Banking and Credit Developments During 1952

During 1952, deposits and loans of Sixth District member banks reached the highest points on record. Although industrial production and general business activity in the nation during 1952 was characterized by "high level stability," this term is an inadequate description of District banking developments. For District member banks, the year was one of growth. The growth of loans and deposits at these banks reflected the general expansion both in the country's money supply and in the Sixth District's business activity, which continued at a greater rate than that experienced by the nation as a whole.

Two credit developments during 1952 affected both the District banks and their customers. On the one hand, regulations on the terms of real estate and consumer credit were removed during the year. On the other hand, the monetary authorities did not supply Federal Reserve credit through the purchase of Government securities as freely as they had in the past, and a "tighter" money market came into existence. Although these two developments added up to more emphasis on general credit controls, basic monetary policy remained committed to holding the line against inflation. Taken together, the two credit developments represented a return to the tradition that a central bank exercises control over the volume of credit but not over its particular use.

Money supply increased . . . .

Changes in credit regulation were not achieved without some further expansion of the money supply during 1952. The decontrolling of terms on consumer and real estate loans was followed by a considerable rise in these types of loans at District member banks. About one-half of the expansion in member bank loans during the year is assignable to these consumer and real estate loan components.

The effects of credit developments during 1952, however, were not solely in the direction of a further expanded money supply. The higher cost of borrowing brought about by the tight money policy undoubtedly acted to limit the increase in lending. The demand for some types of loans probably was decreased because the higher interest costs made borrowing unprofitable. Even more important, the increase in interest rates probably restricted banks from making some loans they might have made and undoubtedly caused them to use funds in a different manner than they would have if interest rates had been lower.

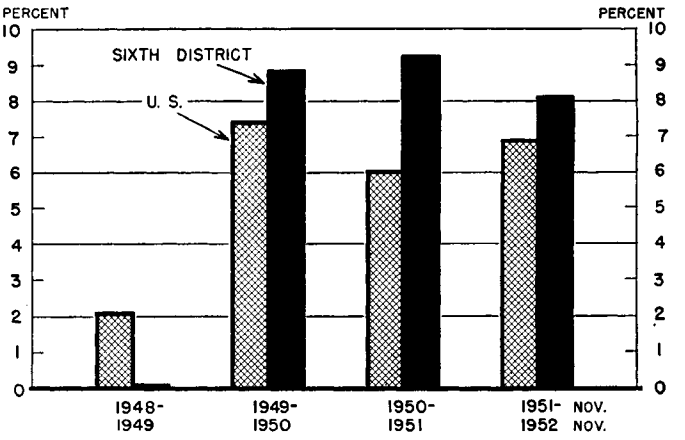
At year-end, the "sixty-four dollar question" was, Had the inflationary threat been abated or was it reappearing? True, loans were expanding at a greater than seasonal rate, but nevertheless, the expanded money supply was not pushing prices upward and commodity and wholesale prices were actually falling. The relative stability of consumer prices in the face of this divergency between these indicators added to the enigma.

Following the slight setbacks in 1946 and again in 1948, deposits in both the District and the United States continued to expand during 1952. Total deposits of the 360 District member banks increased by 327 million dollars. Relative to total deposits, this was a greater expansion than that occurring in the nation as a whole.

And both business and consumer loans expanded

The previous all-time high of total loans extended by District member banks of 2,036 million dollars reached in March 1951 was exceeded in seven months of 1952 and a new record of 2,261 million dollars was established in December. The record loan expansion during 1952, however, was confined to the last three quarters of the year; loans in the early months were somewhat below the year-ago level. By December, total loans of District member banks were 13 percent higher than a year earlier.

