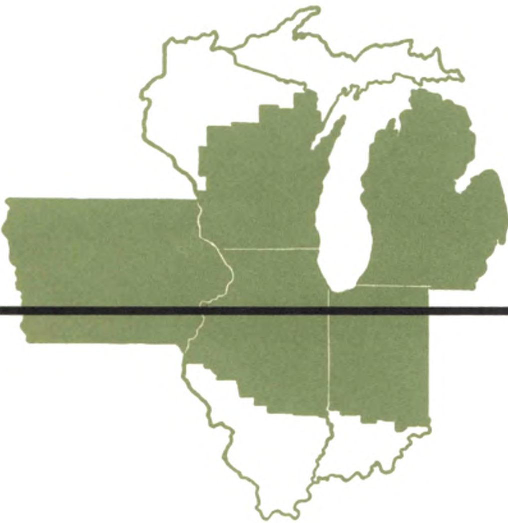
A review by the **Federal Reserve Bank of Chicago**

Business Conditions



1960 June

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THE Trend OF BUSINESS

With midyear looming on the horizon and the economy's performance during the first quarter now analyzed and entered in the records, expectations as to the trend of business during the second half of 1960 appear to have moved toward a middle ground. Some of the exceptionally optimistic forecasts made at the beginning of the year have been scaled down, and some of the more bearish expectations generated by the sluggish first quarter have been boosted a bit.

On balance, the unspectacular performance thus far this year is, in retrospect, interpreted by most analysts as a favorable omen. The adjustments taking place in recent months are thought to brighten the prospects for continuation of a high and gradually rising level of business. Although business inventories were built up rapidly during the first quarter, as had been expected following settlement of the steel strike, the rate of accumulation has slowed and there is increasing evidence that many firms are holding stocks closely in line with current needs. The depressing effects of a sizable liquidation of inventories, therefore, is not now considered a likely possibility any time soon.

With some easing of credit demands, especially in the Federal sector, the availability of credit has increased somewhat. This has been evident, for example, in residential mortgages. And, with credit demands less exuberant than during most of 1959, interest rates in many sectors have been below those at the beginning of the year. Prices of individual commodities have shown diverse movements and the aggregate indexes of wholesale and consumer prices have been relatively stable, indicative of a more or less balanced supply-demand situation.

In the words of one business economist, "We are currently operating in the most prosperous business environment our nation has ever known without symptoms of inflationary boom." And, in the words of the chairman of the President's Council of Economic Advisers, since the end of March "the signs are good."

Retail sales rose in April

Consumer spending at retail rose substantially in March and April. Preliminary reports indicate that April sales, seasonally adjusted, were 3 per cent above March and 5 per cent above April last year. Both durable and nondurable goods stores reported sales gains over the year-ago levels, but with the latter showing the greatest increase. Retail deliveries of new autos continued to exceed the year-ago pace, and in mid-May some production increases were announced even though the total inventory in dealers' hands remained near the million car figure. The major exception to the general trend of retail sales was in building materials, which reflected the reduced activity in residential construction.

The strong rise in retail sales in April was interpreted variously. On the one hand, it was taken to indicate that consumers had

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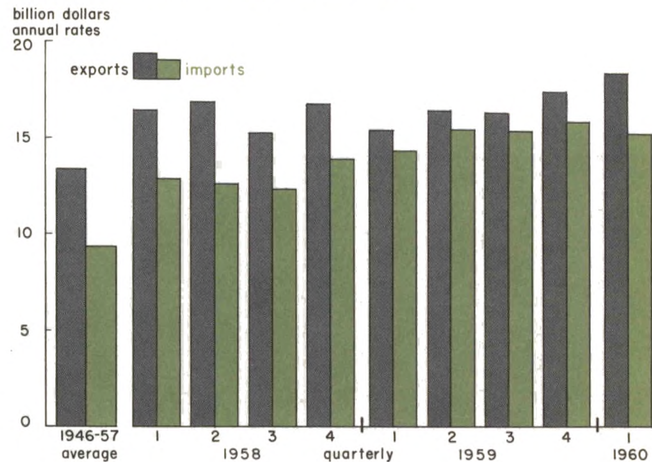
at last boosted spending in step with the rise in personal income and that this higher level of spending would likely continue. On the other hand, some believed that the rise in sales reflected merely a catching up on purchases postponed during the winter—that one month of "springtime" sales doesn't assure a summer of good business.

Early in May, department store sales in the Midwest dropped below the high level of a year earlier. However, sales of household appliances, radios, television and floor coverings continued relatively strong, and the results of another nationwide survey of consumer buying plans appeared to indicate that sales of most "big-ticket" items would remain above the 1959 volume.

