

FEDERAL RESERVE BANK OF RICHMOND

MONTHLY REVIEW

Prices in an Accelerating Expansion
Origins of Industries—Textiles
Operations and Policy Seminar
The Fifth District



MARCH 1967

PRICES IN AN ACCELERATING EXPANSION

Inflationary pressures which began to accumulate in the second half of 1965 erupted during 1966. Nearly one-half of the \$58.4 billion increase in total spending for goods and services during 1966 was caused by rising prices. In contrast, less than one-third of the \$49.5 billion increase in gross national product in 1965 was translated into a price rise.

In 1966 each of the broad price indicators reflected accelerated upward pressures. New highs were reached in prices of industrial commodities, foods, other consumer goods and consumer services. Although in the closing months a slackening in the upward movement in some prices was evident, the price index for all goods and services making up GNP increased throughout the year at a considerably higher rate than in previous years.

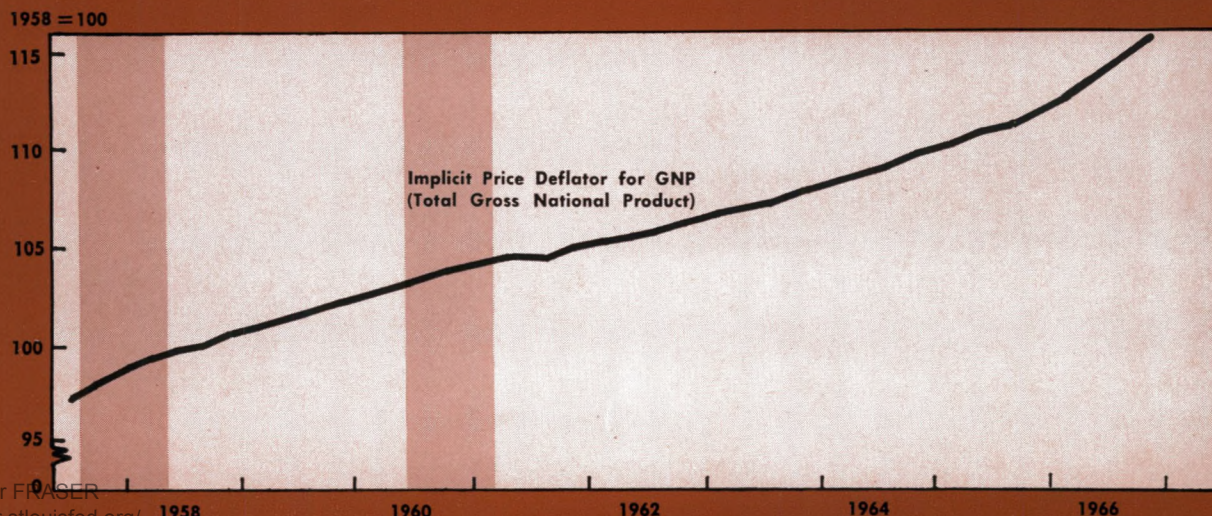
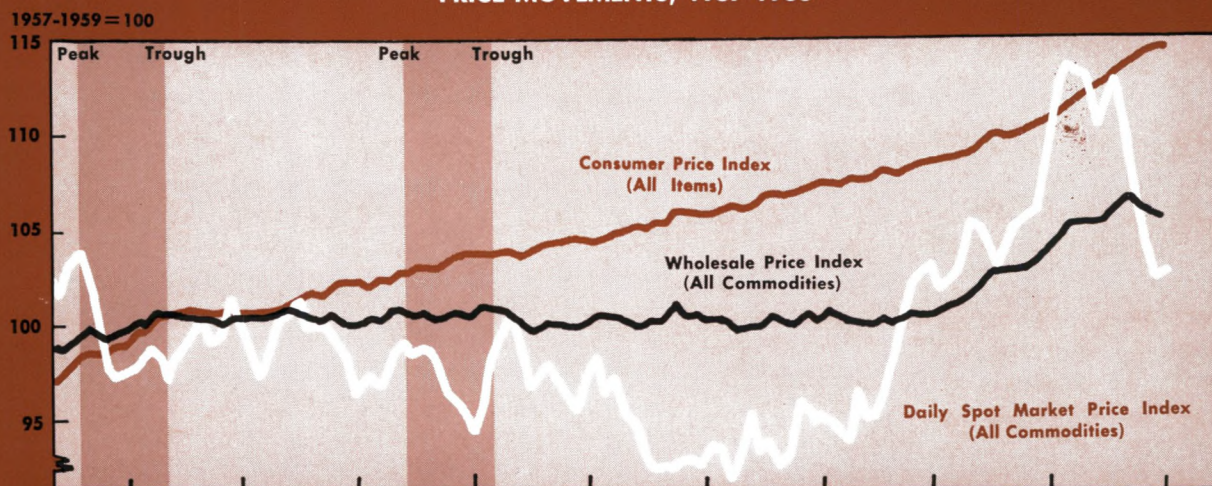
The recent price movements have differed from those in the earlier years of the present business expansion not only in intensity, but in mix. Factors

underlying price movements also changed during the six years of the expansion.

Price Movements, 1961—Mid-1964 The first three and one-half years of the present expansion were characterized by remarkable price stability. The consumer price index moved up in that period at a rate of about 1.2% per year, substantially the same rate as in 1957-1960 and considerably below the rate in the earlier years of the 1950's. Most of the increase was accounted for by a steady rise in the prices of services and sporadic hikes in food prices. Nonfood prices showed little advance.

