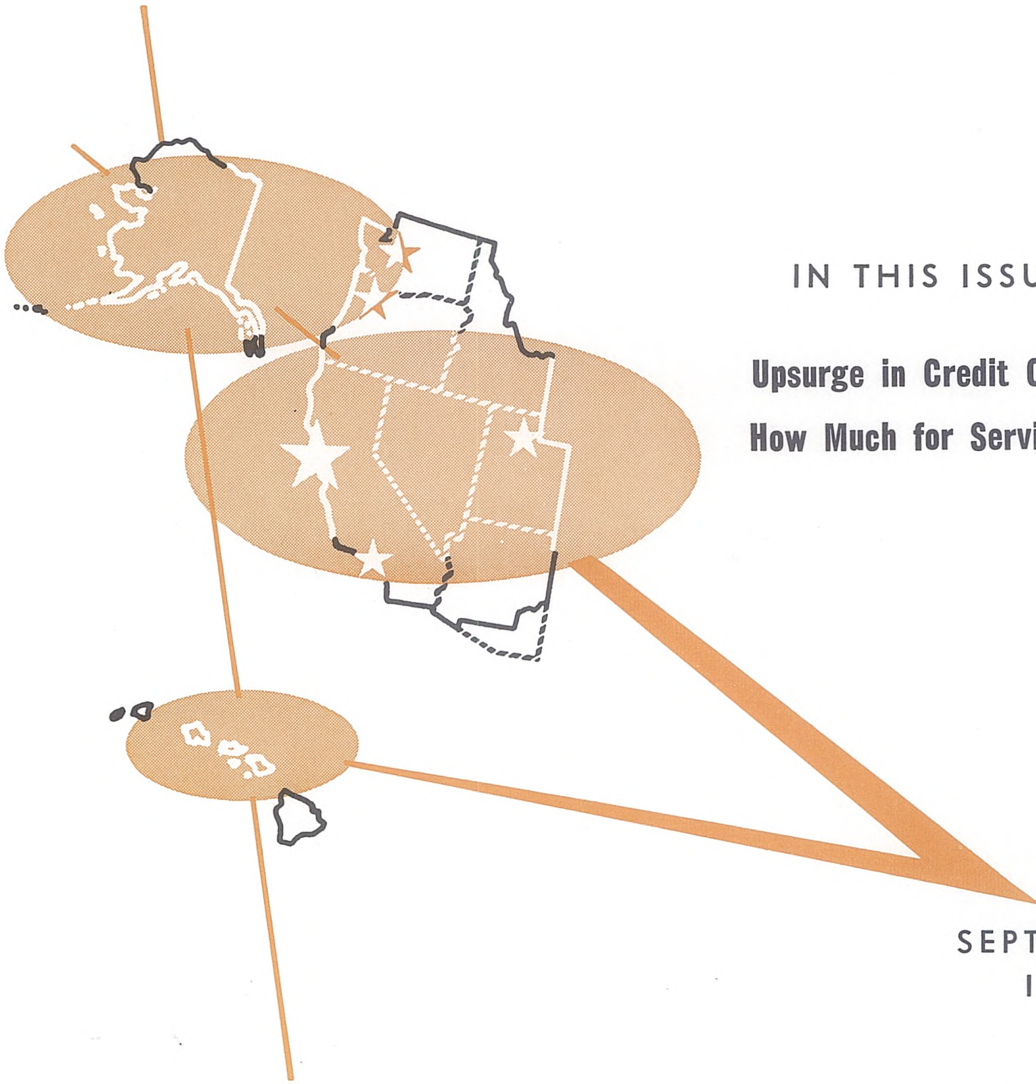
FEDERAL RESERVE BANK OF SAN FRANCISCO

MONTHLY REVIEW



IN THIS ISSUE

Upsurge in Credit Cards

How Much for Services?

SEPTEMBER
1968

Upsurge in Credit Cards

. . . The total volume of activity is rising, and credit-card operators are adding features and moving toward nation-wide coverage.

How Much for Services?

. . . Families now budget over $200 billion annually for services (including housing)—more than two-fifths of total spending.

Editor: William Burke

Upsurge in Credit Cards

The Federal Reserve System recently released a report entitled, "Bank Credit-Cards and Check-Credit Plans." The present article presents some of the highlights of the report — the first comprehensive survey of bank credit plans — along with a brief survey of recent developments in this rapidly moving field.

Credit cards are now a regular fixture of the banking scene—especially in the West, where credit-card plans are operating in every District state and usually on a statewide basis. Not only is the total volume of activity rising, but the character of plans is changing also, since credit-card operators are adding more banking services to the basic charge feature and are moving toward nationwide coverage through interchange agreements. Moreover, the growth of credit cards has gone along with the spread of other kinds of revolving-credit plans of the check-credit or overdraft variety.

Credit-card and check-credit outstandings nation-wide at the end of June 1968 totaled $1,514 million, or almost double the year-ago figure. Moreover, the West continued to dominate this field as before. Twelfth District banks this June accounted for almost one-half ($434 million) of credit-card outstandings, and for almost one-fourth ($143 million) of check-credit outstandings.

