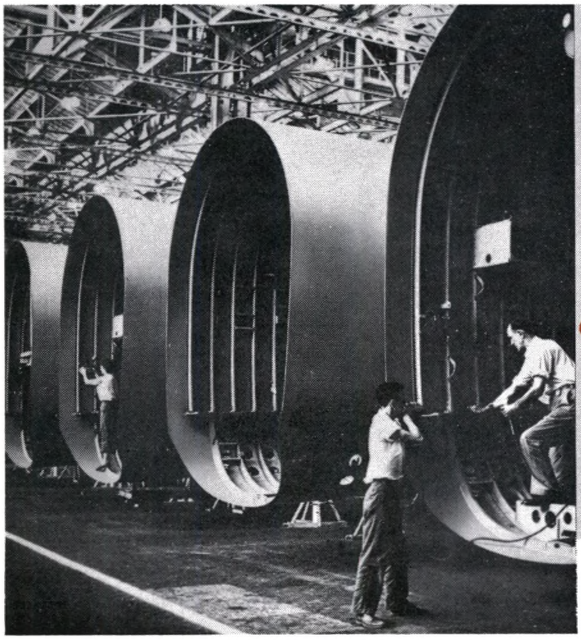
They "flatly disagree" with those who have forecast a recession this year. Their view is that the rate of recovery from the decline in the final quarter of 1957 will be slow during this Spring but will pick up speed in the final six months. The net result, according to their computations, will be a total production of goods and services during the year ranging in value from $440 billion to $450 billion.

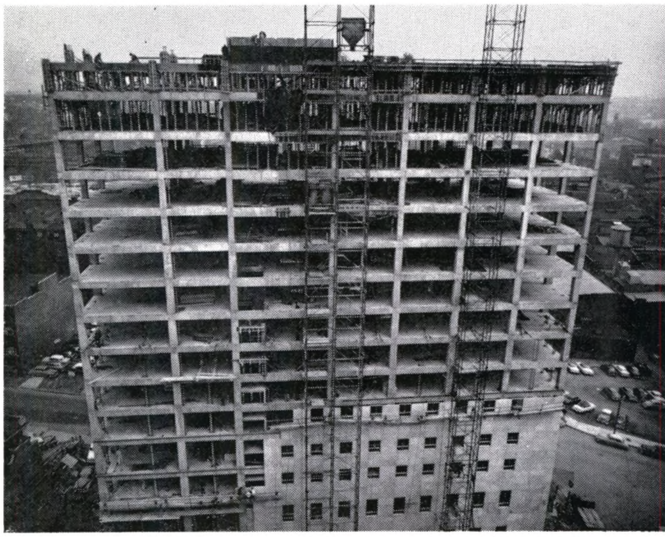
During the final months of last year business began reducing its spending for new plant and equipment. This and the reduction in Federal government outlays because of the earlier cutbacks in the defense program more than offset rises in other sectors of the economy. These developments, the optimists point out, had a sharp reaction in the inventory policy of business firms. Instead of accumulating inventories, business began to live off stocks on hand and effected a net reduction at an annual rate of $3 billion in the fourth quarter. This, it is added, was worse than it might seem since it followed an inventory build-up of $2 billion in the third quarter. Thus the over-all impact of changes in inventories amounted to $5 billion on an annual rate basis, quite a blow to the economic health of even as boom-prosperous a nation as ours.

However, some of the forecasters in this group feel that this has at least one favorable aspect—the severity of the inventory change in such a short time hastens the day when restocking of empty shelves will increase the volume of manufacturers' new orders. "In any case, the rate of inventory reduction can hardly get much worse, and in fact must moderate before long."

"THE MOST PROSPEROUS RECESSION" Aside from basic factors such as population increase, gain in family formation, and technological progress, the main reasons optimists find for forecasting further economic gains in 1958 lie in the areas of government spending and personal consumption spending. Some emphasize the former, implying that the new national security program is the latest recession stopper and recovery starter. Its impact for the first few months of the year will likely be felt mainly in the confidence created among businesses and labor by contract awards and placement of orders. When actual government payments reach full flood and swell the income stream, the upward trend of general business

As 1957 made room for 1958, the prospect for increased outlays for national security was seen as a factor of strength and auto sales appeared as one of the major disquieting forces in the outlook.






