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ECONOMIC REVIEW

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THE PATTERN OF UNITED STATES INTERNATIONAL TRADE

The United States is the largest single participant in the international exchange of goods, accounting for 15.1 percent of the world's imports of goods and 15.6 percent of the world's exports of goods in 1969 (see Table I). Because the United States is a major user and supplier of commodities for international trade, the volume and pattern of United States trade has an important influence on world trade. This article reviews United States merchandise exports and imports and patterns of merchandise trade during the 1960-1969 period.

FACTORS AFFECTING MERCHANDISE TRADE

Early in the post-World War II period, the United States had a large surplus of merchandise exports because of the demand for food, consumer goods, and capital goods by foreign countries. The demand for United States products remained strong throughout the 1950's as the industrial countries of the world rebuilt their industrial base and the less-developed countries began economic development efforts.

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TABLE I

Merchandise Imports and Exports
World and Selected Countries
1969
(Bil. of United States \$)

Country	Merchandise Imports (c.i.f.)*	Percent of World Imports	Merchandise Exports (f.o.b.)†	Percent of World Exports
World‡	\$254.4	—	\$243.0	—
United States	38.5	15.1%	38.0	15.6%
West Germany	25.0	9.8	29.0	11.9
United Kingdom	20.0	7.8	17.5	7.2
France	17.4	6.8	15.0	6.2
Japan	15.0	5.9	16.0	6.6
Canada	14.4	5.7	14.4	5.9
Italy	12.5	4.9	11.0	4.9
Netherlands	11.0	4.3	10.0	4.1
Belgium-Luxembourg	10.0	3.9	10.0	4.1

* Cost, insurance, and freight.

† Free on board.

‡ Excludes Soviet sphere countries and Cuba.