Exports continue upward trend



Employment gained, following slump

Despite layoffs in April in several hard goods manufacturing industries—autos, farm machinery, primary metals and electrical machinery—all of which are important in the Midwest, total employment rose sharply from the reduced level in March. Unemployment, estimated at 5.4 per cent of the labor force in March, declined to 5 per cent in April, about the same as a year earlier.

New applicants for unemployment compensation were substantially below the year-earlier number in the Seventh Federal Reserve District in January and February—a relatively better showing than for the nation. In March and April, however, new applications were about one-fourth higher than in the corresponding months of 1959 in both the Seventh District and the country as a whole.

Unusually severe weather in March apparently was responsible for a large part of the decline in employment in that month and the larger-than-seasonal rise in April. However, at 66.2 million, total employment in April was at a new high for the month and about 850,000 above the year-earlier level, with most categories showing increases.

The average hours worked per week in manufacturing declined further for the fourth successive month, and the number of employees in nonagricultural establishments working part time (1 to 34 hours)was about one-third larger than in April last year. Unemployment continued to be highest among young persons. Those under 25 accounted for one-third of the unemployed in April, twice their proportion in the labor force. Negro youths had an unemployment rate of 18 per cent. The number of long-term unemployed (those out of work 15 weeks or longer) was about the same as a year earlier —1.2 million. Weekly earnings of factory production workers, largely reflecting the decline in hours of work, averaged just under

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$90 in April, more than $1 below March and about the same as in April 1959.

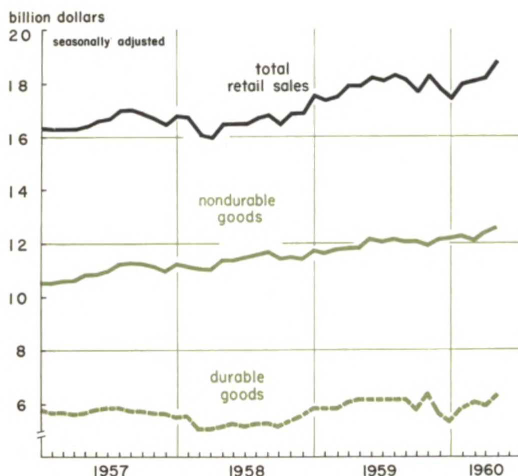
Export demand helps out

A year ago, there was a great deal of interest in the fact that merchandise exports were declining relative to imports. Throughout the postwar period, merchandise exports had run substantially in excess of merchandise imports. In 1959, however, the gap narrowed substantially. Exports exceeded imports by only 8 per cent.

Reflecting the strong demand resulting from boom conditions in Europe, exports from the United States in the first quarter of 1960 were 20 per cent larger than in the same period of 1959, while imports had risen 6 per cent. Exports exceeded imports by 22 per cent. This surplus of exports over imports was not adequate, however, to balance United States foreign accounts.

Goods manufactured in the Midwest have played an important role in the export rise.

Retail trade rose sharply in the spring



Shipments of autos and trucks to overseas customers during the first quarter were substantially higher than in the corresponding period last year. Manufacturers of machine tools report that foreign demand has been relatively stronger than domestic demand. There also has been a good foreign demand for some luxury goods.

There are several reasons for the rise in exports. One factor has been the excellent trend in business in virtually all parts of the world. Another is the gradual lifting of trade restrictions against American goods. Throughout the postwar period, many countries have attempted to bolster their balance of payments position by holding down imports from the United States. The third factor is the increased interest of American producers in expanding their sales abroad. Export sales have been pushed by adaptation of product lines to the needs of foreigners and through increased selling effort.

Construction to pick up?

For several months, total construction contracts awarded have been below the year-earlier figures. However, in April, data reported in *Engineering News Record* show a substantial rise in heavy construction awards—to a record level. This publication also reported that the backlog of work "on the drawing boards" has been rising sharply, suggesting that the gain in awards will continue.

Contract awards for new construction during the first quarter have shown increases over the first quarter of 1959 in each of the states of the Seventh Federal Reserve District, in contrast with a decline of about 6 per cent for the United States. The largest gain in the District—13 per cent—was in Iowa, followed by gains of 12 per cent in Michigan and 10 per cent in Indiana. The

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increases in Illinois and Wisconsin were nominal, 3 and 1 per cent, respectively.

Housing permits issued so far this year in major Midwest centers have been far below the record year-ago figures. Actual housing starts may have been even lower than indicated by the number of permits because of heavy snows, cold and floods in the first quarter. Producers of building materials have experienced declining orders, at least until quite recently.

There is some indication that funds will become more available for home building in the months ahead. Savings and loan associations have reported a higher net inflow of funds, and the low level of corporate security issues has led some insurance companies to seek additional mortgage investments. The Federal Housing Administration recently reduced permissible down payments on insured mortgages. Moreover, the Congress is considering bills that are designed to further increase the supply of mortgage credit.