Most forecasts for 1958 look for strong crosscurrents in construction activity. Factory building is seen declining from year-earlier peaks while construction outlays of state and local governments are viewed as in a rising trend.

activity will be accelerated markedly. All the while, of course, expenditures by state and local governments will continue to expand and provide a sizable element of strength.

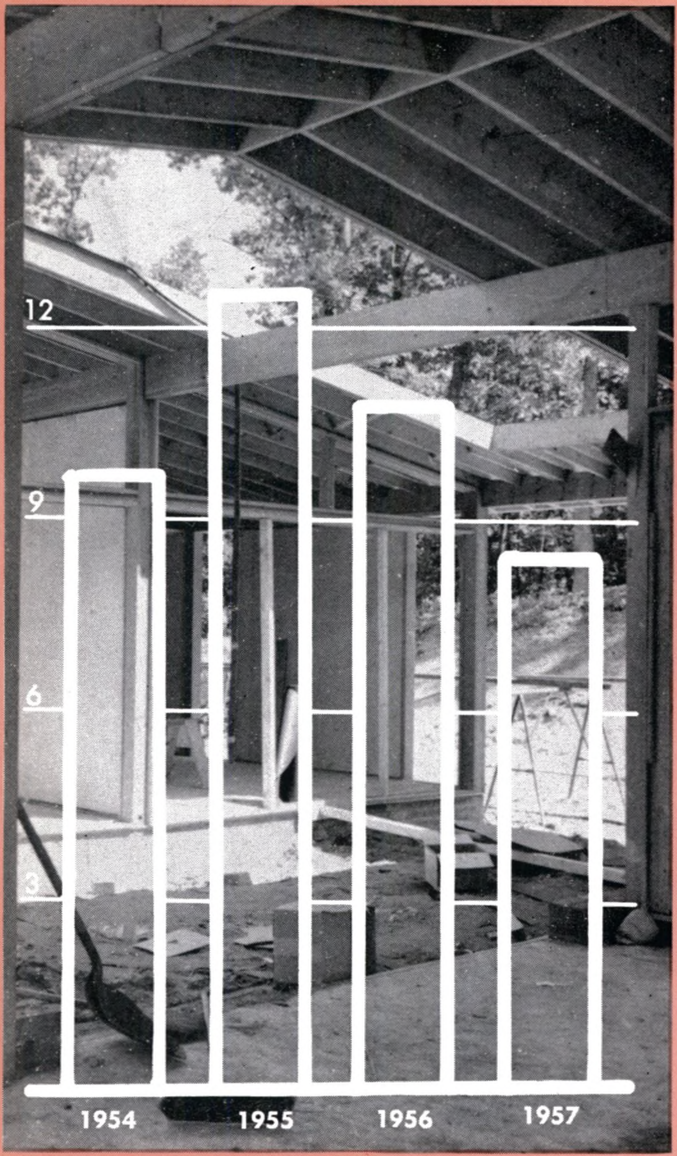
In the main, though, it is the consumer who is going to carry the ball. It is clear that the optimists are not resting their case solely or principally on expansion of government spending for defense and for anti-recession projects. They point out that personal income is at a very high level, only negligibly below last Summer's peak, and will rise to new record levels later this year. Consequently, there are sound, logical reasons for anticipating further growth of consumer spending this year.

In other words, the economy is fundamentally sound; the worst of the downturn may well be behind us, and there is no reason to assume that the private side of the economy needs to be bailed out by the government sector. This being the case, why look at 1958 as a recession year? In fact, if the term "recession" should be insisted upon, it needs to be added that "it is the most prosperous recession you can have without calling it prosperity."

A NEW WRINKLE The three groups referred to—pessimists, moderates, and optimists—shade into each other and overlap on many points. There are, of course, mutual points of agreement and disagreement all through the gamut of forecasts. One of the most notable common meeting grounds is in the field of monetary policy. Those who have commented on the part played by the monetary authorities have generally agreed that "appropriate" action will make a major contribution to recovery and resumption of the growth trend. Some forecasts emphasized this factor: "Easy money will play the key role in combating recession, just as tight money bore the brunt of the battle on inflation last year."

