

STATEMENT OF CHAIRMAN MCCAEE
ON BEHALF OF THE
BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM
ON PROPOSED SMALL BUSINESS LEGISLATION
BEFORE THE
SENATE COMMITTEE ON BANKING AND CURRENCY
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FOR RELEASE

UPON DELIVERY

On behalf of the Federal Reserve Board I wish to express our appreciation of this opportunity to present to your Committee our views regarding pending legislation proposed to aid small business. I am here to testify particularly with respect to those features of the legislation which relate to the Federal Reserve.

At the outset, I should like to make clear that the Federal Reserve, as the agent of Congress charged with responsibility for regulating the supply, availability, and cost of money, is keenly aware of the importance of small business to the commercial banking system and to the economy. The commercial banking system is composed mainly of small banks which depend heavily for their livelihood upon loans to, and deposits of, small business concerns. Small businesses, in turn, are dependent upon banks in their communities to finance a large part of their short- and intermediate-term credit requirements. Mutual interdependence of the small business and the commercial bank over a long period of time has resulted in establishment of close working relationships -- small businessmen know their bankers, and the bankers know the small businessmen, their problems, and their aspirations.

Apart from its interest as a banking organization in the problems of small business, the Federal Reserve System, in discharging its responsibilities for contributing to economic stability, is vitally

concerned with the prosperity of all business -- both small and large.

Small business accounts for a substantial proportion of total business employment and sales in the economy; 35 per cent of the total volume of business and 45 per cent of business employment, according to a report of the Committee for Economic Development. Should small business languish for whatever reason, large business, in fact the economy as a whole, would suffer severely and the problem of maintaining high level employment and a rising standard of living would be far more difficult.

Through its various activities the Federal Reserve System has acquired from experience an intimate knowledge of the financing problems of small business.

During the latter stages of the great depression, the System participated actively in providing financial assistance to small and medium-sized businesses under authority of section 13b of the **Federal Reserve Act**. That section of the law authorizes the Federal Reserve Banks to guarantee loans made by financing institutions to industrial and commercial businesses and also, in exceptional circumstances, to make direct loans to such businesses. The law requires that any such loan guaranteed or made directly by a Reserve Bank must be for the purpose of providing working capital and must have a maturity of not more than five years; loans may be made only to established businesses; and guarantees are limited to not more than 80 per cent of the loss on any loan.

The 13b program, as you are aware, never involved any large volume of Federal Reserve credit. For one thing, the System made every effort to have the loan cases handled through normal credit channels.

For another, the Reconstruction Finance Corporation's activities in small business financing were continually being broadened and its activities naturally limited those of the Federal Reserve. A third inhibiting factor was the nature of the statutory limitations on the kinds and maturities of loans which the System could make or guarantee.

During the war period, the System gained extensive experience in business financing, both large and small, by acting as agent for the Armed Services in guaranteeing 10.5 billion dollars of bank loans to war contractors. Over 90 per cent of the number and one-third of the amount of these guarantees were on loans to small and medium-sized businesses; that is, businesses with total assets of less than 5 million dollars. I might add that the guarantee program was conducted with no cost to the taxpayers. On the contrary, Treasury receipts from this program totaled 23 million dollars by the end of 1949.

Since the Reserve System's inception, its officials and staff members have been called upon from time to time to consult with commercial bankers or businessmen who felt that the financing needs of small business presented a special credit problem. Last fall, when business activity was much below earlier or current levels, the calls for advice and help on the small business problem became particularly numerous and we were visited frequently by representatives of small business groups. At that point, I got in touch with Secretary Sawyer who felt, as I did, that the time had come for the Secretary of Commerce to undertake a conference of interested groups to explore needs and remedies. Numerous conferences and discussions have been held since, both inside and outside of Government. The Federal

Reserve's role has been to hear all sides of the problem and to make available without reservation such technical information and judgment as we were capable of supplying. Almost daily, members of our staff who are experienced in this field, were asked to consult with individuals and groups both inside and outside the Government who sought our advice on various proposals.