More than most industries, home building is sensitive to changes in the availability of credit. This factor has been moving over to the plus side in recent months. Builders report that they are boosting their plans for new houses. Most "experts," however, are sticking with their forecasts that 1960 will likely see a slightly larger total number of housing starts than was indicated by the level of activity during the first quarter of the year.

Hogs boost farm income outlook

Farm income prospects in 1960 have taken a favorable turn. In 1959, farm income dropped as sharply as it had risen in 1958 and, at year end, a further decline was indicated. However, prices of eggs and hogs have climbed substantially since then and are now estimated by the United States Department of Agriculture to remain well above year-earlier levels through the remainder of the year. In addition, prices of beef cattle and milk have been holding up quite well and may remain relatively favorable throughout most, if not all, of 1960. As a result, Government officials estimate that realized net income of farm operators from farming will be just "slightly short" of last year, assuming "average" or "normal" weather. If growing conditions are favorable and crop yields are higher than average, farm income might be "considerably augmented."

Of these changes, the most important by far is the shift in the outlook for hogs. Since hogs are the leading source of cash receipts from farm marketings in the Corn Belt—accounting for more than 30 per cent of the total in Iowa, 25 per cent in Indiana and 20 per cent in Illinois and Missouri—the greatest upward revision in farm income estimates are for those states.

In 1959, farm income in the Corn Belt declined relatively more than the national average largely because of the sharp drop in hog prices. But farmers have cut back hog production this year instead of increasing output further as had been expected. The number of sows that farrowed for the spring pig

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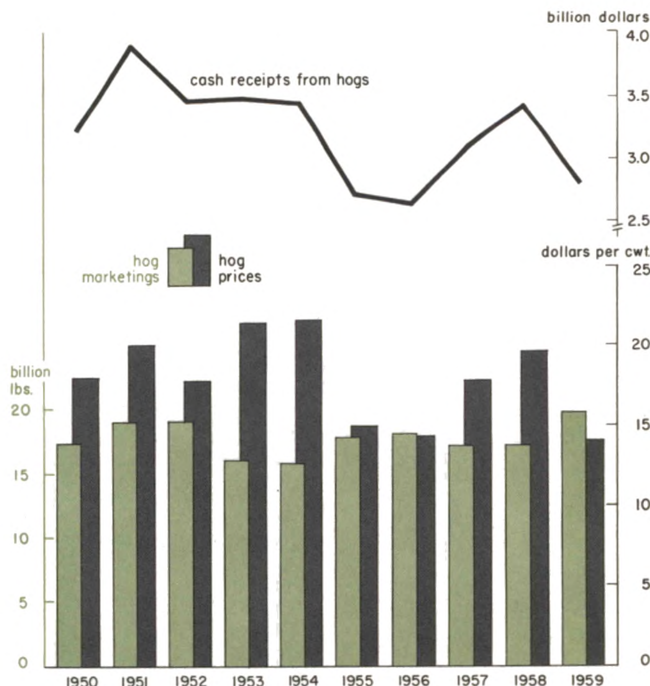
crop of 1960 is now estimated to have been 13 per cent below last year. This will mean sharply reduced hog marketings in the fall and winter of 1960.

Usually, for each 2 per cent change in hog marketings per capita there has been about a 3 per cent change in the opposite direction in farm prices for hogs. Using this relationship, the cutback of 19 per cent in farrowings in December through February could be translated into 30 per cent higher hog prices in July through September compared with the corresponding period in 1959. Similarly, the cutback of 10 per cent in farrowings, March through May, likely would result in 15 per cent higher prices from October through December.

Cash receipts from hogs show inverse response to changes in marketings



For 1960 as a whole, therefore, total cash receipts from hog marketings are indicated to be 5 to 10 per cent above 1959, assuming past relationships between supply and prices hold. In the Corn Belt states of Illinois, Indiana and Iowa, the higher value of hogs could increase total cash receipts from all commodities 1 to 3 per cent. However, net farm income in these states could rise relatively more since higher hog prices would greatly boost the net profit per hog, and, even with a smaller number being marketed, net income of hog producers could be substantially higher than in 1959.

Cyclical pattern

Cyclical fluctuations in hog prices and their effects on income of Corn Belt livestock producers are well known. However, the changing character of the hog production cycle carries with it significant implications for the pattern of income changes. As the hog cycle has become largely independent of fluctuations in corn production (see "The hog cycle in perspective," *Business Conditions,* February 1960), the length of the cycle has shortened and the fluctuations have become sharper. This pattern, together with evidence that many hog producers are rapidly increasing the size of their breeding herds, would indicate that the current cutback in hog production may last for only one year and that 1961 could see the beginning of a new upswing in output. Thus, the optimistic outlook for income of hog producers in 1960 may be reversed a year later.