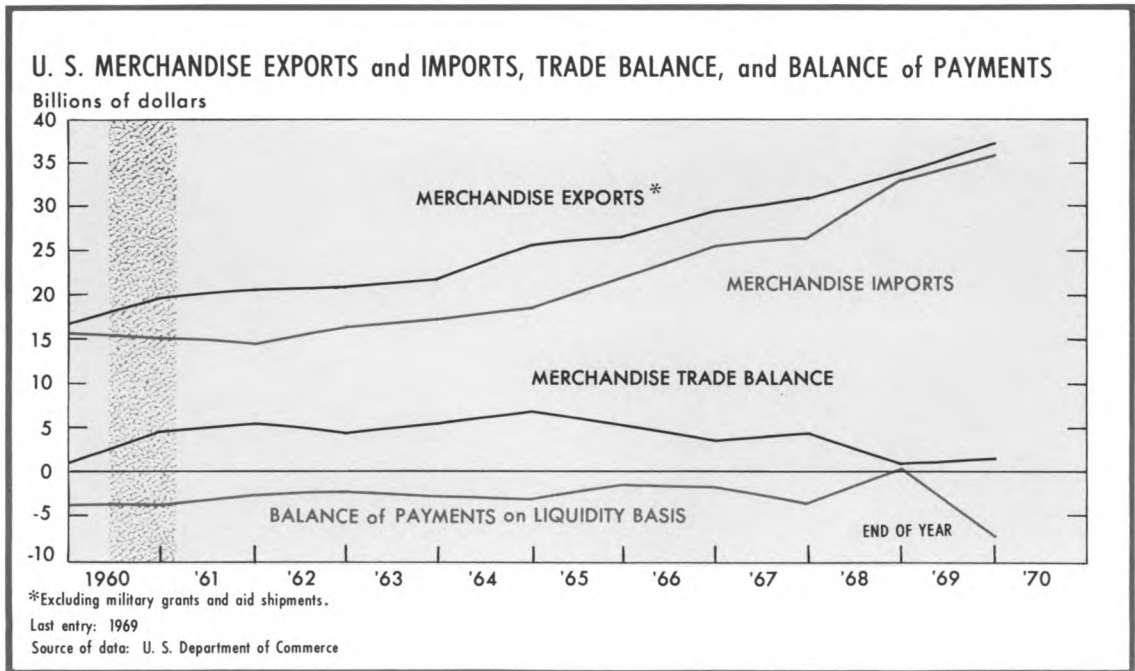
Source: International Monetary Fund

By the early 1960's, the other industrialized countries became strong competitors of the United States in world markets, as a result of new industrial capacity and rapid technological advances. In addition, improvements in agricultural production in the industrialized countries and the developing countries reduced the demand for United States agricultural products. Growing international competition, coupled with inflation in the United States and the effects of this inflationary trend on relative international prices, has been reflected in a deterioration of the United States merchandise trade balance since 1965 (see chart).

Although United States merchandise exports and imports have increased sharply in recent years, imports have risen faster than exports. Many factors affect the balance between United States merchandise exports and imports. In addition to inflation, strikes by dockworkers and other labor

unions, marketing efforts, exports to and imports from foreign subsidiaries of United States companies, foreign production patterns, international trade agreements, trade restrictions, foreign political and social unrest, and domestic and foreign monetary policy may influence changes in international trade patterns. The deterioration in the United States merchandise trade balance was, however, largely the result of inflation and the rapid expansion of economic activity in the United States.

During the 1960's, the rate of increase in gross domestic expenditures (measured in current dollars) in the United States was faster than the rate of increase in industrial production (see Table II). The difference between the two rates of growth widened significantly in the 1965-1969 period, when the index of gross domestic expenditures increased at an annual rate of 8.3 percent, while the index of industrial production increased



at an annual rate of only 4.9 percent. Although the proportion of gross domestic expenditures accounted for by services rose sharply (to 38 percent in 1969), the rapid increase in gross domestic expenditures implies excess demand for goods. Part of this excess demand would normally be supplied through an increase in imports and part would be reflected in the backlog of manufacturers' unfilled orders. The rapid buildup of manufacturers' unfilled orders during the 1965-1969 period substantiates the existence of excess demand in the United States (see Table II). The annual rate of increase in the index of manufacturers' unfilled orders was 7.1 percent during 1965-1969, compared with 6.0 percent during 1960-1964.

Excess demand during the late 1960's, coupled with the inflation that also developed in the United States, is reflected in the increase in the

Gross National Product price deflator—an indicator of changes in domestic price levels. The GNP price deflator increased at an annual rate of 3.3 percent during 1965-1969, compared with an annual rate of 0.5 percent during 1960-1964 (see Table II).

The unit value index of United States exports roughly indicates the magnitude of domestic price changes for goods shipped abroad. Similarly, the unit value index of United States imports roughly approximates the magnitude of price changes in other countries. In turn, these price patterns appear to be closely related to the pattern of the total value of United States merchandise imports (see Table II). As indicated by the GNP price deflator, domestic prices rose at an annual rate of only 0.5 percent during the 1960-1964 period, while the unit value index of United States imports showed no overall increase. During the

TABLE II

Indexes of Selected Economic Indicators*
United States
1960-1969

Year	Index 1957-59=100			Index 1958=100	Index 1957-59=100			
	Gross Domestic Expenditure‡	Industrial Production	Manufacturers' Unfilled Orders	GNP Price Deflator	Unit Value of Merchandise†		Total Value of Merchandise	
					Exports§	Imports	Exports§	Imports
1960	110	109	88	103	101	99	109	108
1961	113	110	92	105	103	98	111	105
1962	122	118	90	105	102	95	115	117
1963	129	124	96	106	102	96	123	122
1964	137	132	111	105	102	99	146	133
1965	149	143	129	109	106	99	152	152
1966	164	156	154	111	109	102	168	182
1967	173	158	159	112	111	103	177	191
1968	189	165	165	118	112	104	195	235
1969	205	173	170	124	117	108	213	254
Average Annual Rate of Increase#								
1960-1969	7.2%	5.3%	7.6%	2.1%	1.6%	1.0%	7.7%	10.0%
1960-1964	5.6	4.9	6.0	0.5	0.3	0.0	7.6	5.3
1965-1969	8.3	4.9	7.1	3.3	2.5	2.2	8.8	13.7

* Based on current dollars.