Need for Special Financing Facilities

The legislation before you will be strongly opposed by those who believe that small business already obtains as much credit and capital as it can efficiently use. These opponents will say that:

- (1) The problems which confront most small business concerns are primarily managerial and competitive, not financial;
- (2) The commercial banking system is meeting all of the legitimate requirements of small business for short- and intermediate-term credit; and
- (3) Such financial difficulties as small business encounters could be overcome more effectively by revision of present income, estate, and inheritance taxes than by the provision of additional financial institutions or facilities.

Each of these points merits careful examination.

Managerial Problems: - Concerning the consideration that most small business financing problems are of managerial character, one does not have to look very far for supporting evidence. Various studies of individual small business enterprises which have failed or have gotten into serious financial difficulty reveal that the majority of such situations arose because of inexperience, or inadequacy in one or more of the wide range of managerial skills required for successful operations.

It is evident that a large number of small businessmen have not had sufficient training for the increasingly complex task of managing an expanding business. A businessman, to be successful today, requires a broad training in the fundamentals of business management. He must be familiar with the theory and practice of marketing, accounting for purposes of management and financial control, personnel management, production engineering, credit practices, and law and Government regulations. He must be able to solve problems, in many cases without the aid of specialized professional assistance, in all of these fields. Frequently, the small businessman is a one-talent man -- an excellent salesman, an inventive genius, or a production specialist. Often he has a limited knowledge of the other aspects of his business and is unacquainted with, does not fully appreciate the need for, or cannot afford specialized services or aids. This in large measure accounts for the high mortality rate of small businesses. On the other hand, we are all familiar with conspicuous examples of ingenious businessmen who, in spite of all handicaps, have developed their small concerns into large enterprises in a comparatively short time.

The acknowledged existence of management problems among our millions of small business concerns does not disprove their need for special and additional financing facilities. It does, however, emphasize that, in addition to the provision of financial facilities, greater efforts should be made to remedy the deficiencies of small business management and to provide needed aids and specialized management counsel. This has been recognized in the legislation which is before you.

Several financing institutions have been organized within the past six years, such as the Industrial Development Bank of Canada, the

Industrial and Commercial Finance Corporation of England, and the American Research and Development Corporation of Boston, to provide predominantly small business concerns with equity capital and long-term credit. From experience, each one has found that the financing need of the enterprises with which it has dealt is closely associated with the need for managerial and technical assistance. In other words, one without the other does not, in the majority of instances, constitute an adequate solution of the financing problem of the concerns which come to the attention of these institutions.

Commercial Bank Lending:- The commercial banking system, by and large, has been doing an outstanding job of meeting the short- and intermediate-term credit needs of small business. No one who is acquainted with the facts would deny this. The National Bureau of Economic Research, a private, non-profit research organization, undertook during the late Thirties an exhaustive study of business financing practices and the major sources of business funds. The study was financed in part by a grant of funds from the Association of Reserve City Bankers. I should like to quote one of the major findings of that study*:

"....the 'typical' short-term borrower [from commercial banks] around 1940 could be described as a small- or medium-sized manufacturing or trading concern, of somewhat less than average profitability. Of the total amount of bank credit used by business around 1940, some 70-80 per cent is estimated to have been used by companies with assets of less than \$5 million."

* See, "Business Finance and Banking," by N. H. Jacoby and R. J. Saulnier, 1947.