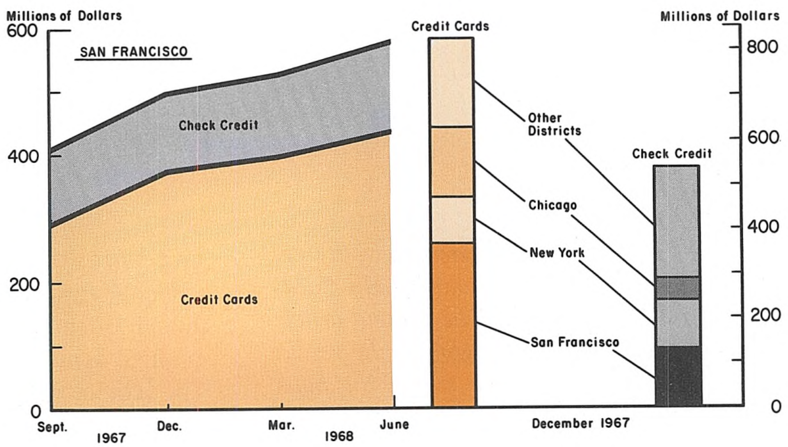
Two types of plans

Credit-card and check-credit plans, although often regarded as substitutes for one another, actually differ in significant respects. The common element in both is a prearranged automatic line of revolving credit available to a customer. But from this base, the operational features of the two plans then diverge.

Typically with check credit, the line of credit is activated by the customer writing a check on his check-credit account. This is a special account set up for check-credit transactions, whether or not the customer also has a regular checking account. A common variation, used especially by Twelfth District banks, is the so-called overdraft plan, whereby the customer activates the credit when he overdraws his checking account and the bank covers the resulting overdraft by automatically transferring funds to cover the check. This link to the customer's regular checking account thus differentiates overdraft-type plans from check-credit plans proper.

With both types of check credit, the customer is usually able to tap his credit line directly for loans in cash. Charges on these plans show many variations, but typically the customer is charged interest on the average amount of funds borrowed. In addition, there are often charges for each check used in check credit, while the regular fee schedule applies to overdraft plans.

Western banks account for one-half of bank credit cards and one-fourth of check-credit activity



The credit card shares with check-credit plans the idea of using a line of revolving credit, but, in addition, it involves a formal arrangement with the retail establishments where purchases are made by the cardholder. The privilege of making charge purchases at many stores is the heart of a credit-card plan. The familiar plastic card identifies the customer to the merchant as someone with an approved line of credit at the bank, and permits the customer to use the card to charge purchases at stores belonging to the credit-card plan. The merchant is reimbursed for the original charge transaction by the bank—less a discount on the transaction—so that the bank, not the merchant, provides the credit extended to the customer.

The customer, when billed by the bank, has the option of repaying the full balance within a grace period (typically 25 days) without any service charge, or repaying on revolving credit with interest charged on the unpaid balance. There are no other charges for the credit card—the cards are issued free—nor is there any requirement to open an account with the bank. Thus if a customer always pays within the grace period, the card is the equivalent of a charge account. In practice though, large numbers choose the revolving-credit option, and thereby provide the principal source of banks' credit-card revenues. Merchant discounts, formerly an important source of revenue for credit-card plans, are now a less important source than customers' interest payments. Merchant discounts, incidentally, now run around 3 percent for most plans at Twelfth District banks.

A bank, desiring to offer some form of credit-card service to its customers, may choose to affiliate with one of the major non-bank travel and entertainment credit-card plans, thus combining elements of both credit-card and check-credit plans. Under these arrangements, the bank does not set up a credit-card operation—this is done by the credit-card company—but instead offers its customer an optional line of revolving credit in addition to the basic card privileges. The customer then can repay his T&E-card bills on revolving credit, rather than in full when billed, and can also borrow at the bank by drawing directly upon his line of credit. Generally, higher credit standards are required for such plans than for bank credit-card plans.

Although a rather sizable number of banks offer this service, the total volume generated is not very large. In October 1967, with 136 banks participating, credit extended through these nonbank card plans amounted to only about 1 percent ($16 million) of total extensions through bank credit-card and check-credit plans. These prime credit-risk customers apparently have a low likelihood of borrowing, which is probably one reason they are such good credit risks.

Operating aspects

Credit-card managers attempt to activate the largest number of accounts within the shortest amount of time when starting a new plan. A high volume is required both as a way of recovering heavy start-up costs and also as an attraction in signing merchants. Therefore, banks frequently resort to the mass issue of unsolicited cards and accept the higher risks entailed. Check-credit managers, on the other hand, typically limit their dealings to relatively small numbers of low-risk customers, each of whom has to apply for an account—and the result normally is a low-volume operation. These general characteristics of course are clearly reflected in the results of the Federal Reserve study.

As of September 1967, credit-card plans covered 14.4 million accounts and $633 million in outstandings, as against 1.1 million accounts and $413 million in outstanding check credit. Credit-card plans were offered directly by 197 banks in addition to about a thousand banks acting as agents, and these plans covered 371,000 participating merchants. Check-credit plans, on the other hand, were operated by 599 banks.

