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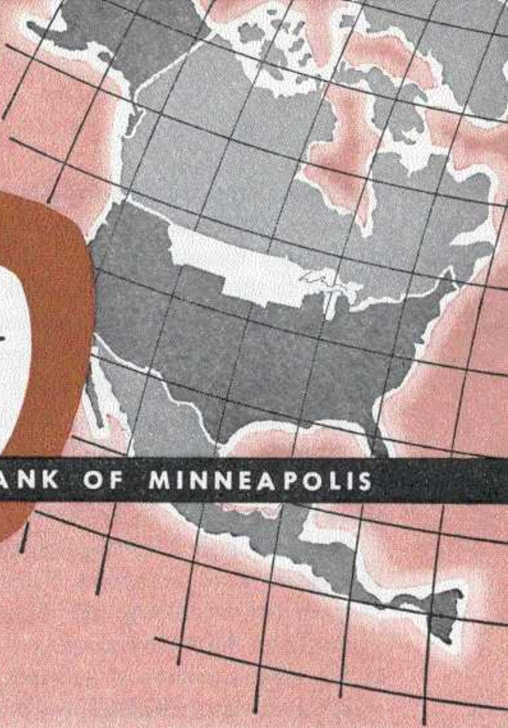

Monthly Review
OF THE FEDERAL RESERVE BANK OF MINNEAPOLIS

Strong seasonal upturn noted

A high level of activity in construction and mining during recent weeks has provided a strong upward push to the district's economy. Total construction in terms of dollar outlays for contract awards and new building permits showed a gain in April of 20 to 22 percent over April of 1958. The economic upsurge on the iron ranges during April is indicated by the shipment of about 3 million tons of iron ore from Lake Superior ports as compared with shipments of less than 100,000 tons in April last year. However, the current tonnage shipments are low relative to previous boom periods. Total district April carloadings, influenced to some degree by the bulge in ore shipments, showed a 44 percent increase over last year.

Employment in all district mining in April this year was up 15 percent from a year ago. In construction employment, the April gain was 4 percent. The total number of insured unemployed people in April was down 22 percent from a year ago and the number of initial claims for unemployment insurance was 28 percent less.

A 15 percent upsurge in the bank debit figures for April is further evidence of the region's economic resurgence from the recession period of a year earlier. (Bank debits represent the estimated dollar volume of checks written against demand deposits.) The demand for bank loans, particularly from farmers and businessmen, has been strong in recent weeks. Total loans and discounts at member banks during April were up 10½ percent from April of 1958. Bank deposits, both demand

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and time, have also showed substantial gains.

Gains in district department store sales during April were disappointingly small, owing in part at least to the early Easter period this year.

The district-wide early season drouth was broken by widespread but by no means general or fully adequate rains. The soil moisture situation remains somewhat spotty as this is written in late May, with topsoil moisture generally good but subsoil moisture supplies inadequate in many parts of the area.

Farmers' cash incomes, however, continue to register at 6 to 7 percent higher levels than a year earlier, thanks to the heavy carryover of grains from the 1958 record crop production and to the large numbers of livestock on farms from which current marketings are drawn. The favorable farm income picture during the past year has been a factor in boosting farm land values from 6 to 10 percent in district states.

An exceptionally heavy winter kill of alfalfa and clover due to cold weather and lack of protective snow cover this past winter is now apparent. Hay supplies could be on the short side in the winter of 1959-60, particularly in view of the continued strong build-up of livestock numbers.

The current economic recovery in the Ninth district apparently has been paralleling that of the nation as a whole, but the district economic outlook is somewhat more clouded because of uncertain crop prospects for 1959 and the lower drift of farm prices.

