MONTHLY REVIEW

TWELFTH FEDERAL RESERVE DISTRICT

DECEMBER 1953 FEDERAL RESERVE BANK OF SAN FRANCISCO

TWELFTH DISTRICT FARES WELL IN THE FACE OF ADJUSTMENTS

The year 1953 ended on a note of caution with respect to what is in store for our economy during 1954. For the entire year, the economy moved to new high ground. In the Twelfth District, gains were made on many fronts; industrial production, most other nonagricultural activities, and retail sales all reached new highs. Agriculture was the only major sector that had less favorable results in 1953 than in 1952, as prices declined for a number of District farm products. However, over-all statistics tend to conceal other developments not so readily apparent as the decline in farm income which reflect downward pressures on the economy. The impact of a change in Federal spending policy, the effect of over-accumulation of inventories in some lines, a tendency for consumers to tighten their purse strings, and a low rate of mortgage commitments for several months all tended to dampen the rate of activity.

In the presence of these downward pressures one might expect a greater decline than has been experienced so far in the Twelfth District. A variety of forces have tended to offset the downward changes. Construction activity has been at a very high and, for part of the year, a rising level because of an unusually large volume of projects started early in the year. The growth of population in the past decade apparently is still creating additional demand for banking, real estate, and personal services—all of which expanded in 1953. In manufacturing, the continued growth of aircraft, electrical machinery, fabricated metals, chemicals, petroleum, and rubber output has been greater than declines in other industries.

District escaped full impact of change in Federal spending

The revision of spending plans by the Federal Government expressed itself in several ways. Many civilian agencies had budget cuts which resulted in staff reduction. In addition, a number of emergency agencies disappeared as a result of control terminations, and military establishments also cut their staffs because of the end of hostilities in Korea and retrenchment in other programs. In almost every District state this resulted in cuts in Federal employment. California alone had a reduction of more than 20 thousand Federal jobs. Offsetting the decline in Federal jobs, however, was increased employment by state and local governments in a number of states. In Arizona, California, Nevada, and Oregon the rise in employment by state and local governments exceeded the decline in Federal jobs. Idaho had no net change in government employment as the gain in local government activities offset Federal cuts. The net effect of changes at the Federal and local levels in Washington was a slight drop in government employment, but in Utah government employment fell by the full amount of the Federal cuts.

As part of the attempt to obtain a better budget position, many Federal construction activities were reviewed and a number were cut sharply. The most pronounced impact in this District came in Utah where total construction declined owing principally to reduced Federal Government programs. In most other states, the expansion of private and local construction more than offset the decline in Federal building during the first half of the year. For the months after July, however, total construction authorized fell below its level in the corresponding months of 1952.

Another aspect of the revisions in the Federal budget involved cancellation and reduction of a number of contracts for military goods, particularly aircraft. This District, however, was affected very little by these cuts during 1953. Most of the cancellations involved either models scheduled for production outside the District or contracts let to engine and parts producers, of which the District aircraft industry has a smaller proportion than the aircraft industry of the rest of the nation. Reductions in future programs that were made by the Defense Department also had no immediate effect. Although ultimate goals were for the most part reduced, the backlog of orders remained largely undisturbed in District states generally, and was of such proportions in California and Washington as to require the expansion of plant activity during 1953. The elimination of some aircraft modification contracts forced a cutback, however, in defense plant activity in Arizona.

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Construction activity declines after strong start

Construction activity in 1953 ran well ahead of 1952 reflecting an unusually large volume of building permits early in the year. Except for June, when a large number of construction workers were idled by a labor dispute in northern California, construction activity rose steadily through August. Starting in September, activity slackened somewhat but remained above 1952. Residential permits in the District were at a record rate from January through April and contributed substantially to the gains for the nation as a whole. Nonresidential construction advanced sharply over 1952 levels from January through May. A tightening of the residential mortgage market prevented builders from taking on programs after May quite as large as those they had anticipated. As a result, residential building authorized started running below the previous year's level and dropped sharply during the fall months. Nonresidential construction, in contrast, was maintained fairly evenly through the summer and early fall and tended to offset the weakness in residential construction during a number of months. In view of the cut in Federal nonresidential authorizations, this record reveals the strength of private nonresidential building demand and local government construction programs.

Industrial production expanded

The large backlog of military and civilian demand resulted in a steady expansion of industrial output and employment during most of the year. Military aircraft production continued to expand because of the large volume of unfilled orders discussed above. Defense orders also resulted in moderate increases in the output of electrical machinery, ordnance, and instruments. Fabricated metals were produced in greater quantity not only for military needs but because civilian demand also grew. Population and income growth induced higher paper, petroleum, rubber, and leather goods production.

In contrast, lumber production tended to weaken during the year. The demand for Douglas fir, which accounts for a major part of the District lumber output, fell somewhat because of a small decline in housing starts nationally. In addition lumber retailers, facing a weak market, allowed inventories to run off, and Canadian producers shifted some of their output to this country as their overseas demand dropped.

Activity in a number of industries during the early part of 1953 was stimulated by inventory accumulation. As the year progressed this gave rise to weakness in a number of lines. For the first time in more than four years the District steel industry cut its employment, and output fell below capacity. In food processing the declines in activity toward the end of the year turned out to be greater than would be expected on a seasonal basis. Production of nonelectrical machinery also dropped from the first-quarter level. The principal force in this industry was a decline in sales of farm equipment which resulted in a piling up of inventories. Automobiles were a fourth industry in which high inventories in the nation as a whole led to cuts in production and employment in automobile assembly plants in the District as well as in the nation. The weaknesses in these industries caused total employment and production to fall below the record levels of late summer, but the over-all rate of activity was still at a level above that in 1952 toward the end of the year.