Not surprisingly, check-credit accounts were more highly active—69 percent active as against 35 percent for credit cards. Since customers must apply individually for a check-credit account, there is no equivalent to mass mailing; presumably someone who goes to the trouble of opening such an account is also more likely to use it. The average line of credit was also higher for check credit, $1,100 compared to $350 for credit cards. Actual usage was similarly skewed: active check-credit accounts had an average balance of $610, and active credit-card accounts, $124. Finally, the interest rate charged on outstanding balances was lower for check credit, commonly 1 percent per month compared to the 1½ per cent per month for credit cards, reflecting the underlying risks and operational costs of each type of plan.

The fact remains that credit-card accounts are more important in terms of total numbers, and in terms of total dollar volume, than the competing form, check credit. The lower rate of usage of credit cards may be due to nothing more than the relatively large number of new card plans. According to the 1967 survey, only 23 percent of the credit-card accounts started in the 1966-67 period were then active, as against a 61-percent rate of usage for plans started in 1958-59. Similarly, utilization of credit lines was much larger for the older plans. Thus, as the credit-card habit becomes established, we may well see a higher percentage of active accounts and larger average balances.

Of the 599 banks which operated check-credit plans at the time of the 1967 survey, 274 offered overdraft plans and 410 offered regular check credit. (As the figures indicate, many banks offered both types of plans.) But among the newer plans, the overdraft variant is the more popular choice: 191 of the 312 new entrants nationally during the 1966-67 period were of the overdraft type, and overdrafts accounted for roughly three-fourths of all check-credit balances at Twelth District banks on the survey date. Thus, banks which are not prepared to start a credit-card operation apparently feel that an overdraft system has certain advantages in being easier to institute and more appealing to customers than the traditional form of check credit.

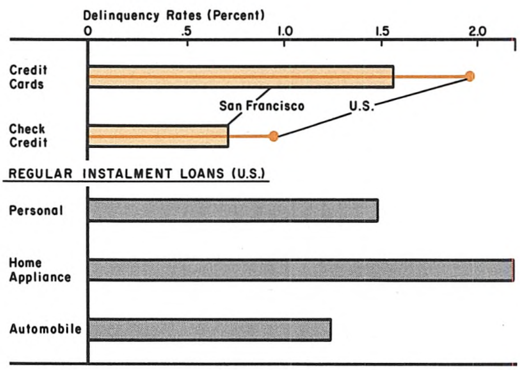
Loss experience

The Federal Reserve study attempted to find whatever substance there is in the credit card's reputation for excessive credit losses by analyzing data on write-offs during the first half of 1967 and delinquencies as of September 1967. The study revealed that credit cards involved heavier credit losses than check-credit plans, but it also showed that these losses were not excessive. In the period examined, credit-card charge-offs amounted to 1.97 percent of outstandings, as against 0.23 percent for check credit—but the higher figure was partly due to the predominance of new plans among the credit-card plans studied. Charge-offs tend to fall quite sharply over time, as is seen from the fact that the ratio dropped to only 1.18 percent when the newest plans were excluded from the computations.

The experience of credit-card plans should perhaps be compared, not to the relatively low-risk check-credit lending, but rather to lending where there is a similar acceptance of higher credit risks and an emphasis on a mass market—that is, to other classes of consumer loans. Delinquencies as of September 1967 amounted to 0.97 percent of outstandings for check-credit and to 1.99 percent for credit cards—but on regular consumer installment loans, the rate was 1.45 percent, and on home-appliance loans (perhaps the closest category to credit-card plans), the rate was 2.19 percent.

Excessive losses certainly are not an inherent feature of credit-card plans; losses indeed can be reduced to the levels acceptable in other types of consumer lending. The techniques of starting and operating a card plan are now better controlled than heretofore—witness recent mass mailings which avoided heavy fraud losses—and the more obvious sources of loss can be eliminated or reduced. Although credit cards do involve extra risks, these are not extreme when compared with the risks encountered in other types of bank consumer lending.

Credit-card delinquencies in line with those on other consumer loans



Mass mailing

The Federal Reserve study concluded that some risks are involved in the mass mailing of cards—but are generally acceptable risks. As for public inconvenience, cases of multiple card issue do occur at times, but these cases usually arise only when several banks are involved in issuing cards at the same time. The cards are not sent indiscriminately; although unsolicited, they are sent only to people meeting specified standards. Current practice in fact is to rely upon internal lists, because of the undependability of outside lists, even those from credit bureaus.

After analyzing the report, the Federal Reserve Board of Governors declared that the use of unscreened, purchased lists for mass mailings was "objectionable," and on grounds of minimizing inconvenience, the Board suggested that banks try to minimize the possibility of duplicate mailings. But neither the Board nor the original committee report advocated the prohibition of mass mailing. The initial unsolicited mailing helps generate quickly the necessary high volume of activity at the start-up of each new plan.

