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Monthly Review

OF THE FEDERAL RESERVE BANK OF MINNEAPOLIS

Business indicators show gain

With the notable exception of agriculture, most measures indicate the economy has been performing reasonably well in recent weeks, both in the Ninth district and nationally. Business generally has not expanded as much as was expected at the year's beginning, but present trends can hardly be called discouraging.

Many measures of business activity in the Ninth district, however, have either advanced less or declined more percentagewise since early last fall than has been true for the nation as a whole. Total district nonagricultural employment during the first quarter of 1960, for example, showed a 1.6 percent gain from the same period a year earlier. For the United States, the comparable figure was a 3 percent gain. Employment in manufacturing has been particularly good during the first quarter, but it too has lagged somewhat behind the nationwide increase. Employment in construction work, up sharply during January and February, slipped below year-earlier figures during March, owing in large part to severe weather conditions.

The March figures for district unemployment show a 6 percent decline from March of 1959. The number of jobless in Minnesota for March was 103,600, or 7.4 percent of the labor force. A year earlier the figure was 8.4 percent.

District department store sales during March were disappointing, but preliminary data for April show a substantial gain from a year ago and store managers are reasonably optimistic as to imme-

Operating Ratios Report

Annual analysis of the operating statistics of Ninth district member banks . . . P. 6

diate future sales prospects.

The Ninth district statistics covering the total number and value of building permits issued have been on the strong side since early last winter. The latest figures (February) show a plus 9 percent and 10 percent respectively. These figures tie in well with the increase in the number of people employed in construction work, and indicate an optimistic trend in building over the next several months.

MARCH ECONOMIC INDICATORS

(Percent change from year earlier)

	9th district	U.S.
Nonagricultural employment	+1.6p	+2.3
Manufacturing	+2.6p	+3.1
Construction	—1.5p	—6.0
Insured unemployment	—6.0	—7.5
Initial claims	—7.9	+6.7
Department store sales	—7.0[1]	+2.9p
Lumber sales	—15.0p	n.a.
Building permits (value)[2]	+9.0	n.a.
Building permits (number)[2]	+10.0	n.a.
Cash farm income[2]	—14.6	—6.7
Personal income (Minnesota)	+4.2p	+4.8p
Bank debits	+6.2	+8.2

[1]Estimated allowing for Easter and number of trading days.
[2]February figures.
p = preliminary; n.a. = not available.

The data on personal income in Minnesota covering the first quarter registered a 3.4 percent gain over last year, with March figures up an estimated 4.2 percent. Bank debits have also been on the plus side during the first quarter, averaging about a 6 percent gain from a year earlier.

The most pessimistic economic situation in the Ninth district is the continued decline in farm income with February statistics (latest available) showing a 14.6 percent decline from the same month a year earlier. The 1960 crop season is getting off to a slow start, but the condition of winter wheat is particularly good. In South Dakota, for example, the condition of winter wheat is reported to be among the best on record.

On the Ninth district banking scene, the demand for loans continues strong, the deposit trend is down, particularly in the larger city banks, and bank investments in securities continue to be reduced to provide loanable funds. Loan - deposit ratios have increased generally from year-ago levels. In short, bankers report a continuing squeeze in their liquidity positions. Many of the larger banks have found it necessary to further increase borrowings from the Federal Reserve Bank of Minneapolis in recent weeks.

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

RETAIL SALES BELOW NATION

Ninth district retail sales thus far in 1960 remain somewhat lower level than elsewhere in the nation. However, they did not plummet as much as national sales in response to adverse weather in February and March.

The percent change in district department store sales from a year ago, which retailers watch closely, reveals a pronounced downward trend during the first quarter. Even with figures adjusted for the late Easter this year, sales in January were up 5 percent, in February down 1 percent, and in March down 7 percent from the corresponding months in 1959. This downward trend in percent change reflects a sharp rise in sales during the first quarter of 1959.

The seasonally adjusted index of Ninth district department store sales in January was 33 percent above the 1947-49 base period, down two points from the latter half of 1959. In both February and March, the adjusted index was 1 percent below the January figure, in spite of temperatures below normal and heavy snow in some parts of the district. The nation experienced a more pronounced downward trend in department store sales during the first quarter than the district; the national adjusted index from January to February declined by 5 points and in March rose only by 2 points.