California shows most strength in manufacturing

California made the principal contribution to an increase of almost 5 percent in manufacturing employment in the District for the year as a whole. The largest percentage gains in the state were recorded in aircraft and electrical machinery employment. Automobile employment, despite a strong decline from April through September, averaged more than in 1952 because of the large expansion of automobile assembly facilities in California early in the year. Gains were also reported for ordnance, instruments, fabricated metals, paper, printing, chemicals, petroleum, rubber, leather, and even lumber employment. Increased reliance by California builders on timber stands within the state boosted the lumber industry in the state, in the face of the decline in lumber production for the District as a whole. Toward the end of the year, however, the gain in manufacturing employment between 1952 and 1953 narrowed because of the lower level of canning employment and a declining number of jobs in lumber, metals, machinery, petroleum, and rubber.

Pacific Northwest manufacturing showed less resistance to weakness

Oregon was the only state which experienced a decline in manufacturing employment for the year as a whole. In addition to a decline in lumber employment the number of jobs was reduced in furniture manufacture. Weakness also appeared from time to time in other durable goods industries and in paper, printing, and textiles and apparel. Washington experienced cuts in lumber and furniture employment, but a substantial increase in aircraft employment and gains in aluminum, steel, and fabricated metals jobs over 1952 resulted in a moderate gain for the year as a whole in Washington manufacturing employment. Toward the end of the year, however, declines appeared in a wide range of industries, including steel, aluminum, fabricated metals, food, and paper.

Manufacturing employment pattern varies in other District states

Idaho showed very little change in manufacturing employment from 1952 to 1953, the decline in lumber having been offset by gains in other industries. Late in the year, however, weakness spread to many industries, and manufacturing employment started falling behind 1952. Utah showed a fair gain for the year as a whole, partly reflecting the depressing effect of the 1952 steel strike, but also due to growth in the textile and apparel, chemicals, and petroleum industries. During the last quarter, employment drops in the primary metals, food, furniture, and stone, clay and glass industries forced total manufacturing employment below the1952 level. Nevada and Ari-

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zona made moderate gains for the year as a whole. Arizona, however, exhibited a downward trend after March because of reduced aircraft employment.

Retail sales react to changes in economic activity

For the first half of the year retail sales in the District were high, but starting in the summer sales in many lines slipped from the spring levels. The most persistent declines appeared in sales of furniture and appliances. Apparel sales held up rather well and sales of food and gasoline continued to expand through most of the year. Sales of automobiles increased substantially over 1952, partly because production last year was limited by materials allocations and the steel strike. Production tended to exceed demand in 1953 and the pressure of large inventories toward the latter part of the year forced many dealers to further liberalize their trade-in policies in order to stimulate sales. The net effect of the varied experience in different lines and the greater weakness toward the end of the year was a level of sales for the year as a whole only a little above that of 1952.

The decline in general merchandise sales, as evidenced in the department store figures, started in early summer when employment and income were still growing. One cause of the decline was the sensitivity of consumers to the scattered layoffs in Federal Government and private industry which had been announced. As the year progressed and declines in some lines became more apparent, an air of uncertainty was created even though the over-all level of employment continued high. The uncertainty led some consumers to spend less even if their own jobs were secure. One retailer explained the situation as one in which "customers don't have an optimistic outlook."

Agricultural output high, but prices and income fall

The price-cost squeeze, continued high production, and further accumulation of stocks of several important farm commodities were agricultural highlights of 1953 in the District and for the United States generally. Although farmers paid slightly lower prices in 1953 for some production items than during the previous year, the prices they received for their products declined even more. By December 15, 1953 farm prices had declined 6 percent from the same date in 1952 and 17 percent from December 15, 1951. The parity ratio now stands at 91 compared with 107 on December 15, 1952 and 95 on January 15, 1953. Market prices of most supported commodities have averaged below support levels during 1953.

The 1953 output was about equal to that of 1952 and this high output together with reduced exports and Government price support activities resulted in a rapid accumulation of stocks of the more important District as well as national farm commodities. Stocks of cotton and wheat have more than doubled in the last year and large increases also have occurred in stocks of corn and of fats and oils. Marketing quotas and acreage allotments have been declared on 1954 production of wheat and cotton.

Prices received by District field crop producers followed the general price decline of the nation's agricultural products and, as of November 15, 1953, were considerably below those received at the same time last year. In the case of potatoes, prices were cut almost in half. Cattle and sheep prices also were lower than last year. However, the downward price changes have been accompanied by increases in production and slaughter.

With the exception of peaches, plums, and a few other relatively minor commodities, smaller fruit and tree nut crops in 1953 have kept prices of these products at or above levels of last year. The 1953 grape crop in California was very much smaller than usual. An increased production in 1953 of vegetables for the fresh market and for processing was accompanied by lower producer prices. Gross income to District producers from fruits and vegetables was about equal in 1952 and 1953. Significant reductions in cash receipts from marketings of livestock and livestock products, however, more than offset a small increase in such receipts from sale of field crops. As a result, total cash receipts from District farm marketings in 1953 were slightly smaller than in the previous year.

THE RECENT COURSE OF BANK LOANS

Statistics on bank loans are among the most currently available economic series. Because bank loans are made to a large variety of businesses and individuals, changes in the published weekly series are often viewed as reflecting the more general changes in economic activity. Speculation as to the significance of changes in bank loans is particularly great in a year when the changes are sharp and do not conform to the usual seasonal pattern. Since 1953 has been such a year, there has been much speculation and interpretation concerning the significance of these changes, particularly in the last six months. To assist in the interpretation of these changes, this article will examine their extent, both for the Twelfth District and the United States, and discuss some factors relevant to any attempt to interpret the course of general business conditions by considering the character of changes in bank loans.

