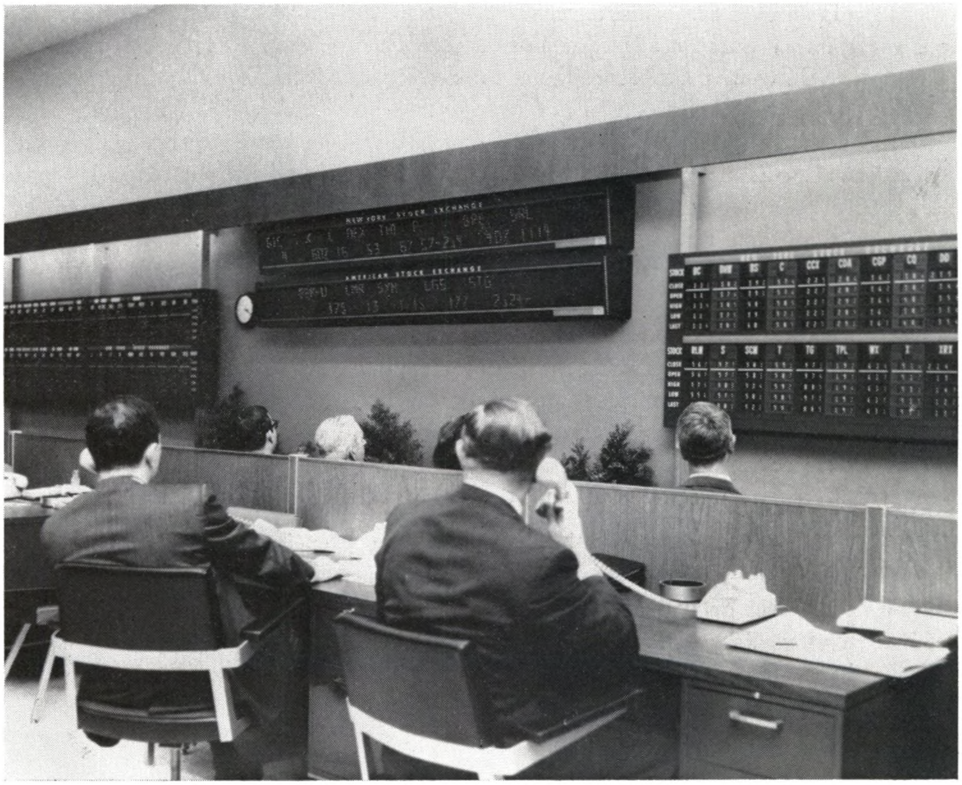
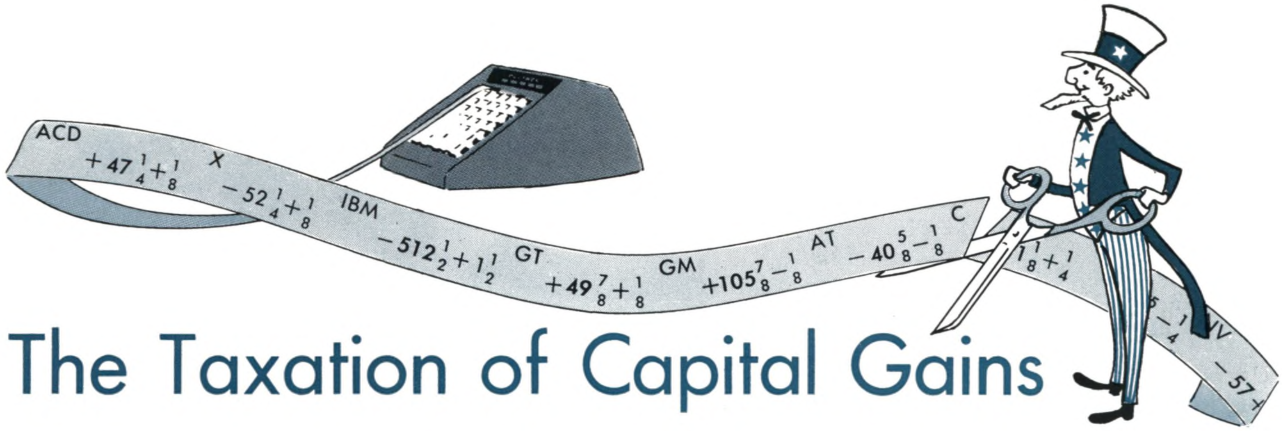
MONTHLY REVIEW



Sales of common stocks account for most of the capital gains realized in the United States.

FEDERAL RESERVE BANK OF RICHMOND MARCH 1966



The Taxation of Capital Gains

Most questions of tax policy are controversial but few have stimulated such heated or prolonged argument as the question of appropriate treatment of capital gains and losses. Debate on the problem has been going on for the past 52 years, since the ratification of the Sixteenth (Income Tax) Amendment, and the end of the discussion is not in sight. The present Federal capital gains tax is criticized both as a severe impediment to the free workings of capital markets and as a flagrant tax loophole. The matter of proper treatment remains a dilemma because it presents an array of unresolved conflicts in and among concepts of income, equity considerations, revenue needs, administrative requirements, the desire to avoid harmful effects upon markets for capital assets and investment incentives, and various other objectives of taxation.

This article reviews the existing system of capital gains taxation and discusses some of the current problems.

Basic Facts A capital asset may be defined generally as any asset or property held for the further production of wealth or as a source of income. A capital gain (or loss) is realized when such an asset is sold at a price higher (or lower) than was paid for it. The gain which accrues from the sale of the source of income may be distinguished, conceptually at least, from the flow of income arising from the asset.

In practice, the distinction between capital gains and income is not an easy one to draw. The legal definition of capital assets is determined by Congress and the Courts. At any given time, it represents a compromise between theoretical exactness and the vagaries which inevitably are present in real world situations. Such definitions can never be clear-cut and always embody numerous specific exceptions.