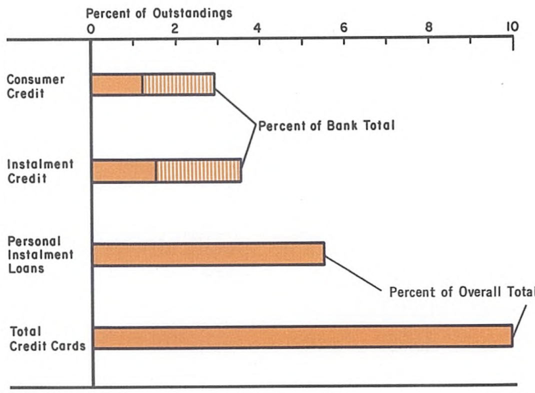
The alternative of issuing on application only seems much less effective. In one case cited, a certain bank obtained a 20-percent rate of usage from an unsolicited mailing of credit cards but less than a 1-percent return from a simultaneous mailing of credit-card applications. But the principal result of a prohibition of mass mailing would be to make the entry of subsequent plans more difficult and thereby to reduce somewhat the competitive pressures on existing plans.

Consumers and prices

The System committee looked into the charge that credit cards encourage excessive growth of consumer credit, but found no convincing proof of that charge, since credit-card outstandings now represent only a small proportion of outstanding consumer credit and bank loans. As of December 1967, credit cards and check credit together accounted for 1.2 percent of all consumer credit, 2.9 percent of bank-held consumer credit—and only 0.3 percent of total bank loans and investments. Meanwhile, these two types of bank credit together accounted for 5.5 percent of total personal loans and 9.9 percent of total "plastic" (credit-card) credit.

The impact of bank credit cards on individual borrowers is of course more difficult to evaluate. The rapid spread of such plans indicates that large numbers of people find credit cards to be convenient, and the relatively low loss record indicates that the bulk of bank customers do not have much difficulty in handling this type of credit. Furthermore, the banks in their own interest try to protect their customers from excessive borrowing—witness the relatively low credits (averaging only about $350), and the adoption of stricter lending standards than many other lenders use. Yet some individuals are still incapable of handling credit cards, and despite the safeguards taken by the banks,

Credit cards plus check credit still represent small share of total



will get into trouble. But the report judged that the benefits somehow must be weighed against the disadvantages with this as with any other credit system, and that consumers on balance obtain a net gain from this new service.

Similarly it would be difficult to prove that credit cards have had a substantial inflationary impact. It is sometimes argued that merchants are forced to raise prices in order to cover the merchant discount on credit-card transactions. If only the increased cost of the merchant discount is considered there would be some tendency to push up prices. But actually credit cards generate other changes, so that their net impact on prices is not at all clear.

First, some merchants not previously able to offer credit should experience increases in sales, which tend more or less to offset the cost increases associated with the merchant discount. Second, to the extent that bank credit-card plans replace existing merchant-credit plans, there can be a net reduction in credit costs to the merchant. This factor is especially important as merchant discounts decline, toward 3 percent or lower, as they have in many areas. But in general, it must be remembered that widespread price rises are primarily due to excess demand forces working upon the whole economy, and that inflationary pressures working from the cost side can hardly be traced to credit cards alone.

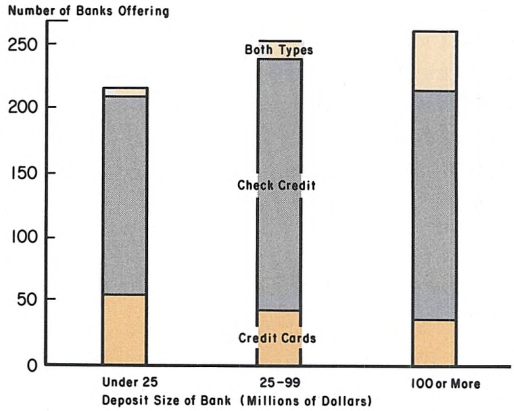
Small-bank participation

The System committee also considered the possible impact of credit-card plans on the structure of banking, specifically regarding the effect of heavy start-up costs on small-bank participation. If credit-card plans should develop into the principal source of consumer credit, and if they should continue to require massive big-bank financial resources, then presumably the long-run competitive position of smaller banks would be weakened. The Federal Reserve study indicated, however, that there is a definite place for small-bank credit cards despite the dominance of large banks in this field, and that, in addition, these banks still have the alternative of check credit available to them.

In September 1967, roughly one-third of the banks with credit-card operations had deposits of less than $25 million, and another quarter had deposits of between $25 and $100 million. Many of these small banks have operated successful plans for years, at a time when larger banks were actually dropping credit cards. Even so, the success of small banks still tends to depend upon the state of local competition. Generally the small independents have not been forced to meet competing bank plans and have thereby been able to maintain their schedule of merchant discounts at levels nearer 6 percent than the 3-percent competitive rate.

Although small banks may now find it increasingly difficult to start independent plans because of the development of large regional and statewide systems, they can of course participate themselves in these larger

Small banks as well as large operate credit-card programs



systems. The most common form of participation is the agency system, where the agent bank signs up merchants and accepts their sales drafts for forwarding to some principal bank. (In some plans, agents participate themselves in the credit granted their customers.) The agent bank has only a limited role, but this limited participation permits the minimization of costs and the maintenance of long-standing relationships with local merchants. There were well over 1,000 agent banks in September 1967, and the number has since continued to grow.

Small-bank alternatives

Two other approaches permit smaller banks to join with large banks so as to offer a more-or-less complete credit-card program. Both of these approaches were developed by Twelfth District banks—the BankAmericard and Master Charge systems.