The sharpness of the changes since mid-1953 is evident whether the period selected for comparison is the comparable period in 1952 or the first half of 1953. The increase in total loans (except interbank) of weekly reporting member banks in the United States since July 1 of this year has been about one half the increase in the comparable period of 1952. The change is even more marked within the Twelfth District—the increase was 17 times greater in dollar amount in 1952 than in 1953. Most categories of loans have behaved the same way, their increases in the second half being less this year than last. One exception is loans on securities which have risen in the last half of this year, both nationally and in the District, while

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last year they declined. This rise is attributable in part to the larger cash borrowings by the Federal Government in the last half of this year and to a reduction in margin requirements to 50 percent in February 1953.

Consumer loans decline in Twelfth District

If the purpose of analyzing bank loans is to interpret changes in business conditions, attention is directed primarily to changes in loans to business and agriculture, loans to finance real estate, and loans to finance consumer goods. The last-named group of loans is included in Table 1 in the category of "other" loans, which are principally loans to consumers. In the first half of 1953 this category of loans showed the greatest increase of any group at weekly reporting member banks, both for the United States and this District. This expansion of bank credit reflected primarily the purchase of automobiles by consumers and was a continuation of an equally sharp increase in the last half of 1952. By contrast, in the second half of 1953 weekly reporting member banks in the Twelfth District decreased "other" loans by $74 million compared with a $181 million increase in the corresponding period last year. A similar contrast was evident in the country as a whole, "other" loans of weekly reporting member banks increasing only $59 million this year compared with a rise of $746 million in the last half of 1952.

There is need for caution, however, in using the weekly figures as a precise guide to what is happening to the volume of consumer credit outstanding at all District member banks. Data for consumer loans of all member banks are available only as of call report dates. September 30, 1953 is the latest of these for which the data have been tabulated. These data indicate that the volume of consumer loans outstanding at all member banks in the Twelfth District did not show as much of a downturn in the third quarter as appears from the change in the broader category of "other" loans of the weekly reporting member banks. Even after all possible adjustments have been made, there is a significant difference in the degree of change indicated by the two sets of data.

The call report data for all member banks provide details as to the composition of the changes in consumer loans which are not available for the "other" loan category of weekly reporting member banks. These data indicate that automobile instalment paper accounted for most of the third-quarter increase in total consumer loans of Twelfth District member banks. However, the increase in automobile loans was less than in the preceding quarter or in the third quarter of 1952. Repair and modernization instalment loans were the only other category of consumer loans that rose during the third quarter of this year at District member banks. All the other categories declined in volume, with perhaps the most significant decline occurring in nonautomobile retail instalment paper. Such paper amounts to only one-third of the amount of retail auto paper at District member banks, but the change was from an increase of over $15 million in the second quarter of 1953 to a decrease of nearly $7 million in the third quarter. The largest contraction, in comparison with the total volume of consumer loans outstanding, was recorded in the single-payment loan category. Loans in this group declined by nearly as much in the third quarter as they increased in the first half of the year.

Changes in consumer loans in the third quarter of this year in the country as a whole were not the same as those in the District. "Other" loans of weekly reporting member banks, instead of declining as they did in the District, rose by over $93 million. The call report data indicate that more categories of consumer loans increased in volume nationally than in the District. For all member banks, there were sharp increases in retail automobile instalment paper, in repair and modernization instalment loans, and in other instalment loans. The increase in retail instalment paper other than automobiles, however, was significantly less than the increase in the comparable period of the prior year. As in the District, a sharp decline occurred in single-payment loans.

In summary, then, there has been a substantially smaller increase on a national basis in "other" loans of weekly reporting member banks in the second half of this year than last and an actual decline in the Twelfth District. However, the detailed call report data for September 30 show an increase in the third quarter in consumer loans, excluding single payment loans, in both the District and the nation. In both cases this increase was less than last year and the relative increase in the District was smaller than in the United States.

Real estate loans continue to rise, but at slower rate

Real estate loans are particularly significant for member banks in this District; their dollar volume is nearly twice as large as that of consumer loans, and larger than that of loans to business. Since mid-year the amount of these loans outstanding at weekly reporting member banks within the District has increased by about one half the amount in the comparable period of last year. This is somewhat less than the national performance.

For more detail, it is necessary to look again at the call report data for September 30, 1953. Member bank loans on real estate within this District increased by nearly $43 million in the third quarter of this year. This compares with an increase of $73 million in the comparable quarter of last year and an increase of nearly $68 million

TABLE 1

CHANGES IN LOANS OUTSTANDING AT WEEKLY REPORTING MEMBER BANKS—TWELFTH DISTRICT AND UNITED STATES

July 2, 1952—December 31, 1952 and July 1, 1953—December 30, 1953

(in millions of dollars)

	Twelfth District		United States	
	July 1, 1953 Dec. 30, 1953	July 2, 1952 Dec. 31, 1952	July 1, 1953 Dec. 30, 1953	July 2, 1952 Dec. 31, 1952
Total loans (excluding interbank)	+40	+667	+1,675	+2,883
Commercial, industrial, and agricultural loans.	+39	+377	+ 795	+2,652
Loans on real estate....	+67	+139	+ 179	+ 283
Loans on securities.....	+ 8	— 30	+ 642	— 798
Other loans	—74	+181	+ 59	+ 746

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in the second quarter of 1953. Despite the over-all increase in mortgage loans, VA mortgages in the portfolios of member banks declined, a continuation of the trend recorded in each quarter during the preceding year. FHA and conventional loans, on the other hand, continued to increase. The pattern of change in real estate lending was not entirely uniform throughout the District, but increases in FHA and conventional loans and declines in VA loans were the rule.

Experience in the country as a whole was not exactly the same as in the District. Holdings of VA and FHA mortgages increased, but the even greater increase in conventional loans resulted in a more pronounced shift away from the lower-yielding insured or guaranteed mortgage nationally than within the Twelfth District.