Percentage Increases in Member Bank Deposits

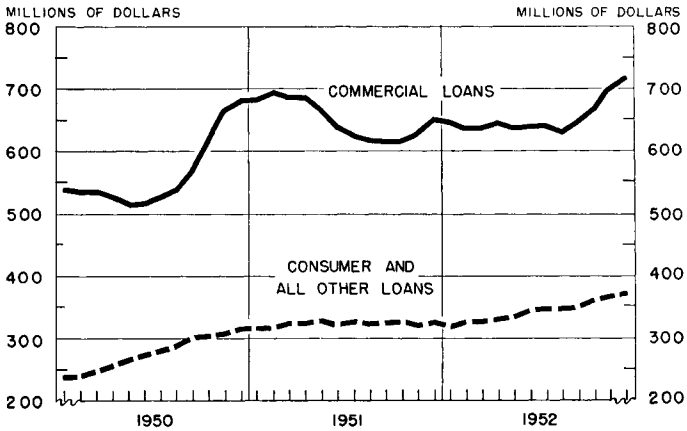


Consumer loans rose spectacularly in 1952. They began to rise in the early months of the year after having remained relatively stable throughout 1951. Perhaps equally important, however, was the increase in bank loans to finance companies and to retailers, many of whom were granting direct credit to their customers. After credit controls were relaxed in May, consumers needed less of a downpayment to purchase articles on credit, and their monthly payments were smaller because they could take a longer period to pay for the articles. The change in credit terms after the removal of controls was striking. Before May 1952, the purchaser of a popular-priced washing machine was required to pay down 15 percent of the purchase price. By the beginning of 1953, the required downpayment had fallen to around 5 percent or in some cases, even less. Since more people were able to make the initial downpayment, credit buying increased.

Removal of controls on real estate credit had somewhat less effect on the volume of mortgage loans made by banks

in the Sixth District than did removal of controls on consumer credit. Although the amount of mortgage loans increased during 1952, the increase was not particularly great when the volume of construction during the year is considered. Two factors probably exerted considerable influence in holding down the amount of these loans. On the one hand, some banks were approaching, or had reached, their legal limit for this type of loan. On the other

Commercial and Consumer Loans of District Weekly Reporting Banks



hand, the increase in interest rates on Government securities made mortgage loans less attractive to bankers as long-term investments. Thus, during 1952 the small growth in bank real estate loans consisted largely of conventional rather than VA or FHA guaranteed mortgage loans with fixed interest rate limits. The average rate of interest charged on real estate mortgage loans, moreover, increased during the year. As the year ended, 4 percent mortgage money was becoming increasingly difficult to find.

Because an increase of one percentage point in the rate of interest charged on a typical 15-year amortized loan results in an increase of almost 7 percent in the monthly carrying charge, the demand for housing loans was probably affected. Nevertheless, non-farm mortgage lending reached an all-time high in 1952 for the nation. Banks and insurance companies, however, were less important as suppliers of such credit than they had been in late 1950, and savings and loan associations were increasingly more important.

Most of the rise in bank loans in the Sixth District during 1952 represented increases in loans to business firms, both manufacturers and distributors. Loans to food, liquor, and tobacco firms and to metals and metal products companies accounted for a large part of the rise in manufacturers loans, judging from the weekly reports on classified loans made by 22 large banks in the District. Although it is impossible to determine how the borrowed money was used, the sharp rise in business loans in the fall coincided roughly with a substantial increase in manufacturers' and distributors' inventories.

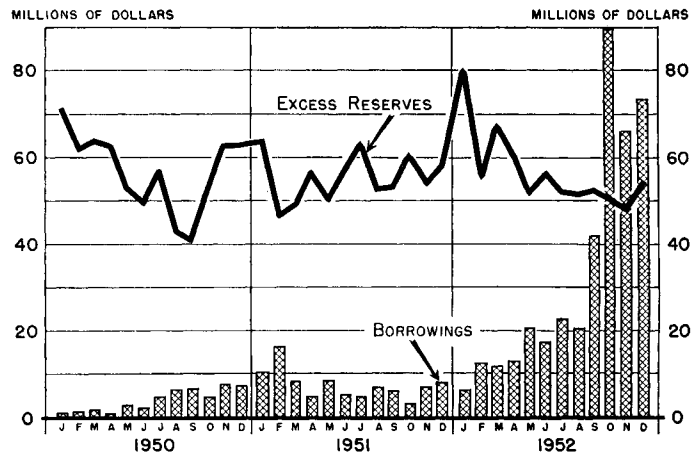
The cost of credit rose . . . .

The rise in volume of loans was apparently accompanied by an increase in the cost of credit to the borrower. From December 1951 to December 1952, average interest rates on business loans of over 1,000 dollars extended by leading banks in Atlanta and New Orleans rose 3 percent. The smallest rates of increase were, of course, registered by small loans, customarily made at relatively high interest rates. Interest rates increased the most on the larger loans—those which customarily receive the lowest rates. About 51 percent of the loans for over 200,000 dollars made in the first 15 days of December 1951 were made for less than 3 percent, compared with 13 percent of this size loan for the corresponding period of 1952. Percentage increases over 1951 in interest rates on business loans made by reporting banks in Atlanta and New Orleans were smaller than those occurring at reporting banks in the entire nation, as measured by reports from banks in 19 cities.