The BankAmericard franchise system licenses certain banks, and these licensees in turn can offer so-called associate status to other local banks. The associate signs up local merchants and issues cards bearing its own name to its own customers. It is responsible for the credit granted its cardholders and, in the eyes of its customers, it is offering its own credit card. The principal licensee provides its associate with a central computerized accounting system and other services, in return for fees based on the volume of business. Although it must pay those fees, the associate avoids the costs of setting up its own computer system and moreover obtains a packaged credit-card plan.

The other approach, the Master Charge System, has been developed by the Western States Bankcard Association in California, Nevada, Utah and Washington. The association, a group of large and small banks originally organized at the initiative of four large California banks — Wells-Fargo, Crocker-Citizens, United California Bank, and Bank of California—operates the necessary central computer system for all members. The association administers the cardholder accounting, as well as the settlement of sales drafts between members, while the members sign up merchants and cardholders, carry cardholder credit, and absorb any resulting credit losses. A small bank thus can issue Master Charge cards on the same terms as a large bank does.

Elsewhere — for example, Chicago — less-centralized organizations have been set up. Under these systems, the central organization does little more than arrange the interchange of sales slips and design the basic credit card. (This is sometimes described as a "compatible" system.) The individual members themselves set up all the other elements of a credit-card organization and can share costs only to a limited extent. This type of system thus is a half-way house between independent operation and membership in a credit-card association.

A small bank of course can become a licensee of a large system or strike out on its own, but these are more costly alternatives than association with a local system dominated by one of the large-bank organizations. The ease of credit-card operations by smaller banks depends largely upon the arrangements chosen by the dominant banks in their area of operations. If the latter decide upon a Master Charge organization or a sub-licensing arrangement with BankAmericard, operations are simplified for the smaller banks. But at the very least, the small banks in almost all cases have agent status available to them.

Recent trends: growth

Since the publication of the statistics contained in the Federal Reserve study, bank credit-card and check-credit plans have continued to show a sustained rate of growth. Between September 1967 and June 1968, consumer installment credit rose by 6 percent overall and by 7 percent at commercial banks —but credit card outstandings jumped by 44 percent and check credit by 24 percent.

The Twelfth District paralleled the national trend, and the District thus maintained its dominant position in this field, accounting in June 1968 for 38 percent of all credit outstanding in such plans. Moreover, credit-card outstandings were three times as large as check-credit outstandings at Twelfth District banks, whereas the totals for these two categories were roughly equal for the rest of the nation.

The important role of District bank credit plans also shows up in comparisons with broad bank lending categories. Credit-card and check-credit outstandings account for about 10 percent of installment loans at District banks, as against less than 4 percent elsewhere. (The proportion jumps from one-tenth to one-fourth of the total when the more relevant comparison is made, with personal loans and non-auto consumer goods in the denominator.) Thus, credit-card and check-credit plans have definitely become a major channel for short-term consumer lending in the West—and presumably the same end-result will occur elsewhere as these plans continue to proliferate.

Recent trends: interchange

Within the past two years alone the banking industry has clearly moved toward the organization of national and regional interchange systems, thus shifting away from the locally based plans previously in vogue. Two nationwide interchange systems are now functioning, along with several important regional systems.

One national system, BankAmericard, consists of BankAmericard licensees. The second, Interbank Card Inc., is a nonprofit corporation whose membership consists of many banks operating their own plans, and includes the Western States Bankcard Association. The best known of the regional groups is the Midwest Card System, which covers Illinois, Indiana, and Michigan. New England also has two interchange networks, and smaller systems are operational in some other parts of the country.

The object of interchange is to broaden the geographic coverage of a bank credit card and hence increase its attractiveness to the cardholder. Banks agree to accept one another's cards on a reciprocal basis; that is, Bank A's merchants accept Bank B's cards, Bank A clears the sales slips to Bank B (the cardholder's bank), and Bank B then bills the cardholder in the usual fashion. The interchange system specifies the mechanics of clearing the sales drafts and settling outstanding balances between banks.

Each system tries to insure that the cards of the various participating banks are readily identifiable (and hence acceptable) by merchants for charge purchases. Both BankAmericard and the Midwest System issue cards with a common design and some space for the individual bank's name. Interbank resolves the recognition problem by printing a common symbol — a lower-case letter "i" within a small circle — on cards whose general design otherwise varies from bank to bank.

Although most credit-card transactions are still local in origin, the competitive pressures to offer a card with potential for wider use are quite strong. Most banks starting new plans within the past year have joined one of the interchange systems, as have many banks with older independent plans. Once one bank announces its intention to join an interchange plan, the other banks in the area typically make matching moves. The consequence is thus a cumulative growth of the interchange networks.

In the West, the interchange concept reigns supreme. One or another of the two national systems has a member in every District state except Alaska, and in five states both are in operation. (One bank in Hawaii belongs to both systems.) Only three District banks remain with independent plans—one each in Alaska, Utah and California.