The following selected topics describe particular aspects of the district's current economic scene:

IRON ORE SHIPMENTS ABOVE YEAR AGO

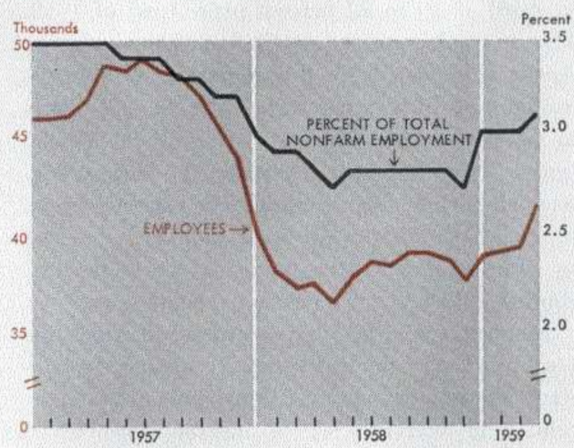
The opening of the iron ore shipping season this spring was delayed by a thick layer of ice on the bays and channels of the Great Lakes navigation routes. Even so, the shipping season was off to a brisk start in April. The first ore boat was loaded on April 10 at Escanaba on Lake Michigan, traditionally the first port to be opened.

According to the figures released by the American Iron association, almost 3 million gross tons of iron ore were shipped in April from Lake Superior to lower lake ports. Of this amount, 2,910,070 tons were shipped from U. S. ports and 67,953 tons from Canadian ports. In 1958, the Great Lakes shipping season was also opened in April but only 62,500 tons of ore were shipped during the month. Of this amount 33,446 tons were taconite pellets shipped from Silver Bay, Minnesota.

However, the almost 3 million tons of ore shipped in April of this year is far from a record. In April 1957, just under 4 million tons were shipped and in 1956, over 5½ million tons. Back in 1949 and in 1953, the tonnage was even larger: 8.9 and 8.4 million tons, respectively.

This year the opening of navigation on the Great Lakes was urgently needed to replenish ore stocks at steel furnaces. Steel production last January began to exceed 2 million tons weekly, and by March stocks of ore at some steel mills were depleted. Furthermore, the fact that the United Steelworkers of America contract expires June 30 has created the contingency of a strike

District employment in mining



which would halt ore shipments as well as steel production. This situation has added urgency to the movement of ore to steel mills.

Even prior to the opening of the Great Lakes navigation season, the activity rose sharply at district iron ore mines. In Upper Michigan and in northern Wisconsin, especially in the underground mines, the workers on short workweeks were put back on a normal week and many laid-off workers were recalled. In Minnesota, employment has continued to increase since the first of the year; in mid-April employment was 5½ percent above the mid-March figure and 26½ percent above the April 1958 figure. Last year there was very little pickup in employment during the ore shipping season. For instance, in the second quarter of 1958 Minnesota employment in metal mining was actually down 7 percent from the average in the first quarter of that year and up only 6 percent in the third quarter.

BANK DEBITS HOLD UP WELL

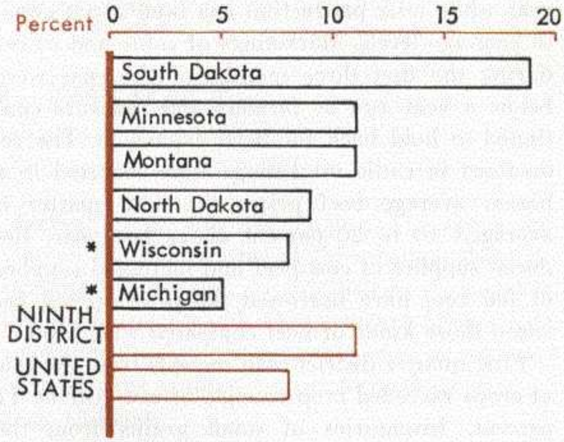
Since the first of the year, bank debits—the amount of checks drawn on banks—has held up well in this district. Generally, debits decline during February, March and April. Because the volume has held up well this year, the percent increase from a year ago has been quite large. In February, debits were up 9 percent and in both March and April, 15 percent.

Bank debits measure the volume of business transacted. The usefulness of the bank debits figure lies in the close relationship observed between debits and such general measures of economic activity as Gross National Product and disposable personal income.

