Volume 7, Issue 2
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monthly statistical report

NINTH DISTRICT CONDITIONS

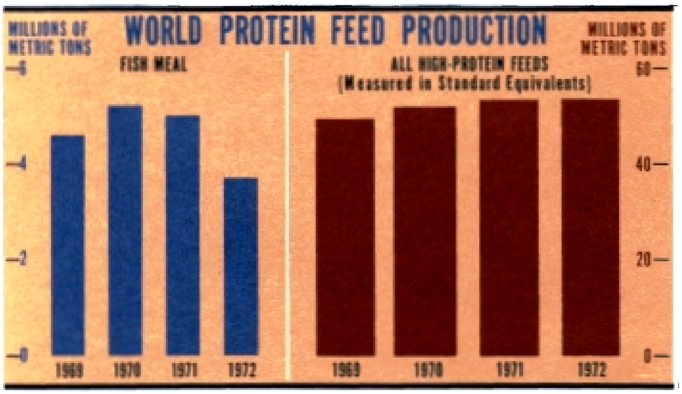
federal reserve bank of minneapolis

DISTRICT INDICATORS LOOK PROMISING

Despite fuel supply problems, boxcar shortages and some miscellaneous woes, the district's basic indicators still point strongly upward. In fact, weak spots are almost difficult to find in recent statistical releases, with the exception, of course, of food prices and short-term interest rates. To stick to the positive side, December ended with a further gain in the industrial use of electric power, a fourth consecutive monthly rise in manufacturing employment, and a continued high level of average weekly hours worked in manufacturing. These indicators, plus the sales expansion foreseen in our Industrial Expectations Survey, add up to solid gains for district industry.

AGRICULTURE: Meat Prices Headed Up Again? World Supplies of High-Protein Feeds Strained

High-protein livestock feeds are scarce this winter. World-wide shortages have forced up the price of all protein feeds and resulted in high costs for both livestock industries and consumers in the district.



Partially responsible for high protein feed prices is the heavy demand for both domestic use and export. U.S. producers, feeding slightly more cattle and poultry this winter, have required larger supplies of protein supplements. Cotton and soybean harvests in the United States in 1972 were, respectively, 29 and 9 percent larger than in 1971, which means that the supplies of cottonseed meal and soybean meal were correspondingly larger. These sources usually provide about 75 percent of total U.S. feed protein. Nevertheless, the demand for protein feeds more than matched these increases in supply.

Foreign buyers have been actively seeking U.S. protein feeds since early last autumn. The winter failure of world fish meal production intensified their search. Fish meal, an important protein feed in most foreign countries, is made primarily from Peruvian anchovies. Because anchovies were extremely scarce in coastal waters this season, fishing was halted to permit fish populations to recover.

Bad Weather Complicates Domestic Production

Supplies of protein feeds in the Upper Midwest this winter have been aggravated by temporary weather problems. Rain at harvest time increased the moisture content of soybeans so much that artificial drying was necessary. Later, drying was curtailed for a short time because of fuel shortages precipitated by unusually cold weather.

While wet weather in the North hampered feed drying, wet weather in the South held up the cotton harvest. Even though cottonseed production was the largest in seven years, the output was delayed by poor harvesting conditions. In the meantime, protein markets became very tight throughout the nation. District ranchers use cottonseed pressed into cake form to feed beef cattle during winter months. Higher prices for proteins in general this year may raise the cost of winter cattle feeding in Montana and the western areas of the Dakotas by 10 to 12 percent. For some ranchers the added costs will be even greater.

Protein Scarcity Leads to High Feed Prices. . .

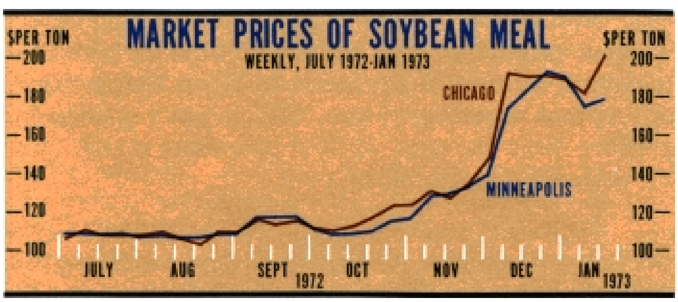
The Minneapolis price of soybean meal, used extensively for manufacturing protein supplement feeds, rose from \$105 to a record \$190 per ton between October 10 and January 2. This was the steepest price climb ever recorded for a three-month interval. Minneapolis prices have since averaged about \$180 per ton, \$93 more than a year ago. Prices for alternatives to soybean meal, linseed and cottonseed meal, have risen proportionally.