Generally, however, land, buildings, manufacturers' equipment, stocks, bonds, and like assets, are classified as capital assets and appreciation realized from the sale of such assets is capital gain. Most gains made in this country today arise from sales of corporate common stocks. Gains on the sale of real estate run a poor second, and gains on other property are of relatively minor importance.

Capital gains are distributed in a highly progressive fashion among income groups. For those in the top brackets, net gains constitute a major source of income, even though total gains are a relatively small fraction of total personal income for the entire population. By contrast, net losses are concentrated heavily in the middle-income groups.

Background of the Tax The capital gains tax is a special form of Federal income taxation. During the first four years of the Federal tax, 1913-1916, no legal distinction was made between capital gains and ordinary income. This policy drew only limited criticism, as income tax rates were quite low, even for those in the highest income brackets. In 1917, income tax rates soared and pressure began to build for special consideration for gains. Four years later, the law was changed to grant special treatment to capital gains of individuals but not those of corporations. The Revenue Act of 1921 defined capital assets as property acquired and held by the individual taxpayer, for a period of more than two years, for profit or investment whether or not in connection with his trade or business. Excepted from this basic definition was property held for the personal use of the taxpayer or his family and stock-in-trade or other property of a kind that would properly be included in the inventory of the taxpayer if on hand at the close of the taxable year. The Act provided that gains from the sales of capital assets should be taxed at a rate not to exceed 12.5%, while losses from sales of such assets could be offset fully against all income. Special tax treatment for gains was not granted to corporations until 1942. The Revenue Act of that year, which provided the basis of the current system, gave corporations tax privileges equivalent to those of individuals.

Since 1921, Congress has made numerous modifications in both the definition of capital assets and the approved treatment of gains. Limitations of space preclude even a listing of the changes here. It may be noted as a generalization that the changing tax laws have been, in a sense, a series of semi-controlled experiments, each of which has drawn sharp criticism from one group or another.

Underlying Principles In each revision of the law, however, two broad principles have been followed. First, only those gains actually realized on sales of assets have been taxed, despite the fact that it has long been argued by competent authorities that taxing gains as they accrued would theoretically be a more desirable system. Second, capital gains consistently have been given preferential treatment relative to income from wages, salaries, and rents—the "ordinary" forms of income.

The "realization principle" has been accepted because Congress has recognized that taxation on an accrual basis would create an unreasonable, if not impossible administrative burden. In attempting to obtain accurate estimates of annual appreciation and depreciation of assets such as houses, land, and capital equipment, for example, the Federal Government would be faced on a nationwide basis with all of the problems that local governments currently confront in administering taxes on personal property.

Given acceptance of the realization criterion, equity would seem to dictate that capital gains of individuals should be taxed at a lower rate than recurring income. The tax on ordinary income is quite progressive. It would be difficult to justify pushing an individual into a tax bracket well above his normal bracket simply because in a particular year he realizes a gain which has been accruing over a longer period. The lower rates on gains serve as a partial substitute for an income averaging provision.

This argument loses much of its force in the case of corporations, because the corporate income tax recognizes only two brackets, under $25,000 and over $25,000. The "need for averaging" justification would be fully valid only if a corporation had ordinary earnings of less than $25,000 and the realization of gains pushed taxable income into the surtax bracket, or if an excess profits tax with a series of progressive graduations were in effect. The principal thesis advanced today to justify special treatment of corporate gains is that tax advantage encourages certain types of useful investment.

Not surprisingly, the lower tax rate on gains has given rise to a multitude of elaborate schemes for avoiding taxation by conversion of ordinary income into capital gains. "Collapsible" corporations and partnerships are perhaps the best known devices.

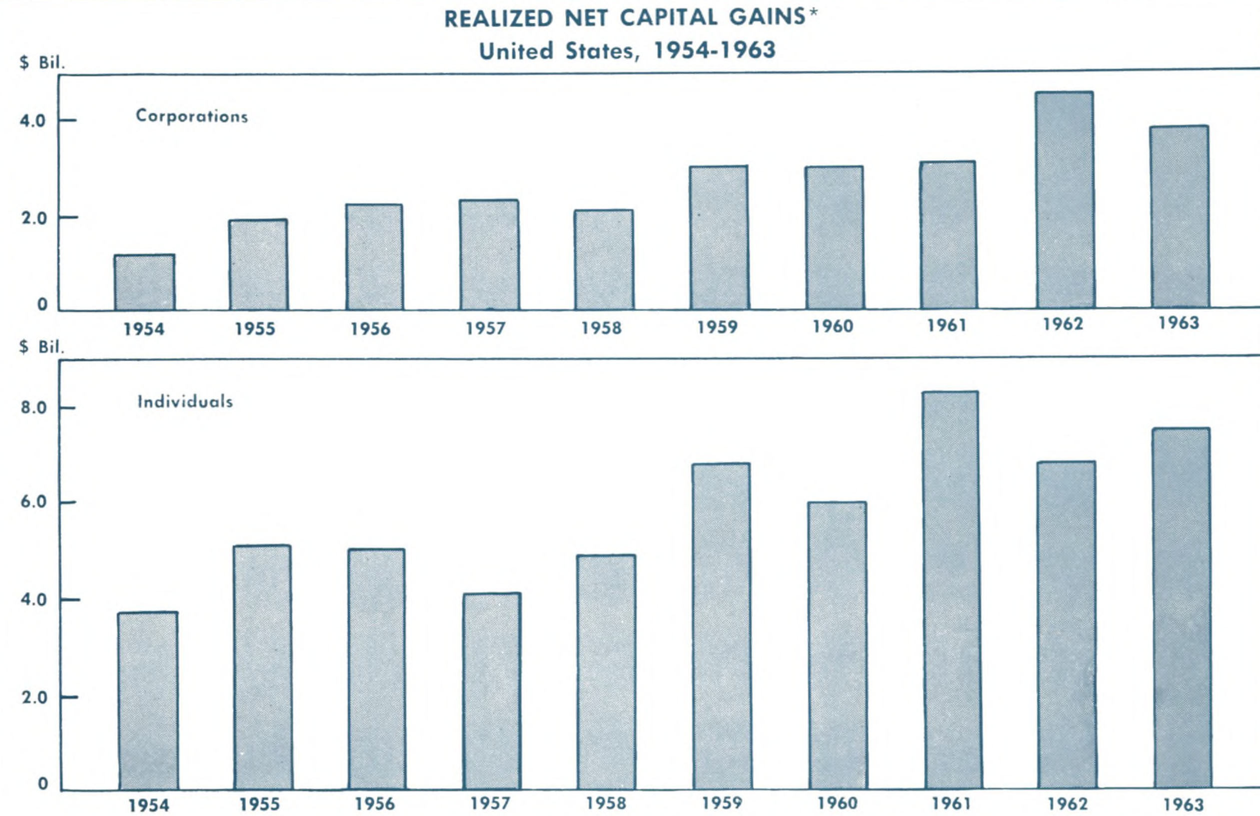
The Tax Law Today The definition of capital assets is more complex in the present law than it was in the Act of 1921. Such assets are defined as all property held by the taxpayer except: (a) stock-in-trade and property includable in inventory, (b) property held for sale to customers in the ordinary course of the taxpayer's trade or business, (c) business property subject to an allowance for depreciation, (d) real property used in business, (e) a copyright, literary, artistic, or musical composition which is the result of the taxpayer's personal effort, (f) notes or accounts receivable acquired in the ordinary course of business, and (g) certain Government obligations sold at a discount. Also, the minimum holding period for eligibility for special tax treatment has been shortened to six months.