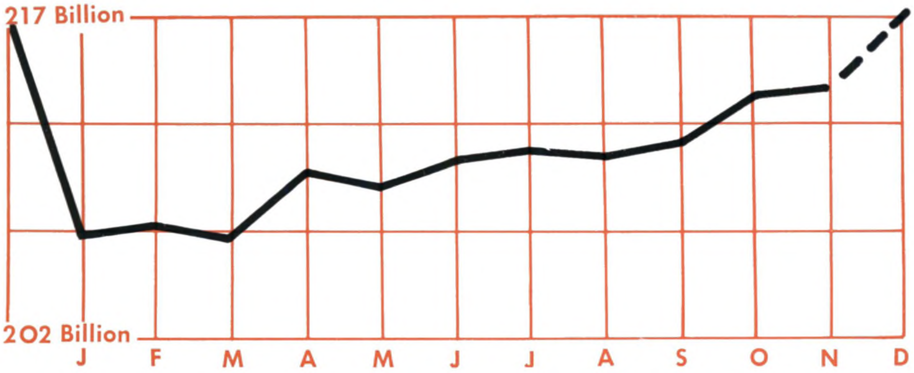
One of the more interesting possibilities advanced by some of the forecasters is that of a concurrent rise in prices and decline in business activity. This innovation in economic development could occur, it is explained, only if the zigging of prices and the zagging of activity were of very moderate proportions. The reasoning here is that the recent rise in prices was brought about mainly by the "push of rising costs." It is likely that many of the upward pressures on costs will not be modified during a mild recession and thus the "cost push" influence in maintaining or raising prices will continue.

This is one of the many interesting possible developments considered in the forecasts. In general, the coverage of principal factors and developments was quite complete, and the forecasts were logically drawn on the basis of the assumptions made.



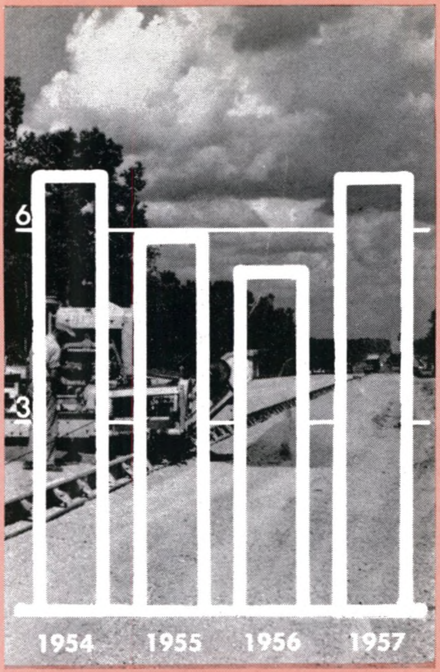
CREDIT IN A YEA

HOME BUYERS added $8½ billion to total mortgage indebtedness on 1- to 4-family houses in 1957. While this represents a substantial flow of money into the residential real estate markets during the year, it was nearly one-fourth less than in 1956 and a third below that experienced in the housing boom year 1955.