It should also be noted that there was a decline in this District during the third quarter of $1.8 million in member bank real estate loans secured by farm properties. This decline was much greater than that recorded in the prior quarter and a reversal of the sharp increase which occurred in the first quarter of this year and the more moderate increases in the last two quarters of 1952. This change is remarkably uniform throughout the District, all states but Nevada showing moderate to sharp declines in farm mortgages held. Another sharp change with past experience, and also in a downward direction, is in real estate loans on commercial property in the District. These loans declined in the third quarter by over $4 million after a steady rise during the preceding year of $46 million. Declines in such loans in California and Washington were more than enough to offset increases in all other states of the District. National experience is at variance with that of the District, farm mortgages continuing to increase and mortgages on commercial property advancing very substantially.

Business loans fail to follow seasonal pattern

The loans which have attracted most attention in terms of their unusual behavior this year are those made to business, industry, and agriculture. Ordinarily, both in the United States and in this District, this group of loans declines in the first half of the year and then rises in the second half. This year was unusual in that these loans declined much less than was expected in the first half and increased much less than was expected in the second half of the year. In this District, the average level of business and agricultural loans outstanding at weekly reporting member banks was $57 million higher in December than in July 1953. On a seasonal basis they might have been expected to increase by over four times that much, or $269 million. The rise in the last half of the year did not quite offset the unusually small decline in the first half of the year—$59 million as compared with an expected $274 million decline—so that the net result has been a small decline in the average level of loans outstanding in December 1953 compared with December 1952. The pattern in the United States is very much the same as in the District. The decline in the first half of the year was less than one-third of what could be expected, and the rise since mid-year has been less than one-quarter that anticipated. The result has been a decline during the year of $166 million in the monthly average of business and agricultural loans outstanding at weekly reporting member banks in the country as a whole.

Separate figures for agricultural loans are not available on a weekly basis, but the evidence is that much of the expansion in commercial, industrial, and agricultural loans has come from this source. To judge by the September 30 call reports for all member banks in the District, there has been some expansion in agricultural loans, about $35 million in the third quarter, while loans to business declined by $20 million in the quarter. The increases in agricultural loans occurred in California, Washington, and Idaho, increases in the last two states being particularly large, but the other states in the District all show declines. Washington and Utah were the only states in the District which showed any increase in business loans, while the other states, particularly California, experienced decreases. The expansion in agricultural loans in the third quarter arises entirely from loans to farmers guaranteed by the Commodity Credit Corporation. This is probably true for the last quarter of the year as well. In this period the CCC marketed two issues of Certificates of Interest to finance price support loans on commodities. Commercial banks in this District purchased $45,828,000 of the November 9 issue and $42,211,000 of the December 17 issue. Since these certificates are reported in the weekly business and agricultural loans, they have swelled the volume of these loans.

To turn to business loans, some information on their composition is available from selected weekly reporting member banks, as indicated in Table 2. The industries in the District which have shown significant increases in

TABLE 2

REPORTED CHANGES IN COMMERCIAL AND INDUSTRIAL LOANS BY INDUSTRY AT SELECTED WEEKLY REPORTING MEMBER BANKS
TWELFTH DISTRICT AND UNITED STATES

July 2, 1952—December 31, 1952 and July 1, 1953—December 30, 1953
(in millions of dollars)

	Twelfth District		United States	
Manufacturing and mining:	July 1, 1953 Dec. 30, 1953	July 2, 1952 Dec. 31, 1952	July 1, 1953 Dec. 30, 1953	July 2, 1952 Dec. 31, 1952
Food, liquor and tobacco	+80	+ 86	+537	+ 791
Textiles, apparel and leather	— 7	— 2	—107	— 33
Metals and metal prod.	—12	+ 8	—326	+ 45
Petroleum, coal, chemicals and rubber	—11	+ 17	+137	+ 247
Other manufacturing and mining	+ 7	— 6	— 49	+ 40
Trade: Wholesale and retail	—39	+ 10	— 6	+ 161
Commodity dealers	+49	+ 87	+391	+ 673
Sales finance companies	—41	+ 61	—137	+ 506
Public utilities and transportation	—10	— 34	+ 91	+ 109
Construction	+ 1	— 9	— 24	+ 15
All other types of business	— 2	+ 28	+100	+ 152
Classified changes—net	+15	+246	+610	+2,705
Unclassified changes—net	+24	+129	+185	— 72
Net change in commercial, industrial and agricultural loans	+39	+375	+795	+2,633

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loans since July 1 of this year are those which are most strongly seasonal in character—the food, liquor, and tobacco industry and commodity dealers. The expansion in loans to the former industry is the only case in the District for which the increase roughly equals the increase in the comparable period of last year. Although loans outstanding to commodity dealers have increased, the increase is $38 million less than last year and reflects in part lower agricultural prices and their repercussions on both lenders and borrowers. The same behavior is evident on a national basis, where loans to commodity dealers by reporting banks increased by one half the increase in the same period of last year. Loans to food, liquor, and tobacco manufacturers have increased nationally by $254 million less than in the same period of last year.

The largest single element accounting for the discrepancy between the loan expansion this season and last is one facet of a subject already discussed—consumer credit. Sales finance companies, rather than being substantial borrowers as they were last year, have made heavy repayments of loans both here and in the nation. The reason is not that these companies have stopped lending, but that they have been borrowing from sources other than banks. The decline in consumer credit extended is partly reflected in the small decline in trade borrowing on a national basis and in the somewhat larger decline of such borrowing in the District. Another important element in the performance of loans since mid-year is the large repayment of loans by the metal working industry which was a net borrower last year.

