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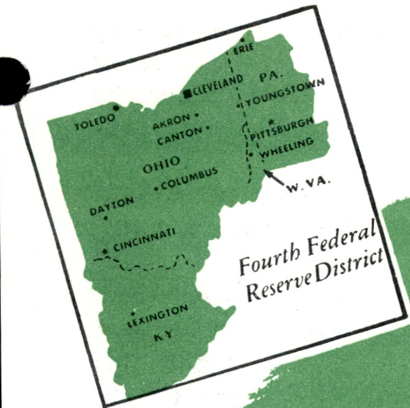

Business Trends

Prepared in the Research Department of the
FEDERAL RESERVE BANK OF CLEVELAND
Serving the Fourth Federal Reserve District

BANK CREDIT DURING RECOVERY

Although economic recovery is now in its sixth month, the resurgence of economic activity during this period has not been accompanied by an expansion in bank loan portfolios. A substantial rise in total credit extended by the banking system did occur during the first seven months of the year, but the expansion took place entirely in holdings of investments, as the amount of loans outstanding during the period showed a small net decline.

The relative weakness in loan demand during the first seven months of the year reflects the interaction of a number of factors. For example, inventory liquidation in some industries during most of the period contributed to reduced demands for funds by business borrowers. In addition, borrowing by nonbank financial institutions such as sales finance companies was down in the first seven months, perhaps mainly because consumers did not increase their indebtedness to purchase durable goods.

Developments in banking activity thus far in 1961 are recorded in the statements of condition of the Fourth District member banks which report weekly to the Federal Reserve Bank of Cleveland. Although changes in the balance sheet of Fourth District banks and banks in the nation, respectively, tend to differ, they usually can be explained by factors such as the differences in industrial composition and financial activity, among others.

Loans. With the exception of temporary increases, for example, over the March and June tax and dividend payment dates, total loans at 26 weekly reporting member banks in the Fourth District have been on the downside during the first seven month of 1961. Over the entire period, total loans at reporting banks in the Fourth District declined nearly 3 percent; at weekly reporting banks throughout the nation, total loans declined by a somewhat smaller rate. An accretion in security loans by banks in money market centers and a smaller decline in commercial and industrial loans elsewhere in the nation accounted for the more favorable showing in the national figures.

The decline in bank loans in the Fourth District in the first seven months of 1961 was substantially smaller than in the comparable period of 1958, when total loans of the District reporting banks declined by more than 6 percent. It should be pointed out, however, that while the first seven months of 1961 included five months of economic recovery, the 1958 period included only three months of the recovery, which may have had some influence on bank lending activity.

In the Fourth District, about two-thirds of the decline in reporting banks' loan volume in 1961 was due to a drop in commercial and industrial loans, which were down about 5 percent from

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the year-end level. Although extensions of new business loans were larger in the seven-month period of 1961 than in the similar period of any other recent year, repayments exceeded extensions by a relatively large amount. More than five-sixths of the net decline in business loans was due to net repayments of loans by manufacturers of metals and metal products, reflecting in part some liquidation of inventories by this group during most of the period. Net repayments of loans by the metals group had not occurred in the first seven months of any year since 1954. The net reduction of indebtedness by public utilities and commodity dealers appears to be somewhat less than usual, while a reduction in loans to textile, apparel, and leather manufacturers was the first such development in many years. Such loans usually increase during the first half of the year and decline during the second half. Loans by reporting banks to construction firms declined substantially in the first seven months, reflecting a lower level of residential construction than a year ago. The decline in loans to trade establishments was much less than in 1958.

Among the business borrowers which have increased their outstanding loans so far in 1961 are the petroleum, chemical, and rubber concerns, and all other unclassified borrowers, but the increase in the loans outstanding to these groups was less than the amount of earlier years.

In addition to business loans, other kinds of bank loans in the Fourth District have also fallen below the year-end levels. At the end of the first seven months of 1961, nonbank financial institutions, principally sales finance and personal finance companies, had repaid nearly one-fourth of their loans outstanding, which compares with little net change a year earlier. At the same time, consumer and all other loans moved up more than in 1960, but the addition reflected a special acquisition of customer receivables from a large retail concern. Bank holdings of real estate loans so far in 1961 have increased slightly, while in the comparable period of 1960 they remained unchanged.

Security Holdings. Holdings of securities by weekly reporting member banks in the District increased by nearly $450 million during the seven-month period under review. A pronounced shift in the maturity composition of U. S. Government securities featured the increase, as holdings of securities maturing within one year nearly doubled. At the same time, banks reduced holdings of Treasury securities with maturities from one to five years. Two factors were mainly responsible for the reduction in such holdings: (1) reclassification of some issues into the category of securities maturing in less than one year due to the passage of time, and (2) a shift to longer maturities associated with a Treasury advance refunding operation at the end of March. Holdings of securities other than U. S. Government securities rose $101 million, the largest increase in many years.

The shift in the composition of bank assets over the period under review contributed to an improved liquidity position of the reporting banks, as measured by both the loan-deposit ratio and the ratio of short-term assets to total deposits. While the former ratio showed only a slight improvement between the end of December and the end of July, the latter ratio moved up substantially, rising from 16.7 percent to 24.4 percent, due to the sharp rise in holdings of U. S. Government securities maturing within one year, as mentioned above.

Deposits. Adjusted demand deposits of individuals and business enterprises, etc., have declined about 2 percent at Fourth District reporting banks thus far in 1961; nationally, such deposits showed a slight increase. While some of the decline in demand deposits in the Fourth District was seasonal, a number of factors, including shifts to time deposits, were responsible for the decline. However, the sharp rise in savings and other time deposits, and an increase in U. S. Government deposits offset the year-to-year decline in demand deposits.

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