With the price of protein feeds almost double since last year, the price of manufactured protein supplement feeds has been boosted 20 to 25 percent. The largest price increases appeared for feeds highest in protein, specifically for those fed to poultry and some dairy cattle. Supplement feeds usually account for about 15 percent of the feeding costs for a beef steer, 10 percent for a dairy cow, and 33 percent or more for hogs and poultry.

Basic feeds are also more expensive than last year: corn, the most widely used basic feed, is up 20 to 25 percent. Roughages are up 10 to 15 percent. Adding all feed expenses together, it now costs about $110 to feed a steer from 425 pounds to market weight of 1,025 pounds in the Upper Midwest. One year ago the cost was $97.

. . . And Unusually Erratic Markets

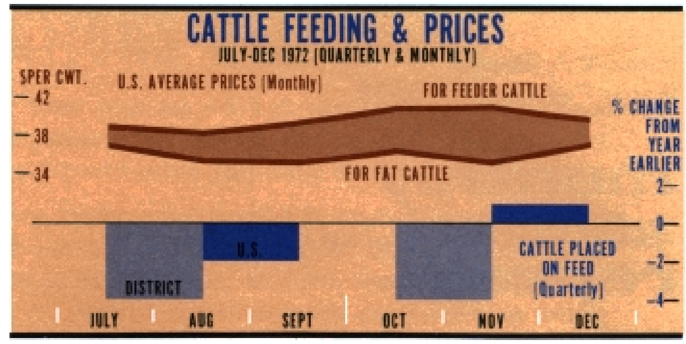
A particularly troublesome feature of the currently tight protein market is the extreme variability of prices at these high levels. Since December 1, the futures prices for soybeans or soybean meal have moved by as much as their allowable daily limits on 26 of 37 trading days. Normally this is a very unusual occurrence. The maximum allowable daily price movement is 10¢ per bushel for soybean futures and $5 per ton for soybean meal. This much variability, occurring as often as it has recently, makes livestock production planning more difficult and increases the risks of incurring losses.



Prices have also varied widely among different markets for protein feeds. Prices for soybean meal at Minneapolis and Chicago demonstrate this variability. From July 1 through mid-September, the average difference between Minneapolis and Chicago was $1.21 per ton. From mid-September through mid-December, however, the difference averaged $5.44 per ton. Erratic price differences, mainly the result of transportation tie-ups at one point or another, made it difficult for manufacturers of supplement feeds to order supplies.

Feeding Costs May Drive Meat Prices Higher

The high and variable protein prices of recent months make feed, livestock, and meat production both risky and costly. This is an especially unfortunate development for consumers faced with already high meat prices. When protein feed prices hit December highs, the price of feeder cattle softened somewhat even though the price of fat cattle strengthened. The high costs of feeding seem to have made cattle feeders reluctant to bid actively for young cattle to fill their lots. Cattle feeders in the Ninth District restricted the number of cattle placed on feed during the fourth quarter 1972 to 4.2 percent



less than in fourth quarter 1971; in the same period, cattle placed on feed increased 1 percent nationally. With high feeding costs, cattle are generally slaughtered at lighter weights, yielding less meat. Lower meat production now may well mean higher meat prices for consumers in the near future.

EXPORTS: District Products Selling Well Abroad

While no official data for manufactured exports from district states are available, national statistics and surveys of individual local companies indicate that district export values grew roughly 10 percent in fiscal 1972. Quite a few smaller- and medium-sized companies registered gains of 20 to 30 percent, although advances were more moderate for other firms. Total U.S. exports of electronic computers and parts, for example, of which an important part originates in Minnesota, increased only 3 percent from the first ten months of 1971 to the same period of 1972.

Growth of district manufactured exports should accelerate somewhat in 1973, with shipments reaching a total of approximately $1 billion.