Wholesale prices exhibited a remarkable stability over the first three and one-half years of the business expansion. The all commodities wholesale price index in June 1964 was no higher than at the trough of the 1960-1961 recession, and was fractionally lower than at the beginning of 1958. Little change

PRICE MOVEMENTS, 1957-1966



was registered in any of the three major components of the index: processed foods, farm products, and commodities other than farm products and foods (all industrials). In addition, the indexes for the major groups within the industrials component showed little or no change during the period. Thus the stability was general and pervasive and not occasioned by offsetting movements in the prices of particular groups of commodities.

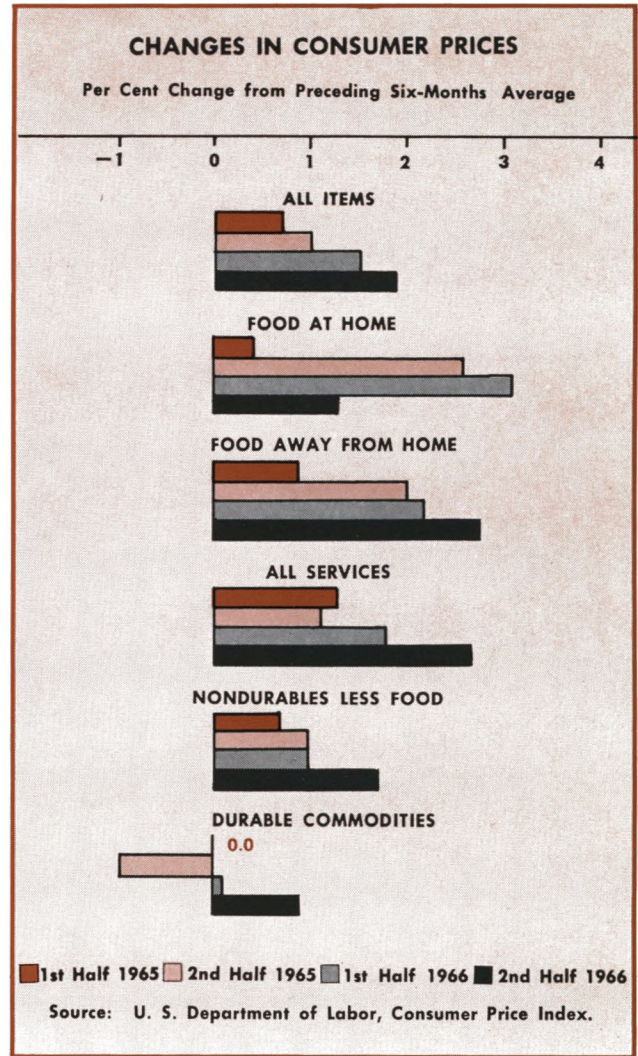
The daily spot market price index, on the other hand, declined in the second year of the expansion and then leveled off during 1963 and the first half of 1964. This index, which is compiled from daily prices of 9 foodstuffs and 13 raw industrial materials as quoted on commodity markets and organized exchanges, is the most volatile of the major price measures. Its restricted coverage makes it more sensitive to current market developments than the comprehensive wholesale price index, which covers more than 2,200 items.

The implicit price deflator for total gross national product rose gradually throughout this period. The quarterly change in these prices averaged only 0.3 of an index point.

Price Pressures, Mid-1964—Mid-1965 Definite upward pressures on prices began to develop in the second half of 1964 and continued to build up in the first half of 1965. The spot market price index rose from 95.8 in July to 103.2 in December 1964. For the first half of 1965 it averaged 103.7, a 3.4% increase from the preceding 6-months average. Most of the price rise was in the area of raw industrials which account for approximately 60% of the total of the 22 commodities in the index.

The comprehensive wholesale price index began to advance in the latter half of 1964 and increased at a considerably faster rate during the January-June 1965 period. This index rose from 100.4 in July 1964 to 102.8 in June 1965, an increase of 2.4%. Prices of farm products and processed foods, which account for around one-fourth of the index, were responsible for most of this increase. Prices of industrial commodities moved upward moderately. Changes in this component of the wholesale price index usually lag the changes in spot market prices of raw industrials.

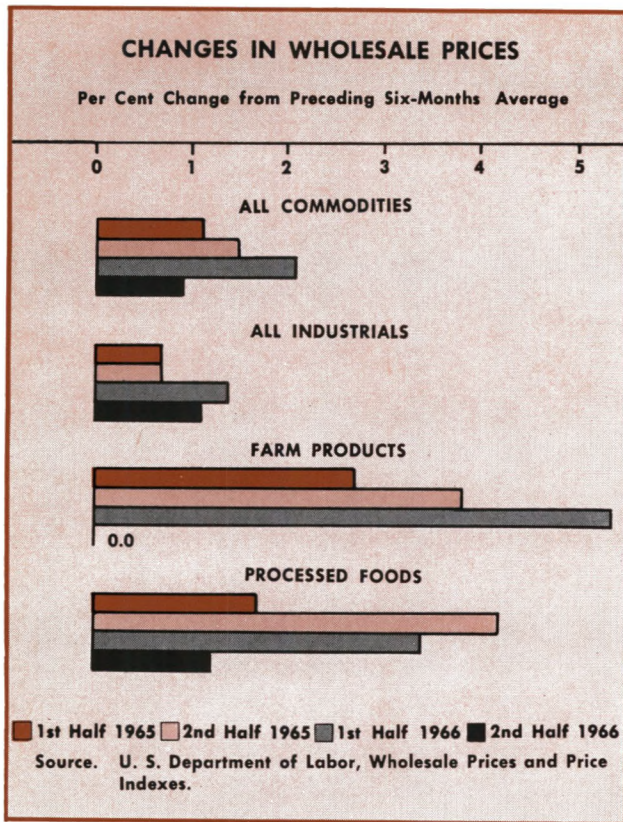
Consumer prices also began to show signs of inflationary pressures. The general index rose from 108.3 in July 1964 to 110.1 in June 1965. Most of the increase, however, occurred in the second quarter of 1965, and was caused primarily by changes in food prices. The index of consumer food prices hovered around a 106.9 average in the period July