Sales of retail stores in the Ninth district as measured by the Bureau of Census sample (which excludes large retail chains) provide a broader measure of consumer purchases than do department store sales. In this sample of stores, total sales in January were up 3 percent and in February up 8 percent from a year ago. Sales of durable goods lagged during the winter. January sales in furniture and appliances were down 32 percent from a year ago. Lumber, building supplies and hardware sales dropped 6 percent, while automotive sales remained the same. In February, furniture and appliance store sales again were down 11 percent from a year earlier, but other durable goods sales had risen above last year's volume.

A strong seasonal rise in automobile sales occurred in the Twin Cities metropolitan area. Registrations during the first half of March were down 11 percent from last year, but in the latter half of the month they were up 34 percent. The increase continued through the first three weeks of April.

Registrations of new passenger cars in the entire district were down in Januuary from year-ago totals. In North and South Dakota, registrations were down by nearly one-fourth and in Montana by about one-sixth. In the eastern half of the district, the decrease was less.

The decline in consumer incomes in some district areas adversely affected retail sales. Cash farm income in January was down from last year by one-sixth in Montana and North Dakota, and one-fifth in South Dakota. In several agricultural areas of these states, department store sales were down 10 percent or more from a year ago. In the mining regions, work stoppages in copper and iron ore mining caused heavy losses in personal incomes and forced idled workers to use credit. Debt repayment following the return to work has acted as a temporary restrictive influence on consumer buying. This has held department store sales down to the levels prevailing during the economic recession of 1957 and 1958. Consumer incomes have been relatively high in industrialized regions—the Twin Cities and other centers in southeastern Minnesota and in a portion of Wisconsin—where department store sales during January and February were also comparatively high.

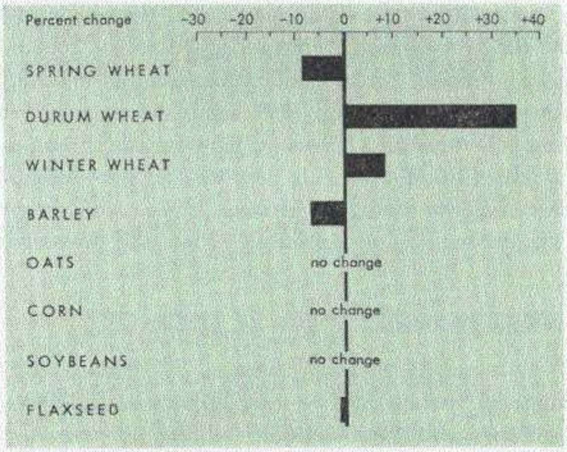
1960 MAJOR CROPS

Plantings for the district's major crops in 1960 are expected to fall approximately 2 percent from 1959 levels. The district's total acreage of wheat, oats, barley, corn, soybeans and flaxseed is expected to total 49,981,000 acres, according to the U. S. Department of Agriculture's March 1 survey of planting intentions.

The acreage of winter wheat seeded in 1959 was 8 percent above the level of the year before; this

Prospective changes in crop acreages in the Ninth district

(1960 compared with 1959)



was likely a response to the favorable moisture situation which developed late in the 1959 season. A large increase—35 percent—is planned in durum wheat production this year, according to the March 1 survey. The planned expansion likely reflects the favorable price and output of durum last year compared with other spring wheat.

The largest declines in planned seedings in the district were reported in spring wheat (other than durum) and in barley; those crops are expected to be down 8 and 7 percent, respectively. A portion

Montana, nonfarm employment was actually down from 3 to 4 percent from a year ago. In the other district states the increase was 2 percent or more.

DISTRICT MEMBER BANK BORROWING HIGH

During the first quarter of 1960, member bank borrowings in the Ninth Federal Reserve district were above the level of recent years. For the quarter, district borrowings were higher relative to deposits than was true of the nation as a whole. Both reserve city banks and country banks in the Ninth district borrowed more in the first quarter of 1960 than in the comparable period of any of the previous three years, as indicated by the table.