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Terms of home mortgage loans

Business analysts are constantly sharpening the tools of their trade to increase the promptness with which significant movements can be detected and evaluated. Among the many indicators which have come into widespread use are measures of changes in credit market conditions.

Interest rates, of course, have long engaged the close attention of economic observers. While doubtless the most meaningful single barometer of prevailing conditions in the credit market, rates do not always tell the whole story. Credit contracts have other features than rates. These also may be sensitive indicators of changes in the credit climate.

A shift in the structure of home mortgage interest rates, for example, may be foretold by some prior modification in terms pertaining to maturity, loan-to-value ratio, loan commissions or fees, lenders' standards relative to property quality and borrowers' creditworthiness, or perhaps even by piecemeal advances or concessions in contract rates before the adjustment becomes general. On the other hand, such developments may take place concurrently with or following the rate movement, thus in a sense confirming or accenting it. Because such changes are essentially equivalent to interest movements, it is necessary to take them into account no less than rate itself if mortgage market developments are to be evaluated adequately.

The economic analyst seeks measures which are sensitive to changes in lending terms arising out of credit market developments. Terms, though, may change—or seem to change—for reasons unrelated to easing or restraint in the market climate. And they may *appear* to occur, moreover, simply because of statistical difficulties inherent in any effort to describe a market quantitatively and portray its behavior through time.

Markets localized; loans varied

Many credit markets are national in character, notably those for Federal securities and the obligations of widely known corporations and municipalities. The Government programs of VA-guaranteed and FHA-insured loans have to some extent created a national market for home mortgages, also. The Government programs, however, have not entirely obliterated differentials in lending practices and rates. This is in part because conventional financing accounts for a much bigger share of the market than the Government programs—twice as much last year for the nation—and conventional loans, unlike the FHA's and VA's, are not standardized in quality and reflect to a significant degree differences in the supply of local savings available for investment in home mortgages.

Market data are scarce

Detailed information on home mortgage terms is not readily available. Both the Federal Housing Administration and the publishers of *House and Home* magazine regularly poll lenders in order to obtain comparisons of mortgage interest rates and discounts in selected local markets and regions. Of necessity, these roundups provide only general indications of the levels of going rates for a few broadly defined categories of home loans, among which conventional loans are treated as a single class.

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In order to secure more specific information than is available from other sources, the Federal Reserve Bank of Chicago, in cooperation with the Federal Home Loan Bank, initiated in the summer of 1958 a monthly survey of individual home mortgage loans made by a sample of savings and loan associations in the Chicago area. Shortly thereafter, the scope of the survey was broadened to provide representation for other lenders in the home financing field—commercial banks, mortgage companies and life insurance companies.

During the year and a half of experience to date, a number of modifications in reporting and processing procedures have been made. The data, as a result, do not provide a completely consistent running account of developments in the Chicago mortgage market. They are, however, highly instructive on the intricacies of market structure and offer guidance to attempts to detect and evaluate changes in mortgage supply and demand conditions.

Home lenders in the Chicago market

Among the classes of lending institutions serving the Chicago market, savings and loans associations have played a dominant role in recent years:

	per cent of recordings			
	Savings & loan assns.	Commercial banks	Individ-uals	Other
1957	63%	6%	6%	25%
1958	66	7	5	22
1959	71	6	6	17
1959*	70	6	6	18
1960*	66	6	7	21

*First quarter.

In Cook County, which includes Chicago and much of the populous, rapidly developing suburban ring, the associations lately have accounted for about two-thirds of all mortgage recordings of $20,000

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NOTES TO TABLE:

Data based on reports from a sample of Chicago-area savings and loan associations.

Each maturity class covers a range: maturities of 12½ to 17½ years appear as 15-year loans, those of 17½ to 22½ years as 20-year loans and those of 22½ years and more as 25-year loans.

A few loans are omitted because their terms were outside the loan-value and maturity ranges shown or because their categories failed to comprise at least ½ of 1 per cent of loans made.