1964 through March 1965, rising 0.4 in April, 0.6 in May and a whopping 2.2 points in June 1965. The earlier rise in wholesale prices of foods thus extended into the consumer sector. Throughout this period, the indexes of nonfood commodities and of consumer services continued their upward movement at approximately the same rates as in the earlier stages of the expansion.

The index of prices received by farmers also recorded substantial increases in the first half of 1965, compared to the last six months of 1964. The average for the crops component was up 2.8% and the livestock component was higher by 4.2%.

Thus, by mid-1965 the major price indexes began to reflect inflationary pressures building up in the economy. The increased spending ability of business and consumers partly caused by the 1964 and 1965 cuts in corporate and personal income taxes added to demands in the private sector. From the second quarter of 1964 to the second quarter of 1965,



personal consumption expenditures rose 7.2% and gross private domestic investment increased 13.0%. In contrast, government purchases of goods and services advanced only 3.2%.

Intensified Pressures, Mid-1965—Mid-1966 Excessive demand developed further after mid-1965. Outlays for Vietnam grew rapidly after mid-1965, placing additional pressures upon an economy that was already running close to capacity. As a result, unused plant capacity and excess labor resources continued to narrow.

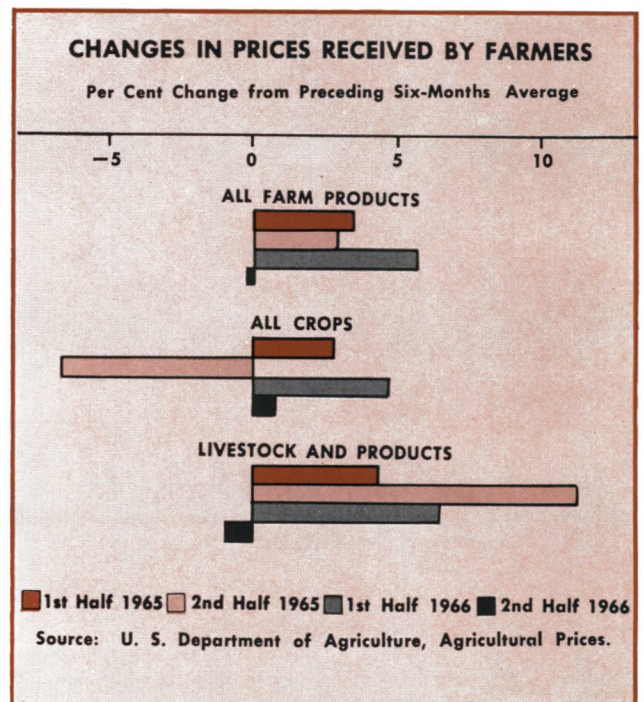
Capacity utilization rates in manufacturing remained at 89% throughout 1965, ran at 91% for the first three quarters of 1966, but edged down to 90% in the last quarter. In contrast, the rate was 78% in the first quarter of the expansion.

Critical shortages of manpower also developed during late 1965 and were evident throughout 1966 as business, already under pressure by civilian demand, geared to meet increased defense orders, and as available manpower was reduced further by stepped-up draft calls. The unemployment rate, which dropped from the current expansion's high of 7.1% in May 1961 to 4.7% in June 1965, declined to 4.1% by year-end. Throughout 1966 the rate hovered around 3.9%.

A large share of the advances in the broad price indicators was caused by the sharp rise in food prices that began in the fall of 1964 in the wholesale sector and in the spring of 1965 in the retail sector. The food component of the consumer price index, the wholesale price index and the daily spot market price index all increased at faster rates in the second half of 1965 than in the first half. The percentage increase was even greater during the first six months of 1966 except in the case of processed foods.

The overall index of prices received by farmers for all farm products continued to advance through mid-1966. The rise in the latter half of 1965, however, was caused completely by higher prices for livestock and livestock products. On the basis of 6-months averages, these prices were 11.2% higher in the second half of 1965 than in the first half, and they rose an additional 6.5% in the first half of 1966. On the other hand, prices received for crops fell by 6.7% in the second half of 1965. While this downturn was reversed in early 1966, the subsequent increase did not bring the 6-months average of the crops component of the index to the high reached in the first half of 1965.

Food prices have been affected more by supply factors than by demand pressures upon available resources. For example, farmers began to curtail hog production in the summer of 1964, and the supply of pork and pork products had reached a low level by the next summer. The dramatic rise of pork prices which followed is now history.



ERRATUM

In the March 1967 issue of the *Monthly Review*, the article titled "Textiles" reported incorrect figures. The error is contained in the last two sentences of the first paragraph of the right-hand column on page 7. These two sentences, corrected, should read:

The total number of establishments has risen from 88 in 1939 to 1,625 in 1963, an increase of almost 1,747%. The total number of employees climbed to 391,143 in 1963 from 14,275 in 1939, an increase of 2,640%.

Prices charged for services, which account for over one-third of the total consumer price index, continued to advance. Their average for the first six months of 1966 was 1.8% above that for the last half of 1965, which was 1.1% above their average for the first half of the year. Also prices of non-durable goods, excluding food items, continued to advance and prices of durables which had declined in 1965 began to edge upward in 1966.

