Banking Responds to Monetary Restraint

Member banks in the Sixth Federal Reserve District began 1969 in a position of liquidity which had been built up before the Reserve System embarked on a course of monetary restraint in late 1968. Throughout 1969, banks adjusted to Federal Reserve actions and to demand pressures for credit.

During the first half of this past year, District banks expanded their total loans and investments about as much as during the same period in 1968 and relatively more than in the nation. Yet, there is no denying that the banks were under pressure to maintain their lending, as declines in deposits caused them to lose reserves. In order for loans to be made, banks sold securities, many of which had just been added to bank portfolios in late 1968. They also turned to augmenting their lending capacity by borrowing Federal funds from other banks. In addition, discount window accommodation increased slightly. In response to rising market interest rates and expanding loan demand, large banks raised their prime lending rate from 6¼ percent to 7 percent. This happened during three successive changes in late 1968 and early 1969. Another hike brought the prime lending rate to 7½ percent in March.

Lending Activity Begins to Moderate

Since June, the expansion of bank credit has shown a noticeable leveling-off. The effects of restrictive monetary actions taken earlier in the year began to be felt. Weak deposit inflows in the first half of the year turned into declines during the second half. Chiefly responsible for this were substantial losses in time and savings deposits.

Following a sharp rise in the prime commercial paper rate in early June, most major banks boosted the prime rate a full percentage point to a record 8½ percent. The expansion of loans continued at a reduced rate through the fall but rebounded in December after a November decline. To maintain even this degree of lending, banks in this region, like those elsewhere, were forced to sell off their investments in a far larger volume than in the first half of 1969. U. S. Government securities, sold to some extent at a loss, made up the bulk.

Confronted with losses on the sale of investments, increasing costs for borrowed funds, deposit runoffs, and heavy loan demands, many banks by midsummer tightened conditions on which they were willing to extend loans to applicants. Required compensating balances were more strictly enforced. Banks became less willing to make long-term loans and loans to buy securities and real estate. In many instances they turned down requests for funds to acquire other businesses. New loan applicants, and especially those outside the local service area, fared less well in getting loans than did previously established and local customers.

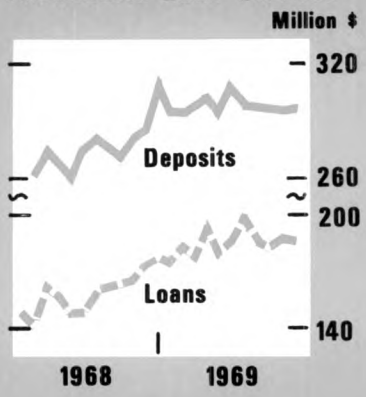
Banks Acquire Funds from Nondeposit Sources

To some degree, these changes in lending policy were in response to the Federal Reserve's efforts to curtail bank credit expansion. Banks have

January 1970

Banking Statistics

Alexandria-Lake Charles



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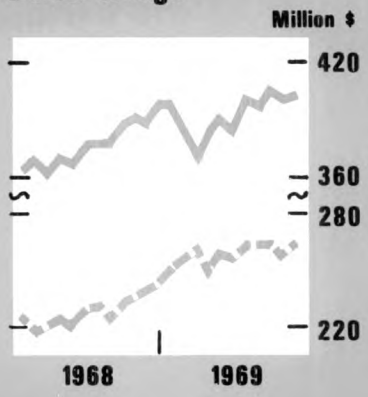

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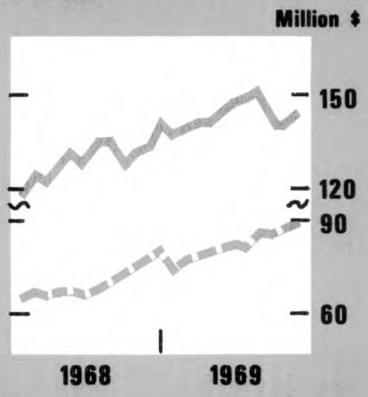