Terms of conventional home loans on existing property, 1958-60

	Oct. 1958-June 1959				July-Dec. 1959				Jan.-Mar. 1960			
Maturity in years	15	20	25	Total	15	20	25	Total	15	20	25	Total
	(per cent distribution of number of loans)											
Contract rate and loan-value ratios (per cent)												
45-64												
Less than 5¼	2	4	1	7	-	1	-	1	-	-	-	-
5¼	1	2	-	2	-	-	-	-	-	-	-	-
5½	5	5	1	11	3	3	1	7	-	-	-	-
5¾	1	-	-	1	2	2	1	5	1	2	-	3
6	3	-	-	3	5	4	1	10	5	6	1	12
6¼	-	-	-	-	1	1	-	2	2	2	-	4
6½ and over	-	-	-	-	2	-	-	2	5	-	-	5
	11	11	2	24	13	11	2	26	13	10	1	24
65-74												
Less than 5¼	-	1	1	2	-	-	-	-	-	-	-	-
5¼	-	1	-	1	-	-	-	-	-	-	-	-
5½	7	11	3	21	2	3	1	6	-	-	-	-
5¾	2	1	-	3	1	1	1	3	-	-	-	-
6	8	1	-	9	7	9	2	18	6	12	3	21
6¼	-	-	-	-	2	1	-	3	3	2	1	6
6½ and over	-	-	-	-	6	1	-	7	10	2	-	12
	17	15	4	36	17	15	3	35	19	17	4	40
75-84												
Less than 5¼	-	-	1	1	-	-	-	-	-	-	-	-
5¼	-	-	-	-	-	-	-	-	-	-	-	-
5½	3	14	7	24	1	3	2	6	-	-	-	-
5¾	1	3	2	6	1	2	3	6	-	-	1	1
6	5	2	1	8	5	9	4	18	3	8	4	15
6¼	-	-	-	-	1	2	1	4	2	4	2	8
6½ and over	-	-	-	-	3	2	1	6	6	4	1	11
	9	19	11	39	10	18	10	38	12	16	8	36
Total	37	45	17	99	40	44	15	99	44	43	13	100
Loans in sample (monthly average number)				400				325				275

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and less—a category which typically is taken to measure the volume of 1-4 family residential financing.

The distribution of recordings by lender class does not clearly indicate the sources of mortgage funds. One reason for this is that some lenders make and record loans on behalf of others. Commercial banks, for example, often originate loans they later sell to insurance companies, pension funds, mutual savings banks and individuals. Originating mortgage loans for investors, of course, is the specialist role of the mortgage companies, which are included under the "Other" heading. Also in this category are the few life insurance companies which make loans directly rather than through mortgage company correspondents.

The proportions given for the savings and loan associations, however, probably measure relatively well the importance of these agencies as suppliers of home mortgage credit in the area, since the associations usually hold loans until they are repaid.

The savings and loan associations are the only mortgage lending institutions whose investments are largely confined to mortgages. Indeed, their earning assets generally include only real estate loans and Government securities. Savings banks, insurance companies, pension funds and commercial banks, on the other hand, have a much wider range of choice. A bank, for example, will weigh the profitability of mortgage lending against the relative attractiveness of yields on Governments, municipal securities, corporate bonds and business and personal loans, as well as a set of liquidity requirements quite different from that confronting a savings and loan association or any other type of mortgage lending institution. A life insurance company has an even more extended range of alternatives. The result is that the savings and loan associations are more or less continuously "in the market" for mortgage loans, whereas activity in mortgages on the part of other lenders tends to vary with shifts in returns on investments other than mortgages. At times when yields on residential loans are comparatively high, the flow of funds into the market from the life companies, the commercial banks and the mutual savings banks increases. And when returns on other uses of funds are the more attractive, mortgage acquisitions by these investors, of course, may tend to decline.

Who are the borrowers?

Among the principal uses of mortgage credit is the financing of new construction. The borrower may be an individual who has contracted to have a home built to his order, or he may be a builder who plans to put up one or more homes, individually or in groups, for sale.

Also important among the users of residential financing are those who borrow in order to purchase existing properties. If the home an individual buys is new and he becomes the first occupant, the chance is good that his loan replaces one already outstanding in the name of the builder selling the home. Indeed, the buyer may borrow simply by assuming the seller's debt. If the home is one previously occupied, it is likely that a "new" loan will result.

Then there are the loans that home owners obtain in order to pay off old ones. It may be that market rates are lower than when the original borrowing occurred so that refinancing promises a saving in interest expense. Or, the home owner may borrow anew, not only in order to pay off an old debt but also to obtain some extra cash for other uses.

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Some lenders specialize

Most savings and loan associations, banks and mortgage companies make loans of all these types. There are some, however, which do not. A few of the associations, for instance, lend only on completed structures. They make advance commitments to provide the long-term "permanent" financing of a new home, or a number of them, but require the builder to finance himself, or obtain outside short-term financing from a bank or other source, for the period up to completion and sale. Similarly, life insurance companies typically make loans only on completed structures, although entering into commitments to do so before building is begun and leaving to the mortgage companies or banks originating the loans the responsibility of financing and overseeing the construction stage. This entails administering the advances to builders and making certain that loan contract provisions and zoning and other code requirements are complied with.

Specialization occurs, too, with respect to the types of financing offered by lenders. While savings and loan associations concentrate on conventional lending, the mortgage companies and commercial banks are relatively active in FHA financing. And within the sphere of conventional lending, the commercial banks tend to make relatively more shorter-term, larger-down-payment loans than the savings and loan associations. The terms in conventional lending offered by the latter institutions, indeed, often come close to matching the generously low down payments and long maturities associated with Government-underwritten loans.