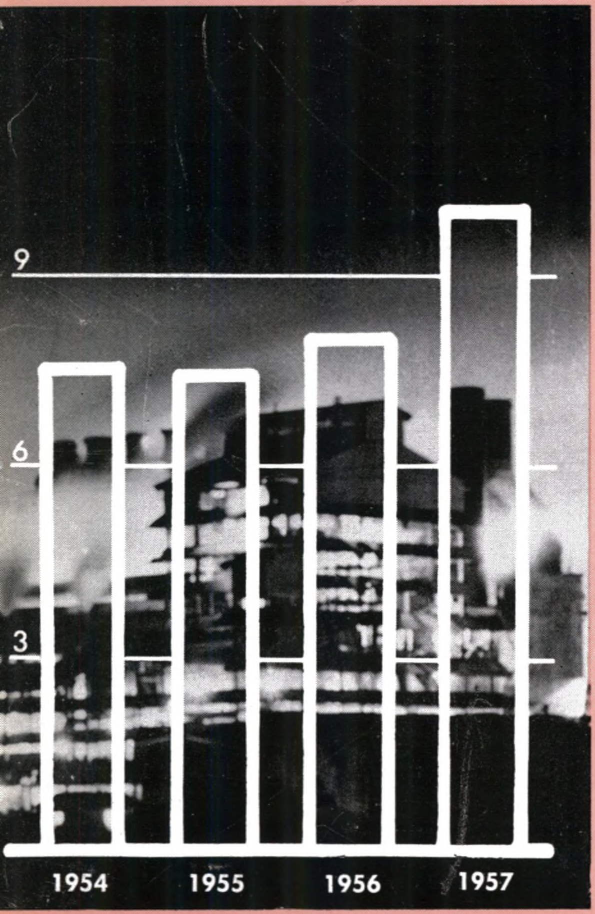
TOTAL ASSETS OF COMMERCIAL BANKS slumped more than is usually expected in the first quarter of the year—by $10.2 billion—and, although they expanded fairly steadily during the next nine months, at the end of 1957 they were not significantly above their level at the beginning of the year.

CONSUMERS received a record amount of credit in 1957. However, because repayments on outstanding credit were also at record levels, the net addition to current purchasing power made by consumer borrowing, $2.7 billion, was nearly one-fifth less than in 1956 and was less than half that in 1955.

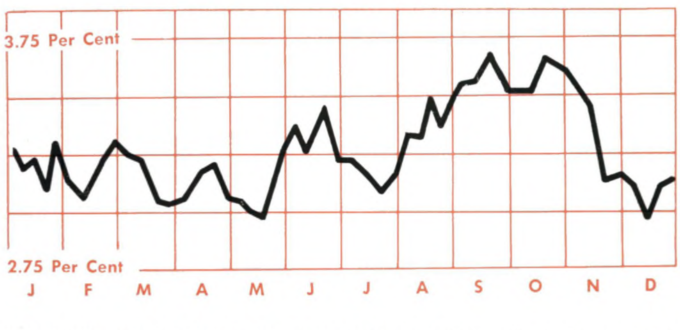


STATE AND LOCAL GOVERNMENTS issued new securities totaling $7 billion in 1957, primarily to support their capital spending programs. This total exceeded that in 1956 by one-fourth and was on a par with the previous record set in 1954.

OF CHANGE



CORPORATIONS put a larger amount of new bond issues into the capital markets in 1957 than ever before. The $10 billion of flotations last year (mostly for new capital) was one-fourth larger than the total in 1956 and a third greater than in each of the two preceding years.



THE RATE ON NEW ISSUES OF TREASURY BILLS reflects the general pattern of interest rate behavior. During most of 1957 demands for funds overbalanced supply and rates reached record levels in early Fall. After mid-November most rates experienced sharp declines.

Peanuts Aren't Just Peanuts

"Just peanuts!" How often this expression is used to denote smallness, triviality, or insignificance. But just as peanuts ofttimes prove to be the staff of life to country squirrels and their city cousins, so also are they of key importance to the peanut-producing counties of southeastern Virginia and northeastern North Carolina.

NUTS AND HAMS These 21 counties, each of which ranks among the nation's leading peanut-producing counties, produce the bulk of all peanuts grown in Virginia and the Carolinas. As late as 1954, most recent year for which detailed figures are available, these same counties produced two-fifths of the nation's peanut crop. Three-fifths of all farms in this 21-county area grow peanuts to be harvested for nuts, and peanut acreage comprises about 20% of all cropland harvested.

Picked-and-threshed peanuts account for 28% of the value of all crops sold and one-fourth of cash receipts from the sale of farm products. Even the vines pay their way: peanut vines saved for hay equal about two-fifths of the value of all hay produced in the peanut counties.

Then, too, there is large-scale hog production within the area. This has resulted largely from the practice of turning hogs into the harvested peanut fields to eat the peanuts which drop from the vines during the digging process. Sale of these porkers, from which come the well-known "peanut-fed hams," provides farmers with an additional source of income and has led to the establishment of local pork-packing plants.