Various factors contribute to this optimistic outlook. The dollar devaluation and high rates of inflation abroad have improved the competitive position of U.S. exports. Furthermore, two specialized facilities make exportation more attractive to smaller firms: Domestic International Sales Corporations (DISCs), set up by individual firms, permit corporate income taxes on 50 percent of export earnings to be indefinitely deferred; the Export-Import Bank (Eximbank) offers improved export financing.

Business conditions in the major markets should also be quite strong. Economic growth is expected to continue at a fast pace in Canada, while Japan and most countries of western Europe should post higher growth rates in 1973 than in 1972.

Another source of optimism: U.S. agricultural exports will total about $10 billion in the current fiscal year—almost $2 billion above the previous record. Although the much-publicized wheat sales to the Soviet Union consisted mainly of hard red winter wheat, primarily grown in regions south of the Ninth District, district wheat growers do benefit from the resulting higher domestic prices.

Foreign markets are strong for other major district crops as well. The U.S. Department of Agriculture estimates that exports of feed grains in fiscal 1973 will top the previous period by 38 percent. Sales of soybeans and soybean products should increase by 13 percent.

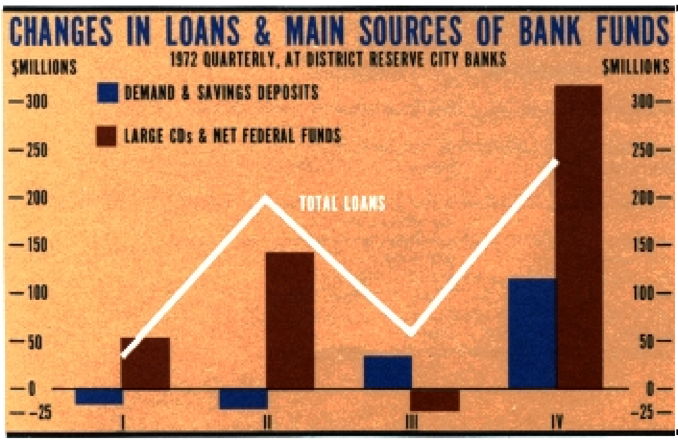
BANKING: Board Raises the Discount Rate

The Board of Governors of the Federal Reserve System recently approved an increase in the discount rate—the rate charged member banks on borrowings from reserve banks—from 4½ to 5 percent, effective January 15. In announcing the change, the Board indicated that the increase should bring the discount rate into better alignment with other short-term interest rates. In the weeks preceding the Board's action, short-term rates increased rather markedly, responding to a surge in economic activity. A widening margin between short-term rates and the discount rate since mid-December led to a sharp increase in member bank borrowing from reserve banks. By raising the discount rate, the Board hopes to dampen borrowing demand.

City Banks Use CDs & Fed Funds to Make Loans

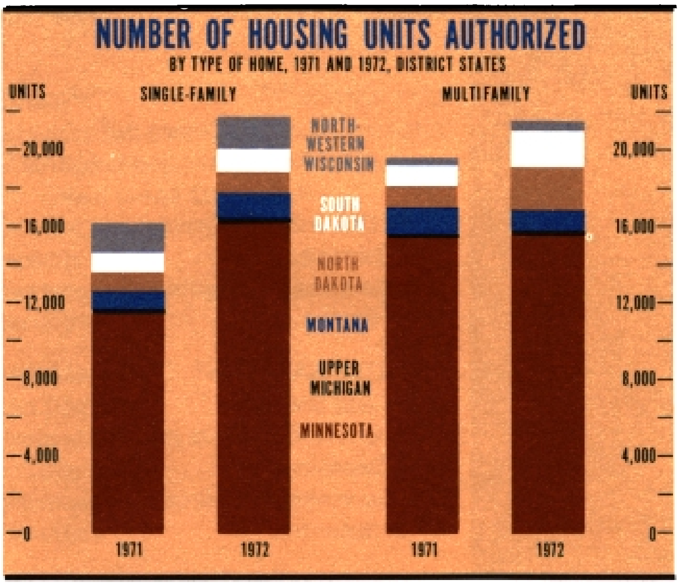
In the face of strong loan demand and an inadequate supply of funds from traditional sources such as demand and savings deposits, district reserve city banks relied rather heavily on large negotiable certificates of deposit (CDs) and federal funds borrowing for new funds during 1972. Negotiable CDs which have a minimum denomination of $100,000 are sold primarily to large corporations or local governmental units. Federal funds represent borrowings from other commercial banks.