Interchange and growth

The nation-wide spread of interchange arrangements undoubtedly has reinforced the upward trend in credit-card (and check-credit) activity. Credit cards originated as locally oriented charge services, to which revolving-credit privileges were soon added. As more banks entered the field, still more features (such as cash advances) were offered to increase the attractiveness of this type of credit. Still, the pace of overall development was uneven until well into 1966, when the rapid spread of the interchange idea helped generate a sharp expansion in activity.

Some areas may remain where credit-card programs are neither planned nor operating, but in general, the average bank customer can now carry a credit card with the privilege of using it practically throughout the nation. Interchange systems must still improve their clearing processes and overcome their credit-control problems, but already they have created the general framework for a major new banking service.

As the Federal Reserve study concluded, credit-card and check-credit plans should show continued growth, since they perform a useful service appropriate to the banking system — although they still play a relatively minor role in the overall picture of bank lending, consumer credit, and banking structure. For small retailers, credit cards might improve their competitive position by opening to them charge services capable of matching those of the giant chains. For the general public, these plans fulfill a need in providing a convenient source of revolving credit. For the banks, credit cards (and check credit, to a lesser extent) can pose complex management problems, but as these problems are surmounted, very successful operations can be expected. On balance, since current examination procedures appear sufficient to prevent the spread of unsound practices by individual banks, and since credit-card and check-credit plans appear to pose no pressing economic problems, the Federal Reserve committee concluded that neither new controls nor new legislation was required.

Robert Johnston

TWELFTH DISTRICT BUSINESS

Year and Month	Condition Items of all members banks (millions of dollars, seasonably adjusted)				Bank debits 22 SMSA's (billions $)	Bank rates: short-term business loans	Total nonfarm employment (1957-59 = 100)	Electric power consumption (1963 = 100)	Industrial production (1957-59 = 100)		
	Loans and discounts	U. S. Gov't securities	Demand deposits adjusted	Total time deposits					Lumber	Refined Petroleum	Steel
1959	15,908	6,514	12,799	12,502		5.36	104		109	101	92
1960	16,612	6,755	12,498	13,113		5.62	106		98	104	102
1961	17,839	7,997	13,527	15,207		5.46	108		95	108	111
1962	20,344	7,299	13,783	17,248		5.50	113		98	111	100
1963	22,915	6,622	14,125	19,057		5.48	117	100	98	112	115
1964	25,561	6,492	14,450	21,300	501	5.48	120	112	107	115	130
1965	28,115	5,842	14,663	21,102	535	5.52	125	122	107	120	138
1966	29,858	5,444	14,341	25,900	618	6.32	133	134	103	123	140
1967: June	30,071	5,265	15,181	27,460	681	......	137	143	93	131	133
July	30,313	5,832	15,189	27,687	712	......	138	145	94	130	129
Aug.	30,473	5,742	15,617	27,859	719	5.95	138	144	94	134	129
Sept.	31,034	5,885	15,632	28,008	709	......	138	149	91	126	136
Oct	30,951	5,867	15,633	27,993	728	......	139	152	98	133	144
Nov.	30,964	5,609	15,588	28,433	738	5.92	140	147	98	133	148
Dec.	31,337	5,772	15,192	28,691	711	6.32	140	150	101	129	147
1968: Jan.	32,181	5,743	15,500	28,849	718	......	141	153	111	133	138
Feb.	32,181	6,149	15,512	29,136	738	......	142	148	101	122	139
Mar.	32,009	5,944	16,015	29,118	734	......	141	154	107	132	149
Apr.	32,611	5,619	15,844	29,200	......	......	141	152	111	134	150
May	32,497	5,801	16,041	29,060	......	......	142	157	102	140	156
June	33,052	5,412	16,306	28,981	......	......	142	151	109	143	152
July	33,764	5,873	16,327	29,493	......	......	143	152	......	......	150

Publication Staff: R. Mansfield, Artist; Karen Rusk, Editorial Assistant.

Single and group subscriptions to the *Monthly Review* are available on request from the Administrative Service Department, Federal Reserve Bank of San Francisco, 400 Sansome Street, San Francisco, California 94120

Redwood National Park

A House-Senate compromise bill has been signed into law providing for the establishment of a 58,000-acre national park in northern California's scenic redwood country. Passage of the measure culminated a 50-year-long battle involving lumbermen, conservationists and legislators.

The new Redwood National Park is composed of a northern unit in the Mill Creek area of Del Norte County and a southern unit in the Redwood Creek area of Humboldt County. The corridor connecting the two includes a 33-mile stretch of beach. The 58,000-acre total was 6,000 acres less than proposed in the Senate bill but more than twice the 28,500 acres submitted in the House version.

The cost for land acquisition will be approximately $92 million. Roughly half of the total property is now in private land and the remainder is in State lands, including three existing State parks. The Park will include 32,476 acres of old-growth redwoods long guarded by conservationists. Additional development costs for the Park are estimated at $10 million.

In addition to preserving the redwoods themselves, the Park will serve as a site for recreation and scientific research. The measure also activates a land-swap arrangement whereby some of the Forest Service's Northern Redwood Purchase Unit is to be turned over to private loggers who give up timberlands for the Park.

Background information on the area affected by the Park and an analysis of the present and future structure of its economy are presented in a booklet, "Trees, Parks, and People," published by the Federal Reserve Bank of San Francisco.