The maximum rate of tax on gains of individuals is now 25%, double the original rate. But relative to existing rates on ordinary income, treatment is more favorable now than in 1921. The taxpayer is given two options in computing his tax on capital gains. Under the first option, he may elect to include in his total taxable income 50% of the excess of net long-term capital gains over net short-term losses. He then pays the regular personal income tax rates upon all income including these net gains. Under the second option, he may elect to exclude net capital gains from his regular taxable income and pay a flat rate of 25%. A similar system of alternatives limits corporate tax liability on net long-term capital gains to the same maximum.

For individuals, losses realized on the sale of capital assets within a given year may be fully offset against gains and against ordinary income up to $1,000. The law also provides for a one year carry-over, with the same offset rules applying in the succeeding year. The rules applying to corporate capital losses differ from those applicable to individuals in that corporations may offset losses only against capital gains, but a five year carry-over is allowed on losses from normal capital transactions and a ten year carry-over is allowed if the loss arises from foreign expropriation of assets.

Beyond its basic tenets, the existing body of capital gains tax law is extremely technical and confusing to most laymen. Over the years, capital gains treatment has been granted to more and more assets, mainly as a result of pressure applied by interested groups, and the granting of these exceptions has greatly increased the complexity of the law.

Generally, contemporary reasoning seems to be that



*The totals for corporations are net long-term capital gains reduced by net short-term capital losses. The totals for individuals are net gains from sales of capital assets in adjusted gross income.

Source: U. S. Treasury Department.

capital gains treatment should be granted for any one of three reasons. First, as noted, special tax consideration is often deemed appropriate in lieu of an averaging device. Second, certain sources are not considered capable of bearing the full burden of ordinary income taxation. For example, sales of land with unharvested crops are granted capital gains treatment on the assumption that such sales normally reflect unusual—"forced sale"—circumstances. Third, preferential tax rules are sometimes felt to be necessary as incentive devices. Under the Small Business Investment Act of 1958, to cite one illustration, special treatment is provided for gains from sales of small business securities on the assumption that this concession acts as a stimulus to a socially desirable form of investment.

Unanswered Questions Despite years of debate, many important questions regarding both the theory and practice of capital gains taxation are still unresolved. Two diametrically opposed schools of thought exist even on the basic questions of whether or not gains ought to be taxed at all. Those who favor the tax contend that capital gains, whether realized or not, add to the wealth of the individual or the corporation in the same way as salaries, dividends, and profits and should be treated accordingly. As a corollary to this general thesis, proponents point out that most gains are realized on common stock of corporations and argue further that stock appreciation reflects mainly corporate policies of retaining and accumulating profits. The undistributed profits that underlie these gains should, according to their view, be taxed just as distributed profits are taxed.

Those who oppose the tax argue basically that gains are not income but capital and that a tax on capital is not sound economic policy. Also, some opponents contend that gains are in large measure illusory, reflecting increases in the general price level. In this connection, however, it should be noted that wage and salary increases are probably no less related to inflationary illusion than capital gains. Whatever its theoretical merits, opposition to the tax is not without significant political support, especially in other countries. In 21 countries, including Austria, Belgium, France, West Germany, and Switzerland, there is no tax on gains after some minimum holding period. England only recently began to tax them.

Among those who agree that capital gains should be taxed, there is virtually no concensus on how the ideal system ought to be set up, or, stated more exactly, how the existing system should be changed. Ideas about definition of assets, rates, and exceptions are as numerous as the "experts" in the field.