Commenting on changes in bank lending practices over the period preceding World War II, the National Bureau's report goes on to say:

"Banks showed increasing responsiveness to the credit needs of small and medium-sized businesses, which provided the bulk of their demand for credit at all times. Because enterprises of these sizes fared badly during the Thirties, the extension of credit to them called increasingly for methods designed to provide greater security for the lending agency and to minimize risks of default and loss. The adjustments which commercial banks made to meet these credit needs more effectively were marked by a willingness to write loans on terms more attractive to such borrowers (for example, term loans with instalment amortization and revolving credits supplying a reasonable guarantee of working capital facilities over periods longer than customary), and by the use of a wider range of security devices (such as the assignment of receivables, liens on income-producing equipment, the trust receipt, and the field warehouse receipts)."

The findings of a comprehensive survey of commercial and industrial loans to business, outstanding at Federal Reserve member banks on November 20, 1946, are also of special interest. This survey revealed that 76 per cent of the number, and 22 per cent of the dollar volume, of all business loans of member banks were to small business. Small business was defined on the basis of total assets as follows: manufacturing and mining concerns, total assets of less than \$750,000; wholesale trade, less than \$250,000; retail trade, utilities and transportation, service, construction, less than \$50,000. This survey further revealed that approximately one-fifth of these small business loans were what bankers call term loans -- loans repayable on an instalment basis with maturities at time of making of more than one year. Large, as well as small, banks were found to be actively engaged in lending money to small business on a term as well as a commercial credit basis.

In view of the greater risks involved in lending money to small business and the relatively higher costs of analyzing credit applications and servicing loans of small amount, the findings of the survey would indicate that the banking system has been active in cultivating small business customers.

These findings relate to a time now nearly three and a half years ago when large companies were borrowing heavily for reconversion needs. Since that time many of the larger loans have been paid off from retained earnings or have been refinanced, in some cases with new credits, through other financial sources such as insurance companies or the capital markets. In the past few years, an increasing number of banks have set up special small business loan departments, and recently several of our very large city banks have instituted new programs to expand their specialized services to small business. I have no doubt that a survey today of bank lending to business would show that the commercial banks are now doing a more effective job of providing credit to small business than was revealed by the System's 1946 survey.

While we commend the commercial banking system for its financing of the short- and intermediate-term credit requirements of small- and medium-sized business, we must recognize the fact that while banks make a great many loans to small business, they are not able to accommodate all small business needs. There are many financial needs of businesses, both large and small, that are not bankable, namely, equity capital and long-term credit needs. Commercial banks have a primary responsibility to their depositors for maintaining loan and investment portfolios in a

sound condition. They cannot undertake business financing which involves undue elements of risk, undue investigational or administrative expense, or the freezing of their funds for relatively long periods of time. In the case of larger businesses, financial requirements which are not bankable may be met from other sources, such as insurance companies and the capital markets; in the case of small business, non-bank sources of funds are less accessible.

Taxation: - There is no denying the fact that the problem of small business financing has been complicated by the structure and rates of Federal and State taxes. As I said last August in a statement on the equity capital situation, prepared at the request of a subcommittee of this Committee, there never seems to be a convenient time for a review of the tax structure. In 1948 when we had a substantial surplus we elected to reduce taxes without revamping the tax structure. Now, faced with deficit financing, we naturally do not want to do anything that will cause even a temporary loss of Treasury revenue. Therefore, a fundamental study that would lead to a reform of the tax system tends to be neglected and postponed.

While some of the difficulties which small business concerns face in attempting to obtain equity capital would be alleviated in part by a basic revision of the present tax structure, I would not want to leave the impression that tax revision alone would eliminate the occasion for the measures that are now before this Committee.

Affirmative View of Small Business Financing Needs

Those who feel that there is a real need for some additional facilities or institutions to provide more effectively for the financing needs of small- and medium-sized business are usually the first to admit that they do not have satisfactory statistical proof of the extent of this need. To obtain such proof would require a specific financial analysis of small- and medium-sized business concerns throughout the country. However, we do have such qualitative evidence as the policy statement on small business of the Committee for Economic Development (1947), the report of the Tulsa Chamber of Commerce (1948) on the number and functioning of the so-called industrial foundations to help small business, and the testimony presented to the Subcommittee of the Joint Committee on the Economic Report (1949) pointing to the existence of unsolved financing problems in the small business area. This evidence indicates that small- and medium-sized business concerns encounter serious difficulties in obtaining outside equity capital and long-term credit needed for expanding productive facilities, broadening the market for their products and services, and launching new projects. The evidence also suggests that very small concerns sometimes meet with difficulties in financing their short-term working capital requirements.