For individual and bulk copies, free of charge, write to

Administrative Services Department
Federal Reserve Bank of San Francisco
400 Sansome Street
San Francisco, California 94120

How Much for Services?

The nation's factories over the years have created a wealth of goods for an increasingly prosperous citizenry, but a mammoth services industry has been relatively even more successful in selling a varied collection of services to American households. In 1967, families spent $204 billion for services, or 41 percent of total consumer spending—whereas two decades ago, when aggregate spending was only one-third of the 1967 total, they allocated only 31 percent of their expenditures for that purpose.

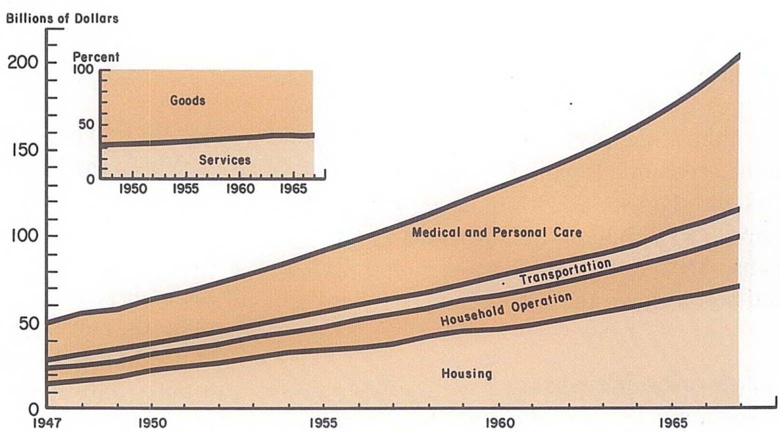
Some of these services may be considered luxuries, but others are necessities—just as some goods fall into each of the categories. For instance, the Commerce Department places in the services category such basic needs as shelter and transportation, along with a wide range of more dispensable items. But perhaps the most notable aspect of the services sector is simply its heterogeneity, since its products range from the impersonal outputs of the capital-intensive telephone and electric-power industries to the tender ministrations of doctors, barbers, and landlords.

Breakdown of the budget

Payments (either real or imputed) for the use of shelter facilities accounted for over one-third of total spending for services last year—$70.9 billion in all. About two-thirds of this amount represented the space-rental value of owner-occupied nonfarm dwellings; about one-fourth represented actual tenant rents, and the remainder went mostly for hotel and motel bills.

Other substantial payments were required for the maintenance of the nation's 62 million households, including $19.8 billion for gas and electricity, $7.5 billion for telephone and telegraph, and $4.3 billion for domestic ser-

Family spending for services rises from 31 to 41 percent of total consumer spending over two decades



vants. The latter category has grown relatively slowly in recent years. Family members, armed with the latest mechanical appliances, increasingly do their own domestic chores, especially since the supply of servants has tended to dry up under the impact of improved job opportunities and broader income distribution. The number of domestics was no higher in 1950 than in 1900 (1.5 million), and the number has declined even further since 1950—which means a precipitous drop in the number of servants per family over the course of this century.

Consumer spending for transportation services was relatively small last year, as this category (like household maintenance) continued to reflect a shift in favor of do-it-yourself service. Ground transportation fares, at $2.7 billion in 1967, were no higher then than two decades ago, as purchased local transportation increased only slowly and intercity transportation actually declined. Auto servicing—parking, washing, repairing, and the like — cost $6.8 billion last year, rising in line with the strong overall uptrend in auto and parts spending. (Airline fares meanwhile were $1.6 billion — which may seem somewhat low until it is realized that this represents a 12-fold increase in only two decades.)

The spending totals also included the costs of a multitude of services which surround the individual almost literally from the cradle to the grave—such items as marriage licenses, divorce fees, brokerage fees, life-insurance premiums, and pari-mutuel tickets. Last year alone, consumers paid $12.5 billion to doctors and dentists, $7.9 billion to private educators, $3.7 billion to barbers and beauticians, $6.2 billion to lawyers and brokers, and so on down the list.

Large price increases

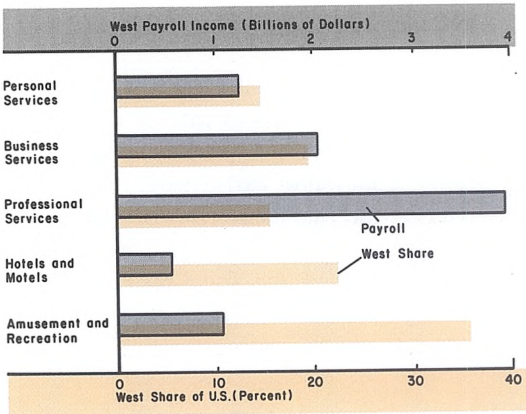
Spending for services thus has increased sharply over the past two decades—but much of this expanded spending results from rising prices, because of such factors as a sharp upsurge in consumer demand as well as supply limitations enforced by a lack of production-line processes. According to Commerce Department data, rising prices have accounted for almost one-half of the 1947-67 increases in spending for housing services and household operation — which in total amounted to 354 and 276 percent, respectively. Over the same time-span, price erosion accounted for roughly two-thirds of the 310-percent increase in spending for medical and personal services, and for fully four-fifths of the 177-percent increase in transportation services. (Price erosion accounted for only one-fourth of the increase in durable goods spending and for less than half of the non-durables increase.)