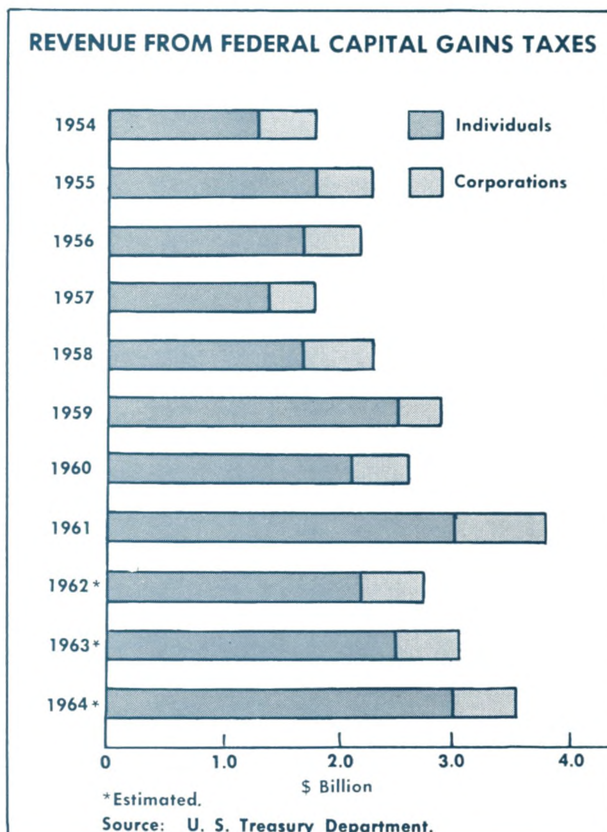
The Economic Effects Economists generally agree that the primary effects of capital gains taxation are on economic growth. How the influence of the tax is to be viewed depends upon the way the analytical question is framed. If the effects of the present system of capital gains taxation are compared to the effects that might be expected if gains were taxed at the same rates as ordinary income, it can be shown that the existing system of preferential treatment is a stimulus to growth. If, however, the tax is considered against the alternative of no tax at all, it may be shown to retard development of the private sector—if possible effects of Federal spending of the revenues are ignored. But this, of course, is true of all taxes.

Detailed analysis suggests that the two most important direct effects of the tax are upon the supply of savings and the mobility of capital. The nature of these direct effects is best pointed up by tax vs. no tax comparisons.

Under the present taxing system, savings are reduced relative to what the supply would be in the absence of the tax. Recent empirical studies have shown that most individuals realizing capital gains save and invest the proceeds rather than spending them for current consumption. Thus, in effect, the tax is paid out of savings, or out of capital, which is the same thing. It does not follow from this analysis, though, that the final effect of the government's action has to be adverse to growth. If, to cite just one possibility, the revenues from the tax are spent to improve schools and thereby upgrade the quality of the labor force, the final net effect may be to accelerate the national growth rate.

The tax rules now in effect restrict the mobility of capital. This is often referred to as the "lock-in" effect. As noted previously, gains are taxed only when realized. Further, there is provision in the existing law which allows transfer of capital assets at death without payment of the tax. Given this combination of rules, some individuals are encouraged to continue to hold assets which they would sell in the absence of a tax upon realized gains. There are no very firm estimates of the magnitude of this lock-in effect, but several recent studies have suggested that the dollar volumes involved are substantial. Critics of the tax point out that this problem could be reduced, without lowering the present tax rates, by requiring periodic constructive realization (appraisal of asset values for tax purposes), or at least, constructive realization at the death of the holder of the assets.

The Growing Importance of Capital Gains The dollar volume of capital gains realized annually has risen rapidly since World War II and is now at a record level. As shown in the chart on page 4, net gains of individuals doubled and net gains of corporations trebled between 1954 and 1963. During the 11 year period ending in 1964, total revenues from the tax doubled, as may be seen in the chart on this page. By contrast to total revenues from the personal and corporate income taxes, the dollar yield from capital gains taxation is still small. In 1964, the gains tax brought in only about 3% of total revenues from the two income taxes. But over the past decade, revenues from capital gains have increased roughly 10% more than total income tax revenues, and gains tax yields appear to be rising at an increasing rate. In the light of these considerations, the question of appropriate tax policy with respect to capital gains should be increasingly in the limelight in the next several years.