AVERAGE BORROWINGS OF DISTRICT MEMBER BANKS IN THE FIRST QUARTER

(millions of dollars)

	1957	1958	1959	1960
Reserve City	26.9	1.2	4.4	29.1
Country	7.0	3.1	6.5	8.9
Total	33.9	4.3	10.9	38.C

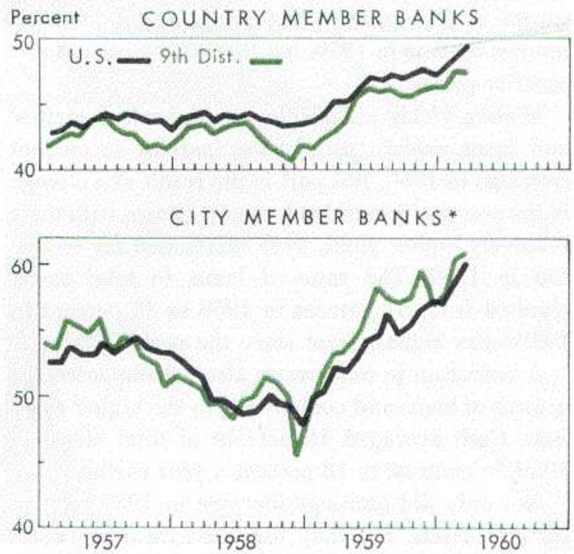
District member bank borrowing has also been high relative to the national pattern. The national total declined in successive months of the first quarter while increases occurred in the district. Thus, while all member bank borrowings in the nation dropped from approximately 4.9 percent of required reserves in the four weeks ended January 27 to 3.7 per cent in the four weeks ended April 6, district member bank borrowings rose from approximately 6.2 percent to 14.8 percent of required reserves.

At city banks, which account for most of the borrowing from the Minneapolis Federal Reserve, loans rose by 2.2 percent and demand deposits fell by 6.4 percent. But the cash drain imposed by the first quarter loan and deposit pattern was not substantially different from that in other recent years. The heavy member bank borrowing this year appears to reflect the fact that the banks entered 1960 in a much less liquid position than at the beginning of 1959. Thus a greater reliance on borrowing was occasioned in recent months to meet deposit withdrawals and loan demand.

For example, at the beginning of the year Ninth district city banks held government securities amounting to $411 million, or 18.5 percent less than a year earlier. The ratio of loans to deposits was 57.2 percent in contrast to 45.6 percent a year earlier. These figures suggest that changed liquidity rather than changed loan and deposit patterns primarily accounts for the borrowings in our district in early 1960.

City bank deposits in the rest of the nation fell proportionately less than those in the district during the first quarter, and loans fell in contrast to a district increase. The loan-deposit ratio rose from 56.2 percent to 60 percent for all city banks in the nation during the first quarter, while the district ratio rose from 57.2 percent to 62.8 percent.

Loan to deposit ratios



*Central reserve city and reserve city member banks.

Bank earnings and liquidity down

The recently released 1959 Operating Ratios report shows that the ratio of net current earnings to total assets of Ninth district member banks rose from 1.2 percent in 1958 to 1.3 percent in 1959. However, substantial cuts in the value of securities during 1959 were reflected in net losses on securities which more than offset the gains in net current earnings. Relative to total earnings, losses averaged 4.3 percent in 1959 in contrast to profits of 2.2 percent of earnings a year earlier. The bulk of these losses were on securities, some of which may have been taken for tax purposes. Despite the more favorable net current earnings in 1959, net profits amounted to an average of 9.6 percent of total capital and .7 percent of total assets, while a year earlier these ratios averaged 11.3 percent and .8 percent, respectively.

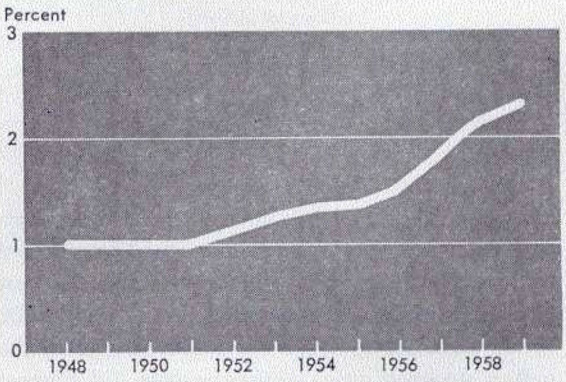
The losses banks took on securities in 1959 illustrate that increasing market interest rates are not as unequivocally favorable for banks as one might expect at first glance. Higher rates did push up interest income in 1959, but they also pushed down security prices.

Higher yields on all classes of bank securities and loans explain part of the increase in current earnings in 1959. But part is the result of a change in the composition of bank assets. Loans, with their relatively higher yield, were substituted for securities in 1959. The ratio of loans to total assets climbed from 37 percent in 1958 to 38 percent in 1959—the highest level since the early 1930s.