Some 33 peanut shelling and crushing plants are in operation in Virginia and North Carolina. In addition, there are 9 processing firms located in or near the heart of the producing area. These shellers, crushers, and processors provide employment for from 50 persons or less to as many as 1,600 per plant.

Suffolk, Virginia, has long been known as the "world's largest peanut market." Located in Nansemond County, one of the 21 leading producing counties, it is but one example of the many communities which benefit from the operation of peanut shelling, crushing, and processing plants.

Nearby Smithfield is the location of several meat packing firms that prepare the lean, distinctively flavored, peanut-fed hams that are esteemed throughout the world.

And so peanuts aren't just peanuts! They're a means of livelihood, feed for livestock, and the source of tasty hams.

HOW IT ALL STARTED The peanut's importance to this area extends over nearly a century. First produced commercially in this country in Sussex County, Virginia, in 1844, peanuts soon became the leading crop of that county. Cultivation spread extensively into surrounding counties, and by 1868 production in Virginia totaled nearly 7 million pounds.

After the War Between the States, the soldiers who had fought in the Virginia campaigns carried their liking for peanuts home with them. Peanut production spread rapidly into other Southern States, and by 1879 total commercial output for the country had risen to about 38 million pounds.

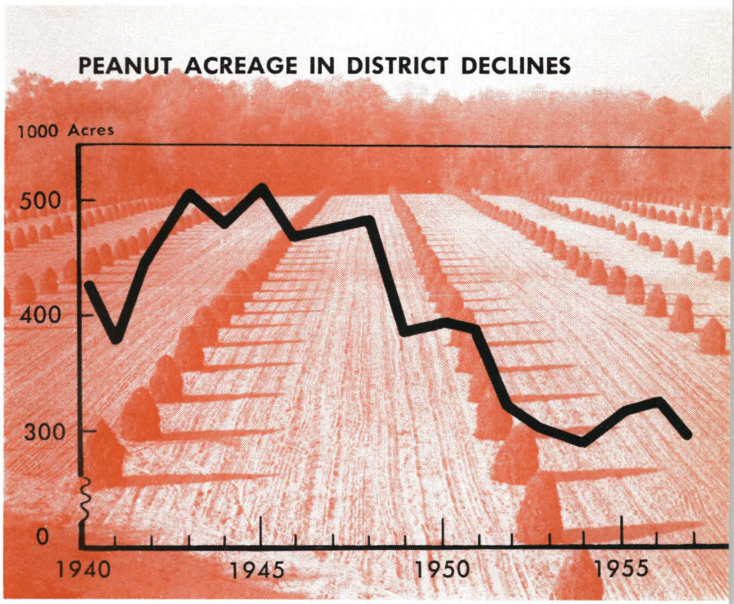
Hand preparation of peanuts for market proved impractical on a large scale, and the growing of peanuts as a business was necessarily restricted until machinery for picking, cleaning, and shelling was invented. The first step in this direction came in 1876 when a plant for cleaning peanuts was erected in New York City, then the leading peanut market. It was soon apparent that the logical place for a peanut plant was the area of production; so, one was built in Norfolk, Virginia, in that same year. A second factory was built in Norfolk in 1878 and another, much larger, one in Smithfield, Virginia, in 1880.

Market expansion followed the introduction of the new marketing methods, and production of peanuts spread quickly throughout the South. By 1909 peanut acreage harvested in Virginia and the Carolinas amounted to 331,000 acres, and production totaled 224 million pounds. This was roughly two-thirds of the nation's output.

Between 1909 and World War II, expansion of both acreage and production of peanuts occurred throughout the country. Expansion in the Virginia-Carolina region was not as rapid as elsewhere, however. This same lag occurred during the war years when marketing quotas and acreage allotments were suspended to encourage an increase in peanut production for war needs. Peanut acreage throughout the nation increased two-thirds; that in the District slightly less than two-fifths. The rise in District production compared even less favorably than the upturn in acreage. As a result, World War II production in the District states averaged around one-fourth of the nation's total.