In summary, loans to business and agriculture did not expand in the second half of 1953 nearly as much as could be expected on a seasonal basis. The principal element in this failure to expand seasonally is a general sagging tendency in the volume of loans to business. This was particularly notable in the repayments made by sales finance companies and the metal working industry. The strongest seasonal increase was in loans to the food, liquor, and tobacco industry.

The course of bank loans and some explanation of their behavior during the recent past is of interest chiefly because of the light it may shed on the future course of economic activity. Such an interpretation is beyond the purpose of this article. It is possible, however, to point out certain general factors which should be kept in view in making any over-all appraisal of loan changes.

Factors that have influenced the volume of consumer credit

In interpreting the general sweep of developments in consumer loans, whether for this District or for the United States, when prior periods are used for comparison purposes it is necessary to consider some of the forces at work in those periods. It is doubtful whether the period from June, 1952 to June, 1953 is sufficiently free from unusual developments in consumer lending to be useful as a "base" period. Consumer credit was restricted by regulation until May 1952. Lifting the regulations at about the same time that increased sales competition appeared in the durable goods markets resulted in an exceedingly rapid rise in consumer credit extended not only directly by banks but by other financial institutions and businesses that borrowed from banks. This increase was so rapid as to pose the problem, in the latter months of 1952 and in early 1953, as to whether the expansion in consumer credit was not more rapid than was consistent with economic stability. Some questions then being discussed were whether even a tight money market could affect consumer loans extended by banks, whether the ratio of consumer credit to consumer income was dangerously high, and whether this rapid expansion was stealing sales from the future. In light of these disturbing implications, it is doubtful whether this period of rapid rise in consumer credit is one against which current performance should be measured.

The course of consumer loans since mid-year has provided a partial answer to the first of these questions. The tight money market in the first half of the year was a factor in inducing banks in this District and the nation to re-examine their portfolios to determine whether their holdings of consumer loans were excessive. This examination, originally induced by a scarcity of reserves for loans of any sort, was not relaxed when the money markets became easier after July, since there then began to appear some uncertainty about the business outlook. The reaction to this situation among banks in this District was to screen applicants for consumer loans much more thoroughly.

It should also be observed that it is often difficult to continue a constant rate of increase in individual economic series. The rapidly growing practice of requiring regular and frequent amortization payments makes this particularly difficult in the lending area because of the resultant progressive growth of repayments to higher levels. In the first six months of 1953 consumer instalment loans outstanding at commercial banks increased by $1,151 million in the country as a whole, compared with an increase of $687 million a year earlier, according to the data on consumer credit published by the Federal Reserve Board. Since consumer loans are fairly short term, a rapid rise in loans in the immediate past places a strong downward pressure on loans outstanding because of repayment. The volume of consumer instalment loans *extended* by commercial banks from July 1 through November of this year is estimated at $4,736 million compared with the extension of $4,824 million in the same period of 1952. The fact that loans outstanding went up over this period only some $206 million this year compared with $852 million last year is due to the larger volume of repayment. In this period repayments were equal to 96 percent of extensions, while in the same period of last year repayments equaled only 82 percent of extensions.

Another factor of significance in interpreting changes in consumer credit outstanding at banks is the course of the money market this year. In the first half of this year, when the money market was relatively tight, many bor-

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rowers were denied loans by banks or had their loan applications reduced in amount. Borowers who were also lenders, such as sales finance companies, obtained some funds in the capital markets rather than from the banks. Recourse to other lenders occurred particularly on the part of those borrowers who thought that funds would be even less available and more costly after mid-year when the normal rise in business and agricultural loans was expected to take place and the Federal Government would be a heavy borrower. Individual borrowers may also have developed contacts with lenders other than commercial banks during this earlier period of stringency, and some of these contacts apparently have endured. One development which lends support to this conclusion is the fact that, even though the volume of consumer credit extended by commercial banks since July 1 of this year has been running at slightly lower levels than last, sales finance companies have extended more loans this year than last.

Some shift in the relative importance of various mortgage lenders

It is doubtful whether any other loan market has faced more serious problems than the mortgage market during the past two years. This is partly a result of the fixed interest rates permissible on VA and FHA mortgages. As interest rates in general rose, commercial banks became increasingly reluctant to enter into commitments for Government-guaranteed mortgages, both because of better current alternatives and because of the possibility of a future increase in mortgage rates. Although the rates on FHA and VA mortgages were increased in May of this year, the market had already outstripped the advance, and bankers remained reluctant to make loans, particularly VA mortgages, even at the new higher rates.

There also appears to have been some shifting away from borrowing from commercial banks to borrowing from other financial institutions. This is evident from Federal Reserve Board estimates which indicate that total mortgage debt outstanding increased by $2.5 billion in the third quarter of this year compared with $2.4 billion in the comparable quarter of last year. Yet it is estimated that mortgage holdings of all commercial banks rose by only $253 million in the third quarter of this year compared with an increase of $414 million last year. The most important element in this shift is the rapid increase in the assets of savings and loan associations which conventionally put nearly all of their funds into mortgages. In the third quarter of 1953 these associations loaned $2,149 million compared with $1,829 million in the same period of last year and increased their mortgage holdings by over $1 billion compared with $850 million in the third quarter of 1952. Life insurance companies also put $60 million more into mortgages in the third quarter of this year than last and increased their outstandings slightly more. Judging by the data for recordings of nonfarm mortgages of $20,000 or less, this shift from commercial banks to other lenders is more pronounced in this District than in the nation. The shift is particularly evident in Washington, Oregon, and Idaho.