Industrial commodity prices moved up in the wholesale markets as a direct result of expanding demand pressures from foreign as well as domestic sources. The index of industrial prices in the comprehensive wholesale price index averaged 104.2 in the first half of 1966; the per cent rise from the

services, however, continued to rise at a steep rate, and those for consumer nonfood commodities remained at a high level. Increases in the overall consumer price index led to additions to wages in those industries where contracts have cost-of-living clauses and to demands for wage increases in other industries.

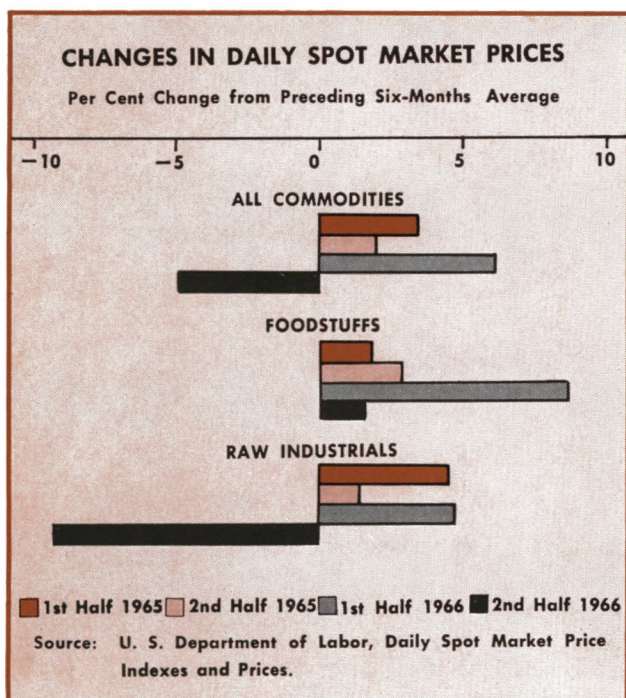
The wholesale price index declined in both October and November from its August-September high and in December remained unchanged from the November level. Here again the decline was accounted for primarily by prices of farm products and processed foods. The average prices of all industrial commodities increased at a substantially lower rate in the last half of the year than in the first half. Prices of crude and intermediate industrial materials peaked around mid-year, reflecting the drop in prices of spot market raw industrials.

A more significant factor in the wholesale sector, however, was the continued rise of producer finished goods prices, which added to production costs. The December-to-December advance of this component was 4.0 points, 1.6 being added in the last quarter.

Labor costs also rose significantly. The index of labor costs per unit of output in manufacturing, which had remained relatively stable throughout the expansion, rose 2.6% in the last six months. Higher operating costs cut corporate profits, which remained at peak levels in the first two quarters of the year, but declined 1.1% in the third. Recent reports indicate a further decline occurred in the final quarter.

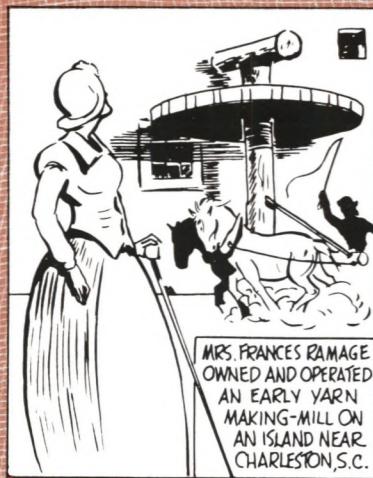
Costs were partly responsible for the slowing in the capital spending boom which has been a major sustaining factor in the present expansion. According to the GNP accounts, the decline in expenditures for nonresidential structures evident since the first quarter was offset by a continual advance in expenditures for durable equipment. The fourth quarter rise for fixed nonresidential investment was only 1.6% or \$1.3 billion. Inventory accumulation, however, amounted to \$16.4 billion. Personal consumption expenditures rose by \$4.2 billion compared with a \$9.8 billion increase in the third quarter. The slackening in the rate of growth in private final sales, however, was offset in part by a rapid rise in expenditures for national defense and State and local government outlays.

Although inflationary demand pressures had eased in the final quarter of the year, many crosscurrents in the economic picture at the turn of the year make it difficult to forecast price changes. Much depends on future costs of the Vietnam war, on the size of the large number of upcoming wage settlements, and the course of public policy, both monetary and fiscal.



average of the last half of 1965 was double that for the two preceding 6-months periods. The price index of raw industrials on spot markets rose from an average of 113.9 in the first half of 1965 to a 115.4 average in the next 6-months period and to a 120.8 average in the first half of 1966.

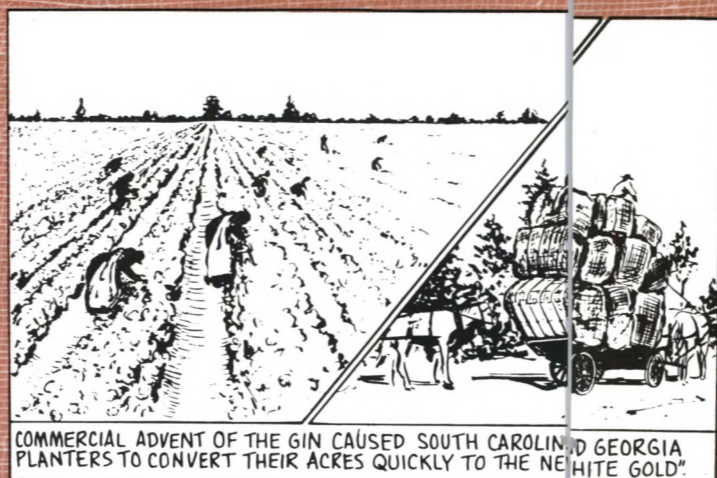
Cost Pressures, Second Half of 1966 In the last half of 1966 and particularly in the fourth quarter, prices of some lines softened. In November and in December, the consumer price index increased by only 0.1 of a point compared with a month-to-month average rise of 0.4 of a point for the period January through October. The slower rate of increase in the last two months of 1966 was accounted for primarily by a drop in food prices. Prices charged for



MRS. FRANCES RAMAGE OWNED AND OPERATED AN EARLY YARN MAKING-MILL ON AN ISLAND NEAR CHARLESTON, S.C.