In 1972 large CDs at district reserve city banks rose by 25 percent and federal funds borrowing nearly doubled. The increase in these two instruments combined was four times larger than the increase in demand and consumer time and savings deposits. Large CDs and federal funds are short-term instruments highly sensitive to small changes in interest rates. Banks are thus able to manipulate these instruments in response to fluctuations in loan demand and deposits. During the first and third quarters when loan growth was quite modest, large CDs and federal funds borrowing combined showed little change. In the second and fourth quarters, vigorous loan growth elicited a substantial combined increase in these instruments.



CONSTRUCTION: The Demise of Subsidized Housing

Although the Nixon Administration's recently announced freeze on subsidized housing will not significantly affect district homebuilding in 1973, it could curtail residential construction in 1974 and 1975. In recent years, subsidized housing programs have contributed substantially to the district's residential construction industry. The 1968 Housing and Urban Development Act's Section 235 and 236 programs accounted for approximately 12 percent of the 45,241 housing units authorized in the district in 1972.



The Section 235 program, which provides mortgage subsidies to low- and moderate-income individuals, comprised 5 to 10 percent of district single-family home construction in 1972. Although there is a backlog of approved Section 235 houses to be built in 1973, district builders' participation in this program has been dwindling. In Minnesota, about 35 builders were at one time building Section 235 homes but currently only 6 remain with the program. Many builders feel that they cannot profitably build a house priced to qualify for the $21,200 maximum mortgage allowed on a three-bedroom Section 235 home.

Between 15 and 20 percent of the district's multifamily housing constructed last year can be attributed to the Section 236 program. Section 236 provides rent subsidies to low- and moderate-income persons residing in multifamily units sponsored by nonprofit or limited-profit developers. District HUD officials report that a sufficient number of projects were under way prior to the freeze so that construction under this program will probably not slacken in 1973. Because Section 236 projects require a 12- to 18-month lead time before construction begins, district multifamily housing construction in 1974 and 1975 could be affected if the freeze remains through 1973 and into 1974.

NINTH DISTRICT income and finance

INDICATOR		UNIT	1973 JAN.	1972 DEC.	1972 NOV.	1971 DEC.	Percent Change DEC.-DEC.
MEASURES OF CONSUMER INCOME & FINANCIAL POSITION	Total Personal Income *						
	Nonagricultural Personal Income *						
	Average Weekly Earnings in Manufacturing [1]	Dollars	n.a.	169.86e	168.58p	158.28	+ 7.3
	Consumer Installment Credit Outstanding [2]	Million $	n.a.	1,811	1,806	1,488	+21.7
	Time and Savings Deposits at Member Banks	Million $	7,540	7,454	7,354	6,490	+14.9
	Savings Balances at Savings & Loan Assoc. [3]	Million $	n.a.	5,179	5,105	4,406	+17.5
	Cash Farm Receipts [3]	Million $	n.a.	517	618	454	+13.9
MEASURES OF FINANCIAL CONDITION OF MEMBER BANKS	CITY BANKS [4,5]						
	Adjusted Loans and Discounts [6]	Million $	3,504	3,439	3,344	2,867	+20.0
	Commercial and Industrial Loans	Million $	1,583	1,565	1,508	1,267	+23.5
	Real Estate Loans	Million $	631	625	615	502	+24.5
	Gross Demand Deposits	Million $	2,162	2,386	2,191	2,435	- 2.0
	Time Deposits	Million $	2,082	2,126	2,068	1,897	+12.1
	U.S. Government Securities	Million $	514	582	488	622	- 6.4
	Other Securities	Million $	798	845	765	651	+29.8
	COUNTRY BANKS [4,7]						
	Loans and Discounts	Million $	5,066	5,080	5,089	4,361	+16.5
	Gross Demand Deposits	Million $	2,738	2,873	2,794	2,708	+ 6.1
	Time Deposits	Million $	5,457	5,328	5,285	4,592	+16.0
	U.S. Government Securities	Million $	1,241	1,232	1,199	1,338	- 7.9
	Other Securities	Million $	1,723	1,706	1,670	1,481	+15.2
MEASURES OF RESERVE POSITION AND "LIQUIDITY" OF MEMBER BANKS	Total Reserves [8]	Million $	743	721	735	770	- 6.4
	Required Reserves	Million $	738	715	726	766	- 6.7
	Excess Reserves	Million $	5	6	9	4	+50.0
	Borrowings from FRB	Million $	21	3	3	3	
	Ratio of Loans to Total Deposits—City Banks [4]	Percent	83.8	77.0	81.9	68.5	+12.4
	Ratio of Loans to Total Deposits—Country Banks [4]	Percent	61.8	61.9	63.0	59.7	+ 3.7
MEASURES OF PRICE LEVELS	Consumer Price Index—Minneapolis [9,10]	Index	n.a.	n.a.	n.a.	n.a.	
	Prices Received by Farmers—Minnesota [9]	Index	145	137	126	111	+23.4