Another factor which must be kept in mind in interpreting the change in real estate loans outstanding by commercial banks is the fact that their stock of mortgages is subject to more rapid liquidation than that of other financial institutions. Commercial banks actually recorded more mortgage loans from June through October of this year than in the comparable period of 1952. Their nonfarm residential loans outstanding, however, have not increased by as much this year. The explanation as to why recordings are greater than the increase in loans outstanding is to be found in the rising volume of repayments and in the sale of mortgages to other investors. The increment in outstanding nonfarm residential mortgages held by commercial banks from July through October of this year was less than 20 percent of the flow of mortgage recordings. In order to continue increasing their stocks of both real estate mortgages and consumer loans, (should that be considered desirable), commercial banks would have to heed the advice of the Red Queen to Alice in Wonderland: "Now, here, you see, it takes all the running you can do, to keep in the same place. If you want to get somewhere else, you must run at least twice as fast as that!"

Factors affecting the less than seasonal increase in business loans

Turning now to loans to business and agriculture, two elements appear important in interpreting the failure of such loans to rise both nationally and in the District: the decline in agricultural prices and the decline in the rate of expansion of consumer credit. The continued decline in farm prices means less funds are needed to finance the loans which are being made, and it has induced more caution on the part of both borrowers and lenders. The decline in prices has also led to a large extension of agricultural credit directly by the Commodity Credit Corporation rather than initially by banks. The CCC has used certificates of interest to finance part of its stocks. Since these certificates have been purchased by commercial banks, some of the initial diversion of lending has been reversed. The effect, however, has been to shift the expansion of agricultural credit by banks to a somewhat later time in the year than might otherwise have been the case.

The decline in the rate of expansion of consumer credit has had some effect on business borrowing since many businesses directly extend credit to purchasers and finance these extensions through bank borrowings. There is a clear difference in the extension of such credit this year from last year. From June through October of this year instalment credit from retail outlets increased by $33 million. In the same period of last year the increase was $265 million. The change in the first half of the two years is equally impressive. In the first half of 1952 retail instalment credit rose by $79 million; but this year it declined by $159 million. The same behavior appears in retail charge accounts which have increased by $30 mil-

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lion from June through October of this year compared with $118 million in the same period of last year. Again there was a much sharper contraction in the first half of this year than last. This change in consumer credit extended is probably most important in interpreting the behavior of loans to wholesale and retail trade.

Another element which has been mentioned as important in the slowdown of borrowing is the behavior of inventories. From July 1 through November, total business inventories increased $955 million this year compared with an increase of $1,769 in the corresponding period of 1952. In 1952, however, the increase in the last quarter was at a very high rate as stocks were being rebuilt after the steel strike. There was also a sharp buildup of business inventories in the second quarter of this year. On balance, the reduced rate of inventory accumulation recently is of some importance in comparing the changes in loans in the last quarter of this year and last.

There are some general factors affecting loans to business in addition to the decline in agricultural prices, the slowing down of growth in consumer credit, and recourse to other lenders. There has been a reduction in the need of corporations to borrow from banks in the last half of the year because of the operation of the Mills Plan. This plan has increased the proportion of corporation income taxes which must be paid in the first half of the year. Another factor which appears to be less important in the second half of this year than last is the desire to borrow because of fear of strain on the working capital position of the firm in the first half of the following year in order to pay income taxes. Corporations have been investing heavily in tax anticipation bills, which have been available in large volume in 1953, and these can be used to help meet their income tax payments in the first half of 1954. There has also been less need to borrow because of fear of further price increases; higher prices require larger amounts of credit to finance a given physical volume of goods. Industrial prices have tended to decline during the last half of 1953, whereas they had risen slowly during the preceding nine months.

The credit stringency in the first half of this year has also played a role in the less than seasonal expansion in the last half. Furthermore, the failure of loans to decline seasonally contributed to the sharp increase in interest rates in the first part of the year and undoubtedly caused many firms to reconsider their borrowing programs, the extent to which they used credit, and the efficiency with which they employed borrowed funds, while at the same time lenders were reconsidering their positions. This caution has carried over into the latter part of the year.

Another element of importance which has not been considered in any of the discussion covering particular groups of loans is that banks have not had large excess reserves as a result of this less than seasonal rise in loans. Security issues, primarily by the Federal Government, have been purchased in very large quantities by the banks. This has prevented interest rates on loans from falling as much as might otherwise have been the case and has kept the reins on lending tighter than would have been the case in the absence of such investments.

There is, of course, an important interconnection between changes in bank loans and the general business situation. Interpretation of this relationship is difficult, however, since the forces at work are not the same at all times. Some of the difficulties briefly mentioned in this article are of a general nature which would apply to any period under study, while others are specifically related to particular developments in 1953, especially the last half of the year. The principal difficulties which have general application are the following: (1) the question of the "normality" of previous periods used for comparative purposes, (2) recourse by borrowers to sources of funds other than commercial banks, (3) the problem of any loan series maintaining a constant rate of increase in the face of mounting repayments, (4) the fact that the experience of weekly reporting member banks (which provide the most current loan data) and of all member banks is not necessarily identical and, in fact, may sometimes be in direct contrast, and (5) the existence of particular circumstances, such as fixed interest rates for some mortgages or the effect of the Mills Plan, which have little to do with the general business situation. All these general factors have been relevant in interpreting relationships between bank loans and business activity in 1953. In addition, there are two specific factors that are relevant to the analysis for the last half of 1953 but do not have general applicability. They are (1) the failure of loans to contract seasonally in the first half of this year and (2) the repercussion of the relatively tight money market in the early months of this year on borrowing and lending habits and practices.

The relative importance of each of these general and specific difficulties in interpreting relationships between changes in bank loans and changes in business activity will vary from time to time. Consequently it is not possible to draw the simple conclusion that a decline or rise in the volume of bank loans outstanding automatically means that business activity is declining or rising. The principal purpose of this article has been to expose some of the limitations of the assumption of any very close and invariant relationship between weekly reporting bank loans and the business situation, particularly when the minimum business data necessary for interpreting the weekly loan statements lag two months behind them. These limitations appear especially important at present when increases in bank loans as shown on the weekly series are compared with increases in the same period of last year and the contrasts are used to support very pessimistic conclusions. Last year at this time the increases in bank loans were widely regarded as excessive and directly contributing to inflationary pressures.