While the financing need of small business is often referred to broadly as a need for easier availability of bank credit, I am inclined to think that it is primarily a need for equity capital and long-term credit, either singly or in some combination. In many of the cases that have come to the System's attention where small business concerns have

complained of credit shortages, close inspection of these businesses has revealed that where there was an actual financial need it usually was for additional equity capital.

The small business financing problem is, however, too complex to be characterized simply as one of insufficient equity capital or long-term credit. There are many small business concerns whose requirements for short-term credit are so small that the commercial banker cannot afford the expense of processing and servicing them in the same manner as larger business loans. Such small business loans, if granted at all, may often be handled in the personal loan department, in which case the small businessman frequently does not obtain needed financial counsel and advice which would accompany a more complete analysis of his business. During the past two decades commercial banks have introduced a number of innovations in lending techniques, including the instalment loan for the purchase of equipment and the loan secured by accounts receivable or by inventory held under field warehouse receipts. The response of business concerns to these innovations suggests that efforts by banks themselves to broaden their lending activities can go a long way toward widening the circle of bank-eligible credit risks.

Within the past year, several large banks have launched special programs which supplement their regular business lending activities and are designed for small business. The response to these programs, as evidenced by inquiries, loan applications, and loans granted by the bank, indicates an unsatisfied demand for credit on the part of small business which, while it may not be large in terms of total dollar volume, is

none the less real. While the loan terms under these special programs have varied from one bank to another, they generally include (1) maturities up to 24 months on miscellaneous loans, and up to 5 years on loans for equipment and other longer-term needs; (2) repayment of principal and interest in regular instalments; and (3) flexibility as to security depending on the circumstances of the particular case. The loans have been granted for a variety of purposes, including financing of working capital requirements, payment of taxes and trade indebtedness, purchase of machinery and equipment, construction of buildings, and acquisition of partnership interests. The number of different types of business represented by borrowers is surprisingly large -- one bank sent me a listing which showed loans outstanding to small businesses in 38 different industrial and trade groups, ranging from advertising, drugs, and furniture to radio supplies, stove manufacturing, and wholesale plumbing. Among the borrowers were candy jobbers, hardware stores, jewelers, used car dealers, electrical contractors, truckers, surgical supply dealers, and ice manufacturers, to mention just a few among many.

Inquiries elicited by these programs revealed that in a number of cases those engaged in small business were unfamiliar with the various services that commercial banks can offer, or with the different types of credit available to meet business needs. In some instances, the banks found that small businesses were seeking managerial advice as much as they were additional funds, while in others it was determined that bank credit was not adaptable to the particular situation. At the same time banks were able to place funds at the disposal of many concerns which had previously been unable to obtain financing.

Appraisal of Conflicting Views

It is difficult to give a satisfactory answer to the question: "How great is the need of small- and medium-sized business for special and additional financing facilities?" I do not subscribe to extremists' views on either side of the question. Many of the so-called statistical facts cited in support of one viewpoint or another are merely opinions. Despite opinions that all legitimate needs for bank credit are adequately served, banks that have recently undertaken to explore the field have discovered an unsatisfied group of borrowers. At this stage, however, there is no way of saying how big that group is.

