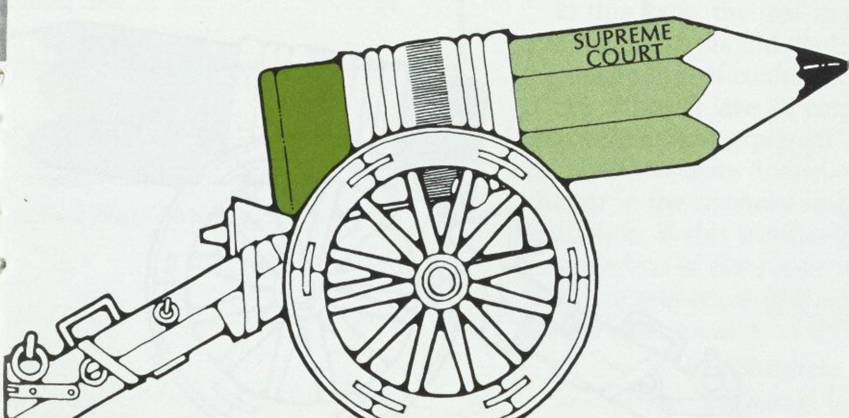
Banking

Economic Review

FEDERAL RESERVE BANK OF ATLANTA APRIL 1982

LINE OF COMMERCE

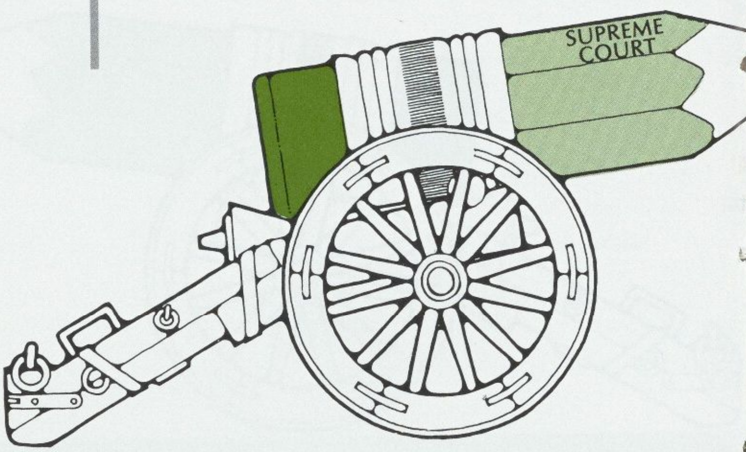


Battle Over Banking

Economic Review

FEDERAL RESERVE BANK OF ATLANTA

The purpose of the **Economic Review** is to inform the public about Federal Reserve policies and the economic environment and, in particular, to narrow the gap between specialists and concerned laymen.



To our readers:

In the last 20 years this nation has seen a dramatic change in the availability of financial services. In 1960, there was one financial service office for every 3,000 people. By 1980, consumers could find financial services not only at the traditional brick and mortar banks, savings and loans and credit union offices, but also at automatic teller machines, securities dealers and life insurance agencies. In the future, interactive cable television networks will carry banking packages into consumers' homes. Bill-by-phone systems are already established throughout the nation and personal computers are beginning to be used for home banking. In the not-too-distant future, perhaps within years, the concept of brick and mortar financial outlets could, in fact, become obsolete.

The "financial supermarket," where a complete menu of financial services may be obtained from a single source, is no longer a theoretical notion but a present day reality. Creative innovation and technological breakthroughs have spurred rapid change in the financial industry, primarily at the expense of regulated depository institutions. The industry which will evolve during the next few decades is in its infancy today. As it matures, competition will clearly increase.

We must recognize these onrushing changes and evaluate the forces shaping the financial industry of the future. To help our readers understand this changing financial environment, we have gathered some of the finest scholars and researchers in the field, including several members of our own research department, who will contribute to a series of special issues of our **Review** charting the industry's future course.

In this issue, the first in the series, we look at whether courts and regulators should continue to treat commercial banking as a separate line of commerce for antitrust purposes. Application of our antitrust laws to commercial banking is largely responsible for our present, fragmented financial industry with its 40,000 separate financial institutions. In a time of rapid change in the financial marketplace and major new financial legislation, is this treatment of commercial banking as a separate line of commerce still relevant? If not, what are the likely consequences of changing our regulatory approach? This special issue focuses on these vital questions.

Sincerely,
Donald L. Koch
Senior Vice President and
Director of Research

INTRODUCTION

In the financial services industry, major changes in legislation usually follow convulsion or revolution from within the industry. The industry's convulsion during the Great Depression of the 1930s brought a wave of federal legislation establishing a set of specialized financial institutions which were segmented by product and by geographic markets. Today this product and market segmentation still exists, but a new revolution within the financial services industry has stimulated the passage of new federal legislation and the introduction of still more legislation with the potential to eliminate the segmented structure of the industry, established five decades ago.

Demanders of financial services are pushing suppliers into expanding the services they provide, and into finding new and innovative means to supply those services. The new services demanded generally cannot be provided by any single supplier under regulations established in the 1930s. As a consequence, financial suppliers are revolting against the product constraints imposed by outdated regulations.

Antitrust laws have allowed the courts to further shape the financial services industry into an industry segmented by types of products. A key to this segmentation was the Supreme Court's 1963 decision establishing commercial banking as an industry offering a unique product, a line of commerce separate and distinct from that produced by any other suppliers of financial services. Commercial banking, in other words, was a separate "line of commerce." Then, through application of the antitrust laws, the courts were able to mandate that there would be a large number of competitors not only within the commercial banking segment, but within each of the other segments as well. Today we find more than 40,000 suppliers of various types of financial services.

Do commercial banks offer a product unique enough to require different treatment from other financial service suppliers for antitrust purposes?

The purpose of this issue of the **Economic Review** is to summarize and evaluate a longstanding controversy—do commercial banks offer a product unique enough to require different treatment from other financial service suppliers for antitrust purposes? Should commercial banks be treated as a separate industry rather than as part of the much larger financial services industry for antitrust purposes? The answers will determine how the financial industry is likely to evolve in this country during the next few decades.

If the courts continue to treat commercial banking as a separate line of commerce, we will see a continuation of our fragmented financial services industry. On the other hand, if the courts decide that commercial banks produce a product which is not unique, but rather is available through many other types of financial firms, the result will be a broadening of the product definition.

Ultimately this would reduce substantially the number of financial institutions, with each of the future institutions potentially offering the same array of services. This development may come either through new legislation or through redefinition of the line of commerce by the courts, or by some combination of the two.

The passage of the Monetary Control Act of 1980 (MCA) is evidence that Congress perceives a need to reevaluate the existing statutory restrictions on financial service suppliers in light of changing market forces. Legislation passed in the next few years will shape the financial services industry, perhaps for decades into the future. The relevance of commercial banking as a separate line of commerce stands at the center of the struggle.

Federal Reserve Bank of Atlanta senior financial economist **David Whitehead** begins with a brief overview of the important forces which have shaped the financial services industry during the past five decades. He also sets the stage for the current controversy by describing the major forces changing the industry today. **George Benston**, economics professor at the University of Rochester and Visiting Scholar at the Atlanta Fed, offers an intriguing alternative to the standard explanation for the wave of financial legislation in the 1930s. This legislation was not so much a result of fears about the financial system's safety, Benston argues, as it was a product of the self-interest of the suppliers of financial services.

> If the courts decide that commercial banks produce a product which is not unique, . . . this would reduce substantially the number of financial institutions.

Section one reviews the legal, legislative, and regulatory history of the line of commerce approach. **Doug Austin**, president of Financialysts, Inc., traces the concept back to 1963, when the Supreme Court surprised the financial world by applying antitrust laws to commercial banking. Since then, the Court has held fast to the idea that the "cluster" of services offered by commercial banks was sufficient to separate commercial banking's product from the products of other financial service suppliers.

Robert Eisenbeis, Wachovia Professor of Banking, University of North Carolina at Chapel Hill, and Visiting Scholar at the Atlanta Fed, outlines the slightly different approaches taken by the various regulatory agencies on the line of commerce question. Despite the recent "revolutionary" changes in the financial marketplace, Eisenbeis concludes that, for commercial customers, commercial banks' cluster of services is as unique today as it has ever been. Thus, as long as the courts continue to direct antitrust action toward the protection of customer classes rather than toward competitors, they are not likely to change their basic opinion on the uniqueness of the commercial banking product.

In section two, we examine the economic rationale for the line of commerce argument. **Ira Horowitz**, Graduate Research Professor of Management at the University of Florida, evaluates the theoretical foundations for defining banking as a separate line of commerce. The courts' definition hinges on the fact that third party transactions accounts are a monopoly product offered in a clustered group of products. Horowitz concludes that the courts were on firm theoretical grounds, if banks in fact tie a group of services together.

B. Frank King, research officer at the Federal Reserve Bank of Atlanta, reviews the economic literature on whether or not these clusters of services actually exist. Although much existing evidence is dated, economists increasingly are recognizing the significance of nonbank alternatives for each kind of financial service offered by commercial banks. Competition between banks and nonbank suppliers has intensified. Evidence on the "clustering" issue, however, is just beginning to come in.

Section three presents three new studies aimed at the crucial "clustering" question. An Atlanta Fed survey of small businesses indicates that small businesses do indeed perceive the commercial bank product as a cluster of services. **Bill Cox**, associate director of research at the Atlanta Fed, approaches the question differently with a survey of price competition between southeastern banks and thrift institutions. His study suggests that banks do not price their NOW accounts, six-month money market certificates, or small savers certificates as if thrift competition matters.

In the third article, **Cynthia Glassman**, economist with the Federal Reserve Board, reports on an interagency survey of lending officers at commercial banks. The survey's findings suggest that nonbank suppliers of financial services are becoming more important and competition is intensifying, but that banks generally do not perceive nonbank sources to be active lenders to small businesses.

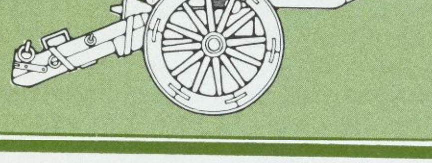
A concluding article presents policy recommendations based on the evidence compiled in this special issue of the **Review**.

The Line of Commerce Issue in Commercial Banking: An Overview

In 1933 and 1935 Congress passed Banking Acts which still influence the structure of the financial services industry. These acts were not contrived in haste but had been debated for years prior to the Great Depression. Partly as a result of the large number of bank failures occurring during the depression, Congress was placed under severe pressure to restructure this country's financial system. As a first priority, Congress was determined to ensure the survival of a large number of independent banks.

The Federal Deposit Insurance Corporation was formed to provide deposit insurance intended to renew public confidence in the banking system, thereby reducing the probability of massive withdrawals by the public which caused many bank failures during the late 1920s and early 1930s. The establishment of the FDIC implicitly assured that almost all banks would come under some type of federal regulation. In addition to insuring deposits, Congress moved to reduce competition among banks by prohibiting the payment of interest on demand deposits. This, in combination with entry regulation by the Federal Deposit Insurance Corporation, assured to an extent the stability of the commercial banking system.

Perhaps more important to the structure of the financial services industry that we see today, Congress during this period strengthened the McFadden Act of 1927 and passed, as part of the Banking Act of 1933, the Glass-Steagall Act. Congress strengthened the McFadden Act by prohibiting interstate banking



"[After the bank failures of the 1930s,] Congress was determined to ensure the survival of a large number of independent banks."

and giving states the discretion to dictate intrastate branching for national banks as well as state chartered banks. This was another way to ensure small bank survival, through reduced competition from large out-of-state banking organizations. The Glass-Steagall Act placed product constraints on banks by separating commercial banking from the securities business, prohibiting commercial banks from dealing in corporate securities. Investment banks also were prohibited from offering deposit services.

Essentially, commercial banks were intended to serve the short-term credit needs of consumers, business, and agriculture. Investment banks served the long-term financing needs of business and government. In addition to this division, financial institutions, such as savings and loan associations, were given separate chartering authorities, regulatory frameworks, and insurance agencies. In effect, the congressional concern for the safety and soundness of the commercial banking system reflected the more basic concern of ensuring the stability of the nation's payment system.

At the time, commercial banks were the only type of financial institution capable of offering third party transaction accounts—demand deposits—to individuals and business. This unique function differentiated commercial banks from all other types of financial service firms. It also provided the rationale through which Congress accorded commercial banking a separate position in the financial services community. To protect the payments system, Congress differentiated the product of commercial banks from that of all other suppliers of financial services.

Congress clearly viewed the various types of financial institutions as serving different sectors of the economy. Commercial banks accepted demand deposits and provided commercial and agricultural loans. Savings and loans associations and mutual savings banks specialized in savings deposits and home mortgages, while investment companies pooled capital and invested in securities.

Even the division of regulatory responsibility among the numerous agencies implied a degree of separability among the financial institutions. To name a few, we have tri-party federal regulation of commercial banks (the Federal Reserve System, the Federal Deposit Insurance Corporation,and the Comptroller of the Currency); the Federal Home Loan

WHY DID CONGRESS PASS NEW FINANCIAL SERVICES LAWS IN THE 1930s? AN ALTERNATIVE OPINION

The rationale for Congress' passage of legislation is very difficult to establish. Nevertheless, it is important that we attempt to understand the circumstances surrounding the passage of the banking and securities legislation of the early 1930s so that we can assess its contemporary relevance. In particular, if the McFadden Act's restrictions on branch banking were enacted to ensure small banks' survival, would the repeal of the act mean that the financial system would be dominated by nation wide giant banks? If investment banking was separated from commercial banking by the Glass-Steagall Act because the combination of services resulted in fraudulently and unsafely run banks, might not this situation occur again were the statute changed?

Was the fact that the Banking Act of 1933 and the subsequently enacted legislation and regulations establishing and reinforcing a specialized financial services system a reaction by Congress to the failure of many banks and thrift associations in the early 1930s? If it was, should we be concerned that the repeal of the legislation and the removal of restrictions on the services that chartered financial institutions can provide might not result in a future wave of failures?

These questions can be answered from two perspectives. One is careful study of the causes of bank failures and frauds. Some research on this question has been done. Little, if any, identifies branch banking, the combination of commercial and investment banking, or the offering by thrifts of traditional commercial banking services as causes of failures*. Indeed, the evidence points to limitations on branching as a major cause of bank failures, since very few branch banks (particularly large

*See George J. Benston, **Bank Examination, The Bulletin**, 1975.

"[Since Congress obviously intended to segment the financial industry,] perhaps it should have come as no surprise when the Supreme Court declared in 1963 that commercial banking was in fact a separate 'line of commerce'."

Bank System; the Securities and Exchange Commission; and the National Credit Union Administration.

Each agency has responsibility for groups of institutions that provide various types of services. But the point is there is not just one agency that oversees the entire financial services industry. There are many with divided lines of responsibility. The legislative segmentation of the financial services industry encouraged Congress to fragment regulation of the industry.

The legislative intent was obviously to segment the financial services industry.Therefore, perhaps it should have come as no surprise when the Supreme Court declared in 1963 that commercial banking was in fact a separate "line of commerce." This decision set a precedent that is still used today by defining the product of commercial banks as a special cluster of services. This cluster of services was unique to commercial banks because, by legislation, they were the only financial institutions that could offer demand deposits to individuals and businesses and make commercial loans. Therefore, the Supreme Court defined the product of commercial banks to be very narrow—the cluster of services only commercial banks could offer.

Either of two events could possibly cause the courts to change their view of the product offered by commercial banks. First would be solid evidence that the array of financial services provided by commercial banks is not provided as a bundle or that at

banks) failed.

Unfortunately, the effect on bank safety of commercial banks offering investment banking services was not similarly studied. But there is good reason to doubt a causal relationship because very few large money market banks, the banks that tended to offer investment banking services, failed. Since thrifts only recently could offer commercial banking services (and still cannot serve most business customers), we cannot look to the past for guidance. But we can acknowledge that commercial banks that offered mortgages and savings deposits were not more prone to failure for that reason.

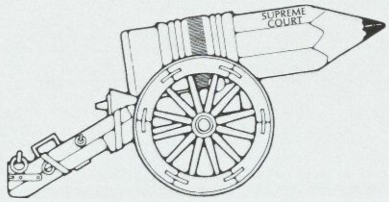
The other perspective from which the possible effects of repeal of the Great Depression legislation can be assessed is an analysis of the reasons for these laws having been passed. As an alternative to the bank safety, small-bank-survival hypothesis explaining congressional intent put forth above, I would like to propose a producer self-interest, horse-trading explanation. If this latter hypothesis were correct, repeal of the legislation is unlikely to result in failures, since it essentially was not passed to prevent failures.

Furthermore, since the legislation no longer benefits the institutions, they and the public would be better served by a repeal of legislation that keeps them from changing to meet present demands. And, if concern for the safety of the banking system were not an important reason for the congressional action of the 1930s, there is less reason to fear a repetition of that unhappy time should the laws be repealed.

The 1930s was a time of great financial distress. Over a third (9,096) of the commercial banks failed between 1930 and 1933. Most of these were small, unit banks. The survivors quite reasonably feared that the people would shift their funds to the larger branch banks, since few of these failed. Hence, the small banks wanted federal deposit insurance. The least consumers of these services view each service as a separable product. If this could be shown—and if it could be shown that there were significant alternative suppliers of each service other than commercial banks—then the courts possibly would broaden the narrow product definition to include other types of financial institutions.

Yet, convincing empirical evidence has not been forthcoming that banks do not package their services as a bundle or that customers in fact view these services as independent and available through significant alternative sources. And, as long as commercial banks were protected by legislation from competition from alternative suppliers and were allowed the unique offering of demand deposits, it was very unlikely that sufficient evidence could be found to reverse the court's bundle of services definition.

The second event which has the potential for at least forcing the courts to reexamine their stand on this question is new financial legislation which expands the array of services potentially provided by alternative suppliers. This latter event may have occurred in 1980 with the passage of the Monetary Control Act (MCA). The emphasis is on the "may" because only in part did this act wipe out the unique position accorded commercial banks within the financial services industry.



Prior to the MCA, commercial banks were virtually the only financial institutions that could offer third party transactions accounts to consumer or business firms and that could offer commercial loans. This unique ability to offer demand deposits and make commercial loans in large measure was the basis for the court's separate treatment of commercial banks. Since the passage of the MCA, the only unique service allowed to commercial banks is the offering of third party transaction accounts to commercial customers. Thrift institutions may offer third party transaction accounts, NOW accounts and share drafts to noncorporate customers. These institutions within rather narrow limits are also able to offer commercial loans and other services.[1]

In effect, thrift institutions may now offer the same range of consumer services as commercial banks, and, on the asset side of

large banks, particularly those in the money centers, didn't need deposit insurance. But they did want to outlaw the payment of interest on demand deposits. The New York banks in particular had tried, at least since 1905, to establish cartel agreements that restricted payments on deposits, particularly those of country banks. But these agreements didn't stick, as some bank or other broke ranks to attract deposits from its competitors.

At the same time, investment bankers were suffering from competition from banks that were offering investment services. The more prestigious brokerage houses also suffered from competition from other, lower quality brokers, most of whom didn't follow the older houses' standards for prospectuses. Add to this the public's apparent (and mistaken) beliefs that the stock market crash of 1929 and shady dealings of the brokers and bankers had caused the depression, and we have the makings of a big horse trade.

The small unit banks (which, being numerous, carried political clout) won strengthened McFadden Act prohibitions against branching. More importantly, they got the FDIC, which was paid for principally by the large banks. (The FDIC insured deposits up to $5,000 per account but assessed premiums on all deposits.) The large banks got a prohibition against interest payments on demand deposits. The brokers got the commercial banks out of the investment business. They also didn't fight passage of the Securities Act of 1933, which imposed prospectus requirements on all but small issuers of securities (but which exempted banks). And the Roosevelt administration received the credit for taking aggressive legislative action that presumably corrected the alleged abuses of the financial system while preserving capitalism.

The savings and loans are another story. The administration wanted to channel funds into the housing industry. But 526 savings and loan associa-

> "[Beyond the MCA,] the financial services market place has seen an explosion of new services . . . [that] provide . . . an attractive alternative to commercial banks."

the balance sheet, thrifts may offer an array of commercial services. It appears to be only on the liability side, providing third party transactions accounts to commercial customers, that thrifts may be different from commercial banks.

The MCA did blur the distinction among classes of financial institutions, making these institutions more homogeneous in their ability to provide financial services. It is now appropriate, therefore, to restudy the significance of viewing commercial banks as unique providers of a specified cluster of consumer and corporate financial services.

Added to the legislative changes we have just mentioned, the financial services market place has seen an explosion of new financial services and instruments offered by both financial and nonfinancial concerns. In large part, these services provide customers with an attractive alternative to commercial banks. For corporate customers, the growth in the number of alternatives has not been so great. Still, commercial finance companies, captive finance companies, leasing companies and inventory financing by suppliers all provide alternatives to commercial banks as a source of funds.

These burgeoning alternatives call for a new look at whether or not commercial banking may realistically be viewed as a separate line of commerce.

—David D. Whitehead

tions had failed. First the administration tried to get the mutual savings banks to expand out of the Northeast. But the savings banks refused; they had survived the depression with hardly a failure (only 10 went under) and were not disposed to taking on new responsibilities. Nor were many commercial banks in a position to expand.

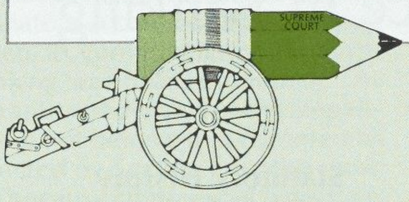
Agents of the newly established Federal Home Loan Bank Board then went to communities and offered savings and loan charters to home builders, lumberyard dealers, real estate lawyers, and others who might benefit from starting an association that would channel funds into their businesses. Bankers couldn't benefit from this coincidence of interest since such related dealings were not considered to be consistent with sound banking practices. Thus many specialized thrift associations were established and, having been given subsidies by way of tax exemptions and having been well-positioned to take advantage of savings during World War II and of the post-war housing boom, they prospered.

But today changes in consumer demands, unexpectedly high interest rates, and improved technology have served to make the 1930s laws punitive. The acts and regulations have prevented or restrained financial chartered institutions from changing effectively. Consequently, other suppliers of financial services have been organized to meet consumer demands and to take advantage of the technology. Whether or not a repeal of the 1930s laws and changes in the regulatory structure are desirable pose important questions that have been much debated. In any event, if this explanation for the 1930s legislation is correct, there seems little reason to fear that changes would result in an unsafe financial system.

George J. Benston

Section I

LEGAL AND LEGISLATIVE HISTORY



As we have seen, Congress, reacting to the financial upheavals of the Depression, segmented the financial services industry in the 1930s. In this section, Doug Austin focuses on the specific legislative and legal developments leading to the separate treatment of commercial banks by regulators for antitrust purposes.

When the Supreme Court in 1963 applied antitrust laws to banking, it ensured the continuation of a fragmented financial industry. Why did the Court rule that commercial banking was a separate line of commerce? And why, despite increasing pressures from regulatory agencies, lower courts, banks, and academics, has the Court held fast to that ruling ever since 1963?

The interpretation is still under attack in the courts, but no cases are now pending at the Supreme Court level which are expected to change this definition.

Also in this section, Robert Eisenbeis examines how the regulatory agencies have approached the line of commerce question. Regulators, which must decide whether to allow mergers and acquisitions of financial institutions, generally have applied the concept of banking as a separate line of commerce. Regulatory treatment has varied, however, from case to case and from agency to agency.

Do the regulatory agencies still believe that the cluster of services offered by commercial banks is unique and that banks therefore should be treated separately? Eisenbeis surveys the agencies' dilemma.

The Legal and Legislative History of the Line of Commerce in Banking

Two decades ago the Department of Justice shocked the commercial banking industry by filing a civil antitrust action against the approved merger of the Philadelphia National Bank and the Girard Corn Exchange Bank, both of Philadelphia. Up until the filing of this suit in 1961, the bankers had felt they were immune from antitrust law, their confidence stemming from the language of the antitrust statutes and other statutes as well.

The **Philadelphia** case proved not to be an aberration, however, as the Justice Department has filed over 60 suits since then attacking various bank mergers. The possibility that bank mergers or acquisitions may result in antitrust violations has become very real, and as such the standards laid down by the Supreme Court and lesser courts need to be examined closely by merger applicants prior to entering into a merger.

The purpose of this analysis is to focus upon the concept of the relevant "line of commerce" as related to commercial banking, which is important for reasons of determining the effect the pending merger will have on competition in the particular geographical area. As will be seen, the original Supreme Court definition of the line of commerce as decided in the **Philadelphia** case has "weathered the storm" for the 20 years that have passed since. Due to some recent statutory developments and some recent District Court opinions, though, a change may be on the horizon.

