# Expansion in Instalment Credit

INSTALMENT CREDIT resumed expansion late last year, and new borrowing has risen above former highs in recent months. The outstanding amount increased at a seasonally adjusted rate of $360 million in January and February of this year, somewhat less than the record rate in 1955 but more than in any month since early 1956.

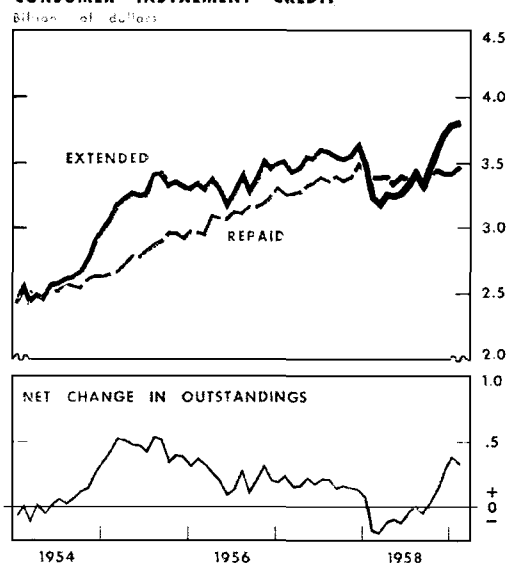
Most types of instalment credit began to rise in the spring of 1958 but the total, held down by lagging automobile demand, did not turn up until the last quarter of the year. Since October, automobile credit has accounted for about one-half of the increase in the total.

Renewed growth in instalment credit has provided additional funds for consumer spending and has contributed to the revival of business activity. Although credit sales of some types of goods, such as new automobiles, have lagged behind cash sales, total borrowing by consumers has increased at a faster rate than total consumption expenditures. Demand for funds by consumers has added to other pressures in credit markets and has contributed to the increase in interest rates.

### RECESSION EXPERIENCE

Instalment credit responded slowly to the business downturn in 1957. Extensions of such credit, the most sensitive indicator of changes in the flow of credit, remained at high levels throughout the second half of 1957. Industrial production and personal income, two common measures of general business activity, turned down late in the third quarter.

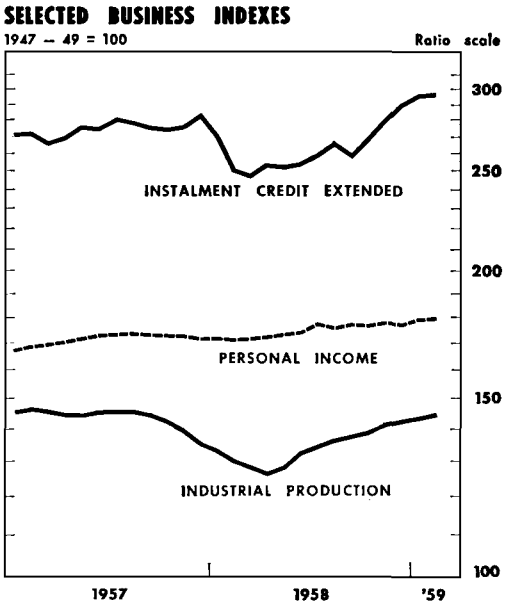
CONSUMER INSTALMENT CREDIT




NOTE.—Adjusted for seasonal variation. Latest data shown, February.

After extensions of credit began to decline, they fell more rapidly than either industrial production or personal income. Percentagewise, the decrease was somewhat smaller than that in industrial production but considerably larger than that in personal income. Extensions of automobile credit, which dropped 25 per cent from the October 1957 high to the March 1958 low, accounted for most of the decline in the total.

The slower rate at which consumers incurred new obligations helped to check the growth of repayments, which remained at the pre-recession rate throughout 1958. With the decline in income, there was a small increase in the ratio of repayments to disposable personal income.




NOTE.—Adjusted for seasonal variation. Latest data shown, February.