Because economic activity in the district mining regions was severely depressed by the recent recession, bank debits in most communities serving these regions were down in 1958 from the preceding year. In the region including northeastern Minnesota, northern Wisconsin and Upper Michigan, debits in February for the first time since

Bank debits for first four months of 1959

(percent change from a year ago)



*Includes only Ninth district part of state.

1957 again were above the corresponding month of a year ago. In February, debits were up 5 percent; in March, 7 percent; and in April, 13 percent. In western Montana, where mining is also important, debits in 1958 also fell off but not as much as in the other mining regions. As compared with last year, debits in the first quarter were up 5 percent and in April, 15 percent.

The largest increases in debits during the first four months of this year from a year ago occurred in South Dakota, eastern Montana and, to a lesser extent, in North Dakota. The large increases in debits in these regions reflects the heavy marketings of 1958 farm crops and livestock.

CASH FARM INCOME HIGHER

According to U. S. Department of Agriculture estimates, first quarter cash receipts from farm marketings in the Ninth district were $811 million; this was 6 percent above a year ago.

Receipts from the sale of livestock and livestock products in the district for the first quarter amounted to $529 million, up 3 percent from last year. Marketings of hogs and poultry products during the first quarter exceeded year-ago levels, while prices for hogs and poultry products averaged 20 to 30 percent below last year. First quarter milk prices have been slightly below last year while milk production has been about equal to year-ago levels. Marketings of cattle and calves during the first three months of the year were below a year ago as farmers and ranchers continued to hold back for herd expansion. The reductions in cattle marketings were reflected in a higher average beef price; the first quarter it averaged 10 to 20 percent above last year. Reduced supplies of cow beef and increased supplies of fed beef have narrowed the price spread between those kinds of beef compared with 1958.

First quarter district cash receipts from the sale of crops exceeded crop receipts of last year by 11 percent. Inventories of small grains from the record crop in 1958 have maintained volumes of marketings above a year earlier. Prices of small grains with the exception of wheat have about equaled year-ago levels; wheat has been priced about 8 percent below last year. On the other hand, the corn crop, which was not large but of good quality, has been moving at prices 25 to 30 percent above the prices received in 1958.

LOAN EXPANSION CONTINUES

District member banks reported that their loans increased $24 million in April. In the like month a year earlier almost no loan gain occurred. Loan expansion this spring plus seasonal deposit decline have required banks to liquidate $36 million in security holdings in April, slightly above the cutback recorded in April last year.

Farm loan increases are contributing to loan expansion in the district according to the March 12 call report. Gains in real estate and other farm loans more than offset a decline in the amount of loans guaranteed by the Commodity Credit Corporation as compared with the March call report of a year earlier. Relative to a year earlier, the over-all gain in farm loans amounted to 3 percent while total district loans advanced 7 percent.

Additional information about the composition of loan demand in the district can be obtained from the loan statistics of the weekly reporting banks. In the five week period ended May 13 total loans other than loans to banks rose $36 million at 19 major banks in the district. Accounting for most of the gain, commercial and industrial loans, often secured by inventory, increased $24 million during this period. The remainder of the over-all gain is attributable to a $12 million rise in 'other' loans. These include loans to individuals and to nonbank financial institutions.

MOISTURE IMPROVES CROP OUTLOOK

Recent crop reports indicate that drouth conditions were alleviated throughout much of the district by moderate-to-heavy rains early in May. Following the rains, top soil conditions were reported as adequate in most areas. However, subsoil moisture continues in short supply throughout most of the Dakotas and much of Minnesota. Substantial subsequent rains will be needed to maintain continued plant growth.

According to the May 1 U. S. Department of Agriculture's estimate, a winter wheat crop of 50 million bushels is expected in the Ninth district; this is 39 percent less than the winter wheat crop which was harvested last year. The May 1 estimate at 50 million bushels was 5 million bushels lower than the April 1 estimate. A revision in the estimate of the winter wheat crop was based on a reassessment of the winter kill and the unfavorable growing conditions experienced during April.