Statutory History of Bank Antitrust Law

The line of commerce as related to commercial banking stems from Sections 1 and 2 of the Sherman Act of July 2, 1890. As stated in the Sherman Act:

> . . . Every contract, combination in the form of trust or otherwise, or conspiracy, in restraint of trade, or commerce, among the several states or foreign nations, is declared to be illegal. Every person who shall make any such contract or engage in any such combination or conspiracy shall be deemed guilty of a misdemeanor and, upon conviction thereof, shall be punished by a fine not exceeding $50,000 or by imprisonment not exceeding one year.[2]

Note that there is no analysis here of the line of commerce. Section 2 reads:

> . . . Any person who shall monopolize, or attempt to monopolize, or combine or conspire with any other person or persons to monopolize, any part of the trade or commerce among the several states or with foreign nations, shall be deemed guilty of a misdemeanor and, on conviction thereof, shall be punished by a fine not exceeding $30,000 or by imprisonment not exceeding one year, or by both said punishments, in the discretion of the court.[3]

Section 2 does not describe the definition of commerce, nor does it delineate what the relevant product line would be for any possible violation. It was not specific as to whether there could be a multi-product or single product line of commerce. The 1950 amendments to Section 7 of the Clayton Act were far more specific. Clauses 1 and 2 of Section 7 stated:

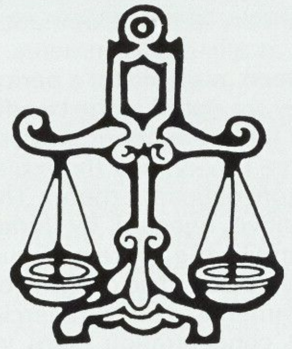
> . . . No corporation engaged in commerce shall acquire, directly or indirectly, the whole or any part of the stock or other share capital, and no corporation subject to the jurisdiction of the FTC shall acquire the whole or any part of the assets of another corporation engaged also in commerce where *in any line of commerce in any section of the country* the effect of such acquisition may be substantially to lessen competition.[4]

When the Cellar-Kefauver Amendment to Section 7 of the Clayton Act passed, neither commercial bankers nor regulatory authorities believed that Section 7 applied to commercial banks since commercial banking was not "commerce." As late as 1955, the antitrust division of the Department of Justice did not believe that commercial banking was affected by Section 7 for the same reason, and also because commercial bank mergers or consolidations were neither an asset acquisition nor a stock acquisition, but were in reality a hybrid.

The Bank Merger Act of 1960, which preceded commercial bank merger litigation, did not incorporate any of the more pervasive language of the amended Section 7 of the Clayton Act. The Bank Merger Act, which amended Section 18 of the Federal Deposit Insurance Act, reads, in relevant part, as follows:

> . . . In the case of a merger, consolidation, acquisition of assets, or assumption of liabilities, the appropriate agency shall also take into consideration the effect of the transaction on competition (including any tendency toward monopoly), and shall not approve the transaction unless after considering all such factors, it finds the transaction to be in the public interest.[5]

Commercial bankers and their trade associations felt that the omission of the relevant line of commerce clause from the Bank Merger Act of 1960 further insulated the banks from any Sherman or Clayton Act antitrust adjudication. Commercial bankers were shocked when less than 1½ years later the antitrust division of the Department of Justice filed a Clayton Section 7 (and Sherman Sections 1 and 2) action against the **Philadelphia National Bank-Girard Trust Corn Exchange Bank** merger.



Case History of Bank Antitrust Law

A. Philadelphia National Bank— The Single Product Doctrine

Judge Clary, speaking on behalf of the District Court for the Eastern District of Pennsylvania, dismissed the Department of Justice's antitrust suit against the **Philadelphia National Bank-Girard Trust Corn Exchange Bank** merger. He felt that Section 7, as amended, did not apply to commercial banking because the commercial banks were not under the FTC jurisdiction and because it was neither a pure stock nor pure asset acquisition.

The Supreme Court, on June 17, 1963, reversed Judge Clary and remanded the case back to the District Court for redetermination of its potentially anti-competitive effects upon applicability of Section 7. The Supreme Court did agree with Judge Clary's determination that the relevant product line was commercial banking; the bundle of services or mutually interdependent services offered by commercial banking made commercial banking itself a unique line of commerce. As stated by the Supreme Court:

> . . . We have no difficulty in determining the 'line of commerce.' . . . We agree with the District court that the cluster of products (various kinds of credit) and services (such as checking accounts and trust administration) denoted by the term 'commercial banking,' composes a distinct line of

commerce. Some commercial banking products or services are so distinctive that they are entirely free of effective competition from products or services of other financial institutions; the checking account is in this category. Others enjoy such cost advantages as to be insulated within a broad range from substitutes furnished by other institutions.[6]

Thus, the Supreme Court in its initial test accepted one major economic theory as to the operation of a commercial bank as a line of commerce.

Two theories have been available for a period of time; summarily they are stated as the bundle of goods, or mutually interdependent services single line of commerce theory, and the multi-product department store of finance theory. The latter was the alternative rejected by Judge Clary's District Court and by the Supreme Court in 1963. Once the Supreme Court had determined the relevant line of commerce to be commercial banking, the resultant concentration ratios included commercial bank competition only, and other non-bank financial institutions were excluded from consideration.

B. Lexington, Continental, and Manufacturers-Hanover

On April 6, 1964, the Supreme Court ruled against a consummated merger of the **First National Bank & Trust Company** and the **Security Trust Co.**, both of Lexington, Kentucky. The merger, approved by the Comptroller of the Currency, had been attacked in 1961 by the Justice Department. After consummation by the parties, the Justice Department sued for divestiture under Section 1 of the Sherman Act.

This case is the only instance in which the Department of Justice sued and won under Section 1 of the Sherman Act, alleging restraint of trade in commercial banking and trust business. The Justice Department won both at the District Court and the Supreme Court levels against the banks. The line of commerce was in this particular case being stipulated as commercial banking for both Section 7 of the Clayton Act and Section 1 of the Sherman Act.

"By 1966, the Justice Department had won five suits either in the courts or by the abandonment of the merger."

Two other major antitrust cases were filed in 1961, against the **Continental Illinois National Bank & Trust-City National Bank & Trust** merger in Chicago and the **Manufacturers Trust-Hanover Bank** litigation in New York. Continental Illinois National Bank and City National Bank & Trust of Chicago had received approval to merge in July 1961, but the Justice Department filed suit the following month against said merger on grounds of both Section 7 and Section 1. Again, commercial banking was defined as the single line of commerce, with emphasis being on demand deposits and business loans.

Almost simultaneously, the Justice Department moved against the combination of **Manufacturers Trust Company** and the **Hanover Bank** in New York City. This merger had been consummated, and, as in **Lexington**, the Justice Department demanded divestiture as the remedy for the anticompetitive combination. In that case, for the first time, the relevant line of commerce was altered. The Justice Department alleged, and the District Court agreed, that the relevant line of commerce was commercial banking, but that commercial banking was segregated into both wholesale and retail. This was important primarily for the relevant geographic market, to be discussed later. But it also revealed that there were at least different product lines within the unique single line of commerce.

In review, the first four cases filed were all won by the Justice Department. One other case not discussed above, the proposed merger of the **Calumet National Bank of Hammond** and **Mercantile National Bank of Hammond**, was abandoned after suit by the Justice Department. Thus, by 1966, the Justice Department had won five suits either in the courts or by the abandonment of the merger. Notice that all were horizontal market combinations, and the line of commerce was specifically tied to such combinations.

C. Crocker-Anglo— The First Potential Competition Case

On October 8, 1963, the Department of Justice filed a suit against the combination of the **Crocker-Anglo National Bank** (San Francisco) and the **Citizens National Bank** (Los Angeles)[7] on Section 7 grounds, alleging the proposed combination would violate antitrust laws. The suit alleged that the proposed merger would be potentially anticompetitive. At the time of the proposed merger, the two banks did little business in each other's service areas and had no branches located within each other's home office counties. In fact, Citizens National Bank had no offices in northern California, whereas Crocker-Anglo had branches only in the suburban counties surrounding Los Angeles.

The most relevant aspect of the **Crocker-Anglo National Bank** case was that the District Court found that the line of commerce was not only commercial banking but other types of financial institutions as well. The District Court enlarged the relevant product line to include savings and loan associations, commercial finance companies, Morris Plan banks, and insurance companies within the state of California. This permitted a decrease in the amount of concentration, and thus had some impact upon the competitive aspects of the case.

The decision in the **Crocker-Anglo** case was rendered in 1967, after passage of the Bank Merger Act of 1966. Thus, by the time the 1966 act was considered, all five cases reaching adjudication had utilized "commercial banking" as the definition of the line of commerce.

The Bank Merger Act of 1966

By 1966, the commercial banking industry had regrouped its forces and legislation passed through Congress amending the Bank Merger Act of 1960. The major import of the Bank Merger Act of 1966 was to strengthen "the competitive aspects" language of the 1960 act. Specifically, Section C(5) of Section 18 of the FDI Act was amended to read as follows:

> (A) any proposed merger transaction which would result in a monopoly, or which would be in furtherance of any combination or conspiracy to monopolize or to attempt to monopolize the business of banking in any part of the United States, or
>
> (B) any other proposed merger transaction whose effect in any section of the country may be substantially to lessen competition, or to tend to create a monopoly, or which in any other manner would be in restraint of trade, unless it finds that the anticompetitive effects of the proposed transaction are clearly outweighed in the public interest by the probable effect of the transaction in meeting the convenience and needs of the community to be served.[8]

> "In 1966, the commercial banking industry regrouped its forces . . ."

Careful reading of the revised Bank Merger Act of 1966, Section C(5), shows that there is no mention of any relevant line of commerce, whether phrased in the terminologies of Sections 1 and 2 of the Sherman Act or the stronger interpretation of the amended Section 7 of the Clayton Act. It is to be assumed that this was deliberate, not accidental, and was intended to alleviate the problem of the line of commerce being strictly interpreted to be commercial banking only.

Furthermore, the intent of the entire act was to bring the commercial banking industry out from underneath Sections 1 and 2 of the Sherman Act and Section 7 of the Clayton Act. The purpose was to replace them with primary jurisdiction by the regulatory authorities following the concepts and disciplines of the antitrust laws in general.

From the standpoint of the relevant line of commerce, however, it is important that the singular lack of attention to this particular ingredient has to be interpreted as being deliberate rather than a legislative oversight. That's especially important since the single product unique line of commerce doctrine had been firmly established by the previous litigation from 1961 to 1966.

Post-Bank Merger Act of 1966 Litigation

The major feature of the antitrust litigation from 1966 to 1970 was the number of banks that withdrew from previously approved mergers when sued by the Department of Justice. From 1966 to 1970, eight of the nine cases filed by the Department of Justice precipitated almost immediate withdrawals by the banks involved, although some preliminary litigation was carried on prior to abandonment by several of the litigants. For example, major cases in Houston, St. Louis, and Pennsylvania were abandoned after litigation was instituted by the Department of Justice.

The most interesting case during this period was the **Provident National Bank-Central Penn National Bank** merger. The Justice Department's original suit was dismissed by the District Court without trial. The Supreme Court, though, reversed the decision and remanded it back to the District Court in 1967. In 1968, the District Court found the merger unlawful and the banks did not appeal. In its ruling, the District Court extended the line of commerce to include not only commercial banking but also mutual savings banks within the Philadelphia area. This case, known familiarly as Philadelphia II, extended the commercial banking line of commerce in the same community where the original line of commerce was drawn.

Thus, by 1970, two lower court cases, in **Crocker-Anglo** and in **Provident**, had extended the line of commerce to be more than simply commercial banking. Furthermore, the regulatory authorities and bank applicants were utilizing lines of commerce beyond those of commercial banking in determining the competitive aspects of proposed mergers during the same period. The honeymoon, however, was short; the **Phillipsburg** case brought the commercial banking line of commerce back to a more strict standard.

A. Phillipsburg—Back to the Single Line of Commerce Test

On June 27, 1970, the Supreme Court reversed a District Court determination that the proposed merger between the **Phillipsburg National Bank and Trust Company** and the **Second National Bank of Phillipsburg** was not violative of the antitrust laws. The District Court, had dismissed the Justice Department's complaint, finding no violation of Section 7. The Supreme Court reversed the District Court on both the relevant line of commerce and relevant geographic market tests, thus remanding the case back for retrial on the needs and convenience issue. The Supreme Court stated that the District Court had erred in finding no violation of the antitrust clause because of erroneous use of their relevant line of commerce and relevant market area tests. The Supreme Court stated firmly and simply that the relevant product line for commercial banking was commercial banking. As the Court stated:

> . . . Indeed, competitive commercial banks, with their cluster of products and services, play a significant role in a small community unable to support a large variety of alternative financial institutions. If anything, it is even more true in the small towns.[9]

The District Court had relied upon the relevant product market being divided into sub-product markets due to the competition between the commercial banks and non-bank financial intermediaries. Furthermore, the District Court felt that the commercial banks operated more like savings institutions than like big city commercial banks. The Supreme Court rejected the contention stating:

> . . . The District Court erred. It is true, of course, that the relevant product market is determined by the nature of the commercial entities involved and by the nature of the competition that they face. . . . But sub-markets are not a basis for the disregard of a broader line of commerce that has economic significance.[10]

The Supreme Court again reiterated the **Philadelphia** standard that a clustering of services delimits commercial banking:

> The clustering of financial products and services in banks facilitates convenient access to them for all banking customers. . . . Moreover, if commercial banking were rejected as the line of commerce for banks with the same or similar ratios of business as those of the appellee banks, the effect would likely be to deny customers of small banks—and thus residents of many small towns—the antitrust protection to which they are no less entitled than customers of large city banks.[11]

Thus, after seven years of litigation, the lower court's attempts to expand the relevant line of commerce to include more than commercial

"The honeymoon, however, was short; the Phillipsburg case brought the commercial banking line of commerce back to a more strict standard."

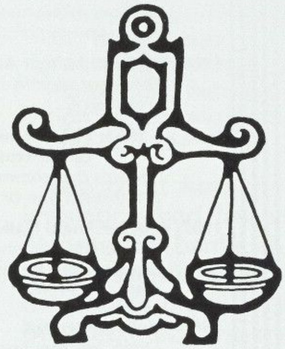
banking were foiled. The Supreme Court returned to its **Philadelphia National Bank** test of a single product cluster of services approach.

B. The Relevant Line of Commerce—The Potential Competition Cases, 1970-1976

Following **Phillipsburg**, two aspects of the relevant line of commerce doctrine are in evidence. The District Courts have continued to expand the relevant line of commerce to include non-bank financial institutions. For example, in the **First National Bank of Jackson-Bank of Greenwood**, Mississippi case, the relevant line of commerce was determined to be financial institutions, including commercial banks, cotton exchanges, and savings and loan associations.[12] Furthermore, in the **Idaho First National Bank of Boise-Fidelity National Bank, Twin Falls** case, Judge Bouldt also included as competitive financial institutions savings and loan associations, trust and savings banks, credit unions, the Production Credit Association, the Federal Land Bank, life insurance companies, and mortgage companies.[13]

Thus, in both the **Jackson** and **Idaho** cases, the District Court enlarged the relevant line of commerce to include other deposit and non-deposit financial intermediaries in addition to commercial banks. Potential competition cases have been characterized as market extension or product extension combinations rather than horizontal market combinations, as in the earlier actual competition cases. Both in the **Jackson** and **Idaho** cases, potential competition was alleged to be a market extension merger (acquisition), thus possibly (or probably) resulting in a violation of Section 7 of the Clayton Act.

Thus, not being a product extension merger, expansion of the relevant line of commerce by District Courts to include more than commercial banking was a significant change. In all fairness, though, it should be noted that the District Courts' actions preceded the **Phillipsburg** decision. Following the **Phillipsburg** case, the commercial banking line was restored in some lower court district cases. The prevalent behavioral pattern during 1970-1976 was abandonment of proposed mergers and acquisitions by either banks or holding companies.



C. The Two Supreme Court Cases—Marine Bancorporation and Connecticut

The first case to go to the Supreme Court under the potential competition theory was the **Greely** case; the *per curiam* opinion of the Supreme Court affirmed on a four-to-four vote the District Court's opinion that the proposed acquisition by a registered bank holding company was not a violation of Section 7 on potential competition grounds. By the time the Supreme Court heard the **Marine Bancorporation** and **Connecticut** cases in 1974, the Justice Department had lost all of its seven potential competition cases brought before the federal courts.

On June 17, 1974, the Supreme Court remanded the **Marine Bancorporation** and **Connecticut** cases back to the District Court for further adjudication, especially disintegrating the attempts by the Justice Department to utilize potential competition as a means of thwarting commercial bank acquisitions and/or mergers. Once again, the Court gave the green light to the single product line of commerce argument of the **Philadelphia National Bank** case 11 years previous.

In both the **Marine Bancorporation** and **Connecticut** cases, District Courts had expanded the line of commerce beyond commercial banking. In **Marine Bancorporation**, the line of commerce was increased to include savings and loan associations and mutual savings banks, and in the **Connecticut** case, mutual savings banks were

TRACING THE LINE OF COMMERCE

July 2, 1890: Sherman Act
Prohibits any trust or contract restraining trade.

1950: Clayton Act
Prohibits acquisition which would lessen competition in any line of commerce.

1960: The Bank Merger Act
Does not identify banking as a separate line of commerce.

June 17, 1963: Philadelphia National Bank — Girard Trust Corn Exchange Bank
Declares that commercial banking's cluster of products is a distinct line of commerce.

1967: Crocker-Anglo National Bank
Justice Department filed suit on grounds that a proposed merger would be potentially anti-competitive.

1966: Bank Merger Act
Omits any mention of banking as a separate line of commerce.

1970: Phillipsburg National Bank
Supreme Court reverses District Court and reaffirms banking as a separate line of commerce.

1974: Marine Bancorporation and Connecticut
Court rejects potential competition as a basis for blocking mergers and reaffirms single line of commerce rule.

1980: New Jersey and Utah
District Courts consider thrifts in bank merger cases.

considered as competitive substitutes and alternatives to commercial banks. In the **Connecticut** case, one reason for reversal by the Supreme Court was the District Court's erroneous drawing of the relevant line of commerce.[14]

Thus, after 18 years of litigation, the Supreme Court has held fast to the relevant line of commerce being that of commercial banking. It has resisted pressures placed upon it by the regulatory agencies, the lower courts, merger applicants, and academia in general. All have pushed for expanding the relevant line of commerce from a single product unique line of clusters of services to a multi-product mutually independent bundle of services.

However, since there has been no litigation in this area at the Supreme Court level for a number of years, and there have been some relatively recent case law and statutory developments in the banking industry, we may see some changes in the standard.

Recent Legal and Legislative Developments

Certain developments that have taken place on both the legal and legislative fronts may signal that a change is forthcoming in the definition of the relevant line of commerce. It is becoming increasingly apparent that the legal distinctions that existed among the various financial institutions at the time of the **Philadelphia** decision no longer conform to reality. This has been a result of both a conscious effort on the part of the federal government, and of private competitive forces.

The most important statutory development has been the passage of the Depository Institutions Deregulation and Monetary Control Act of 1980. That act greatly increased the powers of federally chartered thrifts, and at the same time narrowed the distinctions between the thrifts and the commercial banks. One major provision calls for the phase-out and elimination of the limitations on deposit interest rates eliminating the existing differentials that thrifts may pay over the commercial bank rate. The act also permits all depository institutions to offer NOW accounts to individuals, which will accelerate the trend of depository institution de-specialization.

Further, the "cluster of services" that the **Philadelphia** court attributed to commercial banking is becoming increasingly permissible for thrifts. Federally chartered thrifts may exercise trust and fiduciary services, issue stock, and offer credit card services. All thrifts may employ remote service units similar to those utilized by commercial banks. Further, federally chartered mutual savings banks may now hold up to 5 percent of their assets in commercial, corporate or business loans - a lending power previously denied them. Finally, the uniform reserve requirements imposed on all depository institutions by the 1980 act will also reduce distinctions among them.

Federal courts have begun to take note of the changes in the depository institution industry. In some districts at least, the courts are starting to reassess the **Philadelphia** standard as it applies to new economic realities. In two major instances recently, District Courts considered the impact of the thrifts in cases involving commercial bank mergers.

In the first case, decided in 1980, the Justice Department brought suit to enjoin the proposed merger of two of New Jersey banks. First National State Bank of Central Jersey and the First National Bank of South Jersey. Violation of the Clayton Act was charged, and the Justice Department's basis was that the merger would substantially lessen both actual and potential competition. The District Court of New Jersey affirmed the Comptroller's approval of the merger, however. Although the court did in the end utilize commercial banking as the relevant line of commerce, its decision apparently was influenced by the presence of thrifts in the area. The defendants had introduced substantial evidence showing the scope and impact of all banking alternatives in the area to prove that competition would not be affected, and the court remarked in agreement:

> The overwhelming weight of the evidence establishes that each of the markets is competitive. This ultimate finding stems from numerous subsidiary findings regarding the reliability of concentration ratios as evidence of the competitiveness of markets, the historical trend toward deconcentration in the relevant geographic markets, competition from the thrifts, . . .(etc.)[15]

The court further recognized that the 1980 legislation had lessened distinctions between commercial banks and thrifts. The presence of these essentially similar institutions resulted in the court's finding that competition would not be affected by the merger.

The second instance involved the 1980 merger of Zions First National Bank and the First National Bank of Logan, both of Utah. There the Justice Department claimed that the merger would lessen potential competition. As in the **New Jersey** case, the defendants presented evidence of non-bank alternatives that would absorb any possible anti-competitive effect that the merger could create. And as its **New Jersey** counterpart had done, the District Court of Utah considered the thrifts in its ruling:

> All of these enterprises have an offer of some kind that affects this commercial banking market. And that is just as much a part of the factual backdrop in which these commercial banks compete as is the population or the number of commercial banks.[16]

The court proceeded to approve the merger, thus keeping intact the Justice Department's string of defeats in the area of potential competition.

Although both the **New Jersey** and the **Utah** courts have specifically retained the **Philadelphia** definition of the relevant line of commerce, there is no denying that the standard is again under attack. The potential success of this trend is enhanced by the legislative and private market developments of late. At present, no cases are pending at the Supreme Court level, however, so it will be some time before the issue is resolved.

—Douglas V. Austin

Regulatory Agencies' Approaches to the "Line of Commerce"

The Supreme Court defines commercial banking as the relevant "line of commerce" for evaluating the competitive effects of proposed bank mergers and bank acquisitions by bank holding companies.[17] That definition has remained virtually unchanged since it was first articulated in the 1963 Philadelphia National Bank (PNB) decision.[18] Subsequently, the banking agencies have generally adhered to the Court's cluster of products and services definition of commercial banking as the line of commerce.

However, recent legislative and competitive changes are radically altering traditional financial arrangements and the ways services are being provided. As more depository and nondepository financial institutions have begun to offer closer substitutes for bank services, applicants increasingly have argued that the traditional definition of commercial banking as the relevant line of commerce fails adequately to capture market realities. As a result of these changes, their arguments are generally falling on sympathetic ears; the agencies seem willing to move in the direction of modifying their method of analysis and/or the line of commerce definition. Certainly, there is now ample evidence that the agencies are giving more and more weight to competition provided by thrifts and to other market developments in certain types of cases.

This article reviews the product line concepts applied by the banking agencies in their case analysis and briefly discusses some policy issues the agencies face in significantly broadening the traditional definition. Interestingly, as the next section shows, the concept of commercial banking as a line of commerce did not originate in the PNB case. Moreover, the problem of the appropriate way to consider competition by nonbanks is not a new issue, and the willingness of the agencies to address this issue on a case by case basis is not a recent development.

Agency Actions Prior to the PNB Case

As Shay and Yingling (1981) indicate in their survey article, use of commercial banking as the line of commerce in bank acquisition cases was not originated by the Supreme Court in the 1963 PNB case. Rather, the concept can be traced to previous agency actions dating back as early as the 1952 divestiture decision by the Federal Reserve Board in the Transamerica Corporation case.[19] In that case, the Board reviewed the consequences of Transamerica's bank stock acquisitions on structure and competition in commercial banking. Three reasons were cited for focusing on only commercial banks, reasons similar to the Supreme Court's findings in PNB. The Board noted that commercial banks were unique suppliers of money-payment and money-creation services and, in addition, were the dominant suppliers of short-term business credit.

The Board recognized, but explicitly rejected, the need to consider competition provided by other depository and nondepository financial institutions in certain other service lines. Two reasons were cited. First, these other institutions—such as life insurance companies, S&Ls, production credit associations, finance companies and personal loan companies—all depended upon commercial banks both for short term credit and to carry out their business. Second, none offered services that were effective substitutes for the three major bank functions of money creation, payments services, and business credit.

Despite the analysis in the Transamerica case, the Board did not take a static approach to the line of commerce issue. In a series of at least five subsequent decisions—all involving acquisitions in New York or New England--increasing consideration was given to competition provided by mutual savings banks.

In the 1958 Baystate-Springfield case and in two New Hampshire cases explicit mention was made of the fact that mutual savings banks competed for some, but not all banking services; however, in the 1960 Marine Midland and Baystate cases, deposit shares were cited, first for commercial banks only and then for mutual savings banks and commercial banks combined. Reading between the lines in these latter two cases, we could interpret that the Board gave equal weight to competition provided by mutual savings and commercial banks. But in truth it is difficult to determine from either of these cases, or the previously cited cases, exactly how thrift competition was considered or how the relevant line of commerce was defined.[20]

The inclination on the part of the Board to consider mutual savings bank competition in cases in the Northeast did not carry over to the evaluation of competition provided by savings and loan associations. In 1960 and again in 1961 the Board denied acquisitions by two Minnesota bank holding companies.[21] Citing legislative history and congressional intent as to the definition of banking activities in the Bank Holding Company Act of 1956, the Board rejected applicant's contentions that S&L competition should be considered in evaluating the competitive effects of the applications.

> "[Even before the 1963 PNB case, the Federal Reserve Board gave] increasing consideration . . . to competition provided by mutual savings banks."