Even though the Virginia-Carolinas' share of the nation's peanut acreage and production declined between 1909 and 1945, the peanut's importance to the economies of the counties of southeastern Virginia and northeastern North Carolina assumed major proportions. By 1945 when District acreage reached its peak at 515,000, two-thirds of all farms in the 21 counties were growing peanuts to be harvested for nuts. Peanut acreage comprised nearly 30% of all cropland harvested. Value of the peanuts amounted to a little less than two-fifths of the value of all crops sold and one-third of the value of all farm products sold.

Given impetus by the acreage allotment program in effect since 1949, peanut acreage has declined sharply during the postwar period. Last year, in fact, the District's harvested acreage of peanuts was one-third below the prewar high of 1940 and two-fifths under the wartime peak in 1945. There has been a significant upturn in yields since the war, however, and the District has regained some of the ground it lost to other peanut-producing states prior to and during the war years.



The need for fewer acres of peanuts since World War II has resulted from higher yields and a lower level of demand.

SUPPLY AND DEMAND Why have peanut producers been confronted with smaller acreage allotments during most years since 1949? The answer is a familiar one—the necessity for adjusting production to bring supplies in line with current needs.

During World War II when farmers were urged to plant larger acreages of peanuts as a safeguard against shortages of fats and oils, the increased output also permitted an increase in the consumption of edible peanuts. Consumers were glad of the chance to substitute peanut products for foods in short supply such as butter, cheese, jams and jellies, candy, and imported nuts. Per capita consumption of peanuts jumped from 4.4 pounds in 1939 to 6.6 pounds by 1945.

Peanut consumption per person dropped to the prewar level shortly after the war and has held at about that level since. The war-created demand for sizeable quantities of peanut oil has also diminished. As a result, the Commodity Credit Corporation has found it necessary to purchase large quantities of peanuts during most years since 1948.

There has been a slight rise in the over-all demand for edible Virginia-type peanuts since 1950. The significantly increased yields per acre have provided the product to meet this upturn in demand for Virginias, however, and no appreciable increase in acreage has occurred.

The Fifth District

Recent weeks have brought diverse changes in District business, but on balance the decline in activity continued in December and early January.

Trade, as reflected in reports from department and furniture stores and automobile dealers, made a good showing in December, and department stores continued to report a healthy volume in the opening weeks of the new year. Bank debits showed a better-than-seasonal gain in December, reflecting an increase in total payments made.

Despite these hopeful signs, however, many basic indicators continued downward. December man-hours of work in durable manufacturing industries shrank by 3% from the previous month, and bituminous coal production fell sharply in December and started January at low levels. Despite Christmas week shutdowns, textile manufacturers found little improvement in their situation in January. Farm income showed the decline expected to result from smaller 1957 crops.

Bituminous Coal

The bituminous coal industry started 1957 with hopes of continued improvement but ran into difficulties as the year progressed. Such important consumers as the steel industry and the cement industry bought less than expected tonnage and the general decline in industrial production cut back other industrial purchases.

The strong source of demand on the coal industry during 1957 came from outside the continent, as overseas shipments were one-fifth higher than in 1956. Even with a drop of 8% in Canadian purchases, total exports were up by 12%. This was in contrast to the drop of 4% in domestic consumption and a reduction of nearly 3% in total production.

Production from the mines of West Virginia, Virginia, and Maryland held up better than this, however, due to the favored position of these mines for export. The District's share of bituminous output thus continued to increase as it has done in recent years, rising to 37% of the 1957 national total.