I would sum up the situation this way:

1. There are pockets in which, for one reason or another, existing financing facilities do not fully meet the needs of small business.
2. Short- and medium-term financing generally presents no great problem, except perhaps in some localities and for very small, and often new, concerns. Commercial banks generally have demonstrated their willingness to provide such credit for the latter group. However, many banks, particularly the smaller banks, have not developed the necessary facilities to assure adequate coverage.
3. Easy availability of short- or medium-term credit may encourage businessmen to rely on it too heavily, even using it to finance long-term needs. Should profits decline or credit conditions become tighter, they may then find themselves in serious financial difficulties. What these small businesses

really need is financing that will not be too burdensome when the going gets temporarily rough -- in other words, equity capital and long-term credit. Moreover, they often need more equity capital in order to qualify for short- and intermediate-term loans from banks.

4. Small business concerns do not have access to equity and long-term borrowed capital in the way that large companies do. For one thing, the costs of preparing and marketing a small equity or long-term debt issue are prohibitive. For another, there is frequently neither a new issue market nor a secondary market for the equity or long-term debt instruments of small businesses, either in the community where they are known or on the outside.

5. Neither stock nor bond financing in the forms generally available is what the small businessman is looking for. The sale of bonds and preferred stock is generally impractical, except to relatives and close friends. Frequently, the small businessman does not want to sell common stock. The sale of common stock to outsiders, unless to institutions especially authorized to participate on a limited basis, means that the small businessman will have to share the control of his business with others, or perhaps relinquish control. Most small businessmen value their independence highly -- that is one of the primary reasons why they go into business for themselves. Debt may prove to be a financial "strait jacket" in times of economic adversity.

6. The traditional suppliers of equity and long-term credit funds to small business -- the friend-of-the-family or the local financier -- are becoming less and less important in the local financial picture. The growing difficulty of finding a partner, silent or otherwise, is due in part to tax considerations. Also, it is due in part to a change in investment preferences of individuals. There have been indications in recent years of a trend away from equity investment to life insurance, tax-exempt securities, and other highly liquid assets.

7. There are very few institutions in existence equipped to supply small business with both long-term credit and equity capital. There are, undoubtedly, many cases in which some combination of equity capital and long-term credit would prove more suitable than either one by itself. To meet such needs, financing must be tailored to the requirements of each individual business, and not offered in exactly the same form on a take-it or leave-it basis to all comers.

Some Problems in Establishing Special Financing Institutions

If this summary poses the problem fairly, as I think it does, the question which Congress will want to weigh is what kind of solution will prove most constructive. I am sure that Congress will want the private banking system to continue to provide short- and intermediate-term credit to commercial and industrial borrowers. The main question before you is what kind of supplementary facilities are needed.

Facilitating the flow of equity capital into small business channels is undoubtedly the most difficult problem. In seeking a sound and workable solution to this problem, the Congress will want to explore all possibilities, for it is important to the maintenance of our system of competitive free enterprise that small business make its maximum contribution to sustained high levels of production and employment. There is a great deal to be said in favor of testing experimentally the feasibility of any proposed solution that appears to be sound.

As a believer in a private free enterprise economy, I feel very strongly that any new institution especially established for the purpose of making equity capital and long-term credit more readily available to small business should eventually be privately owned. Such a new institution, however, would have to be experimental because its operations would involve a substantial element of risk. Under these circumstances, I think it very doubtful that capital in sufficient amounts for an effective trial would be subscribed initially by usual private sources. Therefore, I have concluded that the most practicable solution is to have the initial capital of the investment companies advanced as outlined in the bills before you. The experience of similar institutions has made it abundantly clear that substantial capital is necessary if the newly formed investment companies are to avoid deficits during their first years of operation.

There are two reasons why institutions newly established to provide equity capital and long-term credit to small business may incur

operating deficits. In the first place, maintenance of an adequate technical and administrative staff to review applications, grant, and service equity capital or long-term loans, and to provide customers with such managerial and technical advice and assistance as they may require will mean substantial payroll and overhead expense. In the second place, it will take time for a newly established institution of the type envisioned to invest any sizable proportion of its resources in small private businesses. Therefore, if deficits are to be avoided, the initial capital should be large enough to permit coverage of operating expenses through income from temporary investment in Government securities.