What are mortgage "terms"?

Probably the most obvious characteristic of a mortgage loan is the interest rate it bears. The contract rate, of course, is only one of the factors determining the true or effective rate. The loan commission or fee and the discount, if any, must be taken into account also. Both are tantamount to additional interest charges connected with the loan transaction.

Another important aspect of any mortgage loan is the amount, in an absolute sense and in relation both to the value of the property which secures it and to the borrower's income. No less prominent is the duration of the credit, and the provisions governing repayment, i.e., whether the principal is to be completely or partially repaid during the life of the loan or the full amount is to fall due at the contract maturity date, and the size of the penalty, if any, charged for prepayment. Others of the salient features of a specific transaction are the quality, condition, age and location of the property securing the loan—to the extent that these are not implicit in the valuation—and the circumstances of the mortgagor, other than income, that is, age, occupation and quality of his references. Certain additional aspects of the credit itself may vary, such as collateral pledged in addition to the mortgaged property and the willingness or unwillingness of the lender to countenance secondary financing or contract sale in connection with the transaction.

The contractual stipulations, either explicit or implied, with respect to all these matters constitute the terms of a loan, the conditions under which a borrower obtains mortgage credit. To compare the terms of any two loans—and particularly the way in which their rates are related—means that some judgment must be made on pairs of relationships involving a fair number of items of information, some quantifiable and some not. The analyst, not directly involved in the de-

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tails of the transactions, must necessarily make do with the quantifiable items only.

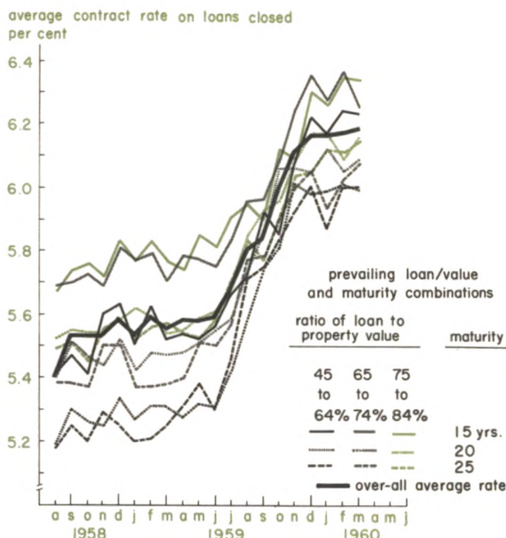
The loan-value relationship, size of loan, term to maturity, date of transaction and type of loan—i.e., whether Government-underwritten or conventional, on the security of new or previously occupied property—are characteristics susceptible of objective and in some cases quantitative expression. The borrower's creditworthiness and the quality of the property securing the loan (other than as this factor may be reflected in its value), of course, are not readily expressed quantitatively.

The structure of terms

The relationship between rate, on the one hand, and loan-value ratio or term to maturity, on the other, is not a simple one. At any given time—other things equal—the longer the term or the smaller the borrower's equity, the riskier the loan, as the lender sees it, and, therefore, the higher the rate. This, indeed, is the form of the "variable-rate" schedules used by many savings and loan associations in the Chicago market. On conventional loans secured by existing property, the "going" rate in the December 1959 survey, for example, was 6 per cent for accounts of not more than 65 per cent of property value and terms not to exceed 22½ years. An 80 per cent loan in the same maturity class at the same time carried an average rate of close to 6¼ per cent (see accompanying chart).

The lowest rates typically go with the largest down payments and shortest maturities, but this is not always the case. Certain of the shorter-term loans are secured by substandard properties. Maturity is short because the lender fears a decline in property value. Some of the high down payment loans, in turn, are advances to borrowers whose

Movements of interest rates in the Chicago mortgage market, August 1958-March 1960



incomes or income prospects are below standard—the bigger the down payment, the smaller the monthly repayment burden. Loans of both kinds are deemed risky and bear relatively high rates. In the December 1959 comparison, loans of less than 17½ years maturity, again conventional and secured by existing homes, carried the highest interest rates reported, the average exceeding 6¼ per cent.