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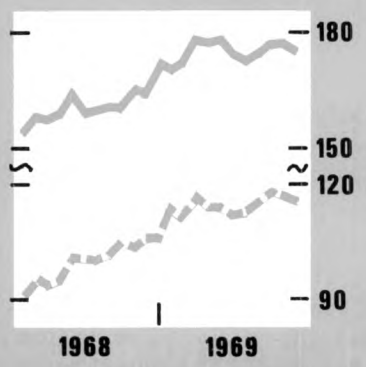

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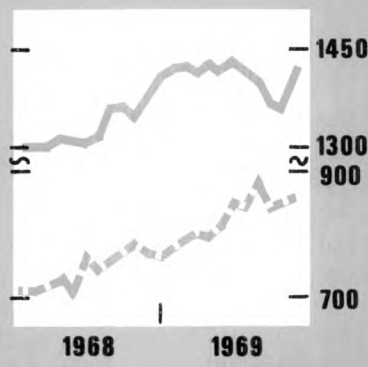

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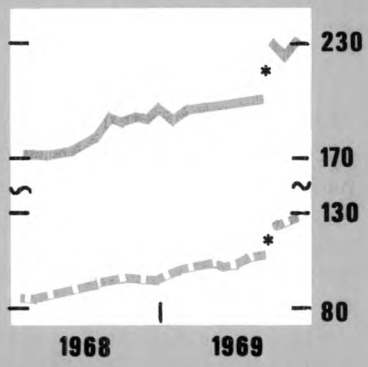

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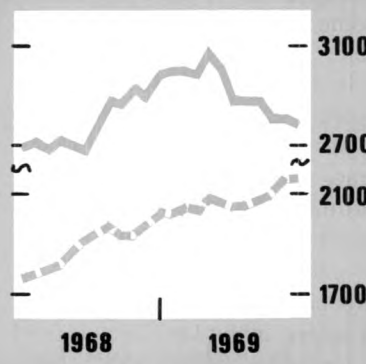

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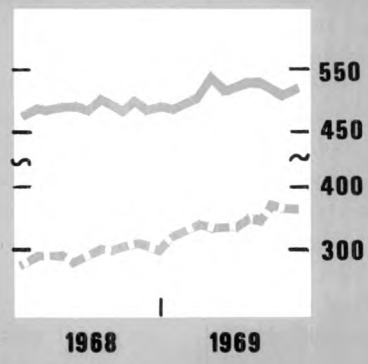

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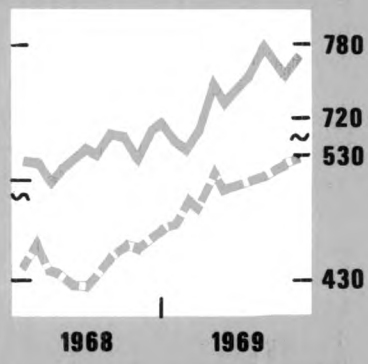

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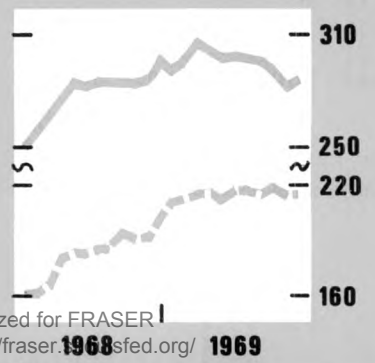

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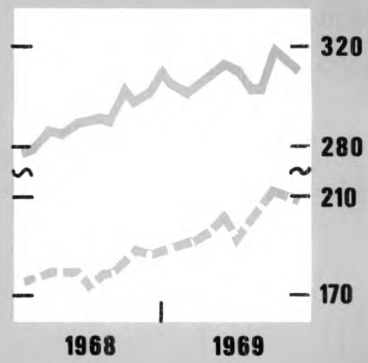

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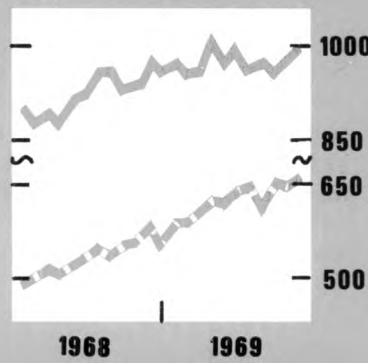