Like the Federal Reserve Board, the Comptroller of the Currency gave weight to thrifts and other competitors on a case by case basis in acting on proposed national bank mergers. Yingling and Shay (1981) indicate a number of decisions in which competition from an array of both depository and non-depository institutions was considered.[22]

Decisions Subsequent to PNB

The problem of how much weight to afford thrifts and other institutions in evaluating the effects of bank acquisitions apparently was resolved in the PNB case, when the Supreme Court held that the cluster of products and services known as commercial banking constituted banks' relevant line of commerce.[23] This definition was reaffirmed in several cases,[24] including the Phillipsburg National Case, and was refined in the more recent Connecticut National Bank case.[25]

The Court recognized in the Connecticut case that thrifts were fierce competitors with commercial banks for many services. Yet it found that commercial banks were still sufficiently unique suppliers of services to commercial enterprises to continue to constitute a separate line of commerce.

Two aspects of the Connecticut definition are worth emphasis. First, as has been the pattern in both nonbanking and previous banking cases, the Court focused on the classes of customers most affected by the proposed acquisition and on the competitive implications for prices and availability of the group of services demanded by the affected customers. The Court chose not to focus on the implications for the merging banks and the variety of competitive forces affecting them. Second, the key class of customers in the Connecticut case was the commercial customer, and, more specifically, the locally limited commercial customer.

This series of Supreme Court decisions has clearly constrained the agencies from making significant modifications to the line of commerce. However, these decisions have had relatively little impact on the agencies' practice, established prior to PNB, of selectively considering thrift and other competitors where they believed appropriate.[26] Moreover, even the explicit findings in the Connecticut case have not significantly affected the agencies' analytic process, which on occasion has been inconsistent with that employed by the courts. Consideration of thrift and other competitors has not only tended to enter the agencies' analysis in different ways, but also has varied from case to case, both among agencies and within agencies over time.

For example, the FDIC was the first agency whose decisions began to contain explicit references to the Connecticut National decision. In approving the 1976 merger of two mutual savings banks in Maine, the FDIC cited recent changes in state law permitting mutuals to offer personal demand deposits, NOW accounts, certain types of commercial loans, and credit cards. The FDIC concluded that commercial realities transcended the Connecticut case—that the increased parity of powers for depository institutions in Maine require a viewing of a combined bank-thrift institution market, as well as the traditional separate (thrift) market, when determining the competitive impact of any proposed mergers in Maine.[27]

"Consideration of thrift and other competitors has not only tended to enter the [regulatory] agencies' analysis in different ways, but also has varied from case to case. . ."

In two subsequent cases—one a year later involving two Maine mutual savings banks and one in 1980 involving two Maine commercial banks—the FDIC again analyzed the proposed mergers in first a narrower market and then in the combined bank-thrift market.[28] While the FDIC did treat all three cases in a parallel fashion, certainly its twin market analysis did not match that suggested by the courts.

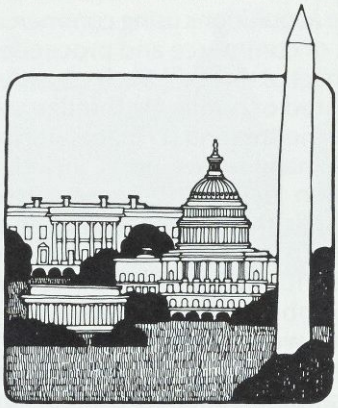
Moreover, the FDIC's finding that there was parity of powers was based upon a service by service comparison rather than on the ability to offer a package of services to particular customer classes. Only one of the products mentioned in the FDIC decision—the limited ability of mutual savings banks to offer commercial loans—would have enhanced the ability of mutual savings banks to service commercial enterprises, the key customer group in the Connecticut National Case. All of the other services mentioned by the FDIC were available only to consumers.

Following the Supreme Court's remand of the Comptroller's approval in the Connecticut National Case, there have been several other important cases in which the Comptroller considered thrift competition. In each instance, the approval decision made broad reference to the competitive influence of thrifts and other types of competitors without concern for particular classes of customers.[29]

Yet the Comptroller did consider the ability of thrifts to serve commercial and other specific customer segments in a 1980 denial of the merger between two Maine banks, Northern National Bank of Presque Isle and Merchants

National Bank of Bangor. In that case, the Comptroller specifically cited both changes in Maine law giving state-chartered mutual savings banks virtually identical powers to commercial banks and changes in federal law due to the Monetary Control Act giving broader powers to federal thrifts.

The Comptroller concluded that the overlap of services made thrifts significant actual or potential competitors...for almost all consumer financial services and an ever increasing number of commercial services.[30] More importantly, it was argued that a more realistic approach to merger analysis should include a disaggregation of the line of commerce into a number of product clusters and should reflect the degree to which thrifts and other financial institutions may compete in certain clusters and not in others. While the Comptroller did not actually apply such a disaggregate product line in the Maine case, it seemed to be attempting to lay the foundation for such an



analysis in a future case.

The Supreme Court's decision in the Connecticut National case had little noticeable impact on Federal Reserve analysis for several

HOW THE FEDERAL HOME LOAN BANK BOARD HANDLES SAVINGS AND LOAN ASSOCIATIONS' MARKETS

Like the bank regulatory agencies, the Federal Home Loan Bank System must approve or deny combinations of the institutions that it regulates. Unlike the banking agencies, the Bank Board has no court precedent defining either the geographic market or the line of commerce of these organizations. The Federal Home Loan Bank must apply competitive standards very similar to those that the commercial bank regulators apply; thus, it must decide on an approach to define relevant geographic and product markets.

The Home Loan Bank System's approach to the product of savings and loan associations contrasts sharply with that of the bank regulators and the courts. The intellectual basis for this approach dates to the early 1970s (Kaplan, 1970; Kaplan, 1971); even the Bank Board's most recent amendments to its merger regulations indicate its continued adherence to that approach (Federal Home Loan Bank Board).

The Bank Board's approach views savings and loan associations as primarily two-product firms. They offer insured savings instruments of small denominations and residential mortgages. Other savings and loan products have not been considered important in the past but may well be later. Since savings and loans are not viewed as having a special monopoly on any service (such as banks at one time had on checking accounts) and since they are not viewed as offering a special or unique cluster of services, the Bank Board has not tied the two products of savings and loans together in its analysis of mergers (Kaplan).

The Bank Board analyzes two markets: the market for small denomination (under $100,000 insured) savings instruments and the market for residential mortgages. Both markets are considered local. Newly amended Bank Board regulations delegating merger approval authority to the Regional Home Loan Banks are written in terms of county market concentration. Suppliers in the savings market include all insured depository institutions with offices in the local market: commercial banks, thrift institutions, and credit unions. Residential mortgage suppliers include all mortgage lenders making loans in the market.

The Home Loan Bank Board, thus, follows a different method of analysis from the banking agencies by identifying separate products and analyzing competition in each product market. Presently the two major markets in which savings and loan associations operate are given primary consideration. As these institutions expand the range of their services, questions of competition involving other products are likely to occur.

years. Prior to December 1979, the Board continued to follow the pattern it established in its 1974 approval of the merger of Northeast Bancorp Inc., New Haven, Conn. with The First Connecticut Bancorp, Inc., Hartford. In each instance, the Board evaluated the acquisitions using commercial banking as the line of commerce and proceeded to consider the impact of thrifts.[31] Such consideration usually consisted of noting (1) the size and number of thrifts in the area and (2) that thrifts and banks competed in many service areas, including consumer transaction deposits.[32] These factors were then used implicitly to discount the competitive significance of the proposed acquisition by an unknown weighting factor. As distinct from earlier cases, no combined commercial bank—thrift deposit shares were computed.

Not until December 1979, in a reconsideration of its earlier denial of an application by United Bank Corporation of New York to acquire the Schenectady Trust Company, did the Board refer to the Connecticut case. In the original application United Bank Corporation argued that New York thrifts had powers and provided services sufficiently similar to commercial banks to be included in the relevant product line. The Board noted that thrifts in New York could offer certain transactions accounts to consumers, but concluded that the cluster of products offered by commercial banks was still sufficiently distinct to constitute a separate product line.[34]

The applicant pressed the point in its request for reconsideration, citing additional changes in New York state law authorizing depository institutions to offer NOW accounts and prohibiting director interlocks. It also suggested that even if thrifts were not considered full competitors, commercial bank deposit market shares "...should be 'shaded' downward to account for direct competition between thrift institutions and commercial banks in certain product lines, and for competition from large out-of-market-based organizations whose small market shares do not adequately reflect their competitive influence in the relevant banking market."[35]

The Board recognized that thrift powers had expanded in many product areas and even the Supreme Court had recognized that the point would be reached where it would be appropriate to modify the line of commerce. The Board went further to indicate that thrifts and commercial banks might be grouped together for certain competitive analyses, but suggested that commercial banking might still be a relevant product line for smaller commercial enterprises. In the end, however, the Board rejected the applicant's arguments to include thrifts in the product line. The rationale is found in a footnote in the decision. The critical fact was that, while New York thrifts had been granted expanded powers, the range of permissible activities (and the extent they had been exploited) were not significantly different from the powers of Connecticut thrifts in 1974 when the Supreme Court refused to expand the product line definition. Thus, the Board concluded that New York thrifts were not yet significant competitors in offering services to commercial enterprises.

> "[In a 1980 case,] the Comptroller concluded that the overlap of services made thrifts significant actual or potential competitors for almost all consumer financial services and an ever increasing number of commercial services."

Despite this negative conclusion, however, the Board still seemed to struggle for a way to give some weight to thrifts. In this regard, it embraced the concept of "shading," or discounting market shares, as the applicant suggested a means to "consider" the competitive thrust of thrifts.[36] While "shading" was not sufficient to carry the day in that case, the Board did begin to employ the methodology in subsequent cases.[37] Conceptually, "shading" is not significantly different from the other methods the Board used to "consider" the role of thrifts.[38] The important point, however, is that such a methodology does not focus on the commercial customer, the key customer class in the line of commerce; rather, it focuses on the broader competitive forces affecting the merging banks and customers not considered users of the critical product line.

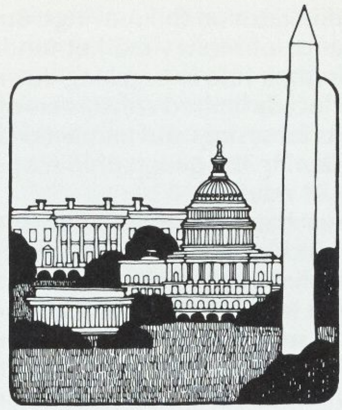
Passage of the Monetary Control Act of 1980 and the broadening of investment and commercial lending powers of federal thrifts has heightened applicants' pressures on all the agencies to broaden the line of commerce. The Board addressed the issue of whether passage of the MCA was sufficient to broaden the line of commerce in its order approving Fidelity Union Bancorporation's acquisition of the Garden State National Bank. In essence, the answer was "maybe, but not quite yet." The Board then followed its previous methodology of subjectively recognizing the presence of thrifts without references to the cluster of services provided for commercial enterprises.[39]

The Board was bothered by the Fidelity Union decision and the dilemma it faced in deciding whether the MCA broadened thrift institution powers enough for thrifts to be included in the line of commerce. The Board clearly felt constrained by the Connecticut National case but wanted to give more weight to thrifts in its merger analysis. In BHC Letter–198 of June 25, 1980 it instructed the Federal Reserve Banks and their staffs on how thrifts should be "considered." It indicated that the analysis should first look at the effects in "commercial banking" as traditionally defined, but then the staff was to collect data and other information to help determine the extent to which other financial institutions were also important competitors in providing transaction, credit and other services. These factors would be considered by the Board in making its final decisions.

Pressures for Change[40]

As the previous analysis shows, the federal banking agencies and the courts have had a difficult time defining the relevant product line

"Despite this negative [1979] conclusion, however, the Board still seemed to struggle for a way to give some weight to thrifts."



to use in bank mergers and acquisition cases. The agencies have never been particularly comfortable with the Supreme Court's delineation in the PNB and subsequent cases. The agencies have always attempted—both before and after PNB—to take into account thrift and other competition, sometimes within, but more often than not outside, the constraints imposed by the Supreme Court decisions.[41]

Since the Supreme Court last addressed the issue seven years ago, pressures on the agencies to modify the line of commerce have heightened substantially. Numerous financial innovations and structural changes in financial markets are eroding the uniqueness of commercial banks as suppliers of demand deposits and the cluster of services that had traditionally set these institutions apart.

Moreover, these developments have reduced banks' cost advantages, and high interest rates have altered consumer preferences which had previously isolated banks from competition. The Monetary Control Act significantly broadened the deposit and asset powers of federal thrifts and authorized NOW accounts nationwide which has served to make banks and thrifts more homogeneous; legislation introduced during 1981 suggests that the realignment of thrift powers is not completed yet.

As interest rates have remained high, both consumers and businesses have also become more sophisticated in unbundling their use of financial services to earn the highest yields on their invested funds and to obtain credit at the most favorable rates. The growth of money market mutual funds has enabled smaller depositors to realize market rates on their savings. But the greater importance of money market funds may ultimately lie in their role in breaking down the dependence of locally limited consumers on local banks and thrifts for savings and transactional services, thus broadening the geographic scope of consumer financial markets.

The last two years have also witnessed the rapid spread of symbiotic financial arrangments in which independent firms cooperate to provide a service that could not legally or economically be offered by either firm separately. The best known example is Merrill Lynch's Cash Management Account. It combines a Merrill Lynch margin account, a Visa debit card and service arrangement provided by BancOne of Columbus, Ohio, and Merrill Lynch's money market mutual fund.

More recently, we've seen the creation of new types of financial institutions resulting from combinations of brokerage firms and other financial institutions, such as American Express-Shearson and Bache-Prudential. These institutions not only have institutionalized certain symbiotic financial arrangements, such as cash management services; they also are positioning themselves to take advantage of their freedom from reserve requirements and other regulations to offer a wide range of consumer and corporate financial, brokerage and insurance services.[42]

Whether these new institutions will be successful remains to be seen. They are, however, able to offer potentially superior substitutes to traditional banking services and can capitalize on the fact that many bank customers have learned it can be both convenient and cost effective to obtain financial services from nonlocal and nontraditional firms. It is important to realize that these recent financial innovations and competitive structural changes which have so concerned depository financial institutions affect primarily the types of services and alternatives available to consumers. For example, Bleier and Eisenbeis (1981) argued that the MCA granted thrifts few, if any, significant powers to enable them to offer services to corporate customers; this is especially true for S&Ls. The act does grant slightly broader authority to the few federally chartered mutual savings banks to offer certain commercial services, but even here quantitative limitations have been imposed. These limitations coupled with thrifts' present financial difficulties and the problems of acquiring the necessary management expertise should limit the overall competitive significances of these changes. Similarly, the cash management and money market fund services are also directed at consumers and not to the corporate customers.

Thus, many of the events now being cited by the applicants and regulatory agencies as the rationale for a re-examination of the line of commerce issue are occurring in the retail banking submarkets. But the Supreme Court has already indicated in the Connecticut National case that "fierce" competition in such submarkets isn't sufficient to cause it to change the line of commerce definition. Thus, to base a case for a change on the need to recognize the market realities of thrift competition in consumer markets is unlikely to be particularly persuasive. In fact, the Court might be convinced that the emphasis it placed in the Connecticut National case on the cluster of services provided to commercial customers is as relevant today as it was then, especially if the Court continues to direct antitrust to the protection of affected customer classes rather than looking at competitors.

So it is tempting to cling to the more traditional line of commerce and to focus on commercial customers. Yet there are also broader policy issues, as well as some potential pitfalls, in clinging too long to such a product line definition in today's changing financial environment, when the product constitutes a decreasing portion of many banks' business.

First, what happens as bank dependence on liability management and access to purchased monies expands as the primary source of bank funding? As commercial lending to small commercial enterprises declines as a portion of lending to consumers and large businesses, it

> "But the Supreme Court has already indicated that 'fierce' competition in [retail banking] submarkets isn't sufficient to cause it to change the line of commerce definition."

may pay many banks to abandon the small-commercial segment of their business. That's especially true if the result is to escape—or at least reduce—antitrust scrutiny. Thus, continued reliance on the traditional antitrust approach focusing on protecting affected classes of customers in a financial environment where funds are increasingly fungible, handicaps those firms whose services happen to be included in the relevant product line.

The traditional approach provides incentive for aggressive, expansion-minded banks to abandon their activities in the relevant product lines. The long run effect may be to drive out suppliers and reduce the number of effective competitiors for those very customers and in those markets the policy seeks to protect. In effect, we are forced back to one of the key public policy issues addressed in the PNB case of whether the antitrust laws should apply to banking and, if so, how?

Second, even within the traditional approach, almost any broadening of the line of commerce would have the practical effect of liberalizing the range of acquisitions that would pass muster under the antitrust laws; the broader the line of commerce, the lower the estimated concentration ratios and the lower the probability of finding a Section 7 violation. Thus, changing the line of commerce definition has the potential to precipitate a consolidation of the banking system.

At the root then, of the line of commerce issue, are three questions: What type of a consolidation movement do we want to promote, how do we want it to proceed, and what role is antitrust to play?[43],[44] To illustrate the potential problems, suppose the arguments of many applicants are accepted and thrifts are included in the line of commerce. Because of the present difficulties of merging banks with thrifts due to statutory prohibitions and because operating a thrift is not a permissible activity for bank holding companies, the main impact of the broader definition would be to accommodate consolidations among banking organizations. But at a time when thrifts are in such financial difficulty, do we want, as a matter of public policy, to rationalize a further skewing of the relative size distribution of the financial industry in favor of banks?

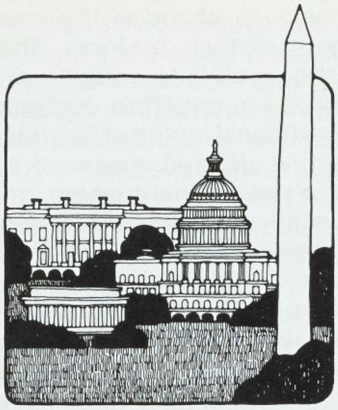
Third, the policy problems are not eased if one follows the path recommended by the Comptroller in the Northern National Bank of Presque Isle case in which multiple "product line" clusters would be analyzed.[45] Such an approach may result in a tightening rather than a loosening of merger policy since a violation in any one of a number of relevant products lines would result in an antitrust violation. Perhaps, more importantly, however, is the increased regulatory burden that would be associated with such an approach. Data would have to be organized and collected on all the relevant product lines, not only from the merging banks, but also from all other institutions in the affected markets. At present, the only reliable data that can be organized on an approximate market basis are the FDIC Summary of Deposit data. Comparable data are not only costly to provide, but also are difficult to collect and process.[46] The problems and costs of extending such data to more than just deposits and to broaden classes of reporting institutions should not be taken lightly.

> "Yet there are . . . broader policy issues, as well as some potential pitfalls, in clinging too long to such a . . . definition . . ."

Finally, if one were to focus procedures of the FDIC and Federal Reserve Board on the competitive forces affecting banking organizations, rather than looking at affected product markets and classes of customers, the result would be a radical redirection of antitrust law from its traditional focus for all industries. In view of the large number of conglomerate acquisitions successfully evaluated using the traditional methodology, it is difficult to argue that banking is so unique and presents such difficult public policy issues as to warrant a rethinking and reorientation of antitrust policy.

The analysis of agency decisions indicated that they wrestled with the problems of delineating the relevant line of commerce long before the

Supreme Court did in the PNB case. The agencies have never truly been comfortable with the Courts finding in that and subsequent cases. They have continually sought to take thrift and other competitors into account, even when such institutions were not significant suppliers of services to the relevant affected classes of customers. At the root of their difficulty is the problem of dealing with financial conglomerates which operate in many different product and geographic markets and are subject to a variety of competitive forces. As a result, the analysis they have employed has not always been consistent with that employed by the Supreme Court. The dilemma the agencies have faced has become more significant as banks have diversified into more product lines and markets, as financial innovations have broken down traditional customer relationships and dependence upon banks as suppliers of clusters of services, and as more and more diverse financial institutions have begun to offer close substitutes for banking services.



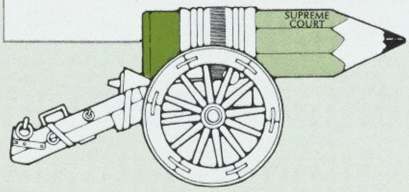
"We should be careful not to take the redefinition of the line of commerce too lightly . . ."

We are now faced with the problem of how to restructure the financial system and how we want the transition to that structure to proceed. In that respect, antitrust policy is but one element that needs to be considered. All the same, we should also be careful not to take the redefinition of the line of commerce too lightly or view it with the blinders of a narrow technical legal focus. For to address the line of commerce issue without regard to the broader policy issues could set the financial system on an evolutionary path that would be difficult to reverse and that might erase the gains that increased competition has brought.

—Robert A. Eisenbeis

Section II

THEORETICAL AND EMPIRICAL EVIDENCE



Following the 1974 Supreme Court decision in the Connecticut National Bank case the court narrowed, somewhat, its interpretation of the relevant product of commercial banks.[47] Prior to the Connecticut case, the Supreme Court had consistently ruled that the cluster of services offered to both consumer and commercial businesses by banks was unique enough to allow banks to be treated separately under the antitrust laws.

Just prior to this case (May of 1973) the State of Connecticut passed an act which would have allowed savings banks to offer NOW accounts. Although the Supreme Court noted that the future ability of savings banks to offer NOW accounts would increase competition between savings banks and commercial banks, the court did not redefine the line of commerce offered by commercial banks.[48] Commercial banking's cluster of commercial services was sufficient, the court said, to establish commercial banking as a distinct line of commerce.[49]

The criteria for viewing a cluster of services as a separate product seem to have been based on two characteristics; first, that banks were the only suppliers of third party transaction accounts, a monopoly product; and second, that bank services were offered as a package.

This section begins with a theoretical discussion of whether both of these characteristics, monopoly service and a bundled package, are necessary to differentiate banking from other financial service suppliers. Ira Horowitz describes the economic logic of defining products and markets. Focusing on the business of banking, he then reviews the theoretical justification for the courts' and regulatory agencies' definition of the product of commercial banks. B. Frank King follows with a review of the empirical evidence on the question of whether or not banks offer a unique cluster of services to commercial enterprises.

Theoretical Review

From the time of Adam Smith down to the present day, economists have been interested in studying the economic behavior of markets. This interest, however, has rather consistently failed to prompt a corresponding interest in how one recognizes or delineates a market. Those economists who have paid more than passing attention to the issue have been motivated principally by the practical need to define relevant markets in order to permit the antitrust authorities and the courts to implement antitrust policy. Specifically, the courts have determined that the "lines of commerce" and "sections of the country" referred to in the antitrust statutes imply what economists mean by "markets." Thus, for the first time, economists have been asked to explain what they mean by, and how they discover, the "market." The explanation has not been wholly satisfactory, but then the concept of a market is more than somewhat ethereal.

In reviewing the history of the market-definition issue, however, we should not overlook the contributions of Alfred Marshall and his followers. Under Marshall's early twentieth-century impetus, the field of industrial organization emerged wherein economists looked to the *industry* rather than the market to find the forces of economic change.

Market Question Neglected

What constitutes an industry still requires some definition, but at least the industry concept has some concrete natural characteristics that make it less nebulous than the notion of a market. Nevertheless, for almost fifty years now, under the combined influence of E. Chamberlin's theory of monopolistic competition, R. Triffin's promotion of the cross-elasticity concept, and the courts' awareness of both, the concept of an identifiable market and identifiable submarkets has been a matter of significant practical concern and theoretical neglect.

On the one hand, the neglect is understandable, because *unambiguously* delineating markets is hard and one needn't delineate a market in order to intelligently discuss what would go on there once it had been accurately identified. On the other hand, as the courts have recognized, if we are to be concerned with erosions of competition and tendencies to monopoly, it seems appropriate that we know what it is that is about to be monopolized, where the monopolist will reign, and exactly who will be adversely affected by the lessening of competition, as well as to what extent and over what period of time. That is, a non-passive antitrust policy demands that economists, whom one would expect to be best positioned to study the matter, be concerned with the market-definition issue. And, the market and the industry are not necessarily, nor likely to be, identical in structure.

An industry is essentially "a grouping of firms on the basis of a similarity both of products and of production processes. The products have to be sufficiently substitutable to permit some

"For the first time, economists have been asked to explain what they mean by, and how they discover, 'the market'"

rough estimate of price and income elasticity of demand. The production processes should be sufficiently similar to permit us to make reliable inferences regarding the...relation of overhead to variable costs, and the responsiveness of variable costs to changes in factor prices."[50] In contrast, the market, however precisely defined, is a multidimensional construct that includes buyers as well as sellers, and that has both product and spatial connotations, in addition to an easily overlooked time dimension. In the eighteenth and early nineteenth centuries, the diverse possibilities that these various dimensions could create would not necessarily leap to mind.

The early economists were principally concerned with studying the economic behavior of the labor and agricultural commodity markets. In the absence of unions, giant food packagers, and large super-market chains, and given the difficulty of travel during this period, both the labor and commodity markets housed a fairly fixed set of numerous buyers and sellers regularly exchanging perishable and reasonably homogeneous goods and services within a compact geographic area. Or, in any event, that was the way reality was perceived. That perception was translated into one of the profound economic truths of the era, notably, that there cannot be two prices for the same good, at the same time, in the same market.