Terms in a changing market

Because mortgage loan contracts are many-faceted, the response of lending practices to shifts in credit supply and demand may take a variety of forms. Principal attention fastens on the behavior of rates, but it is common for lenders to modify other terms of mortgage contracts as well. In a time of tightening in the market, for instance, a

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hike in rates may be the initial response. This may be brought about directly by an explicit increase in the schedule of prevailing contract rates or indirectly by upward adjustment of commissions or discounts. Later on, curtailment in maturities, reductions in loan-to-value ratios and the imposition of stricter requirements relative to property quality or borrower creditworthiness may follow to fortify the rate movement or, in effect, to substitute for further adjustment of rates. Taken by itself, an observed rate increase may understate the extent of the tightening but by a margin susceptible in principle to measurement, inasmuch as loan amount, property value and duration of the amortization period are all numerical magnitudes. The extent to which these magnitudes reflected tightening mortgage credit availability, especially in the second half of 1959, is suggested by the data in the accompanying table. They indicate that a move toward shorter maturities and lower loan-to-value ratios accompanied the rate rise. These data, of course, shed no light on the extent of any further tightening attributable to sympathetic adjustments in lenders' standards as to property quality or borrower creditworthiness, or, for that matter, on the possibility that these "terms" may have undergone offsetting changes.

Detecting changes in the market

The extension of mortgage credit is a complicated process involving a series of stages that usually stretch out over a period of a month or more and frequently a still longer period. Not until a loan is "set up" on the lender's books, a step occurring at or about the time the requisite signatures are affixed to the mortgage and note, is the transaction final. "Closing," however, is anticlimatic because terms of the loan will have taken on essentially their final form at an earlier date—usually the date of formal application by the borrower and approval by the lender.

In general, approval amounts to a firm commitment on the part of the lender to make the loan, while submission of a signed application in effect commits the borrower to take the loan if his request for it is accepted. The application, bearing signatures of both parties to the transaction, specifies the amount of the loan, the term of amortization and the contract rate and describes the property against which the loan will become a lien.

At an even earlier stage, as much as six months or more before with construction loans, certain characteristics of the credit, including the contract interest rate, may have been established as the lender entered into an advance loan agreement with the builder or simply issued a quotation of his prevailing terms—an informal commitment—to an individual. When money market conditions are tightening, the presence of a backlog of advance commitments can, if these are included with reports of currently negotiated agreements, blur any evidence that mortgage rates are being adjusted to changing conditions. The rates specified in current commitments, on the other hand, are keenly sensitive to the prevailing situation.

If the date of closing is taken as the event which brings a given loan into the terms series, the apparent level of rates will tend to lag behind the true level—that is, the rate pattern expressed in current commitments to lend—during a period of tightening. The reason for this is that the terms of a large proportion of the loans closed at any given time tend to reflect market conditions at some past date.

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Clearly, there are difficult questions of timing to be resolved by the analyst of mortgage market trends and conditions. Depending upon the stage of the lending process from which mortgage rate data are obtained —quotation or advance commitment, loan approval, or loan closing—relative timeliness, tardiness or marked sluggishness will be observed in the response of rates on home mortgages to tightening of credit in general. On the easing side, of course, the effect will be less marked; advance commitments to lend at rates that prove to be above the market at the stage of final negotiation generally are allowed to lapse.

A measure of the effect of advance agreements upon the movement of mortgage rates during a time of increasing tightness in the market is provided by the savings and loan data for the Chicago area. Loans secured by existing properties typically involve only short-lived commitments, the effects of which work off promptly. Long-term, low down payment loans on new properties—often in large-scale tract developments—exemplify the kind of lending in which the advance commitment plays a key role. In the first quarter of 1959, contract rates on 17½ to 22½ year, 20 to 25 per cent down payment conventional loans on *existing* properties averaged 5.58 per cent. For the same three months, the comparable average for loans of the same maturity and down payment characteristic but on *new* properties averaged 5.54 per cent, or very nearly the same. In both cases, of course, loans were taken at the stage of closing. But, because the interval between commitment and closing is shorter for loans on existing property than it is for loans on new construction, rates on loans closed tended to respond to credit tightening more promptly in the category of existing property than in that of new. The spread of average rates on existing properties over rates on previously negotiated loans secured by new properties was nominal from March through June, but it rose to about .10 of 1 per cent when signs of tightening became generally evident, and widened to between .15 and .20 per cent in November through January of this year. The relative tardiness of the rise in rates on loans secured by new properties, therefore, reflected the manner in which information was gathered and not the real behavior of interest rates in new loan commitments.

Continuing survey

All types of lenders are currently reporting terms as of the date of loan approval. From these reports, separate tabulations are made for FHA, VA and conventionally financed mortgages, with a further breakdown of loans on new and existing homes. The tabulations show average maturities, loan-to-value of property ratios and contract and effective interest rates. In addition, the loans are tabulated by "bundles" of characteristics, i.e., combinations of interest rates and loan-value ratios for various maturities. Survey findings will be made available to those interested in the structure of the residential mortgage market and accompanying shifts in market conditions.