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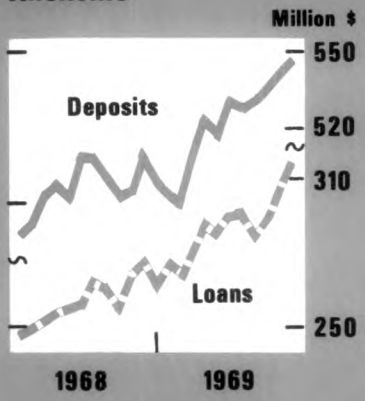

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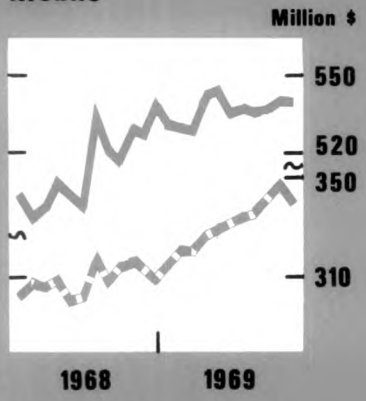

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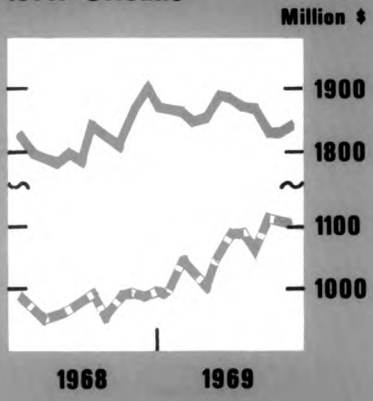

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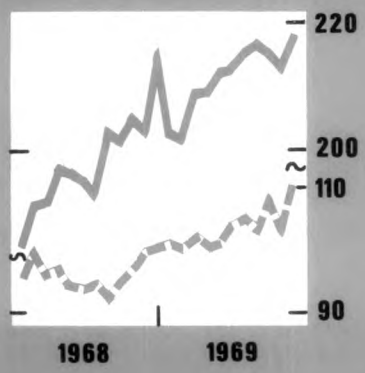

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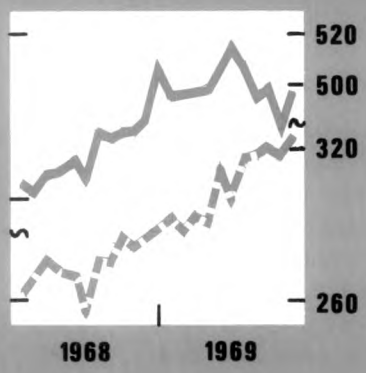

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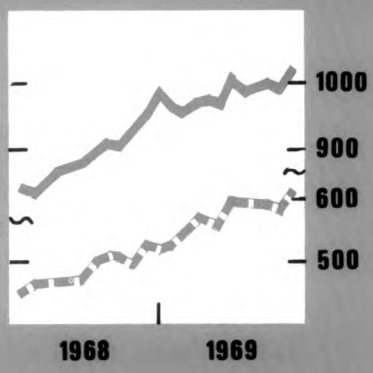

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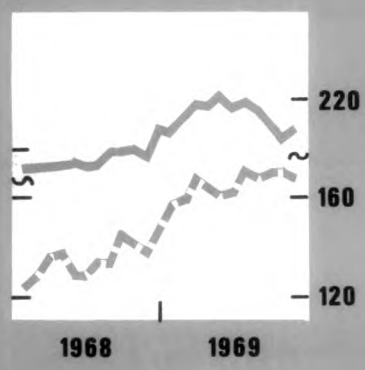

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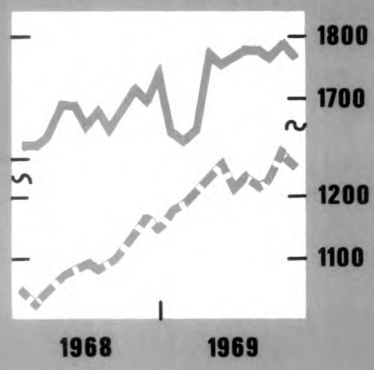