All types of instalment credit reflected the business recession, but the extent and timing of the impact on different sectors varied. Outstanding paper for consumer goods other than automobiles declined in the last quarter of 1957 and the first quarter of 1958, but the net change for the period as a whole was small. Automobile credit did not turn down until January 1958, when it began a decline that lasted without interruption through October. Personal loans continued to rise throughout the recession but at a somewhat reduced rate.

Delinquencies on all types of instalment loans rose in the first quarter of 1958 and repossessions of both new and used cars became more numerous. Repossessions reached a record postwar rate, but the demand for used cars was strong enough to prevent large losses to lenders. Liberal policies in deferring payments or rewriting loans kept down the number of defaults and adjusted the burden of debt repayments for many borrowers.

### FORCES FOR EXPANSION

Improvement in general economic conditions by the summer of 1958 created an environment favorable to renewed expansion of instalment credit. Better incomes and expectations strengthened the willingness and ability of consumers to use credit as well as their demand for goods purchased on credit. Competition among lenders and better collection experience encouraged the expansion of credit operations. On the other hand, relatively large pockets of unemployment and rising costs of funds to lenders were unfavorable factors.

Extensions of instalment credit turned up early in the second quarter of 1958 about the time of the upturn in general business activity. They regained pre-recession levels by December and rose to new highs in the early months of this year.

Financial positions of consumers improved as economic activity recovered. Disposable personal income resumed its upward trend in the second quarter of 1958 and, with consumer prices changing little, the purchasing power of consumers increased. Repayments on consumer instalment debt continued steady and their ratio to disposable personal income declined from 13.3 per cent in the first quarter of 1958 to 12.9 per cent in the first two months of this year. Although some consumers were forced by the recession to reduce their liquid asset holdings, in general consumers were in a favorable position to expand their credit buying.

Early this year consumers viewed their financial situations and prospects more favorably than a year earlier. Forty per cent of the spending units reporting in the Survey

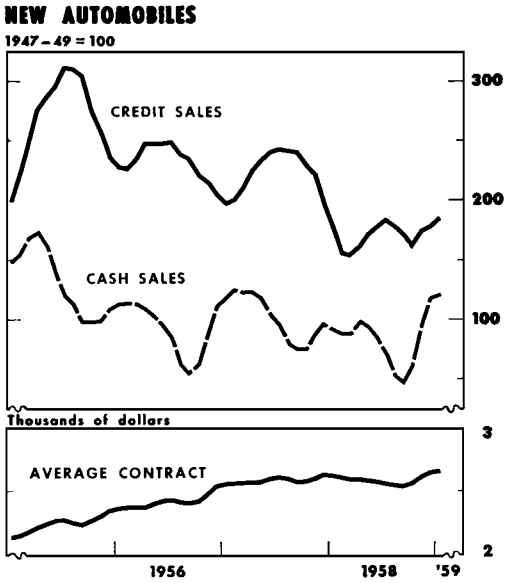
of Consumer Finances indicated that they were earning more, and 42 per cent indicated that they expected their incomes to increase over the coming year. Their plans to buy durable goods were only moderately larger than in early 1958. The proportion of consumers planning to buy new cars was somewhat above the low level of early last year but below levels in the three preceding years. The proportion planning to buy used cars, on the other hand, was above that of most recent years although somewhat below the high of last year.

Following the brief and rather sharp rise in collection problems during the recession, collection experience improved. Delinquencies on most types of instalment loans at commercial banks have been fewer than a year earlier and repossessions of new and used cars have declined from their recession highs. Lenders have been encouraged by their recent experience and by the general business outlook to expand and broaden their financing operations.

### AUTOMOBILE CREDIT

Automobile credit has accounted for most of the recent fluctuations in total instalment credit outstanding. In 1958, the prolonged decline in automobile paper was responsible for most of the reduction and for the delayed upturn in the total. Since October, it has accounted for a substantial part of the increase.