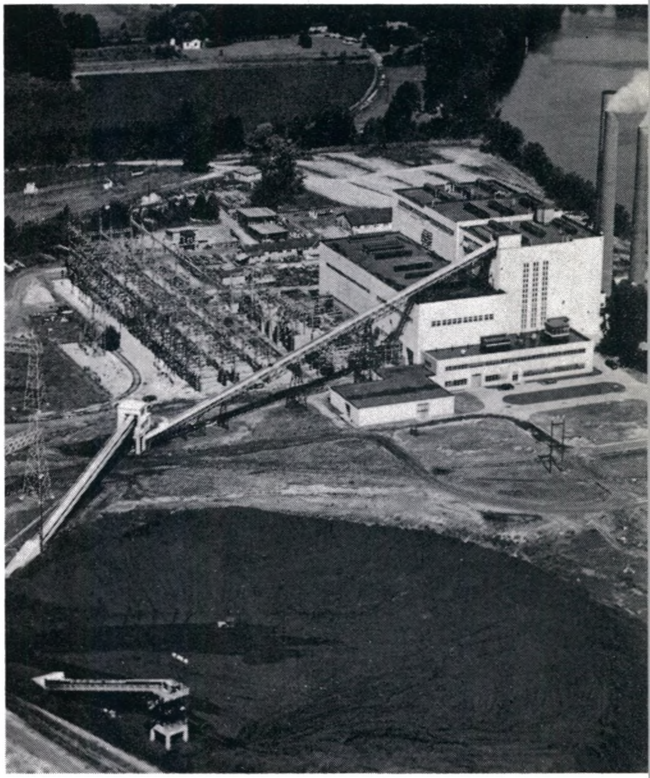
Coal prices rose in the Spring of 1957 but have weakened somewhat as output declined. The premium charged earlier for export coal has disappeared, and some price cutting has been reported in domestic markets.

Current industry forecasts place this year's production and consumption about 3% below last year's. The decline is expected to be centered in coking coal used for steel production and in foreign sales, which trailed off in late 1957 due to a slowdown in industrial activity in northern Europe. The total of 475 million tons, if realized, will call for somewhat higher average production than was achieved in the closing weeks of last year.

Despite stiff competition from petroleum and gas, bituminous coal use by electric utilities increased last year and is expected to show a further gain to 165 million tons in 1958. Aggressive research has produced great advances in efficiency in coal-fired boilers; this has cut coal requirements per unit of electrical power but has maintained coal in a favorable competitive position at substantial distances from the mines.

The railroads have sunk to insignificance as users of coal. Still important as recently as 1951,

Electric utilities consumed one-third of the bituminous coal mined in 1957 and give promise of an increasing demand.

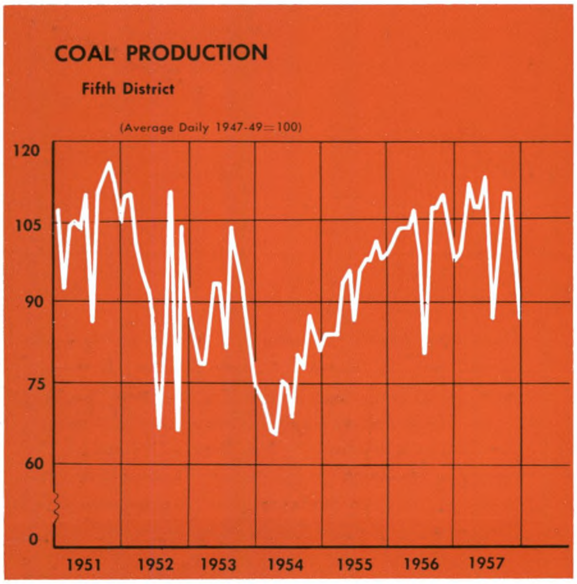


A rare sight is this steam locomotive, for the coal-burning iron horse has been overtaken by the diesel-powered streamliner.

when they bought 54 million tons, they are expected to use 6-7 million tons in 1958. Cement mills—which fire their kilns with bituminous—are now more important consumers than the rails.

Competition from gas and petroleum have driven down "retail" use of coal for heating. The loss amounted to one-third from 1956 to 1957, leading to an expected use of about 36 million this year.

Bituminous coal production topped out in the second half of 1957 after a three-year growth from its postwar low in 1954.