WINTER WHEAT PRODUCTION

	1958	1959*	Percent change
	(bushels)		
Montana	63,369,000	43,368,000	—32
South Dakota	17,250,000	6,090,000	—65
Minnesota	961,000	512,000	—47
Total	81,580,000	49,970,000	—39

*Indicated production based on the May 1 estimate U. S. Department of Agriculture.

1958 Banking score card: The operating ratios report

Early in May this year, the Federal Reserve Bank of Minneapolis sent a list of 37 operating ratios to member banks in the Ninth Federal Reserve district. The source of these ratios was the basic operating data of individual Ninth district member banks. From these data we derived financial ratios for individual member banks. The ratios were then classified according to the deposit size of banks and averaged to yield composite ratios, repesenting the average bank in various deposit size classes in the district. The results were subsequently published as our operating ratios report. This report permits individual banks to compare their own ratios with district averages for comparable banks.

In addition to banker interest, the operating ratios report contains information of general interest to both the financial specialist and the casual observer of the financial picture. The ratios provide an excellent source of information about the structure of banking in the district. They reveal the depth and breadth of significant financial developments which are available only in summary form in most regular sources of banking data.

Size of bank

Most member banks in the Ninth Federal Reserve district are small by national standards. About 60 percent had less than $5 million in total deposits in 1958 in contrast to about 50 percent for the nation as a whole. And only 5 percent of all member banks in this district had deposits totaling over $25 million in contrast to 7 percent in the entire Federal Reserve System. Since each bank is given a weight of one in computing the over-all average operating ratios, district averages, for the most part, reflect the ratios of the smaller banks.

Relative profits and salaries at banks of various deposit sizes

*This ratio increases at larger banks.

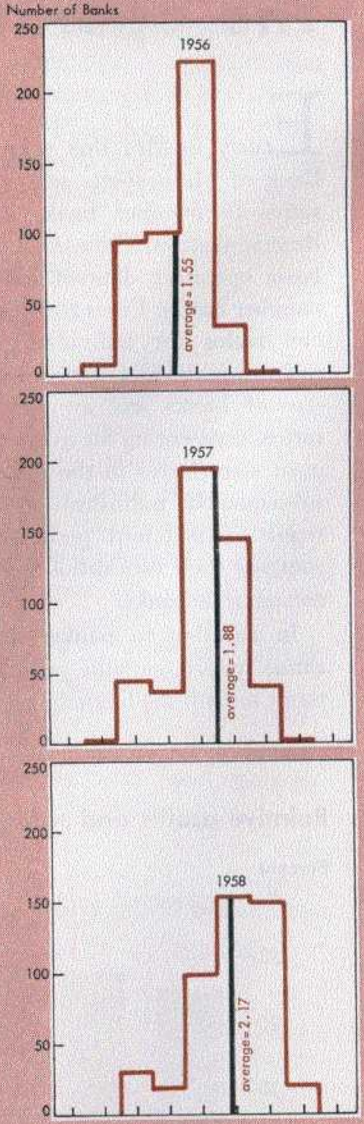
**This ratio increases at smaller banks.

To learn more about what is behind the over-all average ratios, we can look at a stratification of the ratios into size subclasses. Examining the averages of individual bank ratios from the largest to the smallest size class reveals that interest on both government and other securities provided relatively larger sources of earnings at the smaller banks than at the larger ones. Interest on government securities averaged 23 percent of total earnings on the average at the 92 district member banks with less than $2 million in deposits, and only 18 percent at the 23 district banks with over $25 million in deposits. And earnings on other securities accounted for nearly 10 percent of total earnings at the average 'small' bank but only half that at the average 'large' bank. In small measure, higher relative security earnings of the smaller banks resulted from higher average yields on their securities. But to a major degree, the proportionately higher security earnings at the smaller banks stemmed from their relatively greater holdings of securities. Government and other securities averaged 33 percent and 12 percent, respectively, of total assets at member banks with less than $2 million in deposits in contrast to 28 and 7 percent at banks with more than $25 million in deposits. The average of the ratios of earnings on loans showed just the reverse relationship—the result, largely, of loans making up a relatively greater percentage of total earning assets at larger banks than at smaller member banks in the district.