YOUNG WHITNEY INVENTED HIS "COTTON ENGINE", AS IT WAS FIRST KNOWN, WHILE VISITING AT A PLANTATION IN GEORGIA.



COMMERCIAL ADVENT OF THE GIN CAUSED SOUTH CAROLINA AND GEORGIA PLANTERS TO CONVERT THEIR ACRES QUICKLY TO THE NEW "WHITE GOLD".



EQUIPMENT OF THE LINCOLN COTTON FACTORY WAS HAULED OVERLAND FROM PHILADELPHIA TO LINCOLNTON, N.C.



THE ROCK FOUNDATIONS OF THE FIRST ROCKY MOUNT MILLS STAND AS FIRM TODAY AS WHEN THEY WERE LAID.



MT. HECLA MILL IN GREENSBORO, N.C., WAS THE FIRST SOUTHERN PLANT TO USE STEAM POWER. WOOD FROM NEARBY FORESTS SUPPLIED THE FUEL.

Textiles

ORIGINS OF INDUSTRIES

The textile industry has evolved into one of the Fifth District's leading industries from its meager beginnings in South Carolina in the late 1700's. There were a number of significant attempts to start textile manufacturing in the South during the colonial period. One of these was made by a widow, Mrs. Frances Ramage, on John's Island near Charleston, South Carolina. Her efforts eventually failed; nevertheless, it was a beginning in the development of the industry in the South. The invention of the cotton gin by Whitney in 1794 gave great impetus to the textile industry. The South benefited immediately since the new machine enabled cotton to be ginned in large quantities.

Successful attempts in textile manufacturing in the early nineteenth century were made by Michael Schenck near Lincolnton, North Carolina and Joel Battle at Rocky Mount, North Carolina. Schenck's mill at Lincolnton was destroyed by fire during the Civil War, but the one at Rocky Mount is still in operation. It is characteristic of the old multi-story buildings constructed prior to the modern, streamlined one-story plants. William Gregg was another pioneer in southern textiles. In 1845, he founded a mill in Graniteville, South Carolina which also is still in operation. In addition to producing some of the early pioneers in the industry, the South also claims to be the first to use electricity in textile production.

The Civil War left the South in a state of economic chaos. However, it was in this post-war period that the textile industry began to emerge as one of the region's leading industries. It was here that textile manufacturers found abundant labor and land, low taxes and easy access to its major raw material—cotton. But the greatest strides in the textile industry have occurred in the years since World War II. No longer is cotton the only raw material. The emergence of man-made fibers—Dacron, nylon, Orlon, Acrilan, and many others—have completely revolutionized the industry. These synthetic fibers have encouraged investment in the modernization of plants and equipment, and in research, advertising and marketing. With new technology the necessity for skilled labor has increased and the quality of the product has been enhanced. Since the war, the industry has more than doubled in size in the Fifth District. The total number of establishments has risen from 88 in 1939 to 1,625 in 1963, an increase of almost 85%. The total number of employees climbed to 391,143 in 1963 from 14,275 in 1939, an increase of 174%.

Thus, it can be said that the Fifth District textile industry has come a long way from Mrs. Ramage's mill in South Carolina. It is an industry that is geared to modernization and to meeting the demands of the day. It is one of many industries that have brought new prosperity to the South.



GREGG'S FIRST MILL BUILT IN GRANITEVILLE, S.C. IN 1846, REMAINS IN OPERATION TODAY.



INDUCEMENTS OF FREE LAND, BUILDINGS, CHEAP POWER AND LOW TAXES PROMPTED NORTHERN INTERESTS TO TAKE PART IN THE SOUTH'S INDUSTRIAL EXPANSION.



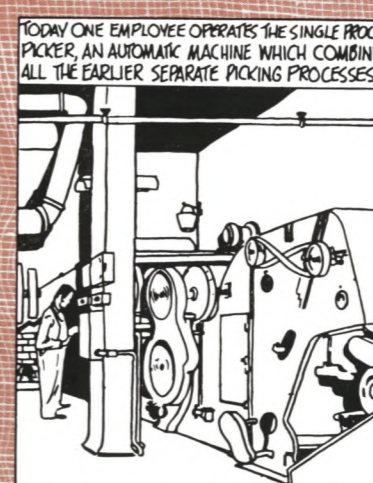
MANY NORTHERN MILLS ALSO MOVED SOUTH TO BE NEAR THE SOURCES OF RAW COTTON.