Historic Old Salem

WINSTON-SALEM, NORTH CAROLINA

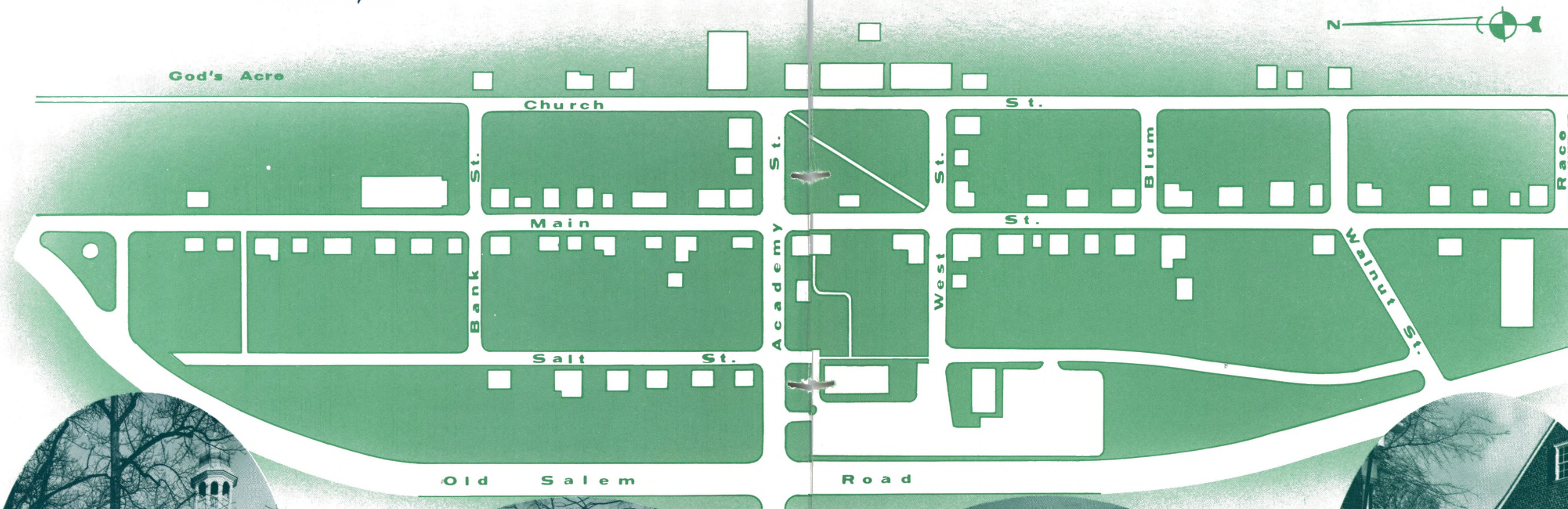
Founded 1766

South of the business district in Winston-Salem, North Carolina, is Old Salem, a small community centered on a town square. Twenty-two buildings, scattered within the four- by eight-block area, have been restored, and seven of these are open to tourists. Others are scheduled for restoration in the near future.

Two hundred years ago last January, a group of twelve men began construction of Salem. The location of the town square and several buildings had been planned and approved by members of the Moravian Church. Salem was to be the religious, cultural, and craft center for villages planned for the area. The men and women who settled here were highly skilled, well-educated, devout people. They never numbered more than 400. They were so far from the major trade centers that they made all they needed except a few items such as glass and some types of hardware.

Restoration of Old Salem has developed under the supervision of Old Salem, Incorporated, with the close cooperation of Salem College and the Moravian Church, and is directed toward re-creating Salem as it was in 1830. Only a small amount of reconstruction has been necessary, and many original furnishings are in use.

Old Salem, Incorporated, has been operating since 1950. It has grown from one paid employee in 1950 to 78 in 1965. Its income is received from rentals of restored buildings, sales of craft items, visitors' admission fees, a biennial grant from the State of North Carolina (the latest one for $100,000), endowment funds (valued at $805,000 in April 1965), and individual gifts. As of July 1965, $3,500,000 had been received through donations. An estimated 40,000 people visited Old Salem in 1965, 22,000 more than in 1950. The number has increased appreciably each year.



The sanctuary of Home Moravian Church, shown here on the right, was dedicated in 1800. The church was the center of community life, and church leaders also served as directors of the town's government and activities.

This brick and frame structure, the Single Brothers House, was the home, meeting hall, and workshop for the single men of Salem. The original brick and timber building was completed in 1769. The all brick portion was added in 1786. Craftsmen work today in nine shops inside.

The furnishings in this classroom of the Boys School, which is now the Wachovia Museum, are representative of those used in 1828. The people of Salem placed strong emphasis on education, and the instrument on the right is indicative of their love for music.

These hostesses are outside the John Vogler House, home of Salem's silversmith and clockmaker. Behind is the Anna Catharina House. Most Old Salem buildings open directly onto the sidewalk, with large yards in back.

District Agriculture and the New Farm Programs

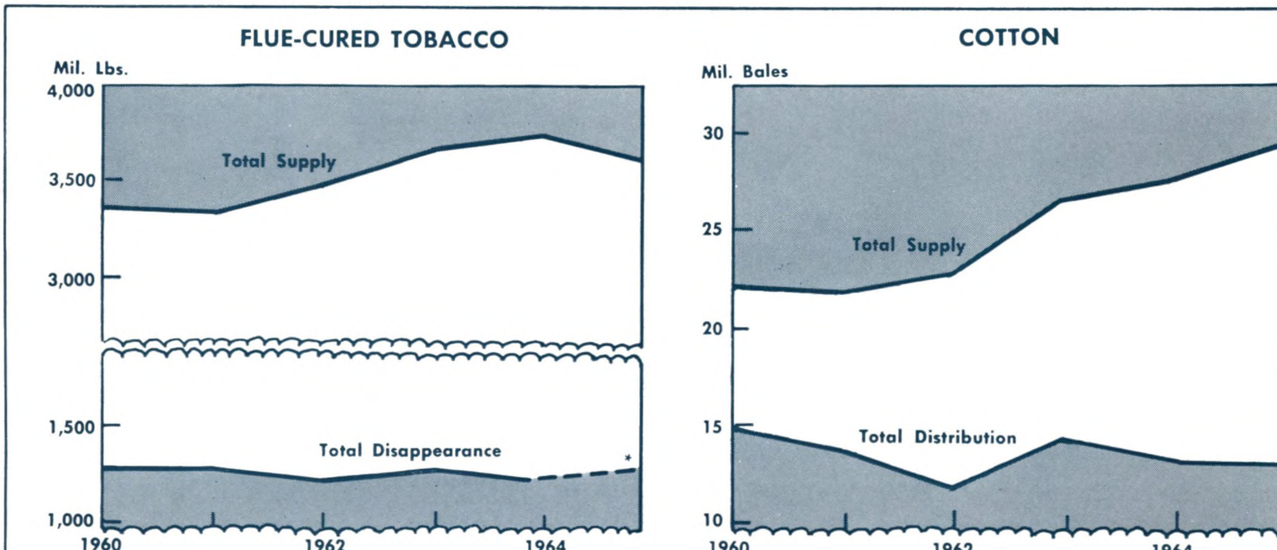
Fifth District agriculture in 1966 is likely to be significantly affected by two major farm laws enacted last year. They are the Tobacco Acreage-Poundage Act and the Food and Agriculture Act. Both are directed at bringing supplies of major farm commodities into line with current demand. They concentrate on tobacco and cotton, two commodities that have been piling up in increasingly burdensome surpluses, and are patterned to some extent after programs which have proven quite successful for feed grains and wheat. Both Acts offer the farmer a wide range of choice as to how he may adjust his individual operations to the objective of surplus reduction.