A reduction in cash assets also accompanied the growth of loans and contributed to the higher earnings. Cash averaged 16 percent of total assets in 1959, in contrast to 18 percent a year earlier.

Not only did earnings increase in 1959 relative to total assets, but they outpaced the rise in expenses. Though wages and salaries increased in absolute terms, they declined as a fraction of earnings and therefore partly accounted for earnings outpacing expenses in 1959. Other expense reductions also helped to more than offset a further increase in interest on time deposits relative to earnings. The increase in time deposit interest expense slowed in 1959 from the pace set in recent years, as did the rise in the ratio of interest payments to time deposits (which might be termed the *effective* rate of interest). The accompanying chart shows effective time deposit rates for the period 1950-1959. Average time deposit rates rose to 2.3 percent in 1959, from 2.2 percent the previous year. Time deposits made up a larger fraction of total deposits in 1959 than was the case in 1958.

Time deposit interest rates at district member banks



With loan to total asset ratios at a peak not matched since the early 1930s, some concern over the liquidity of the banking system is occasionally voiced. Reflecting the liquidity of individual banks are two ratios included in the Operating Ratios report: the ratio of capital accounts to total risk assets (total assets less government securities and cash), and the ratio of loans to total assets.

Bank loans are made to customers and therefore may not be liquidated easily when cash needs

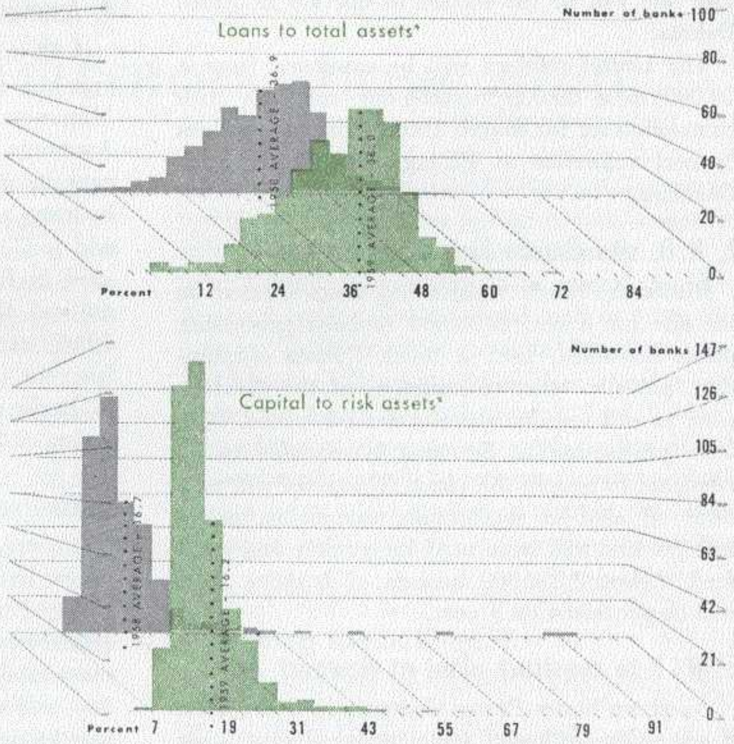
The Operating Ratios Report

During the first part of April the Federal Reserve Bank of Minneapolis sent its 'Operating Ratios' report to the 474 member banks of the Ninth district. The report is a popular one and often gets a thorough reading, since individual banks find it useful in comparing their own operating experience with that of other banks.

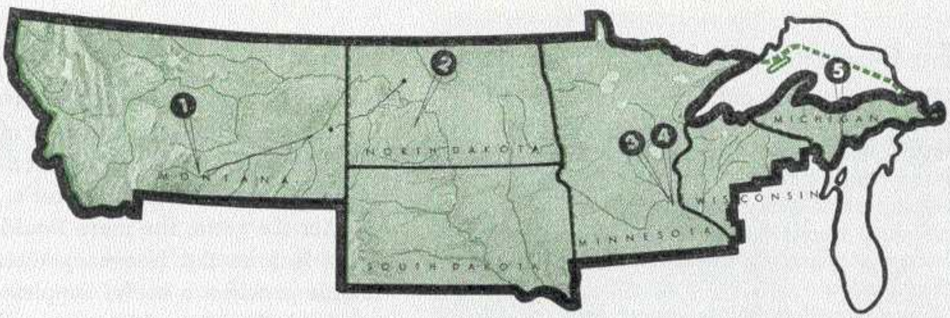
The Operating Ratios report sent to individual banks includes a confidential report of each bank's own ratios, as well as average ratios for other member banks. Average ratios are given separately for several groups of banks classified according to deposit size. Average ratios reflect the operations of the hypothetical 'average' bank of a particular group. Although an individual bank may have many reasons for differing from the average, bank management finds it useful to compare figures of their own bank with the averages and to reconcile differences in terms of the particular situation facing them.