Assuredly, even the early economists weren't sufficiently naive as to believe any of that, except in the broadest terms of general tendencies. Thus, from Smith forward it was recognized that by organizing and regulating entry into the market, and the terms under which they provided their services, members of the various professions could distort the work of the invisible hand. It was also apparent to these economists that the lack of perfect knowledge could in fact lead to the same product being sold in a given market for different prices at the same moment of time, but it was acknowledged that this difference could not long persist. Still further, it was understood that there were indeed large entities, in particular firms engaged in foreign trade and transportation, as well as some manufacturers, that held monopoly positions. Given the analytical tools available to them, however, the early economists were unable to do much more than remark that such monopolists could, and if left to their own devices usually would, exploit their monopolies to the detriment of the general public.

The economist's analytical attention was then directed to the exchange of homogeneous products in the narrow class of well-defined competitive markets with numerous buyers and sellers, each of whom is too small to be of interest to the others, but each of whom is sufficiently knowledgeable as to be aware of alternative buying or selling options. Such markets, however, did in fact encompass a critical part of each (western) nation's economic activity so that the economist's attention was not misplaced. Thanks to the economists, we now know what will happen to the price of wheat and bread if the demand for bread should increase or if a drought should reduce the wheat harvest. Where analytical complications arise is when the products are neither homogeneous, nor perishable, nor traded among unique groups of buyers and sellers, *and* when each of us is not equally well informed and the number of participants in the market, on either side, is sufficiently small so as to lead the individual members to recognize their interdependence.

Theorists Turn to Imperfect Competition

Preceding Marshall, then, economic theorists such as Cournot, Bertrand, and Edgeworth began to reorient the study of markets to consider the problems created when two-seller duopolies initially, and several-seller oligopolies subsequently, replace Smith's numerous-seller markets. It became immediately apparent that in order to make any analysis tractable, one would be forced to make some assumptions about the interrelationships among the sellers, and in particular to provide each seller with some assumptions as to the behavior of the others.

Following Marshall, Joan Robinson from one perspective and E. Chamberlin from another focused attention on imperfect competition and monopolistic competition. Broadly speaking, this focus forced economists to study markets comprised of *any* number of sellers (or buyers) who could operate with *some* degree of independence of the others, but whose activities, and the results of those activities, would be tempered by other *clearly identifiable* sellers (or buyers). This focus in turn led to Triffin's interest in measuring the degree to which a reduction in the price charged by one seller would affect the quantity demanded of another. Triffin's measure of the cross-elasticity of demand, in this context defined as the relative change in the quantity demanded of Seller B in response to a relatively small change in the price charged by Seller A, at first has the pleasant property of being easily interpreted: notably, when a reduction in one seller's price reduces the quantity sold by another, then the sellers and their products are rivals; otherwise they are independent. In practice, however, the measure is not so easily interpreted.

The impact of one seller's price change on the demand for another's products depends upon the prices charged by each (and *all* other sellers of *all* other products). Assuming that all sellers have arrived at an "optimal" (for example, profit maximizing) pricing policy that initially leaves all sellers content with their lots, an unanswered price reduction by one seller will shift consumer demand away from many other sellers including some sellers that never dreamt they were in competition (except broadly speaking) with the price cutter. The extent of the shift, as measured by the cross elasticity of demand, can run a full gamut.

In any case, the size of the cross elasticity is necessarily limited by the seller's own-price demand elasticity. For example, if via a price cut a firm cannot increase the quantity demanded of it, then another seller's price increase also should not increase demand for the first seller's product. Thus, when at existing prices the cross elasticity between Seller A's product and that of Seller B is unity, we know that a 10 percent price reduction by Seller A will effect a 10 percent loss in quantity demanded of Seller B. But while we also know that the 10 percent loss is less than 20 percent and greater than 5 percent, we cannot know how impressive is that 10 percent loss until we know how severely the demand for Seller B's product would be affected by an analogous price increase by Seller B. Moreover, the fact that the A-to-B cross elasticity is unity does not necessarily mean that the B-to-A cross elasticity will also be unity. Finally, even if the data were available to permit the accurate measurement of cross elasticities, there is no reason to expect a single cross elasticity to obtain between, say, Seller A's Brand X and Seller B's Brand Y. Rather, the cross elasticity will depend on the levels of *all* prices for *all* products.

Nonetheless, industrial organization economists and the courts have looked to the cross elasticity as a measure, however imperfect, that would help them to group sellers of like products, or, more accurately, group rival sellers. These rivals, their products, their customers, and the areas within which they sell, constitute the markets to be studied for given time periods. The groupings are arbitrary, to be sure, because the cut-off point on the cross elasticity and the extent of interfirm rivalry that defines the group

Thus, the pertinent point . . . is whether a sufficiently narrow submarket can be defined in which (market power) abuses are likely."

is arbitrary. Indeed, *any* such grouping of buyers and sellers, that is to say any market definition, is arbitrary, whether it is effected through well-defined and historically accepted lines of commerce and geopolitical regions, or through allegedly clear-cut criteria such as unique sets of customers, similar distribution systems, like prices, and so forth. What this in turn implies is that markets can be broadly or narrowly defined, or that there are arbitrarily-defined submarkets within the arbitrarily-defined markets! The critical question for antitrust purposes is: Does this arbitrariness make meaningless an antitrust analysis of any market that has been defined solely for antitrust purposes? Given the appropriate caveats and the need to deal with the realities of a now very complex world, it does not.

The concern of the antitrust laws is whether there exists a line of commerce in a particular section of the country—that is, a market in the legal sense—that has been or is likely to be either monopolized or the victim of lessened competition with the effect of giving one or a small number of sellers market power (the power to raise prices or exclude potential competitors). Thus, the pertinent point for an antitrust court to settle is not whether a sufficiently *broad* market can be defined where these abuses are not likely to occur. Rather, the point is whether a sufficiently *narrow* submarket can be defined in which those abuses are likely. Unfortunately, there is no consensus on which data and arguments are relevant.

Courts Stress Concentration Ratio

The general tendency in the courts (as well as in the industrial organization literature) is to place considerable if not overriding weight on the sellers' concentration ratio and its trend. Since the sellers' concentration ratio depends upon how the market is defined, the litigants in an antitrust case thus have the incentive to argue for the market definition that provides them with "the best" ratios. In practice, therefore, and behind the scenes, the market definition and concentration-ratio-computation processes ordinarily go hand in hand and involve considerable feedback. Accepting the *fact* that the market-definition process is arbitrary, however, and then drawing the logical inference that there can be both actual and *potential* competition between submarkets, reduces the role of the concentration ratio as well as the dangers of working with arbitrary definitions. Instead, it becomes necessary to identify whether or not the delineated submarket, both product and geographic, should be a matter of antitrust concern. One element of that story is the economic performance of the sellers in that market. A second element is the real or apparent market power possessed by the leading sellers in that market, as indicated, among other things, by the extent to which a few sellers hold a large market share. A third and related element is the extent to which the behavior of the leading sellers in the market is constrained by their awareness of the sellers in other markets.

> "The convenience and efficiency of . . . a cluster of services may differentiate the product sufficiently for the consumer to regard no single product . . . as a viable substitute."

With specific respect to the "market for financial services," for example, we observe that a huge but identifiable set of firms of various shapes and sizes provide a wide array of financial services within the United States. This market, the market for financial services (the line of commerce) in the United States (the section of the country), is in little danger of being monopolized. Within this market, however, there are clearly delineable relevant submarkets that might conceivably and in principle be monopolized.

With particular respect to banking as a relevant product market, there are two possible scenarios. In one, commercial banks offer a cluster of services any one of which is available elsewhere; in the other, commercial banks offer one service, notably demand deposits for commercial customers, that is unique to banking.

In the first instance, the cluster of services is a relevant product, and banks are the suppliers. This is so since should these services become

SUPREME COURT: Banking is a separate product line because:	ECONOMIC THEORY:
Offers Unique Product (3rd party transaction account)	A unique product separates banking from other financial service suppliers.
Offers a Cluster of Services	Clustered services separate banking from other suppliers not capable of offering the same cluster.

Conclusion: Courts were on firm theoretical grounds in defining banking as a separate line of commerce.

more costly, others cannot enter the market to supply the cluster, nor will all customers desert commercial banks in favor of individual suppliers. The fact that the latter option exists constrains any power that one or more commercial banks might have in a particular geographic market. That is, the existence of submarkets reflects on the market power and potential competition issues, but not on the relevant market definition.

In the second instance, once banks are the sole suppliers of demand deposits for commercial suppliers, then the latter becomes the relevant product irrespective of whether banks bundle their services. Again, the criteria are that no one else can supply the unique service nor do customers have access to an equivalent substitute. Hence, should the service become more costly, no new suppliers will be attracted to bid the price of the service down, nor will customers desert banks *en masse* to take their business elsewhere. A single commercial bank, however, has good reason to cluster its services. Since the law prohibits interest on commercial demand deposits, banks must compete on a nonexplicit price basis, i.e., offering greater convenience or reducing prices for other services. Thus, reducing the price of at least some services in the cluster implicitly reduces the cost to the customer of a commercial demand deposit account.

Conclusion

What we may conclude from this is that clustering of services is sufficient to differentiate the product of a group of suppliers from the product of any other supplier not capable of offering the same cluster of services. Therefore, the courts were on firm theoretical grounds in differentiating the product of commercial banking as a separate line of commerce, or separate product, if in fact banks are effective in clustering their financial services. The fact that banks offered all their services at one location may be sufficient for this finding if a combination of convenience and efficiency are considered. The ability to obtain most of one's financial services at a single location drives down search and transportation costs for the consumer. At the same time, the ability to offer an array of financial services may allow the firm to offer any or all of those services at a substantially reduced price as compared to a supplier of only one or two of these services.

The combination of convenience and efficiency of offering a cluster of services may differentiate the product sufficiently for the consumer to regard no single product or nonclustered product as a viable substitute for the clustered services. In addition, the fact that banks, at one time, were the only institutions to offer third party transaction accounts to both consumer and commercial customers gave commercial banks a unique position. This unique service is sufficient in and of itself to allow the courts to define the product offered by commercial banks as being different from that offered by any alternative financial supplier. Therefore, the court's decision to define commercial banking as a separate line of commerce is consistent with the theoretical economic rationale for defining products and markets.

—Ira Horowitz

Review of Empirical Literature

Having reviewed the theoretical justification for viewing commercial banking as a separate line of commerce, we are still left with two empirical questions. First, do banks in fact offer a monopoly product and second, do banks in fact cluster their services? Or alternatively, do bank customers view the services offered by commercial banks as a package instead of a set of separable independent products? Since the enactment of the Monetary Control Act of 1980, the uniqueness of the array of services offered to consumers is highly questionable.

What is not questionable, however, is the fact that commercial banks are still the only suppliers of third party transaction accounts for commercial customers. The courts have repeatedly emphasized that as long as commercial banks are the only significant suppliers of a product, a financial service or an interrelated group of services, to a significant group of consumers they would continue to be viewed as offering a separate product from that of all other suppliers of financial services. Therefore, the question of whether or not commercial banking is a separate line of commerce hinges on the empirical question of the existence of significant alternative suppliers of financial services offered to commercial consumers by commercial banks. This article reviews the empirical literature on this question and assesses the evidence.

If local commercial banks currently offer any services that customers cannot get elsewhere at reasonable cost, these must involve services to local businesses. Individuals, nonprofit institutions, and governments all have local sources of financial services other than banks in most areas.

The characteristics of businesses' relations to banks and other financial institutions have been studied in the past in connection with attempts by regulatory agencies to define banking markets and with attempts to determine the adequacy of business financing. Three groups of studies provide most of the systematic empirical evidence that we have about the sources of financial services to small businesses. The largest portion of this evidence comes from a group of surveys of businesses. Only the latest of these covers a broad range of financial services (including trade credit and factoring) or the location of nonbank providers of financial services. Only half cover nonbank providers of financial services at all.

"The question of whether or not commercial banking is a separate line of commerce hinges on . . . the existence of significant alternative suppliers of financial services . ."

However, these studies do provide some evidence on many of the characteristics of the market for business financial services.

The second group of studies originates from surveys of commercial banks about their business lending. Along with other information, these surveys developed data on the location of bank customers. Thus, they provided evidence on the local nature of banking markets. Like the business surveys, they were done mainly in the 1960s. A similar study, grouped with these for convenience, is the recent study of nonlocal competition commissioned by the American Bankers Association. The final type of study uses available aggregate balance sheet data from businesses to paint a picture of the borrowing alternatives of businesses. The single study in this category deals in aggregates and averages.

> "Local banks were the predominant suppliers of most services at the time of these studies, but a significant proportion of businesses used both nonlocal banks and nonbank financial services."

Business Surveys

Only three of the business surveys were national. The others dealt with smaller areas such as towns, metropolitan areas, or states. The areas were quite diverse, ranging from smaller towns in Indiana and Florida to suburbs of New York City to the state of Ohio. The general conclusions of these studies on the extent of the geographic market for financial services produced by banks were, however, quite similar. Much less information about the importance of alternatives to banks as sources of financial services is to be found in them.

Of the rather broad set of topics covered by business surveys, the most relevant to the question of line of commerce and geographic market were number and location of banks used by the firm and other financial institutions used by the firm. This latter topic was covered in seven of the thirteen studies reviewed. The results of the survey related to location of banks and use of nonbank institutions for loans are summarized in Table I.

The model for business surveys, a study done in 1957 by George Katona, deals with very large firms, but its findings are quite consistent with later studies with high concentrations of small firms. Katona's sample of firms generally used more than one bank, but more than half used a bank located in their headquarters city as their primary bank. Katona found also that the number of banks used and the likelihood of using nonlocal banks was lower for smaller firms. A second survey of the **Fortune** 500 industrial corporations found results similar to Katona's. This study (Staats), however, found that a majority of these large corporations had primary banks in areas in which the companies had branches as well as in their headquarters area and that they obtained credit as well as deposit services from these banks.

The business survey studies of the late 1960s and early 1970s generally found strong evidence that businesses chose a primary bank located in their own town and that they acquired most of their financial services from that bank. For example, in the first of two surveys conducted in Elkhart, Indiana, by the Federal Reserve Bank of Chicago, 95 percent of businesses used primary banks with Elkhart locations; in the second study, 94 percent used Elkhart banks (Kaufman 1967b, 1969). Similar results were found in the other studies that dealt with small businesses (Kaufman 1967b, King, Stiles) except for two studies of suburban areas close to large cities. In each of these studies—one of Central Nassau County, New York, and the other of Bucks County, Pennsylvania—only two-thirds of businesses used local primary banks (Kildoyle, Bowers). Most of the other businesses dealt with primary banks in New York City and Philadelphia, respectively. Both of Ware's studies of a sample of all sizes of Ohio businesses found slightly less than 90 percent of the businesses sampled using a local bank as their primary bank. These percentages fall between those of small businesses and those of large businesses.

A single study involving businesses in a large city—St. Louis—(Luttrell) had findings on the

> "The surveys . . . reinforce the evidence that convenience is the most important factor in choosing a lending bank."

number of banks used that were consistent with other studies but found more businesses borrowing from nonbank financial institutions. This survey covered large and small businesses. Most of the larger businesses used more than one bank; most of the smaller did not. Of the large firms, some 32 percent borrowed from nonbank financial institutions; of the small firms, 25 percent did. These percentages exceed those found in studies of small town and suburban firms, which found from 16 to 20 percent of the firms used nonbank financial institutions.

The two most recent business surveys were conducted by the National Federation of Independent Businesses in April of 1980 (Zayas) and the Federal Reserve Bank of Cleveland in the spring of 1981 (Watro). Questions in the former dealt only with the most recent business loan of the businesses surveyed. Consequently, the survey did not cover the volume of loans supplied by various sources, the location of loan sources, and the use of other financing methods. Despite these missing pieces, the survey's results suggest that banks are still important sources of business credit. The firms surveyed reported that banks had provided their most recent business loan in 83 percent of the cases. They named no other lender in more than 5 percent of the cases.

The Cleveland survey (Watro) was broadly based in that it dealt with deposit and credit services and with a broad spectrum of financing. This survey of small businesses (assets less than $5 million) in Ohio found commercial banks to be the almost exclusive source of transactions accounts, coin and currency, lock box, night depository, cash management and trust services. Savings and loans and other institutions supplied business time and savings accounts for almost thirty percent of the businesses. The survey results cast serious doubts on banks' dominance as a source of credit. Respondents indicated that suppliers of goods and equipment were the most widely used source of credit. Banks ranked second but were used by only 56 percent of the firms. Only one sixth of borrowing firms had all their debt with commercial banks.

The business surveys bring out several characteristics of businesses' use of firms providing financial services. Local banks were the predominant suppliers of most services at the time of these studies, but a significant proportion of businesses used both nonlocal banks and nonbank financial institutions. Convenience was evidently a strong motivating factor in the choice of primary bank and alternative banks. Small firms generally relied on one bank while larger firms used two or more banks more often. Alternative banks were more often found outside the firm's local area. The surveys of business lending by banks reinforce the evidence that convenience is the most important factor in choosing a lending bank, although the surveys did not attempt to uncover price differences among banks.

These business surveys have similar strengths and limitations. Except for the Zayas and Watro surveys, each presents evidence on the local nature of small business-bank relationships. Although only two surveys deal with a national sample, the combination of evidence from the other studies presents a convincing picture of business-bank relationships of the 1960s and early 1970s. The findings of each of these studies are quite consistent. Each study concluded that most small businesses used local banks. Whether local banks held a dominant place in supplying all business financial services, however, was not nearly so well covered. Only half of the studies asked businesses about any kind of nonbank services that they used. All but one of these dealt only with loans; consequently, trade credit and equity financing sources and all other financial services were ignored. In addition, it is difficult to determine whether respondents included secured loans on equipment and real estate in their definition of loans. The recent Cleveland study is the exception to the others in its combination of timeliness and breadth. Its results indicate that—at least in Ohio—although small businesses remain tied closely to banks for transactions accounts and related services, they use other sources for a significant portion of their time deposit and credit services. These results cast serious doubts on whether businesses treat banks as providers of an inseparable cluster of services.

Bank Surveys

In addition to evidence from the recent interagency survey of banks about small business lending (summarized below), there are three other studies that develop evidence on characteristics of markets for business financial services from surveys of banks. The earlier two of these were based on a 1955 survey of business loans carried out by the Federal Reserve System (Lozowick, Steiner, and Miller; Eisenbeis). These studies dealt only with the question of the geographic extent of the loan market. Analyzing data on distance between banks and borrowers, the authors of each concluded that businesses, generally, limited their bank borrowing to the SMSA in which they were located. The local limitations were stronger for smaller businesses and smaller loans.

Much more recently, the American Bankers Association sponsored a study of nonlocal competition for banks located in large metropolitan areas (Merrill). Information for the study came from interviews with banks and other institutions. The study found that there were many nonlocal banking competitors of local banks in the large, rapidly growing metropolitan areas of the Sun Belt. These competitors apparently concentrate mainly on providing financial services to middle market business customers. It further concluded that the nonlocal competitors generally shun smaller towns, smaller businesses, and more slowly growing or declining areas.

The studies based on the Federal Reserve's Business Loan Survey deal exclusively with the geographic nature of bank-business loan relationships. They do not explore either the existence or the location of nonbank suppliers of financial services. Their results are also based on data collected in 1955, before the last quarter century of financial developments. The Merrill study, on the other hand, is current but limited to a few large metropolitan areas. Its conclusions are based on a survey of bank and nonbank sources; thus, they eliminate biases based on banker knowledge alone. The conclusions of the Merrill study are of unknown applicability in smaller metropolitan areas or towns. They also touch the issue of services to small businesses only peripherally.

Aggregate Data

A further recent piece of research uses aggregate data from several government agencies to paint a broad picture of the sources of small business financing in the late 1970s (Andrews and Eisemann). This study, like Watro's recent work, casts substantial doubt on banks' present dominance as sources of credit for small business and on the proposition that businesses treat banks as offering a cluster of services rather than individual services.

From the perspective of alternative sources of business financial services, the most important conclusion of this study is that trade credit, finance company credit, and government credit rival bank credit in importance as sources of financing for small businesses. These three sources are covered in only one of the surveys reviewed above so that we do not know if most businesses responding to them followed the same pattern found in the study by Andrews and Eisemann. In the study that did cover these sources (Watro), results are similar to those of Andrews and Eisemann. It is clear from the aggregate evidence, however, that businesses have important financing sources other than banks and that they use these sources despite their continued dependence on banks for demand deposit services. Another important finding of Andrews-Eisemann is that secured loans either based on commercial real estate or from finance companies based on equipment provide

> "The results cast serious doubts on whether businesses treat banks as providers of an inseparable cluster of services."

substantial sources of financing for small businesses also. The study points out that although trade credit and secured loans may seem to involve directly use of credit for the purchase of a specific item, the funds acquired by these means may be used for any business purpose. This means that these financing sources are as general in their uses as unsecured credit typical of commercial banks.

The Andrews-Eisemann study adds breadth to our knowledge of sources of small business financing. It explicitly considers financing secured by real estate and equipment, and trade credit as business financing sources. Its use of dollar value rather than number of relationships provides an alternate measure of the importance of various financing sources. In addition, it is more current than most of the other studies cited here. This study leaves some gaps in our knowledge of small businesses' use of financial services. It does not cover nonbank services other than financing, and it does not say anything about the geographic extent of the business services market.

Conclusion

The evidence that has been gathered in these studies of sources of business financial services indicates that substantial changes may have taken place in these sources in recent years, at least in some geographic markets. The business survey studies (all but two performed before 1974) uniformly indicated that markets for these surveys were local so far as small businesses were concerned. The pre-1974 studies uncovered evidence of use of nonbank loan sources by about one-fifth of small businesses and by a larger proportion of larger businesses. A recent business survey indicates that nonbank deposit and loan sources have become more important over time both as exclusive and additional sources of financial services to small businesses. A recent survey of financial institutions indicates that in some markets—fast-growing relatively large ones—nonlocal institutions are becoming important suppliers of financial services at least to middle market businesses and that these institutions are not necessarily commercial banks. Finally, aggregate data on sources of small business financing indicate that banks are not now the dominant source of financing, but are part of a more extensive menu including trade credit, governments, finance companies, and other mortgage lenders.

> "Equity, trade credit, finance company credit, and government credit rival bank credit . . . as sources of financing for small businesses."

This recent evidence on nonlocal and nonbank sources of financial services for small businesses casts doubt on the generally accepted conclusion that these businesses depend exclusively or dominantly on local commercial banks and on whether they treat banks as providers of a group of services from which they cannot pick and choose. The limited nonbank competition found in early studies is also in part a result of their concentration on loans and of the exclusion of trade credit and equity as financing sources. Limited use of nonlocal banks and nonbank lenders found in the studies done in the 1960s and early 1970s may also have expanded.

While no such dramatic changes as the Monetary Control Act of 1980 have taken place in markets for business financial services, many subtle changes in these markets along with evidence of recent studies lead one to question the importance of commercial banks in offering many businesses individual services and as the source of a cluster of these services. Trade credit provides a large proportion of financing for small businesses. Commercial finance, captive finance, and leasing companies offer businesses financing secured by equipment or real estate *but* not necessarily used to buy equipment or real estate. Savings and loan associations may finance noncorporate business and, if real estate is the security, corporate business. Banking organizations headquartered outside local markets provide financing through nonbank subsidiaries and loan production offices and calling officers.

To conclude, the previous empirical work is,

Table 1
Summary of Business Survey Results
(Percentage of Firms)

Survey	Using Only One Bank	Using More Than One Bank	Using Local Primary Bank	Using Local Secondary Bank	Using Nonbank Financial Institution
Large Businesses					
Katona	21	78	54	*	*
Smaller Town, Smaller Business					
Kaufman 1967a	65	35	94	47	20
Kaufman 1967b	50	49	95	42	18
Kaufman 1969	70	29	94	56	19
King	67	33	95**	90**	*
Stiles	70	30	99	58	*
Mixed Location and Business Size					
Ware 1969	64	36	87	*	*
Ware 1973	58	42	89	*	*
Suburb, Mixed Business Size					
Bowers	70	30	66	60	16
Kildoyle	59	41	66	47	20
Large City					
Luttrell	32/76***	68/23***	*	*	32/25***

*Not available
**Checking accounts
***Large firms/small firms

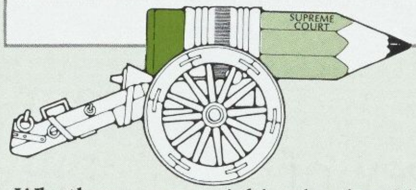
Note: Data reported in Staats and Watro do not fit the categories of this table.

by and large, dated, but existing evidence supports the following conclusions. First, small businesses seem to be constrained to local sources of financing, as the courts assumed. Second, commercial banks are and have been a major source for financial services to businesses, especially small businesses. Third, alternatives to banks for commercial loans and other financial services do exist and are becoming more significant. Perhaps most important, recent studies indicate that businesses make substantial use of non-bank sources of financial services despite their dependence on banks for demand deposits. Although this does not provide evidence that clustering exists or does not exist, the fact that small businesses are obtaining financial services from non-bank sources casts doubt on their viewing the services provided by commercial banks as clustered.

—B. Frank King

Section III

NEW EMPIRICAL EVIDENCE



Whether commercial banks should be treated for antitrust purposes as offering a product separate from that of other financial service suppliers is an empirical issue. The key questions are whether small businesses view the services provided by commerical banks as clustered or unclustered, and how they view these services compared to those provided by other suppliers.

From a theoretical standpoint, we have seen that if commercial banks in fact offer a unique service of significance to small businesses or if they offer a cluster of services for which there are no significant alternatives, then the product of commercial banks may reasonably be viewed by the courts as separate from that offered by other types of financial service suppliers. Since the financial services industry has undergone explosive changes in the last couple of years, and since much of the empirical evidence on this question is now dated, it seems advisable to take a new look at the situation.