THE TOBACCO ACREAGE-POUNDAGE ACT

Government programs to limit tobacco output for price maintenance purposes have been in effect since 1933, except for the 1939 crop. Sharp yield increases have limited their success recently, however, and large amounts of tobacco have moved into Government warehouses through price-support operations. Reduced allotments under the acreage programs retarded but did not reverse the trend. Stocks continued to grow and quality was frequently sacrificed in the race for higher yields.

The Tobacco Acreage-Poundage Act was passed last April. It limits the poundage that can be marketed as well as the acreage that can be planted. In order to allow for different weather conditions and field sizes from season to season, growers are permitted to market up to 110% of their poundage quota, with overages in a given year subtracted from the following year's quota. By the same token, the quota of a farmer who markets less than his quota in a given year will be increased by a corresponding amount the following year.

When given the option of adopting or rejecting acreage-poundage controls in a referendum held in May, growers of flue-cured tobacco voted to operate



* Estimated by the Federal Reserve Bank of Richmond.
Source: U. S. Department of Agriculture.

under the program in 1965-67. The early success of the program is illustrated in the first chart which shows the reversal of the trend of increasing supplies last year. Moreover, in the first year under the program, quality improved and growers received over $6.00 more per hundred pounds than in 1964. A referendum of burley tobacco growers will be held March 10 to determine whether the acreage-poundage program will be extended to this type of tobacco. Other types of tobacco will continue to operate under the older acreage allotment programs.

THE FOOD AND AGRICULTURE ACT

Of equal significance for Fifth District farmers is the Food and Agriculture Act, passed last October. This is an omnibus law which provides for a major change in the cotton program, introduces a cropland retirement program similar to the Soil Bank of the 1950's, and modifies the feed grains, wheat, wool, and dairy products programs. The Act establishes programs for the affected commodities for a four year period, 1966-69.

The following paragraphs outline the provisions of the Food and Agriculture Act that bear most directly on Fifth District farming.

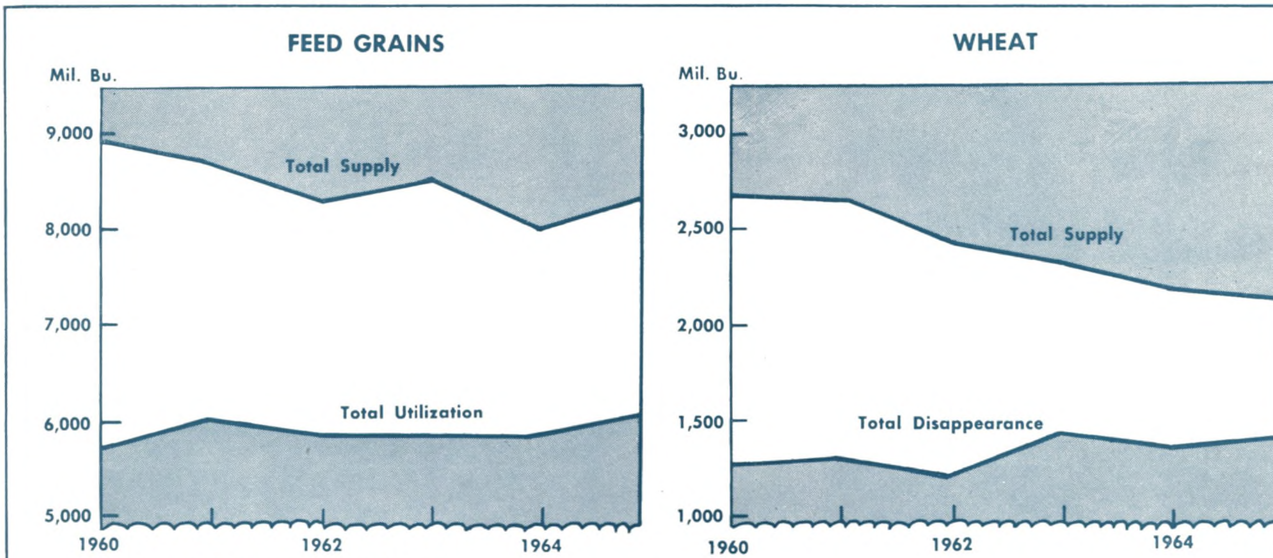
Cotton The cotton program embodied in the Food and Agriculture Act is a sharp departure from those provided by earlier laws, and compared with other commodity programs, offers a wider range of alternatives. The program is voluntary, but non-participating growers will be subjected to a penalty of 50% of the June 15, 1966 parity price on marketings in excess of allotments.

The law specifies a mandatory 12½% cut in acreage for all participating farms and offers additional inducements to those who cut back acreage as much as 25% or even 35%. Price-support loans averaging 21 cents per pound for Middling 1-inch cotton are offered to all participants. Acreage taken out of production and conserved qualifies participants for diversion payments of 10.5 cents per pound times their projected farm yield. In addition a direct price-support payment of 9.42 cents will be paid on 65% of the farm's total allotment. This is the estimated share that would be used domestically and is called the domestic allotment.

Assume a farmer has a 100-acre total allotment and a 500-pound per acre projected yield which he obtains. Assume also that he takes only the mandatory (12½%) cut. He will receive:

87½ acres x 500 lbs. x 21¢ *loan payment* + 12½ acres x 500 lbs. x 10.5¢ *diversion payment* + 65 acres domestic allotment x 500 lbs. x 9.42¢ *price-support payment* = $12,905.25

Special consideration is given to small farmers, those with an allotment of 10 acres or less or total projected production of 3,600 pounds or less, and no acreage reduction is required to receive program benefits. Small farmers will be eligible for the direct price-support payments on their domestic allotment plus diversion payments of 35% on their total allotments even though no acreage is actually diverted. By diverting up to 35% of their total allotments, they may earn additional diversion payments. Par-



Source: U. S. Department of Agriculture.

ticipating growers on small farms are also eligible for price-support loans on the cotton they produce.