New borrowing for automobile purchases returned to the pre-recession high of more than $1,400 million a month in December 1958 and continued at that rate in the early months of 1959. Repayments remained at the reduced level of $1,250-$1,300 million a month and the expansion in outstanding credit resumed at a seasonally adjusted rate of $175 million a month.




NOTE.—Three-month moving averages. Latest data shown, January.

Despite the rise in sales of new cars after the introduction of the 1959 models, growth in credit sales has lagged behind the expansion in cash sales, as the chart shows. The number of new cars sold on credit in the first four months after the introduction of new models was smaller than in the comparable period a year earlier, but cash sales were 25 per cent higher.

Maximum maturities and minimum downpayments on new car contracts have not changed materially since 1957. Most lenders allow up to 36 months to pay on their new car contracts and make loans up to the amount of the dealer cost of the collateral. The proportion of long-term contracts, after rising steadily through the third quarter of 1958, has leveled off in recent months. It is estimated that about 60 per cent of all new car contracts are now written with 36-month maturities.

The size of instalment notes on new cars

has shown little change over the past year. New car contracts averaged $2,640 in January and February as compared with $2,610 in the same months last year. Higher retail prices and the somewhat larger financing charges associated with longer average maturities have been offset in part by an increase in the proportion of lower priced cars purchased.

Continued strength in credit sales contributed to the stability of used car sales throughout 1958 and the early months of this year. The proportion of used cars sold on credit has risen steadily. Maximum maturities of 30 months in contracts for used cars of recent model have become common in the last few years, and there appears to have been a proportionate lengthening of maturities in contracts for cars of older model.

### OTHER CONSUMER GOODS CREDIT

Instalment credit outstanding for the purchase of consumer goods other than automobiles decreased in the latter part of 1957, after allowance for the usual seasonal influences. Such credit began to rise again in the spring of 1958 and in recent months its rate of growth has accelerated.

Consumers have been spending about the same proportion of their income on goods other than automobiles as before the recession and they have been buying about the same proportion on credit. They have used about $1 billion of new credit a month since August 1958 while repayments, which changed little during the recession, have averaged about $950 million a month.

Credit for the purchase of major appliances and furniture continues to account for the greater part of all instalment credit for goods other than automobiles. Nevertheless, an increasing proportion represents credit for purchases of items such as house trailers and pleasure craft, bought on comparatively long terms, and credit for purchases of nondurable goods and small durable goods on revolving credit and similar plans.

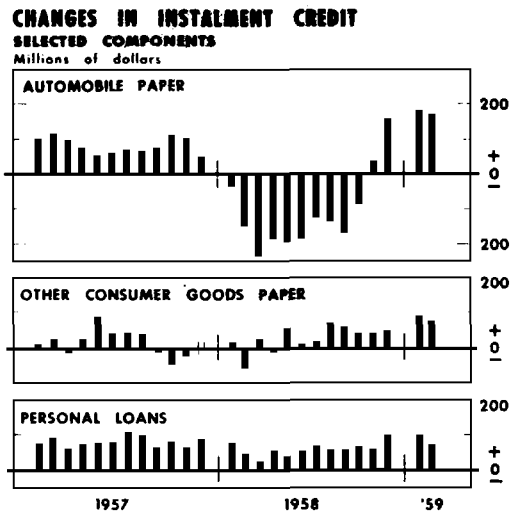
The revolving credit plan, used very widely by department stores, permits purchase, on a line of credit, of items heretofore seldom offered on an instalment basis. It is estimated that the amount of revolving credit outstanding has at least doubled since early 1957, and that about $500 million, or a third, of all instalment credit at department stores is now in this form.

Repair and modernization loans outstanding have resumed a gradual upward course after a brief decline in early 1958. New credit is being extended at a slightly higher rate than at any time since the middle of 1957. The trend toward longer average maturities, which began when the maximum maturity on loans insured by the Federal Housing Administration was lengthened to five years, has continued.