I think it is essential that definite provision be made for transfer of the ownership of the new institutions to private hands as quickly as possible. This is important because the new type of institution, if it is to become a permanent part of our private economy, should compete for its funds in the market place. The judgment of the market place may not always be acceptable to the individual business concern, but it is much sounder than the use of public funds for risk financing of private enterprise. Continued public financing of private concerns in competition with other private concerns is unsound in principle and inconsistent with the precepts of a free enterprise economy.

The provisions of S. 3625 and S. 2975 stipulate that the proposed new investment companies may be organized by the Federal Reserve Banks, who in turn may also provide part or all of the initial capital when necessary. With the Federal Reserve System providing the initial

capital, sufficient operating funds would be assured to launch these institutions and to determine whether they could operate profitably. We heartily approve the provisions in these bills which stipulate that commercial banks and other private institutions and individuals may at any time purchase stock of these investment institutions from the Federal Reserve Banks. We see no reason why, if these institutions prove their profitability, ownership will not pass to private hands. Given time to develop a useful pattern of operations and to grow, there are some grounds for believing that this new type of institution may play an important supplementary role in our private financial organization.

From the beginning, we have thought that the approach through these new institutions should be experimental. No one can predict with confidence in what financial areas they will prove successful. We would favor starting off with enough of them to gain experience and to test their potentiality. The sound approach is to feel one's way and to learn how to meet the over-all problem most effectively.

In view of the difficult operating problems that the proposed new institutions will be up against, it is desirable that their managements be given ample latitude to meet effectively and flexibly the varied financing needs of small business. They should have authority to purchase preferred or common stock in small business, to extend long-term credit on such terms and conditions as individual circumstances may warrant, including participation with banks, or to undertake package financing in which both equity and long-term credit are combined. They should also

have authority to supply technical assistance on a reasonable fee basis where lack of technical skill in some phase of an applicant's operations seems to be critically related to his financing problems. In other words, the proposed institutions must be in a position to tailor the assistance which they supply in accordance with the type of problem which is presented by the individual small business approaching them for help.

From the advice which various bankers have given us, an important part of the business of the proposed investment institutions would represent package financing. Such financing avoids the pledge of all of a borrower's assets as security for a loan, thus leaving him in a position to obtain short-term financing from commercial banks if necessary. One banker told me that he knew of a number of small business financing cases which could be made bankable if some additional equity or equity and long-term debt could be provided. He indicated that his bank, and he thought other banks, would want to cooperate closely with the new investment institutions in working out constructive financing programs for promising small enterprises.

Finally, there is the problem of adequate earnings for the new type of investment institution in view of the costs and risks of financing small business. The riskiness of the business in which the proposed institutions would engage cannot be too strongly emphasized. If the institutions are to perform a useful public service, they must be prepared to incur losses. The interest rate on loans may be prohibitive if it is set

high enough to reimburse costs of investigating an application, servicing a small long-term loan, providing such managerial or technical assistance as may be required, and assuming the attendant risks. Participation through equity financing in the gains of successful ventures will be an essential to offset the high costs of operation as well as losses.

Various critics of the proposed legislation have expressed apprehension that the suggested new type of investment institution would constitute a competitive threat, on the one hand, to the existing commercial banking system and, on the other, to our existing investment banking facilities. I do not share this apprehension.

The new type institution would have to supplement its capital funds by borrowing from banks or in the capital market at market rates of interest. On the basis of this feature alone, it could not compete in its charges with rates of interest which banks, using depositors' funds, can charge their customers. In addition, both the credit appraisal and risk costs of an institution specializing in long-term capital and credit would run much higher on the average than in the case of commercial banks which make shorter-term and better-secured loans. The success of this new type institution would depend largely on its effectiveness in working through commercial banks and in supplementing the facilities which they are able to offer small business customers.