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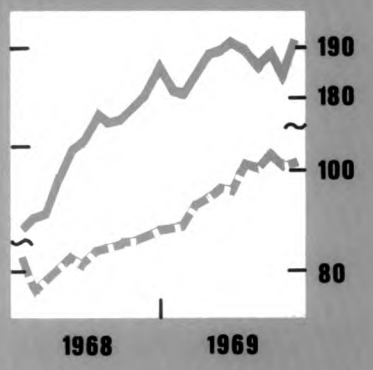

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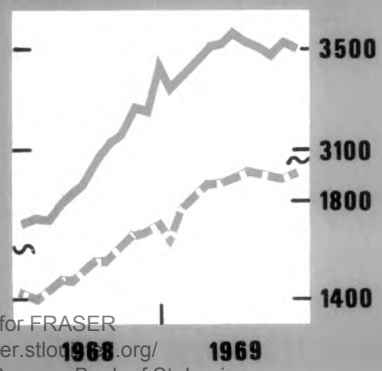

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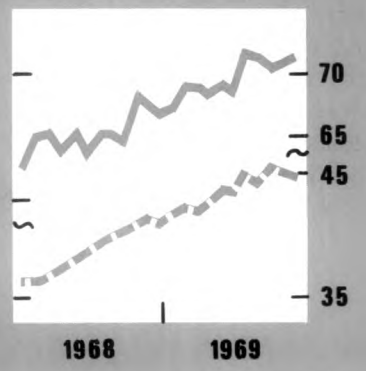

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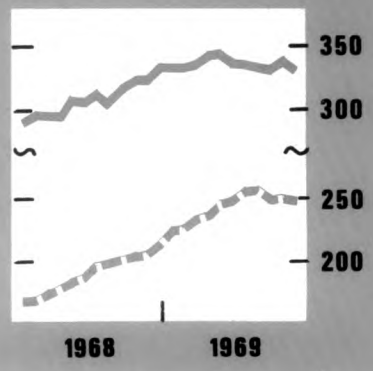
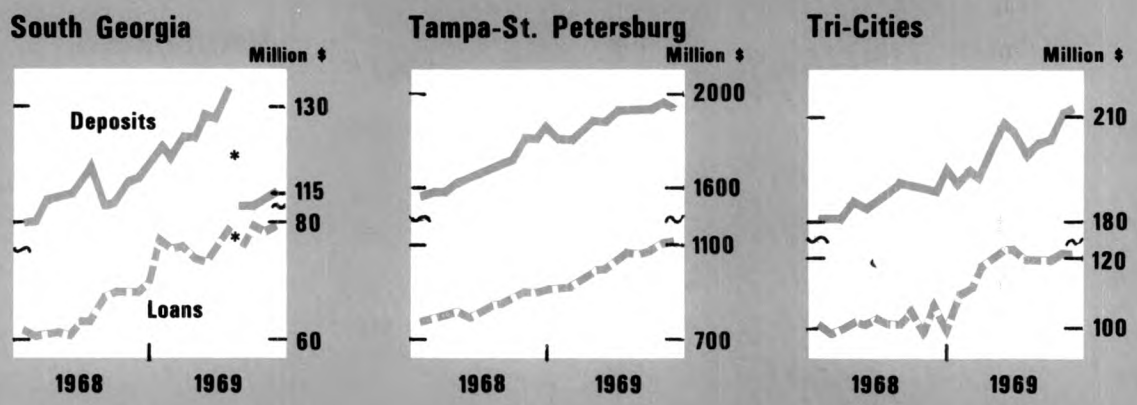




*New Series

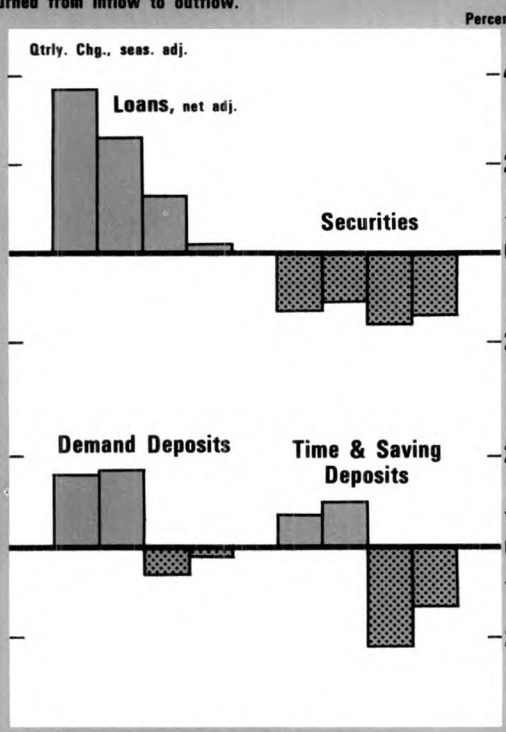
Note: All figures are seasonally adjusted and are shown by trade and banking areas. The areas include several counties surrounding central cities.