This section pulls together the evidence from three recent surveys aimed at the line of commerce question. First, David Whitehead reports on a survey of small businesses in the Southeast which was initiated by the Federal Reserve Bank of Atlanta's Research Department. This survey gathered evidence on where small businesses obtain financial services and what actual and potential sources for these services they perceived. The second survey, described by Bill Cox, was also initiated by the Federal Reserve Bank of Atlanta's Research Department, and gathered evidence on the pricing of NOW accounts by commercial banks and savings and loan associations. The objective of this study was to assess the extent to which commercial banks and savings and loans compete through pricing for NOW accounts. Federal Reserve Board economist Cynthia Glassman presents the third survey, initiated by an interagency task force and aimed at establishing what alternative sources exist for financial services used by small businesses. This survey questioned senior loan officers at commercial banks throughout the country. Each of these surveys offers a new perspective on an old issue.

The Sixth District Survey of Small Business Credit

Since little current evidence is available on sources of small business financing, in October 1981, the Federal Reserve Bank of Atlanta sponsored a survey of small businesses located within the six states which comprise the Sixth Federal Reserve District: Alabama, Florida, Georgia, Louisiana, Mississippi and Tennessee.[51] The survey questionnaire and sample population were designed by the research staff of the Federal Reserve Bank of Atlanta, with the assistance of members of the staff of the Board of Governors and the staff of the University of Florida's Bureau of Economic and Business Research.[52]

Survey Results

The survey supports the court's insistence that small commercial businesses tend to be limited to their local community for financial services. Local banks dominate the supply of every service (except leasing and trade credit). The vast majority of businesses which obtained the following types of services, received those services from their local bank: unsecured personal loans, secured personal loans, unsecured business loans, loans secured by real estate, loans secured by business inventory, loans secured by business equipment, loans secured business receivables, business checking services, night depository facility, and lock box services. Local banks are active in providing business trust services, payroll services, cash management and to a lesser extent leasing facilities.

Small businesses in small communities tend to be more dependent on banks as a source of financial services than are small businesses in larger communities. In nine out of the ten financial service categories listed above, banks in small and/or medium size communities supplied these services to a greater degree than banks in large communities. This fact, in concert with the extremely high percentages in each of these categories, indicates that the Supreme Court's assertion in the Philadelphia case tends to be correct: small businesses tend to be constrained to local sources for financial services and banks are a major supplier of these services at least for small businesses (see Table 1).

The survey found that commercial banks are the major source for most financial services used by small businesses. Table 2 shows that 584 of the 612 small businesses used business checking

Table 1

Percentage of Firms Which Obtained the Given Services Through a Local Commercial Bank

City Size	Unsecured Personal Loans	Secured Personal Loans	Unsecured Business Loans	Loan Secured by Real Estate
Large	76.8	94.2	83.5	64.7
Medium	87.5	91.5	87.5	74.5
Small	91.7	89.6	91.8	70.9
Number of Firms	282	287	283	237
	Loan Secured by Business Inventory	**Loan Secured by Business Equipment**	**Loan Secured by Business Receivables**	**Leasing**
Large	78.7	69.9	79.5	2.9
Medium	71.4	83.8	88.2	4.0
Small	82.3	81.0	73.6	17.6
Number of Firms	161	187	99	15
	Trade Credit	**Business Checking Account**	**Business Night Depository**	**Lock Box Service**
Large	13.1	93.9	95.3	93.6
Medium	28.6	94.8	100.0	94.4
Small	14.1	96.7	96.4	92.8
Number of Firms	28	583	194	138
	Cash Management	**Payroll Service**	**Business Trust Services**	**Other**
Large	38.5	46.2	56.3	25.0
Medium	100.0	63.6	85.7	25.0
Small	37.5	55.0	76.2	50.0
Number of Firms	23	47	31	13

accounts obtained from a local commercial bank; that's better than 95 percent. Only 5 businesses responded that they obtained business checking services from savings and loan associations. Commercial banks, local and nonlocal, supplied 635 of the 655 business checking services provided, or better than 97 percent. Some small businesses used more than one source for a given service; business checking accounts were no exception.

The evidence on this single service is overwhelming. Commercial banks as a group hold an effective monopoly providing checking accounts services to small businesses. In terms of perceived potential sources for business checking account services, 99 percent of the respondents indicate only commercial banks as a potential source for this service. Therefore, the empirical results indicate that commercial banks do hold a monopoly over at least one significant product, checking services, which is sufficient to differentiate commercial banking from all other types of financial service suppliers.

Local commercial banks also supply significant amounts of other services (Chart 1). In the loan categories, these percentages range from 69 percent to 91 percent indicating that commercial banks are a significant source for small business borrowings. Commercial banks are not a significant supplier of leasing services, accounting for only 9 percent of those using this type of service. Better than 93 percent of the local businesses using lock box services or night deposit facilities use local commercial banks. And in the remaining categories of services, a significant percentage of

Chart 1.
Percentage of Business Firms Using a Given Service Obtained from a Local Bank

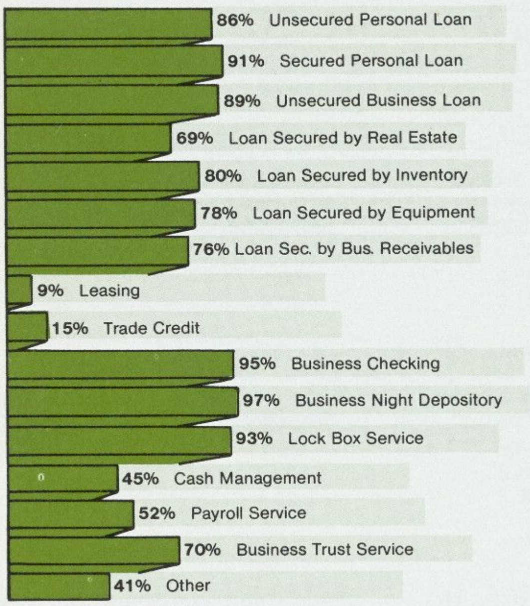


Table 2. Preliminary Summary of Survey Results

SERVICES	Personal	Local bank	Local office of nonlocal but in-state bank	Bank within state with no local area office
Unsecured personal loans	85	282	9	7
	21.3	70.5	2.3	1.8
Secured personal loans	17	288	11	5
	4.6	78.3	3.0	1.4
Unsecured business loans	50	284	17	6
	13.4	76.3	4.6	1.6
Loan secured by real estate	17	237	27	10
	3.8	53.4	6.1	2.3
Loan secured by business inventory	8	161	9	4
	3.5	71.2	4.0	1.8
Loan secured by business equipment	8	187	14	4
	2.9	67.0	5.0	1.4
Loan secured by business receivables	2	100	10	1
	1.4	71.9	7.2	0.7
Leasing	4	15	—	—
	2.3	8.6	—	—
Trade credit	4	28	—	—
	1.9	13.5	—	—
Business checking account	6	584	34	5
	0.9	89.2	5.2	0.8
Business night depository	2	194	8	—
	1.0	94.2	3.9	—
Lock box service	—	139	7	—
	—	90.8	4.6	—
Cash management	1	23	3	—
	1.9	42.6	5.6	—
Payroll service	2	47	1	1
	2.1	48.5	1.0	1.0
Business trust services	1	31	3	2
	2.1	64.6	6.3	4.2
Other	—	13	—	—
	—	39.4	—	—

businesses using these services obtain the service through their local bank.

Evidence on Clustering of Services

The basic question approached in this section is: do small businesses perceive commercial banks as offering a set of independent services or as providing these services in clusters? Our survey suggests that small businesses use a variety of services of local banks, and that they perceive the local banks to be offering a cluster of services.

> "Commercial banks are the major source for most financial services used by small businesses."

Only 59 firms used a single financial service while 642 firms used multiple financial services. Better than 67 percent of the firms which used financial services used between two and six services. The average number of financial services used was 4.78 (Table 3). Thus, the question of whether or not banks cluster services for small businesses is indeed a relevant one.

A second important finding is that there are significant alternative sources for some of these financial services. Quite obviously for business checking services, business night depository and lock box services, there are no significant alternatives to commercial banks; less than five per-

SOURCES

Out-of-state bank with local office	Out-of-state bank	Savings and loan association	Commercial finance company	Mortgage company	Factor	Leasing company	Inventory suppliers	Consumer finance company	Other	Total sources selected Total response	Total samples selected this service Valid cases
—	5	1	1	—	3	—	2	—	5	400	329
—	1.3	0.3	0.3	—	0.8	—	0.5	—	1.3	100.0	
2	10	18	5	3	—	—	1	1	7	368	315
0.5	2.7	4.9	1.4	0.8	—	—	0.3	0.3	1.1	100.0	
—	6	2	1	—	—	—	2	—	4	372	321
—	1.6	0.5	0.3	—	—	—	0.5	—	1.1	100.0	
1	7	87	2	36	—	1	—	—	19	444	342
0.2	1.6	19.6	0.5	8.1	—	0.2	—	—	4.3	100.0	
2	6	2	12	—	3	1	9	2	7	226	202
0.9	2.7	0.9	5.3	—	1.3	0.4	4.0	0.9	3.0	100.0	
2	5	1	19	1	3	17	7	—	11	279	241
0.7	1.8	0.4	6.8	0.4	1.1	6.1	2.5	—	4.0	100.0	
1	4	1	5	2	6	1	1	—	5	139	129
0.7	2.9	0.7	3.6	1.4	4.3	0.7	0.7	—	3.6	100.0	
—	4	—	14	—	—	119	6	—	12	174	161
—	2.3	—	8.0	—	—	68.4	3.4	—	6.8	100.0	
1	4	—	4	—	10	4	141	3	5	207	183
0.5	1.9	—	1.9	—	6.3	1.9	68.1	1.4	2.4	100.0	
2	10	5	1	—	2	2	—	1	3	655	612
0.3	1.5	0.8	0.2	—	0.3	0.3	—	0.2	0.5	100.0	
—	—	1	—	—	—	—	—	—	1	206	201
—	—	0.5	—	—	—	—	—	—	0.5	100.0	
—	—	3	—	—	—	—	2	—	2	153	149
—	—	2.0	—	—	—	—	1.3	—	1.4	100.0	
—	2	1	—	—	—	—	—	—	24	54	51
—	3.7	1.9	—	—	—	—	—	—	44.5	100.0	
1	5	2	—	1	—	—	—	—	37	97	91
1.0	5.2	2.1	—	1.0	—	—	—	—	38.1	100.0	
—	1	2	—	—	—	—	—	1	7	48	44
—	2.1	4.2	—	—	—	—	—	2.1	14.7	100.0	
—	3	2	1	—	1	1	—	1	11	33	32
—	9.1	6.1	3.0	—	3.0	3.0	—	3.0	33.4	100.0	

Note: Top number in each row is the number of firms using a given service. (one firm may use more than one source.) Bottom number in each row is the percent of firms that received a service from a given source.

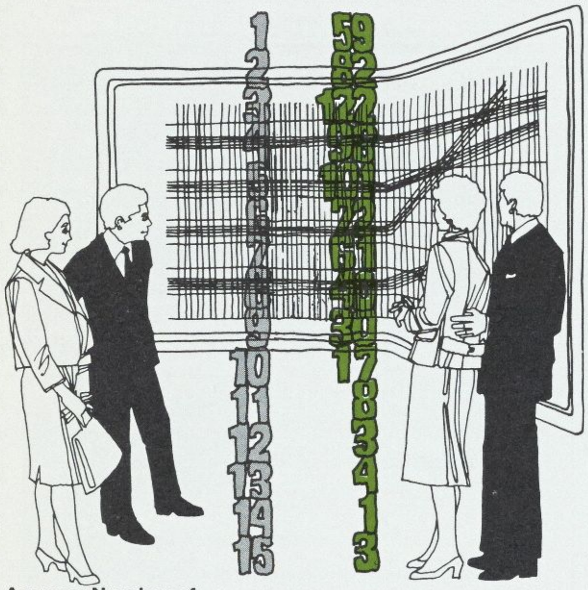
cent of the businesses surveyed which used this service obtained the service from nonbank sources (Chart 2). As far as the loan categories are concerned, the significance of nonbank suppliers of secured personal loans, unsecured business loans, loans secured by inventory and loans secured by business receivables is questionable; more than 80 percent of all small businesses surveyed which used these services obtain that service from commercial banks. However, given that 20 or more percent of those businesses which actually used one of the remaining categories of loans obtained that service from a nonbank source, it seems reasonable to assume that there are significant alternative sources for these services. Therefore, for at least some of the financial services offered by commercial banks, nonbank suppliers represent significant alternatives.

Third, we found strong evidence that businesses behave as if commercial banks are clustering their services. Only 35 of our sampled small businesses used only the checking account ser-

> "Our survey suggests that small businesses use a variety of services of local banks, and that they perceive the local banks to be offering a cluster of services."

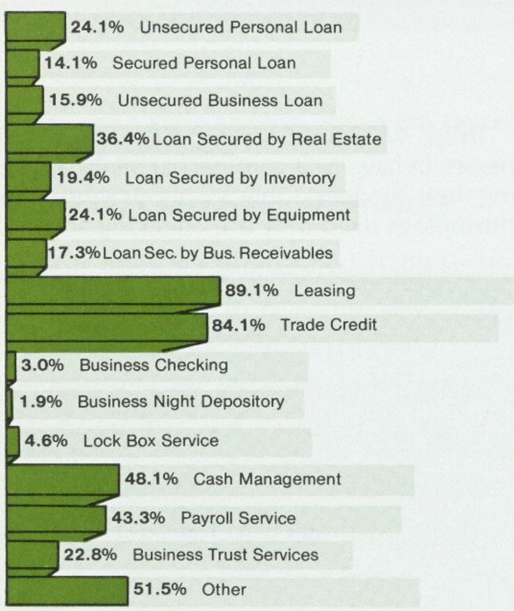
Table 3
Number of Businesses Which Use Checking Accounts at Local Bank and Obtain All Other Financial Services from That Bank

Number of Services Obtained | Number of Businesses



Average Number of Services Used: 4.78 Total: 701

Chart 2.
Percentage of Business Firms Using a Given Service Obtained from a Nonbank Source



vices of local banks or local offices of nonlocal banks. No business reported using only the checking account service at the other three types of commercial banks listed. Since only commercial banks may offer checking accounts to commercial consumers, commercial banks as a group are monopoly suppliers of checking account services. Each commercial bank, however, must compete with every other commercial bank in its market for these deposits. Since legislation prohibits the payment of interest on demand deposit accounts, commercial banks may not compete for customers through explicit prices of their checking account services. Instead, they compete on a nonprice basis, i.e. convenient locations and competitive prices on other financial services. In effect, the price charged commercial customers for another financial service or for a package of other services may partly reflect the implicit price of the commercial checking account. Thus, the lower the price for the other financial service or for the package of services, the higher the implicit price the bank is paying the commercial customer for its demand deposit account.

Therefore, if a large number of firms held just the exclusive service, it would indicate a lack of effective clustering. Since less than 6 percent of the businesses which held checking accounts with local banks used only the checking account services, this is consistent with the clustering of services hypothesis.

In fact, 35 percent of the firms responded that they obtained their checking account services and all other financial services they used from a local commercial bank. Fifty-one percent of the firms holding checking accounts with local banks obtained financial services from the local bank and other sources. This indicates that even if banks cluster their services, a significant number of firms use not only the cluster, but nonbank sources as well. Only 7 percent of firms holding checking accounts at local banks used only sources other than their local commercial bank for other financial services, and each used only one other type of service. Given the large number of businesses using multiple financial services and the large percentage of businesses sampled holding checking accounts at local banks, the 7 percent obtaining other financial services from sources other than their local bank gives strong evidence that businesses behave as if commercial banks are clustering their services. The commercial customer is either taking advantage of one-

"We found that significant nonbank alternatives exist for a majority of the services offered by commercial banks."

stop banking or is taking advantage of the package of services.

Interestingly, 68 percent of the businesses that did not hold checking accounts with a local bank use financial services obtained from a local bank. Of these, 70 percent use more than a single service from a local bank. These businesses represent twenty percent of all businesses in the sample. This evidence indicates that local commercial banks may not be completely successful in linking other services to checking. For a variety of reasons, businesses may use nonlocal banks for checking and local banks for other financial services.

The preliminary results of the survey offer consistent evidence that business firms use multiple services of local banks. This is consistent with the view that businesses perceive commercial banks as offering a cluster of services. In addition, we found that significant nonbank alternatives exist for a majority of the services offered by commercia! banks.

Given the criteria set forth in the Connecticut Case for evidence sufficient to broaden the line of commerce definition for commercial banking, the empirical evidence presented from this survey supports no change at the present time. Although there were significant alternatives for a number of the services provided by commercial banks to small businesses, commercial banks still maintain the exclusive ability to offer small business checking accounts, and small businesses tend to use the services offered by commercial banks as if they were clustered.

—David D. Whitehead

The Sample Design

To choose our sample, we took a slice of cities in our District, then we took a slice of businesses within those cities. The sample population consisted of all businesses listed on membership roles of all chambers of commerce within the six states. We stratified the chambers into three groups, depending upon the population size of their respective communities: greater than one million, less than one million but larger than 250 thousand, and less than 250 thousand. The population figures are based on the 1980 preliminary Census counts.

Within each of these strata, we drew the sample population in the following way. Only four Sixth District SMSAs contain populations greater than one million: Atlanta, New Orleans, Tampa-St. Petersburg and Miami. For this reason, we included all four of these SMSAs. Then we randomly selected ten counties each from the second and third strata. The number of counties selected from each state was based on that state's portion of the District's total population. Table A presents a complete list of the chambers of commerce included in the sample.

From the membership roles of the selected chambers of commerce, we selected at random a sample of 5,031 businesses. We took 40 percent of the sampled businesses from strata one and 40 percent from strata two, with the remaining 20 percent from strata three. The number of businesses chosen from each list was in proportion to the total number of businesses listed on the chamber's membership role within each strata. Prior to the selection, we eliminated all professionals, financial institutions, clubs, public service organizations and individuals, as well as all businesses employing more than 100 people.

For purposes of the survey, we defined a small business as any business employing more than three and less than 100 employees. The selected sample included both small and larger businesses because in many cases no size measure was included on the membership listing. Therefore, each firm surveyed was asked for the total number of full-time employees they employed. If their total was larger than 100 or less than three, they were asked to disregard the remainder of the questions and return the questionnaire.

A total of 5,031 survey questionnaires with stamped return envelopes and cover letters were mailed during the first week in November, 1981. By the end of November, 1,445 questionnaires were returned. Of the questionnaires returned, 734 (51 percent) were small businesses, 426 (29 percent) were not small businesses and 285 (20 percent) were returned as undeliverable due to address changes or businesses which had gone out of existence. All non-respondents who agreed in a telephone follow-up to participate in the survey and who qualified as a small business were mailed a second questionnaire. As of this writing, 733 usable questionnaires have been returned.

Description of Firms Surveyed

Over 27 percent of the firms responding provided services, while 25 percent were in the retail trades. Manufacturing and wholesale firms accounted for 14 percent each of the responses. Financial services accounted for 9 percent, transportation and communication for 4.6 and building materials for 4.6. Agricultural related firms represented the remaining 2 percent. The firms responding to the questionnaire, therefore, cover a broad product spectrum.

The geographic distribution of respondents based on state is heavily skewed (50 percent) toward Florida. The recognition factor by businesses receiving the questionnaires from the University of Florida's Bureau of Economic and Business Research probably had a great deal to do with the heavy response from Florida businesses. Responses from Alabama numbered 102 (14 percent), 98 (13 percent) from Georgia, 97 (13 percent) from Louisiana, 44 (6 percent) from Mississippi and 25 (3 percent) from Tennessee.

In response to the question concerning whether or not the responding firms were affiliated with or a subsidiary of another firm, 88 percent responded that they were independent organizations. In addition, when asked where within their organization financial decisions were made, 87 percent of those responding asserted that financial decisions were made locally, 5 percent said they were made jointly with the home office, and only 8 percent responded that financial decisions were originated by the parent organization. The vast majority of those firms responding, therefore, are assumed to be local operations.

As a relevant measure of firm size, we chose to key on employment. The majority, 55 percent, of firms responding to our survey employed ten or less employees. Thirty percent of the respondents employed between 11 to 30 employees, while nine percent employed between 31 and 50. The remaining 6 percent employed from 51 to 100 employees. This tends to confirm that the firms responding to the survey were indeed small businesses. In addition, most of these small businesses are apparently well established in that they have been in business for five years or longer. Over 88 percent of those responding to this question indicated that their organization had been in business for five years or more, 11 percent had been in business from 1 to 5 years, while only 1 percent had less than a year of experience. Therefore, the firms which comprise the respondent group were not only small, but the large majority of those firms had more than five years of business experience.

Table A

Chambers of Commerce Included in the Sample

SMSAs More Than One Million

	COUNTY	CHAMBER OF COMMERCE
Atlanta	Fulton	South Fulton
		North Fulton
	Rockdale	Conyers Rockdale
	Walton	Walton County
	Henry	Henry County
	Fayette	Fayette County
	Clayton	Clayton County
New Orleans	Orleans	New Orleans
	St. Tammany	Covington
Tampa-St. Petersburg	Pinellas	St. Petersburg
	Hillsborough	South Tampa
	Pasco	West Pasco
Miami	Dade	Hialeah-Miami Springs
		Coral Gables
		North Dade
		Latin
		Miami Beach

Counties in SMSAs of less than one million

STATE	COUNTY	CHAMBER OF COMMERCE
Alabama	Etowah	Gadsden Metro
	Madison	Huntsville/ Madison County
Florida	Leon	Tallahassee Area
	Alachua	Gainesville
	Nassau	Fernandina Beach/Amelia Island
	Polk	Lakeland Area
Georgia	Chatham	Savannah Area
Louisiana	Calcasieu	Greater Lake Charles
Mississippi	Harrison	Biloxi and Harrison County
Tennessee	Sumner	Hendersonville

Counties in Non-SMSAs

STATE	COUNTY	CHAMBER OF COMMERCE
Alabama	Pike	Pike County
	Dale	Ozark-Dale County
Florida	Franklin	Apalachicola
	Calhoun	Calhoun County
Georgia	Appling	Appling
	Johnson	Wrightsville-Johnson County
Louisiana	Plaquemine	Plaquemine-Iberville
	Terrebonne	Houma-Terrebonne
Mississippi	Franklin	Franklin County
Tennessee	Giles	Giles County

Do Banks Price as if Thrifts Matter?

In the Philadelphia National decision, the Supreme Court held that banking is "local, unique and comprised of a cluster of retail financial services," something like a financial department store. In assessing the validity of the 1963 decision in the deregulating financial world of 1982, one of the aspects we need to examine is the competition between commercial banks and thrift institutions in local retail markets. Beginning in 1980, savings and loan associations across the nation were given expanded powers to compete with banks in offering services such as interest-bearing checking (NOW) accounts, consumer loans, and credit cards, in addition to their traditional offerings of consumer savings instruments and mortgage loans.

Do banks in markets where thrift institutions are abundant set cheaper prices than banks in markets where thrift institutions are scarce? If the answer is yes, then it means the banks behave as if the thrifts are competitors, and it would follow that regulatory analysis of retail "banking" markets should include the thrifts as well as the banks.

In this context, the banks are the key actors. It is already evident that savings and loan associations in the Southeast themselves believe they are in competition with the banks.[53] *Some* customers, at least, regard similar products from the two types of institutions as substitutes, for they have signed up with the thrifts for NOW accounts and for other services previously offered by banks. But unless the banks make competitive decisions as if thrifts matter, or unless they can be expected to do so in the future, there is reason to question whether thrifts should be included in the regulatory analysis of banking markets.

"Unless banks make competitive decisions as if thrifts matter, . . . there is reason to question whether thrifts should be included in the regulatory analysis of banking markets."

The simplest and best evidence comes from pricing decisions of the banks. Do the pricing patterns of banks in various geographic markets of the Southeast suggest that banks respond to a competitive presence from savings and loan associations?

To find out, we recognized that competition between banks and thrifts is essentially local and we chose to define "local" as the standard metropolitan statistical area.[54] There are 43 SMSAs within the six states of the Sixth Federal Reserve District. We selected 22 of them to represent the full variety of structural situations in the Southeast.

Next, we developed a measure of the extent of thrift competition in each market: the number of thrift *offices* divided by the number of thrift *and* bank offices in the market area.[55]

Within each of the 22 markets, now characterized by a measure of thrift competition, we looked at the prices posted by banks on three relatively new and important products offered by both banks and thrifts in every market area: (1) NOW accounts represent the entry by S&Ls into the basic bank product of checking accounts. As a "price," we used the minimum balance required for charge-free checking. (2) The small-savers certificate (SSC), offered with a 30-month maturity and no minimum balance requirement by virtually all institutions, represents an offering by banks in the more traditional territory of the thrifts. For the price, we chose the interest rate offered at year-end 1981.[56] (3) For the six-month "money market" certificate (MMC), with a minimum balance of $10,000, we chose year-end interest rates offered by each bank as the relevant price.

"On NOW account minimums at banks, there was no significant difference between high thrift markets and low thrift markets."

For each of the 22 southeastern market areas selected, we called several banks, calling one for every $100 million in total bank deposits in the market area. In all, we called 85 banks, with the number in each market area ranging from seven in the Miami SMSA to two in the Gainesville (Florida) SMSA.