NOTES

e—Partially estimated; all data not available

n.a.—Not available

p—Preliminary; subject to revision

r—Revised

sa—Seasonally adjusted

*—District and U.S. data not comparable

saar—Seasonally adjusted annual rate

FOOTNOTES

1. Excluding Northwestern Wisconsin
2. All commercial banks; estimated by sample
3. Excluding Northwestern Wisconsin and Upper Michigan
4. Last Wednesday of the month figures
5. Selected banks in major cities
6. Net loans and discounts less loans to domestic commercial city banks
7. All member banks, excluding the selected major city banks
8. Average of daily figures of the four or five weeks ending on Wednesday which contain at least four days falling within the month
9. Index: 1967 Base Period
10. Quarterly

UNITED STATES income and finance

Percent Change DEC.-DEC.	1973 JAN.	1972 DEC.	1972 NOV.	1971 DEC.	UNIT	INDICATOR
						MEASURES OF CONSUMER INCOME & FINANCIAL POSITION
+ 10.4	n.a.	983.4p	975.7	890.4	Billion $, saar	Total Personal Income
+ 10.2	n.a.	953.0p	947.2	865.0	Billion $, saar	Nonagricultural Personal Income
+ 8.6	159.20p	163.15p	159.49	150.18	Dollars	Average Weekly Earnings in Manufacturing
+ 16.8	n.a.	59.8	58.9	51.2	Billion $	Consumer Installment Credit Outstanding[2]
+ 14.6	n.a.	242.1	238.5	211.3	Billion $	Time and Savings Deposits at Member Banks
	n.a.	n.a.	203.9	174.5	Billion $	Savings Balances at Savings & Loan Assoc.
+ 9.6	n.a.	5.7	6.9	5.2	Billion $	Cash Farm Receipts
						MEASURES OF FINANCIAL CONDITION OF MEMBER BANKS
						CITY BANKS[4,5]
+ 18.0	n.a.	227.2	217.4	192.6	Billion $	Adjusted Loans and Discounts[6]
+ 8.5	n.a.	91.0	88.6	83.9	Billion $	Commercial and Industrial Loans
+ 19.2	n.a.	45.9	45.6	38.5	Billion $	Real Estate Loans
+ 8.5	n.a.	166.0	152.0	153.0	Billion $	Gross Demand Deposits
+ 14.2	n.a.	161.3	158.9	141.3	Billion $	Time Deposits
- 1.4	n.a.	28.6	27.9	29.0	Billion $	U.S. Government Securities
+ 6.9	n.a.	55.9	55.5	52.3	Billion $	Other Securities
						COUNTRY BANKS[4,7]
+ 16.8	n.a.	85.6	83.7	73.3	Billion $	Loans and Discounts
+ 12.6	n.a.	58.9	55.9	52.3	Billion $	Gross Demand Deposits
+ 15.3	n.a.	80.8	79.6	70.1	Billion $	Time Deposits
+ 1.1	n.a.	18.3	17.9	18.1	Billion $	U.S. Government Securities
+ 15.2	n.a.	31.1	30.8	27.0	Billion $	Other Securities
						MEASURES OF RESERVE POSITION AND "LIQUIDITY" OF MEMBER BANKS
+ 0.0	n.a.	31,252	31,774	31,243	Million $	Total Reserves[8]
- 0.3	n.a.	31,004	31,414	31,085	Million $	Required Reserves
+ 57.0	n.a.	248	360	158	Million $	Excess Reserves
+749.1	n.a.	934	611	110	Million $	Borrowings from FRB
+ 6.5	n.a.	73.5	74.2	69.0	Percent	Ratio of Loans to Total Deposits – City Banks[4]
+ 2.2	n.a.	61.2	61.8	59.9	Percent	Ratio of Loans to Total Deposits – Country Banks[4]
						MEASURES OF PRICE LEVELS
+ 3.4	n.a.	127.3	126.9	123.1	Index	Consumer Price Index[9]
+ 18.1	144	137	130	116	Index	Prices Received by Farmers[9]