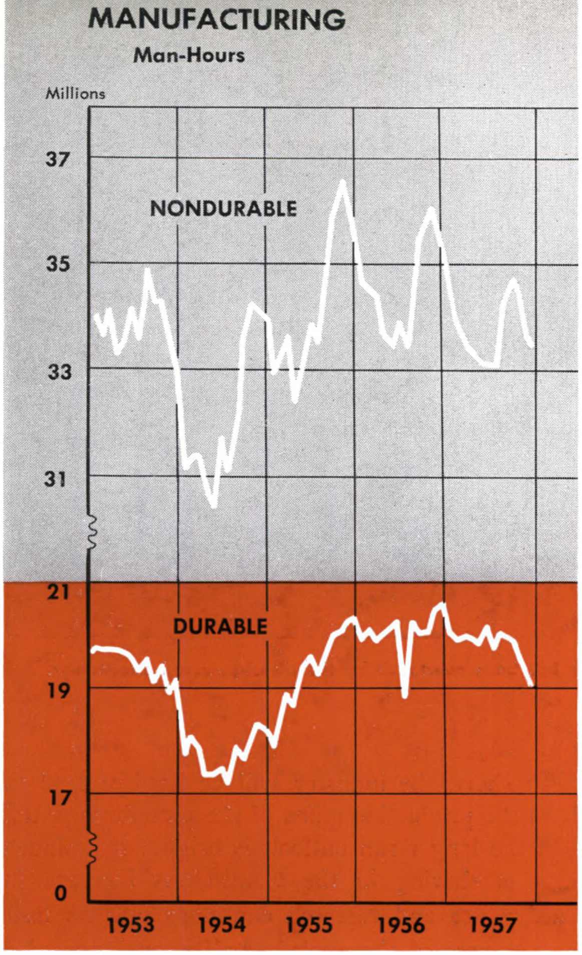
In short, the industry will be hard-pressed to hold the production gains of the past three years. Yet the longer-run outlook is bright: bituminous coal is sharing in the tremendous increase in energy use and research continues into its uses as a source of chemicals. A 1955 estimate of a 10-year increase of 50% in the demand for bituminous may well be realized. West Virginia and the other coal producing states of the District will share in the benefits of this increase.

District Briefs

TEXTILES A weakening of cotton cloth prices in January symbolized the continuation of problems for the textile industry. It had been hoped that the widespread week-long mill closings at Christmas would reduce inventories enough to improve the order position of the mills, but this apparently did not happen.

Together with lower cotton cloth prices, mills face higher raw cotton costs. A relative scarcity of good quality cotton is forcing competitive bidding for supplies at higher prices. The spread between cotton costs and selling prices shrinks as a result.

FURNITURE District furniture manufacturers curtailed production in the closing months of last year and now hold a limited booking of orders. One spokesman forecasts first quarter industry sales at 70-80% of the same period last year,



The rate of decline in nondurable manufacturing eased in December, as durable industries declined 3% from November.

pointing to limited buying at the Chicago Winter Home Furnishings Market in mid-January.

AGRICULTURE Cash farm income continued to lag with the November total 22% below the same month a year ago. Crop income was down 32%, while income from livestock and products was up 5%.

TRADE Department store sales exhibited real exuberance in December, rising 4% after seasonal correction from November to a level almost even with December 1956. This brought the year's total 1% ahead of 1956. The December sales performance was a surprise to store operators, for sales early in the month foretold a poor Christmas season. Sales strength came mainly in the ordinary Christmas gift items and did not indicate any great breadth of demand. Weekly figures in early January, however, continued to show strength.

Retail furniture stores in December maintained substantially their November sales level after adjustment for seasonal forces. Reports from automobile dealers in major Fifth District cities indicate on balance that new car sales in December were somewhat better than in November.

EMPLOYMENT Total nonagricultural employment in December was fractionally above November due largely to a seasonal increase in retail workers. Most other types of employment except Government showed a decline between November and December; this was particularly pronounced in mining and construction.

Insured unemployment in early January rose substantially over December in each state of the District. The largest increase—more than 50% —came in the Carolinas and Virginia, while the District of Columbia had an increase of 16%.

BANKING Nowhere was the Fall slowdown in the pace of District business more evident than in the loan activity at member banks. Typically District bank loans rise throughout a good part of the Fall—particularly during December—because of the strong seasonal upsurge in business. This Fall, however, something was missing. Total loans of District weekly reporting banks edged up only slightly—about 60% less than they rose the last quarter of 1956. Even more important, their business loans—still a better indicator of economic activity—hardly rose at all.

Greater than seasonal weakness in several types of loan demand at these same banks thus far in 1958 provides further evidence of continued softness in the Fifth District economy. For the first three weeks of the year, business loans fell by a shade more than they dropped at this time last year. Roughly the same is true for consumer and real estate loans, which also slid a little further than they did during the first three weeks of 1956.

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