Cotton farmers also have the alternative of leasing or selling their allotments, and owners of more than one farm may transfer their allotments from one farm to another. Such transfers cannot be made across state lines under any circumstances but can be made across county lines if two thirds of the eligible growers voted favorably in the November 23, 1965 referendum. Producers in 73 counties in the Fifth District, 55 of them in North Carolina, voted for transfers out of the county.

Nationally, slightly more than one million acres of cotton allotments have been transferred by one or another of these methods for the 1966 crop year. In the Fifth District allotments on 78,566 acres were leased, 11,453 acres were sold, and 3,305 acres were transferred by owners of more than one farm by the December 31, 1965 deadline.

Even growers who do not wish to participate in the acreage reduction program have an alternative under the 1965 law, i.e., production for export. An export market acreage of 250,000 acres was established for 1966. A grower who produces for the export market is not eligible for price-support loans or payments on any farm on which he has a substantial or controlling interest. Furthermore, his entire production must be sold for export. Farmers applied for slightly over 100,000 acres for the export market, all outside of the Fifth District.

Feed Grains The voluntary program for feed grains, in effect since 1961, is extended for four more years. The objective is a reduction from the 1965 carryover of 55 million tons to a level between 45 and 50 million tons. In an effort to achieve this, price-support loans and price-support payments are made available only to those farmers who remove 20% or more of their feed grain base from production. Diversion payments at the rate of 50% of the loan rate times the projected yield of the farm will be made on that portion of the base above 20% that is diverted. The first 20% of the land which is taken out of feed grain production must be applied to approved conservation uses, but additional diverted land may be planted to soybeans, and growers will still be entitled to the price-support payments they could have earned if feed grains had been planted.

Cropland Adjustment Program The Cropland Adjustment Program is designed to remove about 40 million acres from crop production and to place them in conservation uses under five-to-ten year contracts. Conservation uses include permanent vegetative cover, trees, wildlife, and recreation practices. Additional incentive payments are available if the operator agrees to open the land for recreation purposes. As a possible means of obtaining even more land for recreation uses, the program features financial aid to State and local governments "in the establishment of practices or uses which will establish, protect, and conserve open spaces, natural beauty, wildlife or recreational resources, or prevent air or water pollution. . . ."

While the land retirement feature of CAP is reminiscent of the Conservation Reserve of the Soil Bank Act, the means of attaining the goal is substantially different. Restrictions are imposed on the amount of land that can be retired in any one locality in order to avoid the harsh economic impact that was sometimes experienced in areas of heavy signup under the Soil Bank. Speculative participation is discouraged by a provision that the land must have been in the same ownership for the past three crop years; some exceptions are permitted, subject to review by county Agricultural Stabilization and Conservation Service committees. As was the case with the Conservation Reserve, all or part of the farm may be placed under a CAP contract, but further restrictions are imposed on what are considered eligible farms or eligible lands.

Eligible farms are defined as those which were operated in the prior year for one of the following purposes: (1) crops were planted for harvest or were harvested, (2) acreage was diverted under one of several Government land retirement programs, (3) a Conservation Reserve contract expired on December 31, 1965, and the farm was not operated in 1965 in anticipation of a CAP-type program, or (4) the farm was not cropped, due to natural disaster. Eligible lands must be part of such a farm and must have been devoted to one of the following uses in one of the three years prior to the contract: (1) row crops or small grains planted for harvest or harvested, (2) diverted under the feed grain, wheat or cotton program, (3) certain lands under another Government retirement program on which contracts have expired, or (4) certain tame hay cropland.

Payment rates are based on farm yield and production data. Rates are 40% of the county price-support loan on barley, corn, grain sorghum and wheat, 6 cents per pound for cotton lint, and 3.5 cents per pound on peanuts. Tobacco rates vary from 12 cents per pound on flue-cured and burley down to 6 cents on cigar filler and binder. Other cropland on the farm will be eligible for adjustment payment rates varying nationally from $3.00 to $7.00 per acre.

THE FIFTH DISTRICT

The current business expansion has now lasted half a decade. For about four years, policymakers were concerned mainly with the possibility that demand might weaken, ending the growth process before full employment could be reached. During the fifth year the pattern of growth began to change, but not because of any weakening in aggregate demand. On the contrary, spending continued to rise, and by the end of 1965 attention had shifted from sustaining the upswing to keeping it within sustainable bounds. Consumers continued to buy new cars in record or near-record volume. Construction, planned as well as in process, maintained a strong upward course. Business spending increased as manufacturers attempted to expand capacity and increase inventories in line with demand. In some industries, dwindling supplies of labor and materials spawned upward pressures on costs and prices and added to the problems of planning ahead.

An Uneasy Balance A healthy economy requires a balanced flow of capital, labor, and materials into production in response to the pull of demand. Certain factors emerging in the District economy in recent months seem capable of upsetting this balance if they continue to develop. In the textile industry, for example, capacity already committed to a heavy backlog of civilian orders must be converted to Defense production. Furniture manufacturers report certain hardwoods and veneers becoming more difficult to obtain with prices gradually creeping up. Short or at best uncertain supplies of nonferrous metals are creating problems for many of the District's metalworking industries. Contractors have also found certain essential materials increasingly difficult to obtain. Delays have affected some ordinary items such as reinforcing rods in addition to a variety of special structural components. A widespread labor shortage, however, seems to be the most difficult problem of all.