We analyzed these data two ways. First, we calculated correlation coefficients between the bank prices and the percentage measure of thrift offices, to see if banks adjusted prices when they faced a higher percentage of thrift offices. If banks respond to thrift competition, in other words, the coefficients should be negative for NOW prices and positive for the MMC and SSC rates. They are not:

NOW Minimum Balance vs. Thrift office percentage: (wrong sign)	.22
SSC Rate vs. Thrift office percentage: (insignificant)	-.03
MMC Rate vs. Thrift office percentage: (insignificant)	.00

As a second way of assessing the same data, we ran standard statistical tests to see if bank prices in the eleven markets with the highest percentages of thrift offices differed significantly from bank prices in the eleven markets with the lowest percentages:

On NOW account minimums at banks, there was no significant difference between high thrift markets and low-thrift markets. (Minimums in

Table 1

NOW Analysis by Market
(Minimum dollar balances for free NOW checking)

Market	Bank Average		S&L Average		Bank average minus S&L average	
	1-1-81	12-31-81	1-1-81	12-31-81	1-1-81	12-31-81
Birmingham	1417	1417	513	275	904	1142
Huntsville	1333	1333	50	50	1283	1283
Tuscaloosa	1500	1500	400	275	1100	1225
Daytona	1250	1250	450	450	1100	1225
Gainesville	1000	1000	300	300	700	700
Miami	1386	1386	3683	3517	−2297	−2131
Tampa	1036	1036	313	313	723	723
West Palm Beach	1900	1900	433	233	1467	1667
Atlanta	1143	1071	667	483	476	588
Augusta	900	900	500	500	400	400
Columbus	1000	650	400	275	600	375
Savannah	967	967	425	100	542	867
New Orleans	1429	1457	667	433	762	1024
LaFayette	800	800	500	417	300	383
Lake Charles	2400	2400	525	275	1875	2125
Baton Rouge	1700	1700	500	375	1200	1325
Biloxi	1500	1500	633	533	867	967
Jackson	1500	1500	1050	925	450	575
Chattanooga	1000	1000	300	300	700	700
Kingsport-Bristol	750	625	350	350	400	275
Knoxville	1125	1375	533	300	592	1075
Nashville	1667	1667	150	650	1517	1017

the high-thrift markets averaged $1,370; mimimums in the low-thrift markets averaged $1,173. We tested for a statistically significant difference between the means at a 95% confidence level, and found none.)

On Small Saver Certificate interest rates at banks, there was no significant difference between high-thrift markets and low-thrift markets.

On Money Market Certificate interest rates at banks, there was no significant difference between high-thrift markets and low-thrift markets. (Most banks offered the maximum permissible rate, but there were a significant number of offerings below the maximum in four of the 22 markets sampled. The proportion of banks offering less than the maximum was also unrelated statistically to the percentage of thrift offices.)

So in both the correlation tests and the high-versus-low thrift percentage tests, there is no support for the hypothesis that banks price as if thrifts matter.

Banks, of course, respond to competition from other banks. It is possible that more competition among banks could be masking the price effects associated with less thrift competition, and vice versa. The conventional test for that possibility would be a multiple regression of bank prices on S&L presence and banking structure, with each market contributing an observation. Instead, we substituted a simpler and equally adequate test. Specifically, we are interested in the case in which the "banking structure effect" on bank prices cancels or masks the actual "effect of S&L presence" on bank prices.Such masking of the genuine bank response to thrifts would produce a false "no response" signal, in our correlation tests. For that to happen, S&Ls would have to have a strong presence in markets which have

"... there is no support for the hypothesis that banks price as if thrifts matter."

Chart 1. Spread* Summary

1/1/81 to 12/31/81

Spread Rose (12)

Spread Fell (4)

No Change (6)

*The bank average minimum balance for free NOW account service minus the savings and loan average.

less competition among banks. Assuming that less competitive means more concentrated, we looked for such a systematic relationship in our 22 markets and found none. We accordingly reject the notion that interbank competition is masking the bank response to thrifts.

None of these tests lent any support to the hypothesis that banks adjust their NOW prices in response to S&L competition. However, this cannot necessarily be taken as evidence that they do not. In search of a more conclusive result, we took a slightly different look at the NOW accounts. In a competitive situation, products in the same geographic and product markets should show little variance in price, or at least their prices should be converging. This is one statistical indication that competition exists.

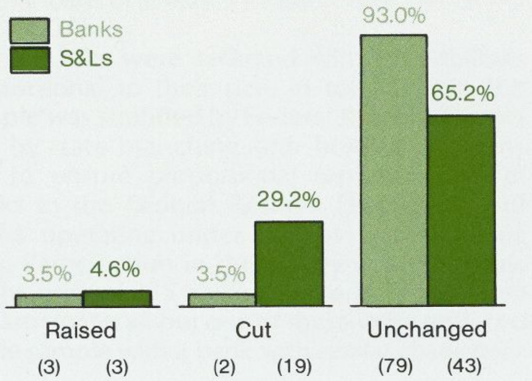
We took another look at our existing sample of banks and savings and loans from the 22 markets.[57] The first thing we observed is that when compared in either January or December of 1981, bank NOW minimums are at substantially higher levels than those of S&Ls: Banks' charge-free minimums averaged $1,305 and $1,292, respectively, for the beginning and end of 1981. Compare this with the $621 and $540 averages at S&Ls in the same markets at the same times. (See Table 1 for a market-by-market breakdown.) Banks, moreover, held the line over the year, whereas the average S&L minimum fell by 13 percent. So the bank-thrift difference widened, rather than shrank.

Next, we looked at each of the 22 sample markets individually to examine how the difference between the bank and S&L NOW minimum balances changed from the beginning to the end of 1981. The difference increased in 12 markets, remained the same in six, and decreased in four (chart 1). In fact, almost 30 percent of the S&Ls cut their prices, while less than four percent of the banks cut theirs (chart 2). None of these observations support the hypothesis of bank-thrift competition for NOW accounts.

The structure of banks and savings and loans relative to NOW accounts at least outwardly

"Banks, however, make no effort to match the S&Ls' lower prices, being content to keep their NOW minimum balances at a high and profitable level while their advantage lasts."

Chart 2. NOW Price Changes by Institution
1/1/81 — 12/31/81



resembles a "dominant group" model of industrial organization. Banks dominate the field of those offering transactions services, of which NOWs are one, because people have traditionally gone to banks for this service. This traditional preference for bank transaction accounts serves as a barrier to entry to S&Ls trying to break into this field of financial services with NOWs. Acting as a competitive fringe, the savings and loans enter the field with NOW prices considerably lower than those offered by the dominant group, banks, and begin competing principally among themselves to gain a larger share of the NOW accounts the banks do not handle. Banks, however, make no effort to match the S&Ls lower prices, being content to keep their NOW minimum balances at a high and profitable level while their advantage lasts.

One implication of this model is that if bank and S&L NOWs are truly substitutes, the S&Ls will eventually gain a large enough share to force banks to cut their NOW prices. As S&Ls become more acceptable as vendors of transactions accounts, the barrier to their entry into this market will dissolve. Then banks would be forced to compete with the S&Ls for NOWs or face losing a significant portion of their market share.

In this analysis we have used price data for NOWs, six-month money market certificates and small savers certificates to test the hypothesis that southeastern banks adjust their prices for these instruments in reaction to local savings and loan competition. We found that correlation coefficients between the strength of S&L presence in the 22 markets and bank prices for these services did not have the expected signs and were not statistically significant as would be necessary if the banks were reacting to the thrifts. We found that there is no statistical difference between the average prices of banks with many S&L offices locally and those with few local S&L offices. And we found that banks price their NOWs much more dearly than S&Ls and that this gap appears to be widening. Our findings did not support the hypothesis that banks in the Southeast price as if thrifts matter.

—William N. Cox
and Joel R. Parker

Evidence from the Banking Side

In deliberations as to whether commercial banking should continue to be treated as a separate line of commerce, the product known as "small-business financing" plays an important role. Lending to small businesses is one of the few—if not only—remaining activities of commercial banks for which there are considered to be very limited alternatives. Changes in the financial environment stemming from deregulation or market forces have resulted in growing competition for the business of most other customers of commercial banks. For example, on the asset side, banks compete with the commercial paper and Eurodollar markets for larger-business loans and with finance companies, credit unions, and credit card companies for consumer loans. On the liability side, thrift institutions and money market funds have become significant factors in the market for savings and transactions accounts.

A recent nationwide survey of commercial bank small-business lending practices sheds light on the questions of whether nonbank sources of credit are available to small businesses and, if so, whether they are active in small-business lending. The survey was conducted jointly by the Board of Governors of the Federal Reserve System, the Office of the Comptroller of the Currency, and the Federal Deposit Insurance Corporation as a part of a study on the extent to which commercial banks are meeting the credit needs of small businesses.[53]

Survey Description

The survey, conducted in September 1981, was a personal interview—by economists from the Federal Reserve District Banks and the Washington, D.C. offices of the three federal bank regulatory agencies—with senior loan officers knowledgeable about small-business lending at the sample banks. A sample of 224 banks was chosen to represent the universe of 10,309

> "Banks believe they provide 63 percent of the total debt of their small business customer."

federally insured commercial banks in the continental United States with commercial and industrial loans of at least $1 million as of December 31, 1980.[54]

The banks were selected with probabilities proportional to their size, in total assets. The sample was stratified by Federal Reserve District and by state branching and holding company law to ensure proportional representation of banks in the Federal Reserve Districts and of banks operating under various state banking laws. Participation in the survey was voluntary. Of the original 225 banks selected, five declined to participate; all but one of these were replaced in the sample with a bank with similar characteristics.

The definition of small business was of primary importance in designing the survey. The basic concept of small business was nonfarm firms that are independently owned and limited to local sources of financing. Banks were told to use their own definition if they had one in responding to questions. Banks without a definition, principally small banks whose business loans are generally limited to small-business loans, were given a definition by the interviewer: under $2.5 million in annual sales; or under $2.5 million in assets; or less than $1.0 million in loans outstanding at the bank.

The survey questionnaire covered six topics: bank organization with respect to small business lending; credit availability; loan characteristics; pricing and profitability; government programs; and data availability. The questions in the section on credit availability are the ones relevant to the line of commerce issue.[55]

Analysis of Data

In the analysis of the survey data, each bank's responses were weighted by the inverse of the probability of selection of the bank. The weight of a bank in the sample can be interpreted as the number of banks in the population that it represents. For example, if a bank was selected with a probability of one-tenth, it can be viewed as representing itself plus nine other banks. Thus, the larger the bank, the lower the weight, since the larger the bank, the fewer other banks it represents. The data presented reflect the weighted responses and therefore are estimates for the population. It must be emphasized that the survey results generally apply only to businesses with which the banks *already* had a relationship and that the estimates presented reflect *only* the banks' perceptions, *not* the perceptions of their competitors or their customers.

Table 1

Of the small businesses to which you provide credit, about what percentage share of their total debt is supplied by your bank and by other commercial banks?

Share of Small-Business Debt Supplied by Commercial Banking Sector
(Percent)

	Average Share[a]		
Banks	Individual bank	All other commercial banks	Total
All banks	63 (55,71)	9 (5,13)	72
By asset size			
<$100 mil.	63 (47,79)	10 (6,14)	73
$100 mil. <$1 bil.	65 (57, 73)	7 (6,8)	72
>$1 bil.	59 (53,65)	6 (5,7)	65
By location			
Urban	67 (53,81)	6 (4,8)	73
Suburban	53 (39,67)	12 (2,22)	67
Rural	65 (55,75)	10 (4,16)	75

a — 95% confidence interval in parenthesis.

The banks were asked a series of questions designed to assess the importance of the commercial banking sector as a source of financing for small business as well as to determine what other sources are available and active. The first of these questions was the following: "Of the small businesses to which you provide credit, about what percentage share is provided by your bank?" On average, the banks believe they provide an estimated 63 percent of the total debt of their small-business customers. In addition, they believe that about 9 percent of their small-business customers' total debt is supplied by other commercial banks. Thus, banks perceive that the commercial banking system provides nearly three-quarters of the total debt of small businesses with which they have a relationship.[56] This perception does not appear to be related to size or primary location of the bank. (See Table 1).

The majority of banks believe that the percentage share of the total debt they supply to their small business customers is about the

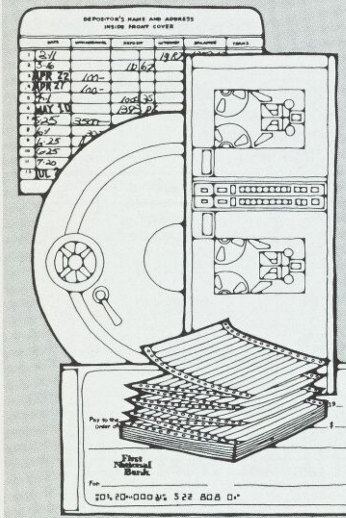


Table 2

Of the small businesses to which you provide credit, is the percentage share of their total debt supplied by your bank higher, lower, or about the same as compared to five years ago?

Change in Share of Total Small-Business Debt Supplied
(Percent of banks)

Banks	Share compared to five years ago[a]		
	Higher	Lower	About the same
All banks	31 (25,37)	7 (5,9)	57 (51,63)
By asset size[b]			
<$100 mil.	30 (16,44)	8 (2,14)	57 (43,71)
$100 mil. <$1 bil.	32 (18,46)	8 (0,16)	55 (41,69)
>$1 bil.	40 (28,52)	2 (0,4)	53 (41,65)
By location			
Urban	34 (14,54)	9 (−3,21)	42 (24,60)
Suburban	34 (10,58)	5 (−3,13)	56 (32,80)
Rural	28 (12,44)	8 (0,16)	64 (46,82)

a — 95% confidence interval in parenthesis.
b — Subgroup totals may not add to 100 due to nonresponse.

same as it was five years before the survey was taken. Close to a third believe their share is higher, while less than 10 percent believe it is lower. This perception does not differ significantly among subgroupings of banks based on size or location. (See Table 2).

The banks were also asked what additional sources of credit were available, and what sources were active, for small-business customers in their local areas. Not surprisingly, on average, more alternative sources were perceived by banks to be available than to be active. Also, differences in both availability and activity were apparent among subgroupings of banks (See Tables 3 and 4).

All banks think other commercial banks are available as a source of credit for small businesses in their local area. With the exception of a small percentage of banks in urban areas or in the South, banks believe other commercial banks are active lenders to small businesses. Thrift institutions (savings and loan associations, mutual savings banks, and credit unions) and finance companies are the two other sources of financing most often considered to be available and, to a lesser extent, active. Thrift institutions are considered to be available local sources of small-business credit by more than three-quarters of the banks. This estimate does not vary widely by primary location of the bank (urban, suburban, or rural). However, by census region, banks in the West appear to perceive greater thrift institution availability than in the other regions.

Substantially fewer banks perceive thrifts to be active, as opposed to available, lenders to small business—generally less than one-quarter of the banks in any of the location or census region subgroups, except in the West where activity of thrifts appears greater. The discrepancy between perceived availability and activity of thrifts in small-business lending may result from the changing legal and economic environment in which these institutions operate. With the passage of the Depository Institutions Deregulation and Monetary Control Act in March 1980, the lending powers of federally insured thrift institutions were broadened to permit more business lending, thus increasing the potential ability of these institutions to

Table 3

In your local area, which of these sources of credit are available to small businesses?

Available Small-Business Credit Sources
(Percent of banks)

Credit	All Banks[a]	By location: Urban	Suburban	Rural	By Census Region: Northeast	South	North Central	West
Other commercial banks	100	100	100	100	100	100	100	100
Thrift institutions	79(75,83)	86(78,94)	72(56,88)	79(65,93)	62(30,94)	83(69,97)	75(59,91)	95(89,101)
Finance companies	81(77,85)	91(83,99)	86(70,102)	76(60,92)	80(60,110)	89(79,99)	69(49,89)	100
Brokerage houses	20(14,26)	35(15,55)	25(9,41)	12(−2,26)	5(−1,11)	22(2,42)	11(1,21)	59(21,97)
Loan production offices	29(23,35)	56(38,74)	37(13,61)	16(4,28)	13(1,25)	31(15,47)	23(9,37)	59(21,97)
Insurance companies	49(43,55)	61(45,77)	45(27,63)	45(27,63)	35(5,65)	55(35,75)	40(20,60)	68(34,102)
Small business investment companies	24(20,28)	45(27,63)	37(15,59)	10(2,18)	61(31,91)	31(15,47)	13(3,23)	10(2,18)
Minority enterprise small business investment companies	10(6,14)	36(16,56)	7(−1,15)	0	28(6,70)	12(0,24)	5(1,9)	6(−2,14)
Noninstitutional sources	29(19,39)	36(16,56)	32(12,52)	25(9,41)	23(1,45)	24(8,40)	29(13,45)	55(19,91)
Direct federal	50(44,56)	75(61,89)	57(33,81)	37(21,53)	80(60,100)	59(39,79)	28(14,42)	80(56,104)
Direct state	22(16,28)	39(19,59)	8(0,16)	19(3,35)	41(9,73)	24(4,44)	14(4,24)	28(−10,66)

a — 95% confidence interval in parenthesis.

Table 4

In your local area, which of these are the more active lenders?

Active Small-Business Credit Sources
(Percent of banks)

Credit Source	All banks[a]	By location: Urban	Suburban	Rural	Northeast	By Census region: South	North Central	West
Other commercial banks	97(95,99)	89(69,109)	100	100	100	94(84,104)	100	100
Thrift institutions	13(9,17)	21(7,35)	19(3,35)	8(0,16)	25(−5,56)	9(−9,19)	9(1,17)	42(2,82)
Finance companies	23(17,29)	21(9,33)	60(40,80)	11(−3,15)	41(11,71)	26(8,44)	10(2,18)	52(14,90)
Brokerage houses	1(.5,1.5)	2(0,4)	2(−2,6)	0	*	1	1	*
Loan production offices	8(6,10)	10(0,20)	2	9(1,17)	1	4(−2,10)	9(−1,19)	25(−13,63)
Insurance companies	2(1,3)	6(0,12)	1	1(−1,3)	4(−2,10)	*	4(−2,10)	1(−1,3)
Small business investment companies	1(.4,1.6)	5(1,9)	1	0	8(−4,20)	*	2(0,4)	*
Minority enterprise small business investment companies	1(−.2,1.8)	3(−1,7)	4(−2,10)	0	2	1(−1,3)	2(0,4)	0
Noninstitutional sources	6(0,12)	3(1,5)	14(−6,34)	5(−1,11)	3(−1,7)	*	9(−1,19)	26(−10,62)
Direct federal	6(4,8)	9(−1,19)	20(−2,42)	0	21(−9,51)	2(0,4)	5(−1,11)	23(−13,59)
Direct state	*	1	0	0	1	*	0	0

a — 95% confidence interval in parenthesis.
* — Less than 0.5.

lend to small business. However, the deteriorating financial condition of many of these institutions, which reflects the volatility of the financial markets in recent years, may have inhibited thrifts from actual expansion into this new activity.

Finance companies are also generally perceived to be a local source of financing for small business by most banks - and by all banks in the West. Perceived activity of finance company financing varies widely among the subgroups, however. Banks whose primary market is a suburban area believe finance companies are active small-business lenders significantly more often (an estimated 60 percent) than do rural banks (11 percent) or urban banks (21 percent). Activity also appears to vary by Census region, with the least activity perceived in the North Central regions and the most perceived in the West.

None of the other listed potential sources of small-business credit was considered to be available in their local area by more than half the banks. These sources, in order of estimated perceived availability, are the following: direct federal lending (50 percent), insurance companies (49 percent), loan production offices (29 percent), noninstitutional sources (29 per-

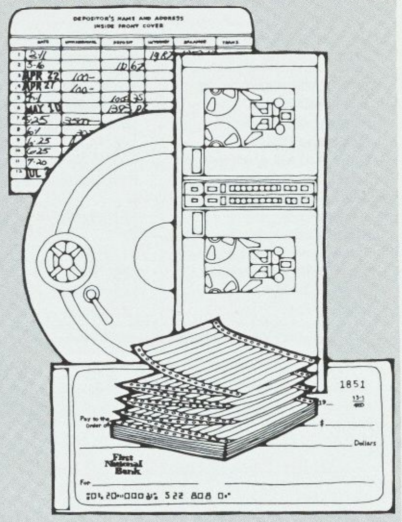
Table 5

In recent years, has the competition among lenders in your local area for small-business loans increased, decreased, or remained about the same?

Change in Competitive Environment[a]
(Percent of banks)

Direction of Change	All banks[a]	By location: Urban	Suburban	Rural
Increase	52 (46,58)	71 (53,89)	82 (70,94)	33 (15,51)
Decrease	3 (1,5)	5 (1,11)	0	4 (−4,12)
About the same	45 (39,51)	24 (6,42)	18 (6,30)	63 (45,81)

a — 95% confidence interval in parenthesis.



cent), small business investment companies (24 percent), direct state lending (22 percent), brokerage houses (20 percent), and minority enterprise small business investment companies (10 percent). None of these is considered an active source of small-business financing by more than 10 percent of all banks.

Despite the reported low levels of activity of non-bank small-business lenders, an estimated half of the banks believe competition for small-business loans in their local areas has increased in recent years, while very few believe it has decreased, and not quite half think the level of competition is about the same. (See Table 5). Bank location appears to be an important factor in whether the banks perceive a change in competition. Significantly more urban (71 percent) and suburban (85 percent) banks believe competiton has increased than do rural banks (33 percent), while significantly fewer urban (24 percent) and suburban (18 percent) banks believe competition is about the same than do rural banks (63 percent).

Reasons given for the perceived increase in competition are about equally divided between the following: a growing perception that small-business lending is attractive (13 percent), entry of nonlocal or nonbank competitors (18 percent), increased aggressiveness of existing competitors (15 percent), other reasons (15 percent).

In sum, the estimates based on the responses to the survey indicate that in general banks perceive that there are nonbank financing options for small businesses in their local area. However, the alternative sources are generally not considered to be active in small-business lending. Nevertheless, the majority of banks believe competition for small-business lending has increased in recent years.

The survey gives no information on whether the lack of activity of nonbank small-business lenders is due to lack of demand by small businesses for credit from the alternative sources, or lack of interest by these other sources in lending to small businesses.

—Cynthia A. Glassman

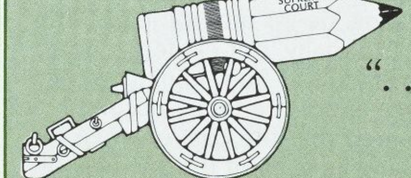
CONCLUSION

Our review of the relevance of the court's treatment of commercial banking as a separate line of commerce indicates that the courts are on solid ground both from a theoretical and empirical perspective. On a theoretical level, either a unique product or the fact that a significant group of consumers view the array of products offered by commercial banks as a cluster of services is sufficient to distinguish the product offered by banks from that offered by suppliers of other financial services. On the empirical side, we found that some small businesses obtain all their financial services from their local commercial bank.

The Monetary Control Act expanded the types of financial services which thrift institutions may supply to consumers and corporate customers. The unique position that commercial banks once enjoyed for consumer and corporate third party transaction services, demand deposit accounts, and commercial loans no longer exists. Effectively, the only unique position still enjoyed by commercial banks is the ability to offer third party transaction accounts to corporate customers.

To a large extent the courts' rationale for separating the product of commercial banks from that of all other suppliers of financial services for antitrust purposes has historically hinged on the uniqueness of commercial banks offering third party transactions accounts and financial services for small, locally constrained commercial customers. Because of the Monetary Control Act and the revolution within the financial services industry in recent years, this distinction between commercial banks and other types of financial institutions is brought into question.

Using the courts' criteria, we found empirical evidence that there are significant actual or potential alternative sources for each of the financial services offered by commercial banks. The legislative monopoly awarded to commercial banks as a group for offering business



"... the courts are on solid ground both from a theoretical and empirical perspective."

> "Because of the Monetary Control Act and the revolution within the financial services industry in recent years, this distinction between commercial banks and other types of financial institutions is brought into question."

checking accounts was found to be sufficient in and of itself to meet the court's criterion for separating commercial banks' product from the product of all other suppliers of financial services.

We also found that for most commercial services offered by commercial banks, there are significant alternative suppliers. We can argue over the term "significant," but all the empirical evidence points to the fact that alternative or potential alternatives exist for most of the individual services offered by commercial banks. The court's criterion, however, centered not on the availability of a single service, but on the availability of the cluster of services offered by commercial banks to a specific set of customers. New empirical evidence indicates that small businesses do indeed use a number of financial services (4.7 on average) and that they tend to obtain the vast majority of these services from local banks.

In short, the evidence supports the view that an identifiable proportion of businessmen operating small businesses obtain a number of financial services from local banks, or behave as if the commercial banks clustered their services. Again, in light of the evidence and the courts' criticism, it is still relevant to view commercial banks as offering a separate line of commerce.

The Supreme Court's definition of the product offered by commercial banks as a cluster of services implies that there are forces which encourage bank customers to view the cluster of services as a single product. There are at least three ways in which a group of services may be joined. First, suppliers of services may establish tie-in arrangements requiring the purchaser of a service to buy all services in the cluster from the supplier. Any number of services and any combination of services may then be presented to the customer as a cluster. Second, users of the services may find it more convenient to purchase all needed services from a single provider. This would effectively cut down on search and information costs to the customer. Or third, offering a wide array of services may allow the suppliers to take advantage of any agglomeration economies or economies of scale which may serve to lower the cost of any individual service to the customer.