Any analysis of fluctuations in business activity in the District or the nation must consider the course of bank loans, but to be realistic the analysis must be broad enough to permit evaluation of at least all the factors discussed as

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affecting the interpretation of bank loans, and include many factors not explicitly discussed in this article. The analysis must go beneath the statistics to the motivations of borrowers and lenders. The fact that inventories rose somewhat from July 1 through November of this year may be relevant in considering the course of business loans; but was this a voluntary or involuntary accumulation? Real estate and consumer loans have not increased as much in the last half of this year as last; but is this because lenders are more restrictive or because the demand for houses and consumer durables is less? Choosing between these alternatives and doing so on the basis of accurate knowledge of the underlying factors is essential if changes in loans are to be related to changes in business activity or vice versa. The weekly reporting series can only contribute statistics which may lead to fruitful questions but the answers require much more research before useful results can be obtained.

Some of the directions that this research should take have been implied at various points in this article. Two aspects of a related type for which research is also necessary are worthy of mention in conclusion. In the previous discussion no emphasis was placed upon the fact that different types of loans (consumer, real estate, business, etc.) play different economic roles. Consequently, the economic effects must be evaluated separately for changes in each type of loan and for each particular set of economic circumstances in which the change occurs. The second consideration is concerned with an analysis of the effects that may flow from the greater recourse by borrowers to lenders other than banks. This shifting carries with it ramifications not discussed in this article. An analysis should be made of these ramifications, including the effect which this shift has upon the utilization of the existing money supply and its rate of turnover, and the general impact of the shift upon commercial banks.

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BUSINESS INDEXES—TWELFTH DISTRICT[1]
(1947-49 average=100)

Year and month	Industrial production (physical volume)[2] Lumber	Petroleum[3] Crude	Petroleum[3] Refined	Cement	Lead[3]	Copper[3]	Wheat flour[3]	Electric power	Total nonagricultural employment	Total mf'g employment[4]	Car-loadings (number)[2]	Dep't store sales (value)[2]	Retail food prices[3, 5]	Waterborne foreign trade[3, 6] Exports	Waterborne foreign trade[3, 6] Imports
1929	97	87	78	54	165	105	90	29	....	....	102	30	64	190	124
1931	51	57	55	36	100	49	86	29	....	....	68	25	50	138	80
1933	41	52	50	27	72	17	75	26	....	....	52	18	42	110	72
1935	54	62	56	33	86	37	87	30	....	47	66	24	48	135	109
1936	70	64	61	58	96	64	81	34	....	54	77	28	48	131	116
1937	74	71	65	56	114	88	84	38	....	60	81	30	50	170	119
1938	58	75	64	45	92	58	81	36	....	51	72	28	48	164	87
1939	72	67	63	56	93	80	91	40	....	55	77	31	47	163	95
1940	79	67	63	61	108	94	87	43	....	63	82	33	47	132	101
1941	93	69	68	81	109	107	87	49	....	83	95	40	52	....	....
1942	93	74	71	96	114	123	88	60	....	121	102	49	63	....	....
1943	90	85	83	79	100	125	98	76	100	164	99	59	69	....	....
1944	90	93	93	63	90	112	101	82	101	158	105	65	68	....	....
1945	72	97	98	65	78	90	112	78	96	122	100	72	70	....	....
1946	85	94	91	81	70	71	108	78	95	97	101	91	80	89	57
1947	97	100	98	96	94	106	113	90	99	100	106	99	96	129	81
1948	104	101	100	104	105	101	98	101	102	102	100	104	103	86	98
1949	99	99	103	100	101	93	88	108	99	97	94	98	100	85	121
1950	112	98	103	112	109	115	86	119	103	105	97	105	100	91	137
1951	114	106	112	128	89	115	95	136	112	122	100	109	113	186	157
1952	107	107	116	124	86	112	96	144	116	130	101	114	115	171	200
1952															
October	108*r*	107	117	142	80	115	96	146	124*a*	143*a*	98*a*	118	113	145	319
November	109*r*	107	118	133	85	116	97	141	126*a*	144*a*	100*a*	117	114	135	194
December	109*r*	108	114	126	78	111	96	138	125*a*	143*a*	102*a*	117	115	148	232
1953															
January	118*r*	107	115	105	77	109	99	141	120*a*	138*a*	100*a*	116	114	151	195
February	117	108	117	131	85	113	92	154	121*a*	138*a*	103*a*	116	112	158	187
March	121*r*	109	123	126	85	116	96	142	122*a*	138*a*	103*a*	119	113	179	336
April	119*r*	108	122	132	83	114	96	165	121*a*	139*a*	102*a*	116	113	164	336
May	112	109	127	142	75	115	91	167	121*a*	140*a*	102*a*	124	113	118	384
June	110*r*	110	121	134	78	105	99	179	122*a*	140*a*	103*a*	120	113	114	372
July	112*r*	110	125	140	64	106	96	172	120*a*	141*a*	98*a*	117	113	123	356
August	108*r*	109	124	134	69	110	92	168	122*a*	139*a*	99*a*	113	113	....	337
September	100	109	126	133	73*r*	111*r*	101	166	124*a*	140*a*	98*a*	110	114	....	....
October	106	109	125	137	69*p*	111*p*	99	163	123*ap*	141*ap*	95*a*	111	114	....	....