SOURCES

PERSONAL INCOME: U.S. Department of Commerce, Office of Business Economics

AVERAGE WEEKLY EARNINGS: Michigan, Minnesota, Montana, North Dakota, and South Dakota Employment Security Departments; U.S. Department of Labor, Bureau of Labor Statistics

COMMERCIAL BANK FINANCIAL DATA: Federal Reserve Bank of Minneapolis; Board of Governors of Federal Reserve System

SAVINGS AND LOAN ASSOCIATIONS: Federal Home Loan Bank Board

CASH RECEIPTS FROM FARM MARKETINGS: U.S. Department of Agriculture

CONSUMER PRICE INDEX: U.S. Department of Labor, Bureau of Labor Statistics

PRICES RECEIVED BY FARMERS: U.S. Department of Agriculture; Minnesota Farm Price Report

NINTH DISTRICT production and employment

INDICATOR		UNIT	1972 DEC.	1972 NOV.	1971 DEC.	Percent Change DEC.-DEC.
MEASURES OF PRODUCTION AND FACTOR INPUTS TO PRODUCTION	Total Industrial Production *					
	Electrical Energy Consumption: Mfg. and Mining [1]	Index, sa	144	141	131	+ 9.9
	Production Worker Manhours: [1]	Index, sa	108p	109	100	+ 8.0
	Manufacturing	Index, sa	111p	112	101	+ 9.9
	Mining	Index, sa	90p	93	96	- 6.2
	Total Construction Contracts Awarded	Million $, sa	249.0	239.7	314.3	- 15.8
	Residential Buildings	Million $, sa	120.6	100.8	71.6	+ 68.4
	Nonresidential Buildings	Million $, sa	84.6	36.6	59.6	+ 41.9
	All Other Construction	Million $, sa	43.8	102.3	183.1	- 76.1
	Bldg. Permits: New Housing Units [2]	Number	8,571	3,013	2,990	+186.7 [7]
MEASURES OF MANPOWER UTILIZATION	Civilian Work Force [3]	Thousands, sa	2,699p	2,669	2,642	+ 2.2
	Total Civilian Employment	Thousands, sa	2,545p	2,533	2,496	+ 2.0
	Number Unemployed	Thousands, sa	154p	136	146	+ 5.5
	Unemployment Rate [3]	Percent, sa	5.7p	5.1	5.5	+ 3.6
	Average Weekly Hours in Manufacturing [3]	Hours, sa	41.5e	42.0p	40.5	+ 2.5
EMPLOYMENT BY INDUSTRY SECTOR	Wage and Salary Employment, Nonfarm [3]	Thousands, sa	2,008p	2,005	1,960	+ 2.4
	Manufacturing	Thousands, sa	382p	379	365	+ 4.7
	Mining	Thousands, sa	30p	31	30	
	Construction	Thousands, sa	94p	96	100	- 6.0
	Transport., Comm., & Public Utilities	Thousands, sa	133p	133	131	+ 1.5
	Trade	Thousands, sa	492p	492	478	+ 2.9
	Finance, Insurance & Real Estate	Thousands, sa	95p	95	92	+ 3.3
	Service Industries	Thousands, sa	336p	334	326	+ 3.1
	Government	Thousands, sa	446p	445	438	+ 1.8
MEASURES OF SPENDING	Total Retail Sales *					
	New Passenger Car Registrations	Thousands, sa	n.a.	n.a.	23.9	
	Bank Debits [4]	Billion $, saar	246.3	235.1	179.3	+ 37.4