Skilled workers were reportedly hard to find more than a year ago. Since then, business has expanded considerably and new additions to productive and distributive facilities continue to approach completion. Thus the search for trained or trainable people has become more and more intense and seems bound to continue for some time at the present fast pace. As a result, the cost of finding and training workers has been rising, a trend that will probably continue.

Help-Wanted Ads Soar Additional perspective on the state of the job market is provided by an index compiled by the National Industrial Conference Board measuring the volume of advertising placed in city newspapers across the country by employers in search of employees. When the national Help-Wanted Index and the unemployment rate are charted together for the past 15 years, they move, of course, in opposite directions but otherwise show quite similar business cycle patterns. In 1964, however, the unemployment rate continued to drop slowly toward 4% while the Help-Wanted Index started rapidly upward. Last fall the index skyrocketed, rising an average of 10 points a month.

When the 52 cities from coast to coast that comprise the index are listed according to November figures, two dynamic urban centers of the Fifth District, Charlotte and Washington, are right at the top, and Richmond is eighth. The national index in November was 180 (1957-59=100) after rising one third from the previous November. In contrast, the Charlotte index was 322, up one half; the Washington index was 313, up more than one third; and the Richmond figure was 247, up more than two fifths. In the December ratings, Washington and Richmond posted further gains while Charlotte declined.

The meaning of such rapid gains is not entirely clear, largely because of the questionable comparability of the base figures from which the changes were measured. Nevertheless, faced with increasingly serious obstacles in their search for workers to staff new offices, factories, and stores in a rapidly expanding economy, employers are turning more and more to advertising and are incurring additional expenses as a result.

National Labor Market Ratings The Department of Labor measures availability of labor in centers of production and employment throughout the country, rating them on both present conditions and the outlook reflected in local employers' estimates of manpower requirements balanced against the expected supply. Despite evidence all last year of a strong demand for labor, the December ratings placed none of the nation's 150 major labor market areas in Group A, which would signify "overall labor shortage." The number of areas classified in Group B, "low (1.5% to 2.9%) unemployment," however, rose over the year from 27 to 48. During the same period the number in Group C, "moderate (3.0% to 5.9%) unemployment," dropped from 94 to 83; and those in Groups D, E, and F, "substantial (6.0% or more) unemployment," numbered 19 in December 1965 compared to 29 a year earlier.

Although these national ratings do not indicate acute shortages in the general labor supply, they do show a significant reduction in surplus labor over the past year. Furthermore, by the Fourth Quarter of 1965 most areas were plagued by specific scarcities of considerable intensity, particularly of experienced workers. As a result, according to the Department of Labor, occupational opportunities were relatively plentiful at the beginning of 1966 for engineers, scientists and technicians, skilled and semiskilled metal workers, medical and health workers, school teachers and college instructors, and certain types of craftsmen, mechanics, and service workers.

In the Fifth District, Charlotte was reclassified in December from Group C to Group B and was one of the nation's three major labor markets that advanced to a higher rating. Among all areas, 47% of those located in the Fifth District were rated "B" compared to 32% nationally, 40% in the District were rated "C" compared to 55% nationally, and 13% were rated "D" or lower in both the District and the nation. The "B" rating was accorded Washington, all four major areas in Virginia, and two of five major areas in North Carolina.

The Statistical Record The following table compares labor force trends in the District since 1960 with patterns of national growth.

	Per Cent Change 1960-1965			Unemployment Rates (%)	
	Civilian Labor Force	Civilian Employment	Unemployment	1960	1965
U. S.	7	8	−12	5.6	4.6
5th Dist.	10	12	−25	5.0	3.4
Md.	12	15	−33	5.6	3.4
Metro. D. C.	25	25	6	2.6	2.2
Va.	11	12	−26	4.1	2.7
W. Va.	−6	−1	−42	11.5	7.0
N. C.	9	10	−15	4.5	3.5
S. C.	5	6	−19	4.4	3.4

The changes shown in the table were accompanied by population increases of 8% in both the District and the nation. Within the District, population changes ranged from a 13% rise in Maryland to a 2% decline in West Virginia. Labor force participation (the ratio of labor force to population) rose a bit in the District while declining slightly in the nation.

A few developments reflected in the table are of special interest. The growth of the labor force in metropolitan Washington since 1960 has been so rapid that the number of unemployed persons rose even though the unemployment rate dropped from 2.6% to 2.2% of the civilian labor force. In West Virginia, part of the striking decline in the number of unemployed reflected continued declines in the labor force. Elsewhere in the District, Maryland registered the largest gains in labor force and employment and the sharpest drop in unemployment.

Local Reports Reflect Strength Labor market reports from localities around the District quite consistently show further increases in employment and employment opportunities. In Maryland, besides strong seasonal increases in retail trade and in Federal Government jobs, substantial gains occurred in December and continued in January in transportation, primary metals, and electrical equipment. Employment in construction has continued at all-time highs. The factory workweek and average hourly earnings in the Baltimore area have continued to rise. Increasing amounts of overtime have been reported in a number of industries.

Washington shows much the same picture except that manufacturing activity is comparatively small. Nearly 50,000 jobs were added in the Washington area during 1965, almost three times as many as in the previous year.

Virginia's record is similar. New workers have recently been hired by producers of textiles, apparel, paper, and chemicals, and high levels of employment prevail in furniture, metals, transportation equipment, machinery, and electrical equipment.

In the Carolinas, jobs and job opportunities have continued to increase in textiles, furniture, chemicals, machinery, and electrical equipment, with smaller but significant gains in stone, clay, and glass products, transportation equipment, paper and paper products, and printing.

Locally, statewide, throughout the District and across the nation, the demand for labor has continued to rise in virtually all sectors of economic activity.

PHOTO CREDITS

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