The rate of return on loans tended to rise as the deposit size of a bank declined. The over-all district average of the individual bank's rates of return on loans advanced again in 1958 for the fourth successive year. In part, this was due to the fact that many loans outstanding during 1958 were contracted before money eased and rates fell during late 1957 and early 1958. And, it may also reflect the fact that interest charges on loans lag more in response to changes in credit availability than do interest rates on government securities which, of course, declined sharply in early 1958. Declining government security yields were recorded in the average of the individual banks' effective interest returns on government securities.

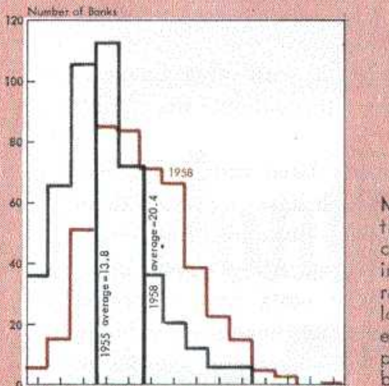
On the expense side of the ledger, the average bank in the smaller deposit classes tended to have proportionately greater salary and wage expenses and time deposit interest payments but relatively less other expenses. As the deposit size of banks decreased, profits fell both as a percent of total capital and as a percent of total assets according to the 1958 operating ratios figures. This fact may be the result of economies of scale in banking. It may also reflect the tendency for smaller banks to hold relatively greater capital per dollar of assets. Or it may simply show that smaller banks have compensated

Effective interest rates*



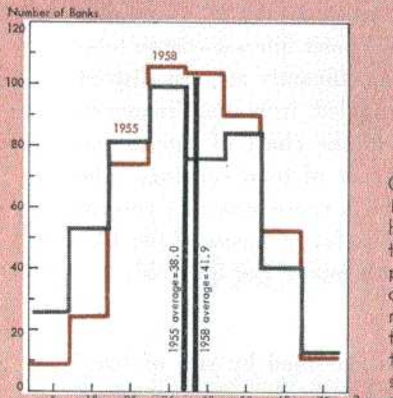
*Interest expense per dollar of time deposits

Interest on time deposits to total earnings



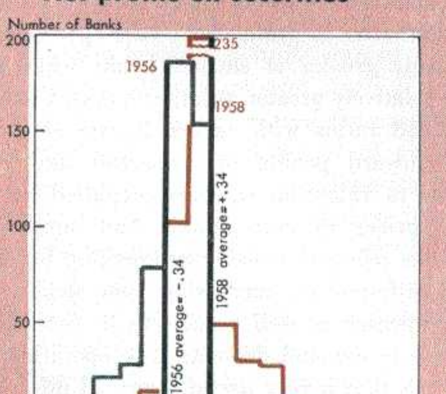
More banks were in the higher ratio classes in 1958 than in 1955. The ratios ranged from very low fractions of total earnings to about 50 percent at some banks.

Time deposits to total deposits



Contrasting 1958 to 1955, more banks had higher ratios of time to total deposits in all but one of the five largest ratio classes, while the reverse held true for the three smallest classes.

Net profits on securities



There were 106 banks recording neither profits nor losses on securities in 1956 and only 70 such banks in 1958. Even though the average bank experienced a security loss in 1956 and a gain in 1958, many banks had a widely different experience.

owners more by way of salaries than by way of dividends. The chart of relative profit and salary averages shows a wide variability in these averages at banks of various deposit sizes. The ratio of net profits to total assets ranged in successive steps from .78 percent at banks with $2 million or less deposits to 1.08 percent at banks with $25 million or more deposits. Salary and wage payments relative to total earnings, on the other hand, tended to be inversely related to size of bank. Taxes took a relatively larger bite out of the profits at the larger banks; being 17.1 percent on the average at banks in the largest size class in contrast to 7.3 percent at the smallest banks. But despite higher taxes, dividends of the large banks on the average were relatively larger than those at the smaller banks. Cash dividends as a fraction of capital amounted to 5.2 percent at the largest banks and 3.2 percent at the smallest banks. Each figure was about one-third of the ratio of net profits to total capital.