Under these circumstances, commercial banks may be capable of providing the clustered services at a lower price than a single service provider.

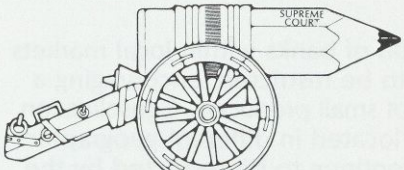
In addition, although commercial banks are unique among financial service suppliers in being able to offer commercial third party transactions accounts, they are prohibited from paying interest on these funds. Therefore, commercial banks must compete among themselves for corporate demand deposits by offering greater convenience, or reducing prices on services. This may mean presenting their array of services as a package or cluster. Reduced prices on any single service or the entire cluster would reduce the implicit cost to the commercial customer of holding non-interest bearing demand deposits. This is the economic rationale for commercial banks offering a cluster of services to small businesses. At the same time, it may explain why small businesses view the commercial bank services as a package or cluster.

Direct empirical evidence on the question of clustering of services is very difficult to obtain. In banking, tie-ins are not legal. They may be used informally, but evidence of tie-ins would be difficult to find. Joining services by convenience almost certainly occurs. It has often been argued that the convenience of one-stop banking links all of the services of the commercial banks and has given banks a substantial advantage in competing with other suppliers of individual services. The best evidence to confirm or deny this type of clustering would be an empirical finding that many consumers use a number of financial services offered by the commercial bank. In other words, do customers behave as if the services supplied by commercial banks are clustered?

Each of the three empirical studies on this question found evidence consistent with the assertion that small businessmen behave as if they perceive commercial bank services as a cluster. In addition, the Sixth District small business survey found that some 35 percent of the small businesses using financial services obtained from banks obtained all of their financial services from banks. In light of the Supreme Court's focus on the probable anticompetitive effects of mergers and acquisitions on a significant group of customers, the 35 percent may be viewed as a significant group of customers and used to assert the validity of the courts' view of banking as a separate line of commerce.

The reader should be cautioned, however, because the same survey showed that 51 percent of the small businesses using financial services from commercial banks also used financial services supplied by nonbanks. The fact that there are alternatives for almost every service provided by commercial banks supports the view that these alternative suppliers may have some competitive impact on price and output decisions of commercial banks. The purpose of the competitive standards in the Bank Holding Company and Bank Merger Act, as well as our antitrust laws generally, is to avoid reducing competitive pressures. To the extent that nonbank suppliers of financial services influence the pricing decisions of commercial banks, either for the cluster of services or for any individual service, they should be viewed as competitors and included in any competitive analysis.

The regulatory authorities and courts have consistently appraised the competitive impact of nonbank suppliers on a case by case basis. Denials of acquisitions and mergers have been handed down in rare cases based on substantial anticompetitive effects on a given service line, such as trust services. The empirical evidence suggests that nonbank alternatives for financial services supplied by commercial banks are growing in significance and both market forces and new legislation are expected to heighten this significance.



Although the evidence presented to date is probably not sufficient to cause the courts to redefine the commercial banks' product, the time is right for the regulatory agencies to emphasize certain service lines in their analysis of bank merger and acquisitions. Following the MCA, all consumer financial services offered by banks are also offered at a number of other financial institutions. Therefore, anticompetitive consequences of bank mergers or acquisitions are less likely to affect this group of customers than business customers. As a consequence, the regulatory agencies should focus on those services provided by banks to business customers. If the agencies find that a merger or acquisition would have substantially adverse competitive consequences on the market, a denial recommendation would be supportable in the courts under our present antitrust laws.

Assuming the courts and regulatory agencies do not change their criteria for defining relevant products for antitrust consideration, our findings are consistent with the courts' present treatment of banks as offering a separate product in local markets. Neither the recent legislative changes nor the new realities of the market place are sufficient to encourage a change in the way the courts view commercial banking.

> "Although the evidence presented to date is probably not sufficient to cause the courts to redefine the commercial banks' product, the time is right for the regulatory agencies to emphasize certain service lines in their analysis . . ."

Consolidation of banks within local markets will continue to be restricted, encouraging a large number of small producers. Consolidation among banks located in different geographic markets will continue to be restricted by the prohibition of interstate banking at this time. Unless we get new legislation, commercial banking will continue to be an industry composed of a large number of competitors, while other types of financial institutions continue to consolidate.

Based on the evidence presented here, however, it is likely that in the near future commercial banking as a separate line of commerce may cease to be relevant for antitrust purposes or as a market place reality. The evidence suggests that the financial market place is changing, and that small businesses are turning increasingly to nonbank institutions for some of their financial services. The once exclusive position enjoyed by commercial banks is coming to an end.

In addition, new technology and the development of new services by nonbank financial institutions is undermining one of the critical pillars supporting the separability of banks from other types of financial institutions, i.e. the convenience element. With the development of in-home computers which may be linked via cable television to financial institutions, financial services of all types will be as close as your television. This will surely undermine the notion that consumers or small businesses are limited to their local area for financial services.

These market changes will force legislative changes which inevitably will result in a new financial infrastructure. As George Benston has pointed out, we should have no fear that a repeal of the 1930s legislation limiting geographic and product segmentation will result in an unsafe or unstable financial system. Market forces of the 1980s will force these changes.

The real questions now are how soon these changes should come and what type of financial infrastructure do we need. The answer to the first question is apparently that market forces have not pushed us to this point yet, but are likely to in the near future. Thus, we must now understand that change is coming and plan for it. We need more research to answer the second question concerning the financial infrastructure necessary in the decades ahead. These questions will be the subject of future issues of this **Review**.

—David D. Whitehead

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NOTES

[1]Charles R. McNeill and Denise M. Rechter, "The Depository Institution Deregulation and Monetary Control Act of 1980," **Federal Reserve Bulletin**, June 1980, pp. 444-453.

[2]26 Stat. 209.

[3]**Id.**

[4]David D. Martin, "Mergers and the Clayton Act," 1959, 257-8. Paragraphs 3-5 are omitted because they are not relevant to this particular article.

[5]Public Law, 86-463; 73 Stat. 129.

[6]**United States v. Philadelphia National Bank,** 374 U.S. 321 (1963), 356.

[7]**United States v. Crocker-Anglo National Bank,** 277 F. Supp. 133 (N.D. Calif. 1967).

[8]Public Law, 89-356; 80 Stat. 7,8.

[9]**United States v. Phillipsburg National Bank & Trust, et al.,** 399 U.S. 350 (1969), 358.

[10]**Id.,** at 360.

[11]**Id.,** at 360, 361-2.

[12]**United States v. First National Bank of Jackson,** 301 F. Supp. 1161 (S.D. Miss. 1969).

[13]**Idaho First National Bank,** 315 F. Supp. 261 (D. Idaho 1970).

[14]**United States v. Connecticut National Bank,** 418 U.S. 656 (1973).

[15]**United States v. First National State Bancorporation,** 1980-2 Trade Cases (CCH) paragraph 63, 445 at 76, 339 (D.N.J. 1980)

[16]**United States v. Zions Utah Bancorporation,** C79-0769A (D. Utah 1980), at Tr. 3526.

[17]See preceding article for a discussion of the legal history.

[18]**United States v. Philadelphia National Bank,** 374 U.S. 321 (1963).

[19]38 Federal Reserve **Bulletin** 382-384 (1952).

[20]See decisions involving applications by (1) Baystate Corporation, Boston, Mass,. to acquire Union Trust Company of Springfield, Springfield, Mass., 44 Federal Reserve **Bulletin** 432 (1958), (2) New Hampshire Bankshares, Inc., Nashua, N.H., to acquire the New Hampshire National Bank of Portsmouth, Portsmouth, N.H., 44 Federal Reserve **Bulletin** 432 (1958), (3) New Hampshire Bankshares, Inc., Nashua, N.H., to acquire the Peoples National Bank of Claremont, Claremont, N.H., 46 Federal Reserve **Bulletin** 742 (1960) and (4) Marine Midland Corporation, Buffalo, N.Y. to acquire the First National Bank of Poughkeepsie, Poughkeepsie, N.Y., 46 Federal Reserve **Bulletin** 1228 (1960) and (5) Baystate Corporation, Boston, Mass. to acquire Manufacturers National Bank of North Attleborough, North Attleborough, Mass., 46 Federal Reserve **Bulletin** 1230 (1960).

[21]"Bank is by far the largest of four commercial banks in the primary service area. However, a mutual savings bank in Poughkeepsie, one of two such banks in the area, is much larger than Bank and it appears appropriate to consider competition afforded by mutual savings banks as well as by commercial banks." 46 Federal Reserve **Bulletin** 1229 (1960). "It is appropriate to consider competition afforded by mutual savings banks as well as by commercial banks in connection with the fifth factor." 46 Federal Reserve **Bulletin** 1231 (1960).

[22]Application of First Bank Stock Corporation, Minneapolis, Minnesota to acquire Eastern Heights State Bank, Minneapolis, Minnesota, 46 Federal Reserve **Bulletin** 487 (1960). Application by Northwest Bancorporation, Minneapolis, Minnesota to acquire The First National Bank of Pipestone, Pipestone, Minnesota, 47 Federal Reserve **Bulletin** 408 (1961).

[23]Yingling and Shay (1981) cite the following mergers: (1) Lincoln Bank and Trust Co., Louisville, Ky. and The First National Bank of Louisville, Louisville, Ky., Comptroller's **Annual Report,** 1960, p. 89, (2) West End Bank, Pittsburgh, Pa. and Western Pennsylvania National Bank, McKeesport, Pa., Comptroller's **Annual Report,** 1962, p. 26, (3) First National Bank of Brunswick, Brunswick, Maine and First National Bank of Portland, Portland, Maine, Comptroller's **Annual Report,** 1962, p. 34, and (4) National Mohaive Bank of Great Barrington, Great Barrington, Mass. and First Agricultural National Bank of Berkshire County, Comptroller's **Annual Report,** 1963, p. 93.

[24]The discussion in this paragraph is based on the analysis and conclusions in Bleier and Eisenbeis (1981) and Eisenbeis (1981).

[25]See United States v. National Bank of Lexington, 376 U.S. 665 (1964) and United States v. Third National Bank of Nashville, 390 U.S. 171 (1968).

[26]United States v. Phillipsburg National Bank and Trust Co., 399 U.S. 350 (1970) and United States v. Connecticut National Bank, 418 U.S. 656 (1974).

[27]For example, in several cases between 1963-1974 the Board first analyzed the competitive effects using commercial bank deposit shares only and then added in mutual savings banks as well. See applications by (1) Depositors Corporation, Augusta, Maine to acquire The Liberty National Bank in Ellsworth, Ellsworth, Maine, 52 Federal Reserve **Bulletin** 1635 (1966), (2) Baystate Corporation, Boston, Mass. to acquire the Merchants National Bank of New Bedford, New Bedford, Mass., 53 Federal Reserve **Bulletin** 59 (1967), (3) Lincoln First Group, Inc., Rochester, New York to become a bank holding company, 53 Federal Reserve **Bulletin** 382 (1967), (4) State Street Boston Financial Corporation, Boston, Mass. to acquire the Union National Bank, Lowell, Mass., 59 Federal Reserve **Bulletin** 526 (1973) and (5) Northeast Bancorp, Inc., New Haven, Conn. to merge with First Connecticut Bancorp, Inc., Hartford, Conn., 60 Federal Reserve **Bulletin** 375 (1974). Similarly, the Comptroller of the Currency also considered nonbank competition in many cases. See (1) National Mohaive Bank of Great Barrington, Great Barrington, Mass. to merge with First Agricultural National Bank of Berkshire County, Comptroller's **Annual Report.** p. 93, 1963, (2) Winchester National Bank, Winchester, New Hampshire to merge with Cheshire National Bank of Keene, Keene, New Hampshire, Comptroller's **Annual Report,** p. 93, 1964, (3) Martin State Bank, Michigan to merge with First National Bank and Trust Co. of Kalamazoo, Kalamazoo, Michigan, Comptroller's **Annual Report,** p. 81, 1965-66, and (4) Rutland County Bank, Rutland, Vermont to merge with Howard National Bank and Trust Co., Vermont, Comptroller's **Annual Report,** p. 48, 1967.

[28]Application of Bangor Savings Bank, Bangor, Maine to merge with Piscataquis Savings Bank, Dover-Foxcraft, Maine, **FDIC Annual Report,** footnote, p. 78, 1976.

[29]Application of Bangor Savings Bank, Bangor, Maine to merge with Eastport Savings Bank, Eastport, Maine, **FDIC Annual Report,** p. 60, 1977 and Competitive factor report to the Comptroller of the Currency on the proposed merger of the Northern National Bank, Presque Isle, Maine and Merchants National Bank of Bangor, Bangor, Maine, 6/16/1980.

[30]See for example, National Bank and Trust Co. of Norwich, Norwich, New York to merge with The First National Bank of Sidney, Sidney, New York, Comptroller's **Annual Report**, p. 101, 1978, BancOhio National Bank, Columbus, Ohio to merge with Citizens Bank of Shelby, Shelby, Ohio, approved order Jan. 7, 1980, First National State Bank of Central Jersey, Trenton, New Jersey to merge with First National Bank of South Jersey, Egg Harbor, New Jersey, approval order May 8, 1979, Pacific National Bank of Washington, Seattle, Washington to merge with American Commercial Bank, Spokane, Washington, approval order February 21, 1980 and National Bank of Paulding County, Paulding, Ohio to merge with National Bank of Defiance, Defiance, Ohio, approval order Dec. 12, 1980.

[31]Northern National Bank, Presque Isle, Maine to merge with Merchants National Bank of Bangor, Bangor, Maine, approval order Dec. 12, 1980.

[32]Northeast Bancorp, Inc., New Haven, Conn., to acquire The First Connecticut Bancorp. Inc., Hartford, Conn., 60 Federal Reserve **Bulletin** 375 (1974).

[33]For example, see First Bancorp of N.H., Inc., Manchester, New Hampshire to acquire Londonderry Bank and Trust Company, Londonderry, New Hampshire, 64 Federal Reserve **Bulletin** 967 (1978) and United Bank Corporation of New York, Albany, New York to acquire The Schenectady Trust Company, Schenectady, New York, 64 Federal Reserve **Bulletin** 894 (1978).

[34]See note 33.

[35] United Bancorporation of New York, Albany, New York to acquire The Schenectady Trust Company, Schenectady, New York, 66 Federal Reserve **Bulletin** 61 (1980).

[36]"Shading was not in fact a new concept. The Supreme Court in the PNB case used "shaded" to arbitrarily reduce certain of the market shares in that case in an attempt to recognize the role of nonlocal competitors.

[37]See for example the Board's denial of the application of Toledo Trustcorp, Inc., Toledo, Ohio to acquire The National Bank of Defiance, Defiance, Ohio, 66 Federal Reserve **Bulletin** 462 (1980). As was indicated previously, this case was subsequently approved by the Comptroller of the Currency who not only defined the relevant geographic market differently, but also gave weight to the role of S&L's in the market. Also, the denial of the formation of Heritage Racine Corporation, Racine, Wisc., 66 Federal Reserve **Bulletin** 419 (1980).

[38]In its denial of Republic of Texas Corporation's, Dallas, Texas, application to merge with Fort Sam Houston Bankshares, Incorporated, San Antonio, Texas, 66 Federal Reserve **Bulletin** 580 (1980), the Board appeared to revert to its previous method of subjectively giving weight to thrifts after analyzing the market including only commercial banks.

[39]The Board stated that it continued to view commercial banking as the "line of commerce" but then indicated in a footnote the following: "The Board notes that under the Monetary Control Act of 1980, the commercial lending and investment powers of federally-chartered thrift institutions were broadened. However, in view of the uncertainty with respect to the extent to which thrifts will exercise their new powers, the Board believes that it would be premature to give full credence to thrift institutions as full competitors of banks until the effects can be ascertained." Fidelity Union Bancorporation, Newark, New Jersey to acquire the Garden State National Bank, Paramus, New Jersey, 66 Federal Reserve **Bulletin** 576 (1980). Essentially the same conclusion one year later appeared in the Board's approval of the application of United Bank Corporation of New York, Albany, New York to acquire The Sullivan County National Bank of Liberty, Liberty, New York, 67 Federal Reserve **Bulletin** 358 (1981). In denying the acquisition by the Independent Bank Corporation, Ionia, Michigan to acquire The Old State Bank of Fremont, Fremont, Michigan, 67 Federal Reserve **Bulletin** 436 (1981), the Board met applicant's contention that thrifts should be included by noting the lack of evidence that thrifts competed over a range of services sufficient to warrant their inclusion. Even if they were, the Board cited market shares for thrifts and banks combined that were sufficiently high to warrant denial of this case.

[40]This section is taken in large part from Eisenbeis (1981).

[41]It is noted that all attempts by applicants, the agencies, or the District Courts to formally broaden the "line of commerce" definition set forth in the Philadelphia National Bank case have been reversed by the Supreme court. Most recently, the U.S. District Court for the District of New Jersey relied on the Connecticut National decision's emphasis on the uniqueness of the cluster of products provided to commercial entities and declined to expand the "line of commerce" definition. United States v. First Nat'l State Bancorporation, 499 F. Supp. 793 (D.N.J. 1980).

[42]Prudential, for example, has recently announced that its general agents will also begin to sell mutual funds.

[43]The recent rulings by the District Court in the Mercantile and Republic cases virtually wipe out application of the potential competition doctrine. Thus, antitrust will not play a significant role in affecting the structure of banking in market extension situations.

[44]It can be argued that antitrust, which focuses on case-by-case factual situations, is not well suited nor can it deal effectively with such broader transitional issues.

[45]Northern National Bank, Presque Isle, Maine, to merge The Merchants National Bank of Bangor, Maine, approval order Dec. 12, 1980.

[46]They also are becoming less and less relevant since they are collected on a banking office basis rather than on a customer location basis.

[47]**United States v. Connecticut National Bank,** 418 U.S. 656 (1973)

[48]418 U.S. 656, 41 L.Ed. 2-1016, United States v. The Connecticut National Bank, pp. 2794-2795.

[49]Ibid, page 2794.

[50]Edward Mason, **Economic Concern and the Monopoly Problem** (Cambridge, Mass.: Harvard Univ. Press), 1957, p. 6.

[51]Julie W. F. Shih with the Bureau of Economic and Business Research at the University of Florida was responsible for conducting the survey and tabulating the results.

[52]Recognition to Joe Cleaver, Staff Board of Governors, Julie W. F. Shih, University of Florida, Bureau of Economic and Business Research

[53]See "NOW Pricing: Perspectives and Objectives," this **Review,** January 1981.

[54]Generally, the competition between banks and savings and loan associations takes place in markets which are less than statewide. The SMSA is the most common definition of each city. For some purposes, analysts of retail banking competition have defined markets more narrowly than the SMSAs, which typically comprise several counties. For other purposes, the SMSA may be too limited a definition. The SMSA definition seems sensible in the case of the products whose prices we examine, however, because even where institutions on one side of a market may not compete directly with ones on the other side, they were advertising NOW account terms widely throughout the SMSA and perhaps over a larger territory. As a result, branching institutions cannot price NOW accounts differently within the same advertising market.

[55]The rationale for this measure is simple. Convenience is a primary consideration determining where people open new transaction accounts. A relative abundance of offices should increase S&Ls' ability to compete, and vice versa.

[56]In general, thrifts can offer the small-savers certificates at a quarter-percent premium over the banks. At the time we sampled bank prices, however, the premium was not in effect because the yield on 2½-year Treasury securities was high enough to trigger an exception clause.

[57]The S&L sample consists of 65 institutions in the 22 markets. The individual institutions were chosen using a stratified sampling process similar to that used to choose the banks.

[58]Studies of **Small Business Finance,** A Report to Congress prepared by the Interagency Task Force on Small Business Finance, February 1, 1982.

[59]The total number of federally insured U.S. banks as of December 31, 1980, was 14,422.

[60]For the results of the entire survey see Cynthia A. Glassman and Peter L. Struck, "Survey of Commercial Bank Lending to Small Businesses" in **Studies of Small Business Finance, op. cit.**

[61]This is an overestimate to the extent that some banks appeared to ignore trade credit in responding to the applicable questions; it may be more representative of the banks' share of institutional lending to small businesses.

Next Month in the REVIEW

☐ **Highlights of a Conference: "Supply-Side Economics in the 1980s"**
Friedman, Feldstein, Weidenbaum, Kemp, Klein, Sprinkel, Ture

☐ **IRA Survey: Competition Heats Up in Southeast**
Insurance companies, securities dealers are "in the game" with banks, S&Ls, credit unions.

☐ **Banking's challenges in the '80s**
Lessons from deregulation of trucking, airlines

☐ **The Vanishing Tax Cut**
Will it be offset by inflation and increased state, local and Social Security taxes?

☐ **Southeast Exports**
Surge in exports through region's ports should continue.

☐ **1981 Business Tax Cuts**
How will key southeastern industries fare under new depreciation rules?

FINANCE

STATISTICAL SUPPLEMENT

	MAR 1982	FEB 1982	MAR 1981	ANN. % CHG.		MAR 1982	FEB 1982	MAR 1981	ANN. % CHG.
UNITED STATES									
Commercial Bank Deposits	1,107,074	1,099,303	998,599	+ 11	Savings & Loans				
Demand	286,543	289,113	298,370	- 4	Total Deposits	524,297	521,441	510,074	+ 3
NOW	54,550	53,777	34,819	+ 57	NOW	8,667	8,377	4,093	+112
Savings	148,047	148,282	157,545	- 6	Savings	91,811	92,743	100,227	- 8
Time	647,213	634,123	540,915	+ 20	Time	424,412	420,811	405,142	+ 5
Credit Union Deposits	43,030	41,552	35,578	+ 21		JAN	DEC	JAN	
Share Drafts	2,769	2,685	1,835	+ 51	Mortgages Outstanding	508,240	509,133	495,415	+ 3
Savings & Time	37,602	36,283	31,955	+ 18	Mortgage Commitments	15,547	15,163	15,893	- 2
SOUTHEAST									
Commercial Bank Deposits	119,830	118,492	107,556	+ 11	Savings & Loans				
Demand	34,317	34,161	34,941	- 2	Total Deposits	77,150	76,566	74,240	+ 4
NOW	7,169	7,030	4,329	+ 66	NOW	1,425	1,372	624	+128
Savings	14,711	14,714	15,616	- 6	Savings	11,708	11,766	12,824	- 9
Time	67,075	65,409	56,192	+ 19	Time	64,037	63,471	60,592	+ 6
Credit Union Deposits	4,225	4,088	3,253	+ 30		JAN	DEC	JAN	
Share Drafts	293	278	211	+ 39	Mortgages Outstanding	74,418	74,633	71,593	+ 4
Savings & Time	3,621	3,487	2,827	+ 28	Mortgage Commitments	3,364	3,488	3,382	- 1
ALABAMA									
Commercial Bank Deposits	13,511	13,409	12,196	+ 11	Savings & Loans				
Demand	3,420	3,504	3,477	- 2	Total Deposits	4,412	4,404	4,369	+ 1
NOW	622	612	397	+ 57	NOW	74	71	32	+131
Savings	1,523	1,530	1,642	- 7	Savings	571	579	654	- 13
Time	8,389	8,190	7,058	+ 19	Time	3,791	3,782	3,692	+ 3
Credit Union Deposits	734	717	526	+ 40		JAN	DEC	JAN	
Share Drafts	56	55	46	+ 22	Mortgages Outstanding	3,979	4,003	3,969	+ 0
Savings & Time	625	617	478	+ 31	Mortgage Commitments	49	51	138	- 64
FLORIDA									
Commercial Bank Deposits	39,636	39,219	36,312	+ 9	Savings & Loans				
Demand	12,362	12,174	13,067	- 5	Total Deposits	46,917	46,371	45,151	+ 4
NOW	3,164	3,107	1,892	+ 67	NOW	998	962	461	+116
Savings	6,352	6,374	6,886	- 8	Savings	7,868	7,893	8,676	- 9
Time	18,681	18,152	15,361	+ 22	Time	37,958	37,444	35,792	+ 6
Credit Union Deposits	1,925	1,845	1,502	+ 28		JAN	DEC	JAN	
Share Drafts	163	156	118	+ 38	Mortgages Outstanding	45,536	45,702	43,188	+ 5
Savings & Time	1,523	1,431	1,176	+ 30	Mortgage Commitments	2,913	3,059	2,721	+ 7
GEORGIA									
Commercial Bank Deposits	16,352	16,151	14,030	+ 17	Savings & Loans				
Demand	5,837	5,877	5,865	- 0	Total Deposits	9,657	9,720	9,431	+ 2
NOW	1,010	997	621	+ 63	NOW	146	143	53	+175
Savings	1,578	1,573	1,589	- 1	Savings	1,166	1,183	1,329	- 12
Time	8,893	8,634	7,070	+ 26	Time	8,380	8,430	8,050	+ 4
Credit Union Deposits	778	755	551	+ 41		JAN	DEC	JAN	
Share Drafts	25	23	14	+ 79	Mortgages Outstanding	9,324	9,349	9,336	- 0
Savings & Time	720	703	524	+ 37	Mortgage Commitments	113	111	175	- 35
LOUISIANA									
Commercial Bank Deposits	21,605	21,511	19,062	+ 13	Savings & Loans				
Demand	6,194	6,227	5,934	+ 4	Total Deposits	7,577	7,519	6,972	+ 9
NOW	977	941	572	+ 71	NOW	88	83	31	+184
Savings	2,394	2,380	2,428	- 1	Savings	1,208	1,216	1,210	- 0
Time	12,716	12,493	10,718	+ 19	Time	6,298	6,238	5,742	+ 10
Credit Union Deposits	115	114	83	+ 39		JAN	DEC	JAN	
Share Drafts	12	8	4	+200	Mortgages Outstanding	7,151	7,140	6,810	+ 5
Savings & Time	107	106	77	+ 39	Mortgage Commitments	235	208	225	+ 4
MISSISSIPPI									
Commercial Bank Deposits	10,002	9,799	8,910	+ 12	Savings & Loans				
Demand	2,362	2,336	2,419	- 2	Total Deposits	2,382	2,378	2,354	+ 1
NOW	536	521	326	+ 64	NOW	40	37	14	+186
Savings	734	731	780	- 6	Savings	221	222	242	- 9
Time	6,637	6,449	5,678	+ 17	Time	2,136	2,131	2,100	+ 2
Credit Union Deposits	N.A.	N.A.	N.A.			JAN	DEC	JAN	
Share Drafts	N.A.	N.A.	N.A.		Mortgages Outstanding	2,200	2,205	2,188	+ 1
Savings & Time	N.A.	N.A.	N.A.		Mortgage Commitments	15	17	61	- 75
TENNESSEE									
Commercial Bank Deposits	18,724	18,402	17,046	+ 10	Savings & Loans				
Demand	4,143	4,044	4,179	- 1	Total Deposits	6,205	6,173	5,963	+ 4
NOW	860	852	521	+ 65	NOW	78	75	33	+136
Savings	2,130	2,125	2,291	- 7	Savings	5,474	5,445	5,216	+ 5
Time	11,758	11,491	10,307	+ 14	Time	673	657	591	+ 14
Credit Union Deposits	673	657	591	+ 14		JAN	DEC	JAN	
Share Drafts	37	36	29	+ 28	Mortgages Outstanding	6,228	6,234	6,102	+ 2
Savings & Time	646	630	572	+ 13	Mortgage Commitments	39	42	62	- 37

Notes: All deposit data are extracted from the Federal Reserve Report of Transaction Accounts, other Deposits and Vault Cash (FR2900), and are reported for the average of the week ending the 1st Wednesday of the month. This data, reported by institutions with over $15 million in deposits as of December 31, 1979, represents 95% of deposits in the six state area. Savings and loan mortgage data are from the Federal Home Loan Bank Board Selected Balance Sheet Data. The Southeast data represent the total of the six states. Subcategories were chosen on a selective basis and do not add to total.
N.A. = fewer than four institutions reporting.