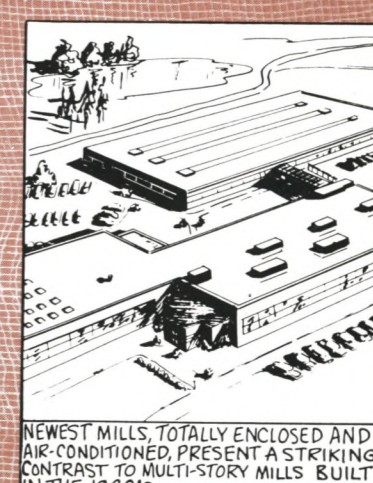
THE FIRST USE OF AN ELEVATOR DRIVE IN A COTTON MILL, AT ROCKY MOUNT, 1893, MARKED A MILESTONE IN INDUSTRIAL PROGRESS.



MECHANIZATION OF A GREAT INDUSTRY NOW EXTENDS TO THE COTTON FIELDS THEMSELVES.



TODAY ONE EMPLOYEE OPERATES THE SINGLE PROCESS PICKER, AN AUTOMATIC MACHINE WHICH COMBINES ALL THE EARLIER SEPARATE PICKING PROCESSES.



NEWEST MILLS, TOTALLY ENCLOSED AND AIR-CONDITIONED, PRESENT A STRIKING CONTRAST TO MULTI-STORY MILLS BUILT IN THE 1920'S.



Fifth District bankers register upon arrival at the Fed.



The tour begins.



Check clearing by high speed electronic equipment is explained.

OPERATIONS

AND

POLICY

SEMINAR

Plans are now underway for the tenth annual Operations and Policy Seminar of the Federal Reserve Bank of Richmond. The two-day seminar, which has been offered each spring for nine years, has attracted a total of almost 2,000 member bankers from throughout the Fifth Federal Reserve District. As a result of numerous requests from nonmember banks, the seminar will be opened this year to non-member as well as to member bankers. To accommodate the anticipated additional enrollment, two identical sessions will be held in April, one on April 3-4 and the other on April 24-25.

The first day of the seminar will open with registration and a comprehensive tour of the Bank, conducted by the Bank's corps of tour guides. After the tour, guests will assemble in the auditorium of the Bank for a series of discussions regarding the day-to-day operating relationships between the Reserve Bank and District commercial banks. Sufficient time will be allowed for question and answer periods following each session.

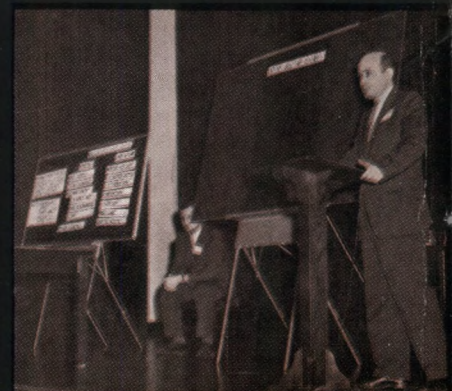
Research Staff discusses "What's Behind Your Money?"



Members of the Reserve Bank's staff meet the visiting bankers.



A discussion of factors affecting member bank reserves.





The nerve center of the Federal Reserve System communications network is at the Richmond Reserve Bank's Telegraph and Switching Center.



Approximately 250 bankers from throughout the Fifth District attend the Seminar each year.

There will be a change of subject matter on the morning of the second day, when the session will feature a discussion of monetary policy and its implications for commercial banks. Included will be a review of the nation's monetary structure as well as a rundown by top Bank officials on the objectives, mechanics, and problems of monetary policy.

The seminar will adjourn following lunch on the second day. Persons attending the meeting will be luncheon guests of the Bank both days.

There is the feeling, both at the Reserve Bank in Richmond and among bankers throughout the Fifth District, that the seminar provides an unusually good opportunity for many bankers, particularly the younger ones, to see firsthand the operations of a Federal Reserve Bank, meet some of the Bank's officers, and gain a better understanding of the effects of monetary policy on the commercial banking business.



Top: The First Vice President relinquishes the rostrum to the President who, right, welcomes the bankers. Bottom: The Chairman of the Board of Directors of the Richmond Bank speaks.

Comments on monetary policy.



Summation of the conference closes the Seminar.



The Richmond Reserve Bank hosts a luncheon on both days of the Seminar.



THE FIFTH DISTRICT



BANKING DEVELOPMENTS IN 1966

After more than five years of vigorous growth, banking activity in the Fifth District slowed to a more moderate pace in 1966. Nonborrowed reserves in the District fell steadily from December 1965 until May, pulling down total reserves in spite of heavy borrowing. More reserves were available in the second half of the year, but total reserves rose substantially above the July level only in the last few weeks of the year.