Security profits

Reflecting the general credit situation, bond prices increased substantially in early 1958 and many district banks sold securities at a capital gain. The over-all average of district member bank profits on securities increased to .34 percent of total securities in 1958 reversing an average loss situation a year earlier. Since banks may credit capital gains to valuation reserves or to profits, part of the bond value gains recorded in 1958 were reflected in credits to valuation reserves.

The chart of profits on securities compares the distribution of the number of banks experiencing various losses and gains on securities in 1958 with the distribution in 1956. A great many banks in both years had neither profits nor losses on securities. Some of these probably did not sell any securities but followed the practice of holding bonds until maturity if possible. But fewer banks reported neither losses nor gains on securities in 1958 than in 1956 and many more banks reported profits.

This shifted the distribution to the right. Even though some banks still recorded losses on securities in 1958, the number was far less than in 1956. Profit taking was most pronounced at larger district banks. Relative to total earnings security profits averaged 6 percent and 8 percent, respectively, at banks in the $10 to $25 million deposit size class and in the over $25 million class in contrast to a district average of only 2 percent.

Time deposit interest

What happened to time deposits in 1958 is further evidence of the effect of the economic climate on individual member banks in the district. The relative attractiveness of yields as well as the uncertainties associated with the recession led savers to pump a substantial volume of funds into time and savings accounts at district member banks in 1958. As a result, the average of individual member bank ratios of time to total deposits climbed to 41.9 percent in 1958, up from 39.5 percent a year earlier and 38.0 percent in 1955. Relative to 1955, most banks in the district experienced significantly greater growth in time than in demand deposits as is shown in the chart of time deposits as a fraction of total deposits.

Effective January 1, 1957, the Federal Reserve Board increased the maximum permissible interest rates on time and savings deposits. Subsequent adoption of a higher rate schedule by many banks is reflected by the shift in the effective interest rates of district member banks since that time. The ratio of interest payment to time deposits, the effective rate paid on time and savings deposits, increased to 2.2 percent in 1958, up from 1.9 percent a year earlier and from 1.6 percent in 1956.

The chart of interest expense per dollar of time deposits records the number of banks with various average interest rates on time deposits. The distribution has shifted to the right since 1956, the result of increasing numbers of banks paying higher rates on time deposits. This fact no doubt reflects the increased competition of commercial banks among themselves and with other financial institutions for savings throughout the Ninth district.

Increased time deposits have provided banks with additional funds which have permitted them to hold more earning assets. But added funds have not been without their cost. All expenses other than time deposit interest costs have increased greatly but relative to earnings have been stable in recent years. The ratio of wages and salaries to earnings, on the average, was 29.5 percent in 1958, only 1.3 percentage points below the average for the past 19 years. And other current expenses have shown comparable stability in recent years. But the percentage of time deposit interest cost to total earnings has jumped significantly at most district banks as is clearly revealed from the frequency distribution recorded in the chart of interest on time deposits as a percent of total earnings. The average of individual bank ratios was 20.4 percent of total earnings in 1958, far in excess of the 13.8 percent interest to earnings average for 1955.

Summary

The operating ratios classified by size of bank provided evidence that earnings on loans were relatively more important to larger district member banks than to smaller ones. Salaries and wages, an alternative to profits for owner-operators, were relatively greater at smaller banks while profits were relatively greater at larger banks. Comparing the 1958 ratios with earlier figures showed the shift toward profits on securities and toward credits to valuation reserves permitted by rising bond prices in early 1958. And similar comparisons reflected growing competition for savings as manifested by increasing time deposit rates and expenses as well as growth in time deposits relative to demand deposits. The operating ratios report is thus a very useful source of information. It provides us with a view of banking conditions as most bankers experienced them. And it provides bankers with an annual score card matching their performance against that of the other banks.