Western families allocate their budget for services a little differently from families elsewhere, according to a recent Labor Department study which differs slightly from the Commerce Department concept. According to this study, the average Los Angeles family spent less than the typical U.S. family for housing in 1966, but allocated substantially more for medical and other services. San Francisco, Seattle, and other Western cities were more in line with the national housing-expense figure, but (like Los Angeles) reported substantially above-average spending for medical care.

Large payrolls for services

Yet in the West as elsewhere, services provide a substantial source of income as well as a charge against consumer budgets. (Personal income from services, in Commerce Department terminology, encompasses fewer items than the services category in consumption expenditures.) Nationwide, service payrolls totaled $50.2 billion in 1967, on the heels of a 6.0-percent average annual gain in em-

Thanks to tourists, West accounts for bulk of hotel, amusement payrolls



ployment over the 1960-67 period (after a 4.5-percent average gain in the earlier post-war era). District states accounted for 17½ percent of 1967's service income, as against only a 15½ percent share of payrolls in other industries.

Western payroll workers in 1967 received $3.9 billion for professional services, $2.0 billion for business services, and $1.2 billion for personal services. In each of these categories, income figures were roughly in line with the national pattern. At the same time, Westerners received 35 percent ($1.1 billion) of the total income from amusement services and 22 percent ($0.5 billion) of the total income from hotel-motel services—not surprisingly, in view of the region's well-justified attractiveness to tourists. California and Nevada, which provide on-screen and off-screen entertainment for all the nation's millions, received almost one-third of the entertainment industry's total payroll. (In addition to this $9 billion in service payrolls, roughly $3½ billion went to individual proprietors, for whom detailed data are not available.)

Over two decades, then, consumers have sharply expanded their spending for services, but workers in the services industry have just as sharply increased their earnings from the provision of services. While income from this source has increased over three-fold in the rest of the nation, it has increased four-fold in the West alone. And as more and more individuals require more and more services to accompany them from cradle to grave, the continued expansion of the diverse services industry is practically assured.

Joan Walsh

Federal Reserve Publications

"Reappraisal of the Federal Reserve Discount Mechanism"—A System committee report, which proposes ways of making the "discount window" play a more active part in enabling commercial banks to meet their communities' credit needs. (Price: 25 cents a copy, or 20 cents each in quantities of 10 or more.)

"Bank Credit-Card and Check-Credit Plans"—A System task-force study, which evaluates the impact of bank credit-cards on consumer spending and assesses the implications of such plans for bank competition and bank supervision. (Price: $1.00 a copy.)

Copies of these System publications are available from Publications Services, Division of Administrative Services, Board of Governors of the Federal Reserve System, Washington, D.C. 20551.

Western Digest

Discount Rate Reduction

The Federal Reserve Bank of San Francisco lowered its discount rate by ¼ point (to 5¼ percent) on August 29, thus climaxing the shift to a lower rate pattern which was initiated by the Federal Reserve Bank of Minneapolis two weeks earlier. The rate was last reduced during the sluggish economic situation of early 1967, then it was raised three times, in equal ½-point steps, during the financial crises of November 1967 and March-April 1968. . . . The lower discount rate reflects the easing of money markets that became evident after Congress passed the fiscal-restraint package just before midyear. For example, the 90-day Treasury-bill rate stood at 5.08 percent in mid-August, down from a late-May peak of 5.85 percent.

Sharp Credit Expansion

Total bank credit at large commercial banks in the Twelfth District expanded by $1.3 billion during the first half of the third quarter—roughly twice as fast as during the year-ago period. Security holdings increased $927 million as banks added both U.S. Government and municipal issues to their portfolios. Loans rose by $344 million (exclusive of loans to domestic banks). . . . The expansion in the loan category reflected a substantial increase in loans to U.S. Government securities dealers, who held unusually high inventories during this period. Business loans recorded a seasonal decline, while mortgage and consumer instalment loans continued to expand.

Heavy Deposit Inflow

During the first half of the quarter, large Western banks posted an increase of slightly over $1 billion in total deposits (less cash items in process of collection). Private demand deposits rose by nearly $450 million, and time deposits increased about $650 million. . . . Individuals made net withdrawals from their passbook savings during this period, but an increase in consumer-type time certificates more than offset this decline. Holders of large-denomination CD's meanwhile added nearly $500 million to their outstandings.

Alaskan Oil Strike

According to conservative estimates, the Alaskan oil strike reported at midyear may cover 75,000 acres and contain 5 to 10 billion barrels of recoverable oil—in other words, this Arctic field may rival all but the largest Middle Eastern oil reservoirs. But heavy capital outlays will be required to bring the oil from this and other Alaskan fields to market. (Oil firms spent $227 million in the state in 1967 for the exploration and development of oil resources.) . . . The level of costs in Alaskan production is relatively high. Alaskan drilling costs of $159 per foot are roughly 2½ times average California costs, and pipelines in offshore producing areas cost $618,000 per mile in Alaska as against $185,000 per mile in California.