NOTES

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r–Revised

sa–Seasonally adjusted

*–District and U.S. data not comparable

saar–Seasonally adjusted annual rate

FOOTNOTES

1. Index: 1967 Base Period; Weights: 1967
2. A sample of permit-issuing centers
3. Excluding Northwestern Wisconsin
4. Six standard metropolitan statistical areas
5. A sample of centers blown up to represent total permits issued
6. 226 standard metropolitan statistical areas, excluding the seven leading centers
7. Much of this increase can be attributed to the Service Availability Charge (SAC) effective January 1, 1973 throughout the seven-county Minneapolis/St. Paul metro area. To avoid paying this special assessment on sewer systems, builders took out permits in December for buildings to be constructed later this year.

UNITED STATES production and employment

Percent Change DEC.-DEC.	1972 DEC.	1972 NOV.	1971 DEC.	UNIT	INDICATOR	
+10.4	119.3p	118.4	108.1	Index, sa	Total Industrial Production	**MEASURES OF PRODUCTION AND FACTOR INPUTS TO PRODUCTION**
					Electrical Energy Consumption: Mfg. and Mining *	
+ 5.3	99p	99p	94	Index, sa	Production Worker Manhours: [1]	
+ 6.4	100p	100p	94	Index, sa	Manufacturing	
	94p	94p	94	Index, sa	Mining	
+ 2.9	7,323.7	8,240.7	7,114.3	Million $, sa	Total Construction Contracts Awarded	
+ 3.6	3,598.6	4,195.9	3,472.7	Million $, sa	Residential Buildings	
+14.2	2,477.0	2,381.7	2,168.2	Million $, sa	Nonresidential Buildings	
-15.3	1,248.1	1,663.1	1,473.4	Million $, sa	All Other Construction	
	n.a.	n.a.	169.9	Thousands	Bldg. Permits: New Housing Units [5]	
+ 2.4	87,267p	87,023	85,225	Thousands, sa	Civilian Work Force	**MEASURES OF MANPOWER UTILIZATION**
+ 3.3	82,780p	82,525	80,098	Thousands, sa	Total Civilian Employment	
-12.5	4,487p	4,498	5,127	Thousands, sa	Number Unemployed	
-15.0	5.1p	5.2	6.0	Percent, sa	Unemployment Rate	
+ 1.2	40.7p	40.9	40.2	Hours, sa	Average Weekly Hours in Manufacturing	
+ 3.8	74,024p	73,899	71,291	Thousands, sa	Wage and Salary Employment, Nonfarm	**EMPLOYMENT BY INDUSTRY SECTOR**
+ 4.9	19,421p	19,324	18,519	Thousands, sa	Manufacturing	
- 0.5	608p	609	611	Thousands, sa	Mining	
	3,468p	3,524	3,468	Thousands, sa	Construction	
+ 2.9	4,559p	4,549	4,432	Thousands, sa	Transport., Comm., & Public Utilities	
+ 3.9	15,924p	15,954	15,333	Thousands, sa	Trade	
+ 3.5	3,989p	3,981	3,855	Thousands, sa	Finance, Insurance & Real Estate	
+ 4.3	12,562p	12,497	12,042	Thousands, sa	Service Industries	
+ 3.5	13,493p	13,461	13,031	Thousands, sa	Government	
+11.5	38.9	38.8	34.9	Million $, sa	Total Retail Sales	**MEASURES OF SPENDING**
	n.a.	954.0	826.0	Thousands, sa	New Passenger Car Registrations	
+17.1	4,682.2	4,763.5	3,999.4	Billion $, saar	Bank Debits [6]	

SOURCES

INDUSTRIAL PRODUCTION: Board of Governors of Federal Reserve System

ELECTRICAL ENERGY CONSUMPTION: Federal Reserve Bank of Minneapolis

PRODUCTION WORKER MANHOURS: Federal Reserve Bank of Minneapolis

CONSTRUCTION CONTRACTS AWARDED: Board of Governors of Federal Reserve System; F. W. Dodge Corporation

NEW HOUSING UNITS AUTHORIZED: Federal Reserve Bank of Minneapolis; U.S. Department of Commerce, Bureau of Census

EMPLOYMENT, UNEMPLOYMENT, AND HOURS: Michigan, Minnesota, Montana, North Dakota, and South Dakota Employment Security Departments; U.S. Department of Labor, Bureau of Labor Statistics