found it difficult to retain time deposits and compete for new funds. Although interest rates on competing financial instruments rose substantially, member banks were limited (under Regulation Q) by the Board of Governors of the Federal Reserve System as to how much they could increase their rates on time deposits. The greatest deposit losses, therefore, were in negotiable time certificates of deposit issued in denominations of $100,000 and more. Though 1969, the large commercial banks in the District lost 36 percent of the $657 million in certificates of this type held at the first of the year. In Atlanta, where the competition of the national money market is most keenly felt, the decline has been proportionately more severe.

The loss of deposits has caused some District banks, like those nationally, to turn to nontraditional methods of acquiring funds through nondeposit sources. The sale of loans under repurchase agreements (the bank sells a loan with the understanding that it will buy back the loan, thus protecting the purchaser from any capital loss) provided one method early last summer for banks to pay more than the 6¼-percent maximum rate on certificates of deposit. When this practice began to involve a substantial source of funds for banks, the Board of Governors in late July moved to bring this form of bank liability under reserve and interest regulations. Since then, sales under repurchase agreements have decreased in use.

With the curtailment of one nondeposit source of funds, some banks began to rely more heavily on the sale of short-term commercial paper. In late October, the Board became concerned over the volume of commercial paper outstanding and restricted its sale by banks and their affiliates.

District member banks had in 1969 gradually slowed down their loan expansion and stepped up their sale of securities. Deposits turned from inflow to outflow.



Note: Fourth quarter figures are preliminary estimates.

The Board also indicated that it is considering regulating commercial paper sales by the banks' parent holding company.

The Impact of Restraint is Varied

While few banks, if any, have escaped the influence of Federal Reserve actions and have generally tightened credit conditions, individual banks have been affected differently, depending upon size and location. The reserve city banks had been losing deposits since January, and the decline accelerated after July. As a result, these banks reduced their rate of lending after June and began selling off investments in increasing amounts. In addition, they stepped up their purchases of Federal funds and their usage of nondeposit sources of funds. Country banks, on the other hand, managed to increase deposits throughout the first half of 1969. They have been particularly successful in holding on to their time and savings deposits, which carry a lower reserve requirement than demand deposits. Encouraged by the high interest rates earned on Federal funds, the country banks lent large amounts of such overnight reserves, but since midsummer, these banks were pressed to hold deposits. Their lending activity since August, therefore, moderated somewhat.

The very large rebound in total deposits in Tennessee last spring was accounted for by the nearly 18-percent increase in time deposits. Time deposits made a rapid reversal after the Tennessee legislature enacted new legislation which took effect in April 1969. This allowed Tennessee banks to pay the maximum interest rates established by the Board of Governors.

Not only were banks of different location and size being differently affected, so were the volume and types of loans made. Rapidly expanding demands for commercial and industrial loans help explain why lending for these purposes rose more in 1969 than in 1968. Credit extended to manufacturing concerns, public utilities, and the service industry was especially large. Since midyear, real estate loans and lending for construction purposes have slackened relative to a year ago. These loans are typically among the most sensitive to changed credit conditions.

JOHN M. GODFREY

Bank Announcements

The **Second National Bank of North Miami Beach,** North Miami Beach, Florida, a newly organized member bank, opened on December 10. Officers are Alfred W. Slobusky, president; Jack Hanish, vice president; and Anthony P. Cassinelli, vice president and cashier. Capital is $300,000; surplus and other capital funds, $450,000.

CHANGE IN PAR STATUS

Effective January 1, 1970, checks drawn on all banks in Georgia may be cleared through the Federal Reserve System at par. This is the result of legislation passed by the Georgia General Assembly last spring.