I should like to stress particularly the point just made that the success of the new type investment institution will depend largely on its effectiveness in working through commercial banks. The local

bank is in a unique position to discover and evaluate investment opportunities for such institutions, even if the bank itself is not in a position alone to extend direct long-term aid to the business. Moreover, the local banker is in a strategic position to handle the servicing and supervision of longer-term investments of the new institution, if such assistance is deemed helpful. The credit analysis and administration which the local banker is in a position to provide cannot be duplicated elsewhere under existing financial mechanisms.

As for competition with established investment banking facilities, these facilities are not now adapted to meet the equity and long-term credit needs of small business. This fact, which is generally admitted and fully substantiated by objective evidence, constitutes the principal case for providing for new, specialized investment facilities for small business.

The two bills differ in the tax relief that would be specially available to the proposed investment institutions. We feel that some special provisions adapted to the peculiar needs of this type of institution are desirable, in view of its experimental nature and the high risk exposure to be incurred. The Committee will, of course, give great weight to the advice of the Treasury Department in determining what tax provisions may be practicable.

I have emphasized the need for combining managerial and technical assistance with any financial aid to small business. Therefore, we heartily endorse those sections of the proposed legislation that

would provide for the collection and dissemination of information of benefit to small business.

As a means of assuring greater availability of credit to small, and particularly very small, businesses, the proposed legislation would authorize an insurance program for small business loans. The program would be administered by the Secretary of Commerce under S. 3625; it would be handled by the investment companies under S. 2975.

Loans would be insured without any preliminary review of individual loans. However, because of this automatic feature of the plan, the insurance would be limited to very small loans with maturities of not more than five years -- loans which would not justify the expense and work of reinvestigation by the insuring agency on an individual basis. The principal amount of an insured loan could not exceed \$25,000 under one bill, or \$10,000 under the other. The total insurance protection afforded to any financing institution would be limited to 10 per cent of the aggregate amount of its total insured business loans. Also, in order to make certain that the financing institutions would carry a reasonable share of the risk, the insurance coverage on any one specific loan would not be more than a certain percentage of the unpaid balance, 90 per cent under one bill and 95 per cent under the other.

Reasons for the loan insurance program can be summarized about as follows: Because of the expense of credit and risk appraisal, loans to many small and to most very small business concerns must ordinarily be made on a banker's personal knowledge of the applicant's abilities, character,

and financial worth, without the benefit of costly investigations. Where the businessman's banking contact is impersonal or casual, information of the type needed for negotiating a loan may be inadequate and the work and expense of getting the information may be too great.

No one can say how large a volume of insured small business loans would be generated by the banking system under the proposed program. We have noted an expansion of specialized plans for loans to small business by insurance companies and by banks in some areas of the country. Considering the favorable experience of these institutions, it is anticipated that other new plans will be developed, particularly since there is considerable interest on the part of private financial institutions to cultivate the demand in this field. In view of this rapidly changing situation, I would prefer to see this program of insuring loans placed in the hands of the proposed investment companies where it could be flexibly adapted to the needs of various areas of the country.

In conclusion, I would like to say that the proposal for the investment companies contained in this legislation was originally conceived not by the Federal Reserve but by private finance. The role projected for us was first suggested in the Fennelly Report of the Investment Bankers Association in 1945 and later by the Committee for Economic Development after

an exhaustive study of small business problems. After full hearings by his subcommittee of the Joint Committee on the Economic Report, Senator O'Mahoney undertook to give the suggestion concrete legislative form. Recently, in his message to the Congress, the President endorsed this same proposal.

We would like to have it distinctly understood that we do not wish to be placed in the role of asking that Congress increase our powers. However, if the Congress elects to place these responsibilities in our hands, let me assure you that the wishes of the Congress will be carried out as vigorously, soundly, and expeditiously as we know how.