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Debt expansion slows

The first few months of 1960 have been marked by a sizable decline in the demand for capital and credit. During the first quarter, the increase in the principal types of indebtedness amounted to only one-third the increase in the first quarter of 1959, the record year thus far for expansion of debt. The easing of credit demands has been associated with a less exuberant business climate than existed at the turn of the year, and together these have resulted in lessened inflationary pressures and lower interest rates.

The most dramatic change from a year ago, in the capital and credit markets, has been in the fiscal position of the Federal Government. In the first quarter of 1959, Treasury obligations held by the public—that is, outside Government agencies and trust funds and the Federal Reserve Banks—increased slightly, in contrast with a usual seasonal decline during that period. This year, in the first quarter, the publicly held debt declined by 2.6 billion dollars, as the Government's budgetary position shifted from a massive deficit in fiscal 1959 to a near balance in fiscal 1960. This change in the Treasury's requirements accounts for the bulk of the shift to slower debt expansion compared with last year, but other demands for capital and credit have moderated as well.

New security issues, especially those of state and local governments, have been well below last year's levels, and, as a result, the increase in outstanding securities, aside from Treasury obligations, was about 10 per cent below the 1959 increase in the first quarter. The largest reduction in credit demands in the private sector has been in the mortgage area. With housing starts running at a rate nearly one-fourth below 1959, the increase in outstanding mortgage credit has been much smaller this year. Also, consumer credit, which usually declines in the first quarter of the year, dropped off somewhat

Debt changes in the first quarter

	1959	1960*
	(billion dollars)	
Increase in outstanding securities:		
Corporate	2.0	1.9
State and local governments	1.3	1.1
U. S. Government, public heldly	0.3	-2.6
Other (Federal agency, foreign government, and international organizations)	0.4	0.3
Increase in outstanding mortgages	4.1	3.3
Change in consumer credit	-0.7	-0.9
Change in bank loans other than mortgages and consumer loans	-1.1	-1.1
Total increase in above types of debt	6.3	2.0

*Estimated.

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more this year than last. The decline in other bank loans was about the same as in the first quarter of 1959.

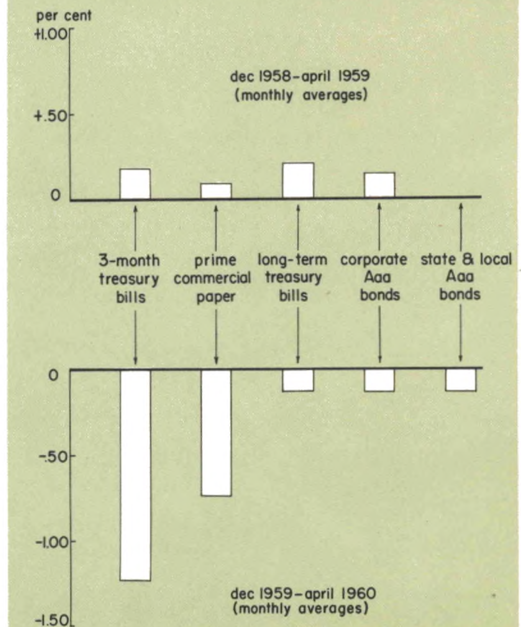
Faster rise in second half

What about the rest of 1960? Even in 1959, when credit demands were heavier than ever before, first-quarter debt expansion was low relative to the rest of the year due to the seasonal patterns of borrowing by the Federal Government, consumers and business. As 1960 wears on, seasonal factors, especially the Treasury deficit in the second half of the year, will cause debt to expand much more rapidly than in the first quarter.

But fragmentary estimates for April and May suggest that over-all credit demands continue to be well below those of last year. Corporate and state-local government security issues in April and May are estimated to have totaled around 400 million dollars less than in 1959, a decline of one-eighth. In April, total bank loans increased 1.4 billion dollars, 500 million less than a year earlier, largely because of smaller increases in real estate and consumer loans. The Treasury's cash deficit for April, traditionally a deficit month, was 1.2 billion dollars smaller in 1960 than in 1959, and the increase in the publicly held debt was 1.5 billion dollars less this year. All in all, if the economy continues to expand at a moderate pace, as projected in most forecasts for the rest of the year, debt expansion in 1960 could very well total 20 or more billion dollars less than last year's record 66.7 billion dollars.

Interest rates decline

The easing of credit demands so far this year has been reflected in a parallel easing of interest yields on open market debt instruments, just as increasing credit demands in early 1959 pushed yields up at that time. Early last year, yields rose on both short- and long-term instruments by amounts ranging up to nearly one-fourth of a percentage point. Between last December and April of this year, yields declined modestly on long-term bonds and very sharply on short-term instruments, with large fluctuations within the period ranging from very high yields in early January to quite low yields in late March. Also, the average interest rates on new loans to business made by large banks declined slightly in the early months of this year, whereas they had risen in 1959. However, interest rates have remained above the year-ago levels.



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