unexpectedly develop. As a result, other factors remaining unchanged, the more loans a bank makes relative to its total assets, the less liquid it tends to be. Thus, the ratio of loans to total assets is a liquidity measure. A lower ratio indicates more bank liquidity. From the viewpoint of depositors (and bank examiners who have their interests to protect), deposits are less apt to lose their ordinarily almost perfect 'cash quality' if bank capital is large enough to act, for the depositor, as a buffer against the ups and downs of the cash value of a bank's assets. Bank capital accounts are funds that owners have invested in a bank or retained from its earnings. Other things equal, an increase in capital relative to those assets that are most subject to value changes, reflects an increase in liquidity from the point of view of bank depositors. Thus, the ratio of capital to risk assets is a liquidity measure from the depositor's standpoint. The higher the ratio, the more liquid are deposits.

A look at the frequency distribution of these ratios provides a useful supplement to the report on bank liquidity which appeared in the February 1960 *Monthly Review*. On the accompanying charts, these two liquidity measures record the way individual banks in the district fared in 1959 relative to the previous year. Comparing 1959 with 1958, the chart shows a notable downward shift in the distribution of capital to risk assets—and an upward shift in the distribution of loan to deposit ratios. Both factors indicate a decline in liquidity that is widely distributed throughout the district banking community.



*Average ratios at Ninth district member banks.



Economic Briefs

1. Petroleum pipeline to connect Mont., N. D.

The Farmers Union Central Exchange has scheduled construction of a $5 million 200-mile petroleum products pipeline for this spring. The 8-inch pipeline will extend from Glendive, Montana to Minot, North Dakota. Products from the Farmers Union refinery at Laurel, Montana will be transported to the new line for distribution. The line will be the second to operate in North Dakota.

The Laurel refinery will be expanded from a 19,000 to a 25,000 barrel-a-day capacity, with completion set for March 1961. Existing pipelines connect refineries at Billings and Laurel with Glendive.

2. N. D. site chosen for soybean plant

Bismarck, North Dakota has been selected as the site for a new $680,000 soybean processing plant. Soybeans, Inc., a North Dakota corporation, plans to start construction of the plant as soon as soil tests on the site are completed. Soybean production in the area is expected to be adequate to supply the plant. The plant will produce oil used in shortenings, margarine, paints and plastics, and meal used for poultry and stock feed. About 2,250,000 bushels of soybean meal will be processed each year.

3. NSP to construct plant at Newport, Minn.

Northern States Power Company will construct a one-million-killowatt steam powered generating plant at Newport, Minnesota, on the Mississippi River. Cost of the project is estimated at $170 million to $180 million, including a 286-acre site at Newport, south of St. Paul. Construction probably won't begin for another four to five years.

The company has also acquired a site at Red Wing, Minnesota for another one-million-kilowatt plant, to be built after completion of the Newport facility.

4. Ammonia plant to expand in Pine Bend

A $4 million expansion is planned for the three-year-old ammonia products plant in Pine Bend, Minnesota, just south of the Twin Cities. St. Paul Ammonia Products, Inc., plans to increase the capacity of its plant to 110,000 tons a year of anhydrous ammonia and nitrogen solutions, and to add facilities for making solid nitrogen materials used in fertilizers. Built at a cost of about $16 million, the plant had an original capacity of 70,000 tons, which was expanded to 88,000 tons last year. Construction of the addition is scheduled to begin this fall and completion is set for the spring of 1961.

5. First refinery built in Upper Michigan

Construction of Upper Michigan's first oil refinery has been completed at Rapid River. The Upper Peninsula Oil Refinery, Inc., moved the refinery from Louisiana to the Michigan site for reassembly. It has a capacity of 1,580 barrels a day, and will refine Canadian crude oil into gasoline, kerosene and other products for Upper Michigan consumption.