BANKING AND CREDIT STATISTICS—TWELFTH DISTRICT
(amounts in millions of dollars)

Year and month	Condition items of all member banks[7] Loans and discounts	U.S. Gov't securities	Demand deposits adjusted[8]	Total time deposits	Bank rates on short-term business loans[9]	Member bank reserves and related items[10] Reserve bank credit[11]	Commercial operations[12]	Treasury operations[12]	Coin and currency in circulation[11]	Reserves	Bank debit index 31 cities[3, 13] (1947-49=100)[2]
1929	2,239	495	1,234	1,790	......	− 34	0	+ 23	− 6	175	42
1931	1,898	547	984	1,727	......	+ 21	− 154	+ 154	+ 48	147	28
1933	1,486	720	951	1,609	......	− 2	− 110	+ 150	− 18	185	18
1935	1,537	1,275	1,389	2,064	......	+ 2	− 163	+ 219	+ 14	287	25
1936	1,682	1,334	1,791	2,101	......	+ 6	− 227	+ 454	+ 38	479	30
1937	1,871	1,270	1,740	2,187	......	− 1	− 90	+ 157	− 3	549	32
1938	1,869	1,323	1,781	2,221	......	− 3	− 240	+ 276	+ 20	565	29
1939	1,967	1,450	1,983	2,267	......	+ 2	− 192	+ 245	+ 31	584	30
1940	2,130	1,482	2,390	2,360	......	+ 2	− 148	+ 420	+ 96	754	32
1941	2,451	1,738	2,893	2,425	......	+ 4	− 596	+1,000	+ 227	930	39
1942	2,170	3,630	4,356	2,609	......	+ 107	−1,980	+2,826	+ 643	1,232	48
1943	2,106	6,235	5,998	3,226	......	+ 214	−3,751	+4,486	+ 708	1,462	60
1944	2,254	8,263	6,950	4,144	......	+ 98	−3,534	+4,483	+ 789	1,706	66
1945	2,663	10,450	8,203	5,211	......	− 76	−3,743	+4,682	+ 545	2,033	72
1946	4,068	8,426	8,821	5,797	......	+ 9	−1,607	+1,329	− 326	2,094	86
1947	5,358	7,247	8,922	6,006	......	− 302	− 510	+ 698	− 206	2,202	95
1948	6,032	6,366	8,655	6,087	......	+ 17	+ 472	− 482	− 209	2,420	103
1949	5,925	7,016	8,536	6,255	3.20	+ 13	− 930	+ 378	− 65	1,924	102
1950	7,093	6,415	9,254	6,302	3.35	+ 39	−1,141	+1,198	− 14	2,026	115
1951	7,866	6,463	9,937	6,777	3.66	− 21	−1,582	+1,983	+ 189	2,269	132
1952	8,839	6,619	10,520	7,502	3.95	+ 7	−1,912	+2,265	+ 132	2,514	140
1952											
November	8,805	6,808	10,281	7,331	......	+ 72	− 29	+ 79	+ 34	2,616	141
December	8,844	6,627	10,504	7,498	3.95	− 299	− 240	+ 422	− 12	2,514	157
1953											
January	8,816	6,633	10,390	7,490	......	+ 138	− 263	+ 136	− 77	2,565	146
February	8,838	6,474	9,911	7,551	......	+ 83	− 119	− 13	+ 22	2,491	150
March	8,983	6,299	9,937	7,560	4.01	− 220	− 147	+ 240	− 18	2,394	164
April	9,054	6,173	10,011	7,597	......	+ 16	− 277	+ 239	+ 11	2,378	153
May	9,092	6,020	9,843	7,627	......	− 12	− 174	+ 293	+ 22	2,463	150
June	9,156	5,997	9,899	7,703	4.18	− 39	− 531	+ 435	+ 39	2,274	155
July	9,167	6,675	10,005	7,729	......	+ 75	− 184	+ 275	+ 3	2,452	148
August	9,229	6,589	9,950	7,749	......	− 100	− 98	+ 176	+ 36	2,397	142
September	9,241	6,481	10,018	7,794	4.17	+ 113	− 308	+ 217	− 4	2,425	149
October	9,255	6,556	10,248	7,854	......	+ 19	− 391	+ 394	+ 7	2,449	142
November	9,248	6,693	10,255	7,815	......	− 137	− 149	+ 330	+ 23	2,476	149

1 Adjusted for seasonal variation, except where indicated. Except for department store statistics, all indexes are based upon data from outside sources, as follows: lumber, various lumber trade associations; petroleum, cement, copper, and lead, U.S. Bureau of Mines; wheat flour, U.S. Bureau of the Census; electric power, Federal Power Commission; nonagricultural and manufacturing employment, U.S. Bureau of Labor Statistics and cooperating state agencies; retail food prices, U.S. Bureau of Labor Statistics; carloadings, various railroads and railroad associations; and foreign trade, U.S. Bureau of the Census. 2 Daily average. 3 Not adjusted for seasonal variation. 4 Excludes fish, fruit, and vegetable canning. 5 Los Angeles, San Francisco, and Seattle indexes combined. 6 Commercial cargo only, in physical volume, for Los Angeles, San Francisco, San Diego, Oregon, and Washington customs districts; starting with July 1950, "special category" exports are excluded because of security reasons. 7 Annual figures are as of end of year, monthly figures as of last Wednesday in month or, where applicable, as of call report date. 8 Demand deposits, excluding interbank and U.S. Gov't deposits, less cash items in process of collection. Monthly data partly estimated. 9 Average rates on loans made in five major cities during the first 15 days of the month. 10 End of year and end of month figures. 11 Changes from end of previous month or year. 12 Minus sign indicates flow of funds out of the District in the case of commercial operations, and excess of receipts over disbursements in the case of Treasury operations. 13 Debits to total deposits except interbank prior to 1942. Debits to demand deposits except Federal Government and interbank deposits from 1942. *a*—New revised series. *p*—Preliminary. *r*—Revised.

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