Higher costs of credit to District bank borrowers during 1952, of course, resulted from the supply and demand situation in the national market for loanable funds. Although commercial banks do not participate extensively in supplying funds directly to the long-term funds market, the wide demand for long-term loans did influence the cost of credit. Business firms borrowed heavily to expand facilities both because of the favorable sales outlook and because technical features of the tax laws have encouraged borrowing to finance new construction and equipment. Demand for home mortgage money continued high, and borrowing by state and local government more than doubled in 1952, compared with 1951. On top of this, the Federal Government borrowed more new money than in any year since 1945. The rate of personal and business saving, however, did not keep up with the rising demand for loanable funds. The third-quarter personal saving rate was down slightly from the corresponding period of 1951. In addition, business profits were down slightly although dividend payments actually were up. This meant that business firms, in the aggregate, were retaining less of their profits and needed to borrow more from outside sources for operational purposes and for expansion of facilities.

Monetary developments during 1952 affected commercial bank lending activity in the short-term markets. These developments also reacted upon the long-term markets, not only by affecting certain long-term lenders directly

Excess Reserves and Borrowings of District Member Banks



but by influencing the addition to the money supply by commercial banks. These monetary developments were largely the product of Federal Reserve policy.

Federal Reserve Policy played a restrictive role

The effects of the famous "March accord" between the Treasury and the Federal Reserve System in March 1951, whereby the System changed its policy of supporting Government security prices, were not realized fully until 1952. As a result of the accord, the prices of some issues of Government bonds fell below par, and one source of loanable funds—the sale of Government bonds to the Federal Reserve Banks—was restricted. Commercial banks and other financial institutions could not sell some of their longer-term issues of Government securities before maturity without the possibility of incurring capital losses and thus were encouraged to hold on to them until they fell due. Additional loanable funds could still be obtained without loss by allowing 90-day Treasury bills to mature. Banks apparently took advantage of this source of funds, for bill holdings of District member banks declined during the year.

The lessened commercial bank demand for Treasury bills and the negligible changes in Federal Reserve holdings of these instruments resulted in a marked increase in the yield on Treasury bills, from 1.73 percent in December 1951 to 2.13 percent at the end of the year. Increased bill issues were another factor. Because Treasury bills are an alternate outlet for bank funds that might otherwise be used for prime business loans, it is not surprising to find that interest rates to business borrowers also rose.

Because of the reluctance of the Federal Reserve to purchase Government securities, commercial banks as a group could obtain additional reserves to meet the rising demand for loans primarily through borrowing from the Federal Reserve Banks. This they did in increasing amounts as the year progressed, despite their tradition against borrowing. The daily average amount of discounts and advances extended by the Federal Reserve Bank of Atlanta to member banks reached a peak on December 5, 1952, and was the highest it had been since the 1920's. Although much of this borrowing by individual banks was encouraged by certain tax advantages, it undoubtedly eased the tight money situation for the banking system as a whole.

Borrowing by commercial banks added to reserves, upon which a loan and deposit expansion became possible. But banks also economized more in the use of reserves. Member banks generally keep more deposits with the Federal Reserve Bank than is required by law. During 1951 and the early months of 1952, these excess reserves ranged between 6 and 8 percent of total required reserves of District banks. Beginning in July 1952, however, the ratio of excess to required reserves was only slightly over 5 percent. This meant that District banks as a group were extending credit and experiencing a consequent rise in deposits at a greater rate than they were adding to reserves through borrowing or through an inflow of funds into the area.

Prospects for a continued growth of District bank deposits and loans, of course, depend in part upon the spending plans of consumers, private business, and Government. Although Federal expenditures for 1953 are already partially determined by the defense program of the previous administration, the fiscal policies of the new administration will become an increasingly important influence on the national economy as the year progresses. In the business and consumer sectors of the District economy, it appears that the impetus of the increase in activity in the fall and the consequent rise in the demand for loans is going to carry through into the early months of 1953.

Bank loans normally decline after the first of the year as loans made to finance Christmas inventories are paid off. So far in 1953, however, the seasonal decline has been less than normal in the District. The liquidation of inventory loans was apparently offset by an increase in other loans. This appears to be evidence that customers of banks are optimistic about their prospects for 1953.

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