EMPLOYMENT

	JAN 1982	DEC 1981	JAN 1981	ANN. % CHG.		JAN 1982	DEC 1981	JAN 1981	ANN. % CHG.
UNITED STATES									
Civilian Labor Force - thous.	108,014	108,574	106,885	+ 1	Nonfarm Employment- thous.	89,781	91,915	89,988	- 0
Total Employed - thous.	97,831	99,562	98,139	- 0	Manufacturing	19,449	19,818	20,075	- 3
Total Unemployed - thous.	10,183	9,013	8,746	+16	Construction	3,691	4,153	3,995	- 8
Unemployment Rate - % SA	8.5	8.8	7.4		Trade	20,726	21,403	20,366	+ 2
Insured Unemployment - thous.	N.A.	N.A.	N.A.		Government	15,884	16,129	16,216	- 2
Insured Unempl. Rate - %	N.A.	N.A.	N.A.		Services	18,503	18,754	17,972	+ 3
Mfg. Avg. Wkly. Hours	36.8	39.9	39.9	- 8	Fin., Ins., & Real Est.	5,327	5,351	5,235	+ 2
Mfg. Avg. Wkly. Earn. - $	308	329	308	0	Trans. Com. & Pub. Util.	5,047	5,140	5,063	- 0
SOUTHEAST									
Civilian Labor Force - thous.	13,793	13,867	12,992	+ 6	Nonfarm Employment- thous.	11,413	11,570	11,321	+ 1
Total Employed - thous.	12,440	12,691	12,025	+ 3	Manufacturing	2,231	2,266	2,281	- 2
Total Unemployed - thous.	1,353	1,175	967	+40	Construction	671	708	682	- 2
Unemployment Rate - % SA	9.3	8.7	7.3		Trade	2,691	2,751	2,630	+ 2
Insured Unemployment - thous.	N.A.	N.A.	N.A.		Government	2,131	2,144	2,179	- 2
Insured Unempl. Rate - %	N.A.	N.A.	N.A.		Services	2,199	2,201	2,091	+ 5
Mfg. Avg. Wkly. Hours	33.0	40.5	40.3	-18	Fin., Ins., & Real Est.	633	635	621	+ 2
Mfg. Avg. Wkly. Earn. - $	238	289	268	-11	Trans. Com. & Pub. Util.	697	707	687	+ 1
ALABAMA									
Civilian Labor Force - thous.	1,673	1,666	1,632	+ 3	Nonfarm Employment- thous.	1,336	1,353	1,343	- 1
Total Employed - thous.	1,428	1,483	1,480	- 4	Manufacturing	350	356	359	- 3
Total Unemployed - thous.	245	183	152	+61	Construction	62	66	64	- 3
Unemployment Rate - % SA	13.8	11.2	8.8		Trade	274	278	268	+ 2
Insured Unemployment - thous.	N.A.	N.A.	N.A.		Government	292	293	298	- 2
Insured Unempl. Rate - %	N.A.	N.A.	N.A.		Services	212	212	207	+ 2
Mfg. Avg. Wkly. Hours	*29.2	40.0	40.1	-27	Fin., Ins., & Real Est.	59	59	59	0
Mfg. Avg. Wkly. Earn. - $	228	287	276	-17	Trans. Com. & Pub. Util.	70	72	71	- 1
FLORIDA									
Civilian Labor Force - thous.	4,511	4,569	4,254	+ 6	Nonfarm Employment- thous.	3,804	3,824	3,698	+ 3
Total Employed - thous.	4,165	4,236	3,982	+ 5	Manufacturing	468	471	467	+ 0
Total Unemployed - thous.	346	333	272	+27	Construction	273	283	279	- 2
Unemployment Rate - % SA	7.4	7.7	6.1		Trade	1,024	1,030	975	+ 5
Insured Unemployment - thous.	N.A.	N.A.	N.A.		Government	612	617	626	- 2
Insured Unempl. Rate - %	N.A.	N.A.	N.A.		Services	906	900	853	+ 6
Mfg. Avg. Wkly. Hours	40.3	41.1	41.2	- 2	Fin., Ins., & Real Est.	277	277	264	+ 5
Mfg. Avg. Wkly. Earn. - $	237	282	259	- 8	Trans. Com. & Pub. Util.	234	234	223	+ 5
GEORGIA									
Civilian Labor Force - thous.	2,604	2,611	2,376	+10	Nonfarm Employment- thous.	2,155	2,185	2,172	- 1
Total Employed - thous.	2,386	2,424	2,222	+ 7	Manufacturing	504	510	518	- 3
Total Unemployed - thous.	218	187	154	+42	Construction	96	101	102	- 6
Unemployment Rate - % SA	8.2	7.3	6.4		Trade	495	515	500	- 1
Insured Unemployment - thous.	N.A.	N.A.	N.A.		Government	436	435	440	- 1
Insured Unempl. Rate - %	N.A.	N.A.	N.A.		Services	360	360	349	+ 3
Mfg. Avg. Wkly. Hours	*30.2	40.0	40.2	-25	Fin., Ins., & Real Est.	114	114	113	+ 1
Mfg. Avg. Wkly. Earn. - $	205	267	249	-18	Trans. Com. & Pub. Util.	142	143	143	- 1
LOUISIANA									
Civilian Labor Force - thous.	1,852	1,863	1,748	+ 6	Nonfarm Employment- thous.	1,620	1,651	1,585	+ 2
Total Employed - thous.	1,675	1,702	1,617	+ 4	Manufacturing	209	218	215	- 3
Total Unemployed - thous.	178	161	131	+36	Construction	132	140	132	0
Unemployment Rate - % SA	9.4	9.0	7.0		Trade	371	381	358	+ 4
Insured Unemployment - thous.	N.A.	N.A.	N.A.		Government	308	311	303	+ 2
Insured Unempl. Rate - %	N.A.	N.A.	N.A.		Services	294	295	279	+ 5
Mfg. Avg. Wkly. Hours	34.7	43.4	41.4	-16	Fin., Ins., & Real Est.	75	75	76	- 1
Mfg. Avg. Wkly. Earn. - $	326	382	342	- 5	Trans. Com. & Pub. Util.	130	132	129	+ 1
MISSISSIPPI									
Civilian Labor Force - thous.	1,051	1,046	1,001	+ 5	Nonfarm Employment- thous.	807	822	816	- 1
Total Employed - thous.	939	951	914	+ 3	Manufacturing	213	218	219	- 3
Total Unemployed - thous.	112	94	87	+29	Construction	40	41	39	+ 3
Unemployment Rate - % SA	10.0	9.1	8.1		Trade	161	167	160	+ 1
Insured Unemployment - thous.	N.A.	N.A.	N.A.		Government	185	187	194	- 5
Insured Unempl. Rate - %	N.A.	N.A.	N.A.		Services	121	122	120	+ 1
Mfg. Avg. Wkly. Hours	*28.6	38.8	39.1	-27	Fin., Ins., & Real Est.	33	33	32	+ 3
Mfg. Avg. Wkly. Earn. - $	179	241	226	-21	Trans. Com. & Pub. Util.	40	41	40	0
TENNESSEE									
Civilian Labor Force - thous.	2,102	2,112	1,981	+ 6	Nonfarm Employment- thous.	1,691	1,735	1,707	- 1
Total Employed - thous.	1,847	1,895	1,810	+ 2	Manufacturing	487	493	503	- 3
Total Unemployed - thous.	254	217	171	+49	Construction	68	77	66	+ 3
Unemployment Rate - % SA	10.9	10.4	7.5		Trade	366	380	369	- 1
Insured Unemployment - thous.	N.A.	N.A.	N.A.		Government	298	301	318	- 6
Insured Unempl. Rate - %	N.A.	N.A.	N.A.		Services	306	312	283	+ 8
Mfg. Avg. Wkly. Hours	*34.9	39.9	39.8	-12	Fin., Ins., & Real Est.	75	77	77	- 3
Mfg. Avg. Wkly. Earn. - $	251	277	258	- 3	Trans. Com. & Pub. Util.	81	85	81	0

Notes: All labor force data are from Bureau of Labor Statistics reports supplied by state agencies.
Only the unemployment rate data are seasonally adjusted.
The Southeast data represent the total of the six states.
The annual percent change calculation is based on the most recent data over prior year.
*Survey taken week of ice storm.

CONSTRUCTION

12-Month Cumulative Rate	DEC 1981	NOV 1981	DEC 1980	ANN. % CHG.		DEC 1981	NOV 1981	DEC 1980	ANN. % CHG.
UNITED STATES									
Total Construction Contracts					Residential Contracts				
Value - $ mil.	150,189	149,232	148,393	+ 1	Value - $ mil.	60,063	61,998	63,668	- 6
Nonresidential Contracts					Number of Units - Thous.	1,123.7	1,170.1	1,331.4	-16
Value - $ mil.	58,249	58,234	52,491	+11					
Sq. Ft. - mil.	1,166.3	1,179.5	1,200.4	- 3	Residential Permits - Thous.				
Nonbuilding Contracts					Number single-family	557.5	575.8	704.0	-21
Value - $ mil.	31,877	29,001	32,234	- 1	Number multi-family	411.6	424.4	466.9	-12
SOUTHEAST									
Total Construction Contracts					Residential Contracts				
Value - $ mil.	25,597	25,843	26,326	- 3	Value - $ mil.	12,296	12,829	13,107	- 6
Nonresidential Contracts					Number of Units - Thous.	262.3	274.6	312.2	-16
Value - $ mil.	8,383	8,188	7,688	+ 9					
Sq. Ft. - mil.	195.5	194.2	183.7	+ 6	Residential Permits - Thous.				
Nonbuilding Contracts					Number single-family	117.9	123.5	154.4	-24
Value - $ mil.	4,919	4,825	5,530	-11	Number multi-family	100.9	106.7	124.1	-19
ALABAMA									
Total Construction Contracts					Residential Contracts				
Value - $ mil.	1,774	1,792	1,919	- 8	Value - $ mil.	847	864	903	- 6
Nonresidential Contracts					Number of Units - Thous.	21.7	22.3	25.0	-13
Value - $ mil.	577	566	558	+ 3					
Sq. Ft. - mil.	14.0	13.3	13.9	+ 1	Residential Permits - Thous.				
Nonbuilding Contracts					Number single-family	5.4	5.8	9.2	-41
Value - $ mil.	350	361	458	-24	Number multi-family	5.5	6.0	7.4	-26
FLORIDA									
Total Construction Contracts					Residential Contracts				
Value - $ mil.	12,299	12,598	12,847	- 4	Value - $ mil.	6,860	7,301	7,458	- 8
Nonresidential Contracts					Number of Units - Thous.	146.4	155.8	176.6	-17
Value - $ mil.	3,732	3,614	2,928	+27					
Sq. Ft. - mil.	90.8	89.5	78.5	+16	Residential Permits - Thous.				
Nonbuilding Contracts					Number single-family	70.4	74.6	89.1	-21
Value - $ mil.	1,707	1,683	2,461	-31	Number multi-family	72.9	77.9	86.2	-15
GEORGIA									
Total Construction Contracts					Residential Contracts				
Value - $ mil.	3,841	3,896	3,939	- 2	Value - $ mil.	1,755	1,819	1,820	- 4
Nonresidential Contracts					Number of Units - Thous.	37.0	38.3	44.4	-17
Value - $ mil.	1,202	1,193	1,320	- 9					
Sq. Ft. - mil.	33.4	32.9	36.3	- 8	Residential Permits - Thous.				
Nonbuilding Contracts					Number single-family	21.1	21.4	26.7	-21
Value - $ mil.	884	885	799	+11	Number multi-family	8.8	8.3	8.6	+ 2
LOUISIANA									
Total Construction Contracts					Residential Contracts				
Value - $ mil.	3,775	3,526	3,270	+15	Value - $ mil.	1,321	1,316	1,136	+16
Nonresidential Contracts					Number of Units - Thous.	24.5	25.2	24.0	+ 2
Value - $ mil.	1,508	1,341	1,213	+24					
Sq. Ft. - mil.	24.4	23.8	18.5	+32	Residential Permits - Thous.				
Nonbuilding Contracts					Number single-family	9.9	10.1	11.6	-15
Value - $ mil.	946	869	921	+ 3	Number multi-family	8.1	8.3	8.3	- 2
MISSISSIPPI									
Total Construction Contracts					Residential Contracts				
Value - $ mil.	1,343	1,406	1,561	-14	Value - $ mil.	556	551	601	- 7
Nonresidential Contracts					Number of Units - Thous.	12.6	12.6	14.9	-15
Value - $ mil.	307	356	629	-51					
Sq. Ft. - mil.	7.1	8.4	9.6	-26	Residential Permits - Thous.				
Nonbuilding Contracts					Number single-family	3.5	3.6	5.1	-31
Value - $ mil.	480	499	331	+45	Number multi-family	1.7	1.8	5.1	-67
TENNESSEE									
Total Construction Contracts					Residential Contracts				
Value - $ mil.	2,565	2,625	2,789	- 8	Value - $ mil.	956	979	1,189	-20
Nonresidential Contracts					Number of Units - Thous.	20.1	20.5	27.3	-26
Value - $ mil.	1,056	1,117	1,040	+ 2					
Sq. Ft. - mil.	25.7	26.3	26.9	- 4	Residential Permits - Thous.				
Nonbuilding Contracts					Number single-family	7.6	8.0	12.7	-40
Value - $ mil.	553	528	560	- 1	Number multi-family	3.9	4.5	8.4	-54

Notes: Contracts are calculated from the F. W. Dodge Construction Potentials. Permits are calculated from the Bureau of the Census, Housing Units Authorized By Building Permits and Public Contracts. The Southeast data represent the total of the six states. The annual percent change calculation is based on the most recent month over prior year.

GENERAL

	JAN 1982	DEC 1981	JAN 1981	ANN. % CHG.		FEB 1982	JAN R 1981	FEB R 1981	ANN. % CHG.
UNITED STATES									
Personal Income-$ bil. SAAR					Agriculture				
(Dates: 3Q, 2Q, 3Q)	2,412.9	2,340.5	2,155.8	+12	Prices Rec'd by Farmers				
Retail Sales - $ bil.- SA (FEB.)	87.6	86.2	86.0	+ 2	Index (1977=100)	133	132	144	- 8
Plane Passenger Arrivals (thous.)	N.A.	N.A.	N.A.		Broiler Placements (thous.)	79,341	78,942	80,404	- 1
Petroleum Prod. (thous. bls.)	8,695.1	8,607.6	8,508.3	+ 2	Calf Prices ($ per cwt.)	59.50	57.10	70.60	-16
Consumer Price Index					Broiler Prices (¢ per lb.)	27.0	27.1	30.4	-11
1967=100 (FEB.)	283.4	282.5	263.2	+ 8	Soybean Prices ($ per bu.)	5.96	6.13	7.13	-16
Kilowatt Hours - mil. (OCT)	168.7	183.6	170.1	- 1	Broiler Feed Cost ($ per ton)	209	211	238	-12
SOUTHEAST									
Personal Income-$ bil. SAAR					Agriculture				
(Dates: 3Q, 2Q, 3Q)	282.1	272.8	249.2	+13	Prices Rec'd by Farmers				
Taxable Sales - $ mil	N.A.	N.A.	N.A.		Index (1977=100)	120	119	129	- 7
Plane Passenger Arrivals (thous.)	4,239.7	3,719.3	4,026.2	+ 5	Broiler Placements (thous.)	31,402	31,337	32,169	- 2
Petroleum Prod. (thous. bls.)	1,406.7	1,407.8	1,441.5	- 2	Calf Prices ($ per cwt.)	55.15	53.55	66.30	-17
Consumer Price Index					Broiler Prices (¢ per lb.)	25.5	25.6	29.3	-13
1967=100	N.A.	N.A.	N.A.		Soybean Prices ($ per bu.)	6.22	6.27	7.24	-14
Kilowatt Hours - mil. (OCT)	27.7	31.5	29.0	- 4	Broiler Feed Cost ($ per ton)	205	207	234	-12
ALABAMA									
Personal Income-$ bil. SAAR					Agriculture				
(Dates: 3Q, 2Q, 3Q)	32.4	31.4	29.1	+11	Farm Cash Receipts - $ mil.				
Taxable Sales - $ mil.	N.A.	N.A.	N.A.		(Dates: NOV, NOV)	1,876	-	1,668	+12
Plane Passenger Arrivals (thous.)	105.2	102.4	113.5	- 7	Broiler Placements (thous.)	9,874	9,684	10,854	- 9
Petroleum Prod. (thous. bls.)	59.0	59.4	61.5	- 4	Calf Prices ($ per cwt.)	54.00	53.00	61.40	-12
Consumer Price Index					Broiler Prices (¢ per lb.)	24.5	23.5	28.5	-14
1967=100	N.A.	N.A.	N.A.		Soybean Prices ($ per bu.)	6.17	6.22	7.08	-13
Kilowatt Hours - mil. (OCT)	3.9	4.5	4.3	- 9	Broiler Feed Cost ($ per ton)	225	230	240	- 6
FLORIDA									
Personal Income-$ bil. SAAR					Agriculture				
(Dates: 3Q, 2Q, 3Q)	102.4	98.3	88.8	+15	Farm Cash Receipts - $ mil.				
Taxable Sales - $ thous. (FEB.)	67,204	66,806	59,334	+13	(Dates: NOV, NOV)	3,610	-	3,379	+ 7
Plane Passenger Arrivals (thous.)	2,109.3	1,725.5	2,182.1	- 3	Broiler Placements (thous.)	2,006	1,904	1,866	+ 8
Petroleum Prod. (thous. bls.)	89.0	90.4	117.5	-24	Calf Prices ($ per cwt.)	57.50	54.50	64.30	-11
Consumer Price Index - Miami	**JAN**	**NOV**	**JAN**		Broiler Prices (¢ per lb.)	27.5	25.0	29.0	-5
Nov. 1977 = 100	155.2	153.6	263.0	-41	Soybean Prices ($ per bu.)	6.17	6.22	7.08	-13
Kilowatt Hours - mil. (OCT)	7.8	8.6	8.1	- 3	Broiler Feed Cost ($ per ton)	225	220	245	- 8
GEORGIA									
Personal Income-$ bil. SAAR					Agriculture				
(Dates: 3Q, 2Q, 3Q)	48.7	47.6	43.7	+11	Farm Cash Receipts - $ mil.				
Taxable Sales - $ mil.	N.A.	N.A.	N.A.		(Dates: NOV, NOV)	2;913	-	2,446	+19
Plane Passenger Arrivals (thous.)	1,599.1	1,464.9	1,697.5	- 6	Broiler Placements (thous.)	12,182	12,344	12,374	- 2
Petroleum Prod. (thous. bls.)	N.A.	N.A.	N.A.		Calf Prices ($ per cwt.)	53.60	51.10	63.80	-16
Consumer Price Index - Atlanta	**FEB**	**DEC**	**FEB**		Broiler Prices (¢ per lb.)	25.0	25.5	29.0	-14
1967 = 100	279.8	282.2	263.0	+ 6	Soybean Prices ($ per bu.)	6.13	6.10	7.10	-14
Kilowatt Hours - mil. (OCT)	4.1	4.7	4.3	- 5	Broiler Feed Cost ($ per ton)	189	194	240	-21
LOUISIANA									
Personal Income-$ bil. SAAR					Agriculture				
(Dates: 3Q, 2Q, 3Q)	40.4	39.1	35.3	+14	Farm Cash Receipts - $ mil.				
Taxable Sales - $ mil.	N.A.	N.A.	N.A.		(Dates: NOV, NOV)	1,546	-	1,469	+ 5
Plane Passenger Arrivals (thous.)	255.2	259.6	253.8	+ 1	Broiler Placements (thous.)	N.A.	N.A.	N.A.	
Petroleum Prod. (thous. bls.)	1,164.3	1,164.0	1,166.5	- 0	Calf Prices ($ per cwt.)	55.50	56.00	63.00	-12
Consumer Price Index					Broiler Prices (¢ per lb.)	27.0	28.5	31.0	-13
1967 = 100	N.A.	N.A.	N.A.		Soybean Prices ($ per bu.)	6.37	6.52	7.36	-13
Kilowatt Hours - mil. (OCT)	4.8	5.5	4.7	+ 2	Broiler Feed Cost ($ per ton)	245	245	260	- 6
MISSISSIPPI									
Personal Income-$ bil. SAAR					Agriculture				
(Dates: 3Q, 2Q, 3Q)	18.3	17.7	16.5	+11	Farm Cash Receipts - $ mil.				
Taxable Sales - $ mil.	N.A.	N.A.	N.A.		(Dates: NOV, NOV)	2,041	-	1,924	+ 6
Plane Passenger Arrivals (thous.)	30.8	30.0	33.7	- 9	Broiler Placements (thous.)	6,035	6,102	5,884	+ 3
Petroleum Prod. (thous. bls.)	94.4	94.0	96.0	- 2	Calf Prices ($ per cwt.)	56.40	55.60	72.40	-22
Consumer Price Index					Broiler Prices (¢ per lb.)	27.5	29.0	31.0	-11
1967 = 100	N.A.	N.A.	N.A.		Soybean Prices ($ per bu.)	6.18	6.31	7.24	-15
Kilowatt Hours - mil. (OCT)	1.9	2.3	2.0	- 7	Broiler Feed Cost ($ per ton)	189	183	210	- 10
TENNESSEE									
Personal Income-$ bil. SAAR					Agriculture				
(Dates: 3Q, 2Q, 3Q)	39.8	38.8	35.8	+11	Farm Cash Receipts - $ mil.				
Taxable Sales - $ mil.	N.A.	N.A.	N.A.		(Dates: NOV, NOV)	1,607	-	1,521	+ 6
Plane Passenger Arrivals (thous.)	140.1	136.8	140.1	0	Broiler Placements (thous.)	1,305	1,303	1,191	+10
Petroleum Prod. (thous. bls.)	N.A.	N.A.	N.A.		Calf Prices ($ per cwt.)	53.60	51.40	62.00	-14
Consumer Price Index					Broiler Prices (¢ per lb.)	25.0	24.0	28.0	-11
1967 = 100	N.A.	N.A.	N.A.		Soybean Prices ($ per bu.)	6.17	6.07	7.33	- 16
Kilowatt Hours - mil. (OCT)	5.1	5.8	5.5	- 7	Broiler Feed Cost ($ per ton)	191	210	210	- 9

Notes:
Personal Income data supplied by U. S. Department of Commerce. Taxable Sales are reported as a 12-month cumulative total. Plane Passenger Arrivals are collected from 26 airports. Petroleum Production data supplied by U. S. Bureau of Mines. Consumer Price Index data supplied by Bureau of Labor Statistics. Kilowatt hours are monthly sales to ultimate consumers published by U. S. Department of Energy. Agriculture data supplied by U. S. Department of Agriculture. Farm Cash Receipts data are reported as cumulative for the calendar year through the month shown. Broiler placements are an average weekly rate. The Southeast data represent the total of the six states. N.A. = not available. The annual percent change calculation is based on most recent data over prior year. R = Revised

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