RETAIL SALES: U.S. Department of Commerce, Bureau of Census

NEW PASSENGER CAR REGISTRATIONS: Automotive News Magazine

BANK DEBITS: Board of Governors of Federal Reserve System

BOARD MODIFIES REGULATIONS D & J

Last November the Board of Governors of the Federal Reserve System instituted changes in Regulations D and J intended to introduce a greater degree of equity into the banking system and speed up the check collection mechanism. The alteration in Regulation D restructures reserve requirements applicable to demand deposits of member banks. The modification in Regulation J requires all banks served by the Federal Reserve check clearing system to pay for checks drawn on them in immediately available funds on the same day the Fed presents the checks for payment.

REGULATION D: RESERVE REQUIREMENTS

The Board's amendment to Regulation D which affects net demand deposits (total demand deposits less checks in process of collection and amounts due from other banks) is set forth in the following graduated schedule:

Net Demand Deposits ($ mil.)	Marginal Reserve Requirement Ratio (%)
0-2	8
2-10	10
10-100	12
100-400	13
Over 400	17½

Before the change, member banks designated as "country banks" were required to hold reserves equal to 12½ percent of the first $5 million of net demand deposits and 13 percent of the remainder. Banks categorized as "reserve city banks," the larger banks in Minneapolis and St. Paul, had reserve requirements of 17 percent on the first $5 million net demand deposits and 17½ percent on the excess.

The change in Regulation D makes the reserve requirement ratio schedule more progressive and eliminates reserve requirement differences between "country" and "reserve city" banks. The revised schedule enables smaller banks to allocate a greater proportion of assets to loans and investments. By standardizing reserve requirements, Regulation D insures that banks of equal size are subject to the same reserve ratio regardless of location.

REGULATION J: CHECK COLLECTION

The modification in Regulation J, requiring banks to pay immediately for checks presented by the Fed, makes universal a requirement which formerly applied only to banks located in cities with Federal Reserve offices or in areas served by Regional Check Processing Centers (RCPCs). The new collection procedures mean that reserve balances at the Fed are drawn down on the same day the checks are presented for payment. Previously, banks located outside reserve cities and RCPC areas were allowed one day of grace before their reserves were drawn down. Although the change reduces the reserve balances of some banks, it is a step toward more equitable treatment for all.

The faster collection of funds resulting from this change permits the Fed to speed up its payments to depositing banks. This, in turn, may lead depositing banks to permit some deposit customers to make withdrawals sooner.

When paying and depositing banks are located within the same Federal Reserve territory, the Fed normally reduces the reserve account of paying banks on the same day that it increases the reserve accounts of receiving banks. Therefore, shortening the collection process by one day also shortens by one day the interval depositing banks must wait for credit from the Fed. Banks generally credit small customer deposit accounts at the time of deposit and allow these balances to be drawn down immediately. Large deposit customers, however, may be required to await collection of funds by the bank before withdrawing. A faster collection period may, therefore, result in faster availability of funds and increased earnings for certain bank customers.

Another expected result of faster check collection is a reduction of Federal Reserve float. Fed float results from the practice of increasing the reserve balances of depositing banks for checks presented to the Fed for collection before reducing the reserve accounts of some of the paying banks—primarily those located in other Federal Reserve districts. Because Federal Reserve float directly and unpredictably affects bank reserves and the amount of credit in the economy, monetary authorities have long desired to reduce the level of float.

COMBINED EFFECT ON BANK RESERVES

The Board expected the reduction of required reserves (Regulation D) to exceed the contraction in member bank reserves (Regulation J) by $1.5 billion. In the absence of offsetting action by monetary authorities, the increase in excess reserves resulting from these regulatory changes would permit banks to expand loans and investments. Since expansion was not the purpose behind the changes, the Board prepared to eliminate excess reserves through open market operations.

Although the changes had a neutral effect on total bank reserves, they did affect the reserve positions of individual banks. To help banks whose reserve positions suffered—mainly because of the change in Regulation J—the Board authorized reserve banks to temporarily waive penalties on certain reserve deficiencies. In addition, Federal Reserve credit was made available to both member and nonmember banks if the changes impaired either their liquidity positions or community service activities.

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