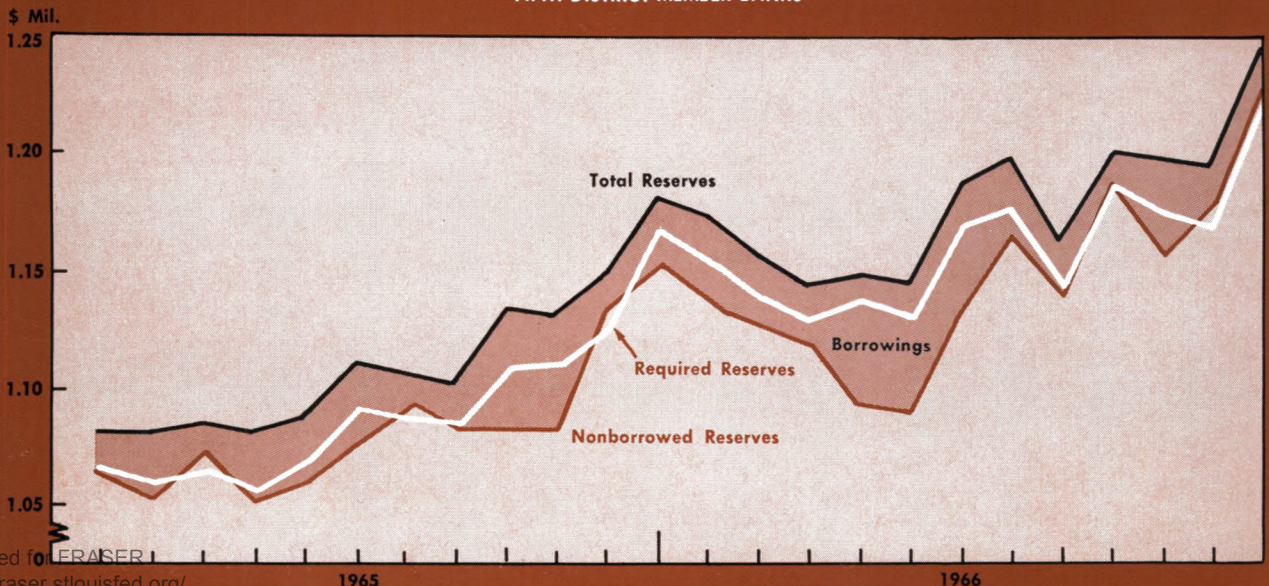
The discount rate remained at $4\frac{1}{2}\%$ throughout 1966, although heavy loan demand pushed bank lending rates to record levels. But in spite of the wide gap between the discount rate and bank lending rates, member bank borrowings generally remained at levels comparable with those of the previous year.

Loans and Investments The slowdown in the rate of growth of Fifth District banking activity last year is evident in every category of loans. Gross loans at weekly reporting banks grew less than 9% in 1966, compared with an increase of over 16% in 1965. All major loan categories expanded at a slower pace. Commercial and industrial loans rose less than 13% last year, compared with 16% in the previous year; but the greatest weakness appeared in real estate loans. They expanded only about 10% after rising almost 16% in 1965.

Total investments at District weekly reporting banks declined slightly last year, compared with a very small increase in the previous year. The drop was the result of a larger percentage reduction in holdings of U. S. Government securities and a smaller gain in holdings of other securities, primarily municipals. Many banks liquidated sizable amounts of municipals as well as short-term governments in order to meet intense loan demand. The net reduction in investments and slower growth in loans held the increase in total credit extended by District weekly reporting banks to less than 6%, compared with more than 11% in 1965.

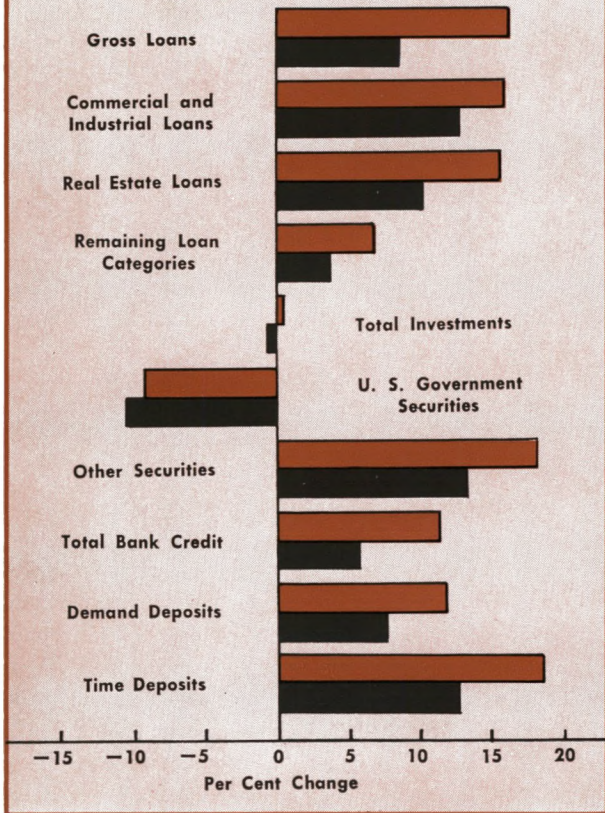
Deposits Growth in both demand and time deposits was well below the 1965 level, but the rate of growth of time deposits did not fall as much in the Fifth District as it did in the country as a whole. At all U. S. weekly reporting banks, time deposits rose only about 5% in the first half of 1966, compared with 9% in the first half of 1965. They continued to rise in July, but fell sharply in the next three months, and even after a substantial upturn in the last few weeks of the year, they ended the year with about a 5% annual increase, compared with a gain of over 15% in 1965. At Fifth District weekly reporting banks, however, time deposits rose almost