### PERSONAL LOANS

Personal loans have expanded without pause since World War II, but at a variable rate. The expansion slowed during the recession but has accelerated in recent months, as the chart shows. These loans amount to about a fourth of total instalment credit outstanding.

Growth in personal loans reflects increased experience with, and confidence in, the unsecured loan on the part of lenders, and the use of this type of loan by consumers for a wider variety of expenditures. Personal loans have long been used for consolidation of debt, for medical and dental payments and for emergencies. While these purposes still predominate, such loans are now used more often than they used to be for purchasing consumer goods and services.




NOTE.—Adjusted for seasonal variation.

Greater interest in personal loans on the part of commercial banks and the growth in the number of credit unions have expanded the sources of these loans. Special credit plans have also furthered the use of the personal loan. Among these are check credit plans that extend the features of revolving credit to the personal loan field, and the arrangements of travel agencies and airlines to finance travel.

### FINANCING OF INSTALMENT CREDIT

Commercial banks financed most of the recent growth in instalment credit as well as the peak seasonal demands at the end of 1958 through direct participation in consumer lending, purchases of paper, or loans to other holders of consumer paper. On balance, sales finance companies returned funds to the credit markets during most of 1958 but, as their needs increase with seasonal requirements this spring, their demands are likely to add to other pressures on available supplies of funds.

Costs of borrowing to finance instalment lending operations are higher than they were in early 1958 but lower than they were in 1957. The rate on 3- to 6-month directly placed paper of large finance companies has been 3¼ to 3⅜ per cent in recent weeks, compared with 1⅜ per cent in the second quarter of 1958 and a high of 3⅞ per cent in 1957. Bank rates on loans to finance companies and other borrowing rates have also increased.

The earnings experience of lenders in 1958 was mixed. Operating costs and losses charged to bad debt reserves were larger than in 1957 but these higher costs were offset in part by the lower interest rates on money borrowed. Many lenders specializing in automobile financing, where volume declined, reported reduced earnings. Prospects for better earnings this year have been enhanced by the rise in loan volume and the improvement in collection experience.

Retail stores and automobile dealers originate a large proportion of all instalment credit but they sell most of it to commercial banks or sales finance companies. At the end of 1958 banks held 38 per cent of all instalment credit and finance companies 26 per cent, as the table on page 352 shows. Distribution of holdings has changed little in recent years except for declines in the proportions held by retail outlets and sales finance companies.

Recent changes in the relative importance of sales finance companies reflect two partly offsetting tendencies. The proportion of automobile credit held by these companies has declined from a temporary high of 51 per cent at the end of 1955 to 45 per cent in recent months as commercial banks and other financial institutions, primarily credit unions, have expanded their share of this market. On the other hand, the proportion

HOLDERS OF INSTALMENT PAPER

[End-of-year figures]

| Type of holder | Amount (in millions of dollars) 1958 | Percentage distribution | | |
|---|---|---|---|---|
| | | 1958 | 1956 | 1954 |
| Total | 33,865 | 100 | 100 | 100 |
| Financial institutions: | | | | |
| Commercial banks | 12,730 | 38 | 37 | 37 |
| Sales finance companies | 8,740 | 26 | 29 | 26 |
| Consumer finance companies | 3,381 | 10 | 10 | 9 |
| Credit unions | 2,664 | 8 | 6 | 6 |
| Other | 1,428 | 4 | 4 | 4 |
| Retail outlets | 4,922 | 14 | 15 | 18 |

of credit for other consumer goods held by the sales finance industry has increased from 12 per cent in 1954 to about 18 per cent in 1958 as financial subsidiaries have been formed by manufacturers and retailers to handle their paper.

Small commercial banks have expanded their operations in the automobile credit market more than medium-size and large banks. Small banks reported the largest relative gains in purchased paper and they also expanded their share of the direct loan market. In the sales finance industry, small and medium-size companies reported slightly more growth from 1955 to date in the new and used car fields than the average for the three largest companies. Growth in automobile credit operations has been less rapid among all sizes of sales finance companies than among small banks.