RESERVES AND BORROWINGS
FIFTH DISTRICT MEMBER BANKS



CHANGES IN LOANS, INVESTMENTS, AND DEPOSITS FIFTH DISTRICT WEEKLY REPORTING BANKS

1965 1966



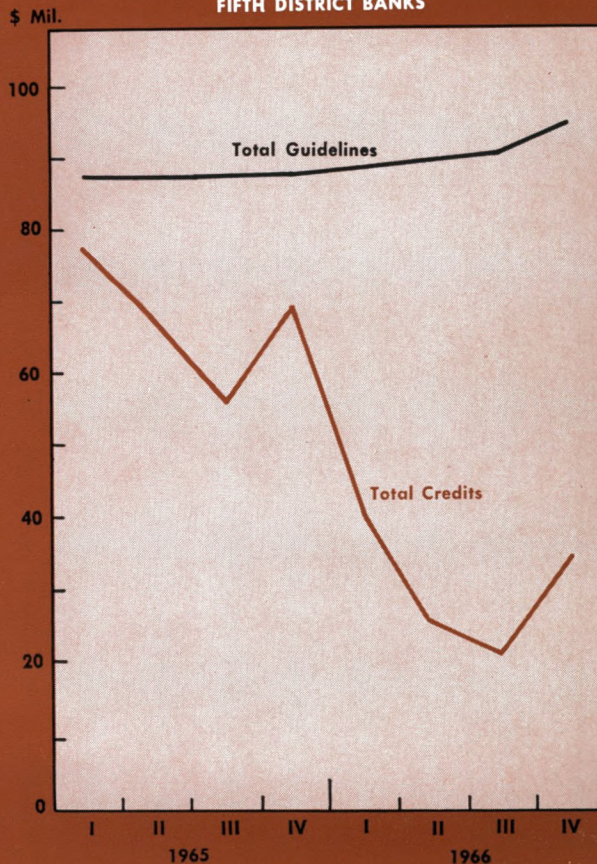
as rapidly in 1966 as in 1965 through the first half of the year. In the second half, growth lagged below the 1965 rate, but for the year as a whole, time deposits at District weekly reporting banks rose almost 13%, compared with 17% in 1965.

The more favorable time deposit experience in the Fifth District apparently was due primarily to a different pattern of certificate of deposit sales. During the first six months of 1966, while the total volume of large negotiable certificates of deposit outstanding in the country as a whole was rising from \$16 billion to more than \$18 billion, the volume of such certificates outstanding in the Fifth District was substantially reduced. The total volume of certificates of deposit reported jumped sharply at the end of June when the number of weekly reporting banks was increased; but a few weeks later, the volume outstanding for all U. S. weekly reporting banks began to fall precipitously, while the volume reported by Fifth District banks continued to rise. The volume of certificates for the nation as a whole fell from over \$18.5 billion in August to less than

\$15.5 billion in November, while the volume at District banks grew from \$291 million to \$310 million.

Foreign Lending The Federal Reserve's monetary policy apparently had a substantial impact on foreign lending by Fifth District banks. Under the President's Voluntary Foreign Credit Restraint Program, the guidelines for foreign lending were liberalized in 1966. The guidelines called for each bank to limit its outstanding foreign credits in 1965 to no more than 105% of the amount outstanding at the end of 1964, and the 1966 ceiling was arrived at by adding 1% each quarter to the 1965 ceiling. Credits outstanding dropped well below the guidelines in 1965, apparently reflecting the efforts of lending banks to comply with the request that their foreign lending be curbed. But in the first three quarters of 1966, actual credits fell even further below the guideline ceilings. The size of the gap suggests that the curtailment of foreign lending was due largely to the tightness of money. The banks engaged in foreign lending were also those which

FOREIGN CREDIT UNDER VOLUNTARY CREDIT RESTRAINT PROGRAM FIFTH DISTRICT BANKS



CHANGES IN NUMBER OF BANKS AND BRANCHES

December 1965 to December 1966

<u>All Commercial Banks</u>	<u>D. C.</u>	<u>Md.</u>	<u>Va.</u>	<u>W. Va.*</u>	<u>N. C.</u>	<u>S. C.</u>	<u>Total</u>
Number of banks, beginning of period	15	122	262	187	146	129	861
New banks organized	....	1	4	2	....	1	8
Mergers and absorptions	1	1	15	....	10	3	30
Number of banks, end of period	14	122	251	189	136	127	839
Net change							- 22
 <u>Branches and Additional Offices</u>							
Number of branches, beginning of period	82	383	538	....	733	264	2,000
New branches established	5	30	44	....	51	32	162
Banks converted into branches	1	1	15	....	10	3	30
Branches discontinued	....	2	1	....	2	....	5
Number of branches, end of period	88	412	596	....	792	299	2,187
Net change							+ 187
<u>Change in Banking Offices</u>							+ 165

*Including six West Virginia counties which fall outside the Fifth District. Source: Board of Governors of the Federal Reserve System.

utilized their reserves most fully and were therefore hit hardest by the credit squeeze. When they were forced to ration credit, they apparently turned down foreign borrowers as well as domestic companies.

Banking Structure In 1966, the number of banks and branches continued to change rapidly in the Fifth District. The Virginia banking system is still

undergoing the metamorphosis set in motion in 1962 by an amendment to permit statewide branching through mergers; and in many parts of the District, new banks are being organized and existing banks are opening new offices to serve a growing population.

As in other recent years, the largest number of changes in bank structure occurred in Virginia. Four new banks were organized, but 15 were absorbed by merger, reducing the total from 262 to 251. Forty-four new branches were established, and all of the 15 merged banks were converted to branches. With one branch discontinued, the total rose from 528 to 596. There were 10 mergers in North Carolina, reducing the number of banks from 146 to 136. North Carolina led the District in new branches established with 51. Two branches were discontinued, and the total rose from 733 to 792.

In Maryland, there was one new bank established and one merger, leaving the total for the state unchanged at 122. There were 30 new branches opened, however, and with one conversion and one branch discontinued, the total rose from 383 to 412. One new bank was established in South Carolina, but three mergers pulled the total down from 129 to 127. South Carolina added 32 new branches to the three resulting from mergers, raising the total number of branches from 264 to 299.

No new banks were established in the District of Columbia. One merger reduced the total from 15 to 14. Five new branches were opened, and these, with the merged bank that was converted into a branch raised the total number of branches to 88. In West Virginia, two new banks were opened, raising the number in the state from 187 to 189. West Virginia does not permit branch banking.

CERTIFICATES OF DEPOSIT OUTSTANDING