† Unit value indexes—constructed from prices of selected import and export commodities. The grouping of commodities and the content of the sample used in constructing the indexes has changed over the years. In general, however, selections are closely comparable from one year to the next and are fairly representative of the leading classes of exports and imports.

‡ GNP—net exports.

§ Excluding military grants and aid.

Compounded.

Source: U. S. Department of Commerce

same period, the annual rate of growth in the total value of United States imports was 5.3 percent. In contrast, during the 1965-1969 period, the unit value index of United States imports increased at an annual rate of 2.2 percent, while domestic prices rose at an annual rate of 3.3 percent. From 1965 to 1969, merchandise imports increased sharply at an annual rate of 13.7 percent, compared with an annual rate of 5.3 percent during 1960-1964. Apparently, when domestic prices increase faster than prices of imports, the demand for imports rises.

SHARE OF WORLD MARKETS AND BALANCE OF PAYMENTS

United States merchandise exports showed continuous growth from 1960 to 1969. On average, the value of merchandise exports increased by about \$1.8 billion a year, or at an annual rate of 7.0 percent (see Table III). When compared with exports of other industrialized countries, the relative strength of United States merchandise exports has diminished. Of the major industrialized countries, only the United Kingdom had a smaller annual rate of increase in exports during the period under review (see Table III). In contrast, the growth rates of exports from Japan and Italy were more than twice as great as the growth rate of exports from the United States.

Although the United States is still the world's largest exporter, its share of the world market has declined. Between 1960 and 1969, the United States share of all free world markets dropped from 18.2 percent to 15.6 percent (see Table III). If the United States had been able to achieve the same proportion of the world market in 1969 as it had in 1960, its value of merchandise exports would have been \$8.2 billion greater.

Among other things, the reduction in the United States share of the world market reflects both the rapid increase in United States imports (the exports of other countries) and a decline in United States agricultural exports since 1966 (see Table IV). In turn, the lack of growth in agricultural exports was a result of an increase in the world's grain supplies and an expansion of world crop production. These increases reduced the demand for United States agricultural products and heightened the competition in world markets among the other countries that export agricultural products.

Changes in the United States merchandise trade balance are significant because of their impact on the nation's balance of payments. Total exports and imports of goods and services are the largest component in the balance of payments, while merchandise exports and imports account for the major proportion of the goods and services component (see Table V). In 1960, merchandise exports accounted for 71.3 percent of the total export of goods and services, in contrast to 67.3 percent in 1969. Merchandise imports represented 64.1 percent of the total import of goods and services in 1960 and 67.7 percent in 1969. (The remaining portion of the total goods and services account of the balance of payments is composed of military sales and expenditures, transportation income and expense, travel income and expense, income from foreign investments and remittances to foreign investors, and the inflow and outflow of funds made in payment for other services.) The decrease in merchandise exports' share of total goods and services was associated with the increase in income from United States foreign investments that occurred during the 1960's. In 1960, investment income accounted for 11.6 percent of the

TABLE III

Merchandise Exports* of Selected Industrial Countries
1960–1969
(Bil. of \$)

Year	World†	United States	United States as Percent of World	West Germany	United Kingdom	France	Japan	Canada	Italy	Netherlands	Belgium- Luxembourg
1960	\$113.4	\$20.6	18.2%	\$11.4	\$10.6	\$ 6.9	\$ 4.1	\$ 5.8	\$ 3.6	\$ 4.0	\$ 3.8
1961	118.6	21.0	17.7	12.7	11.1	7.2	4.2	6.1	4.2	4.3	3.9
1962	124.8	21.7	17.4	13.3	11.4	7.4	4.9	6.2	4.7	4.6	4.3
1963	136.1	23.4	17.2	14.6	12.2	8.1	5.5	6.8	5.1	5.0	4.8
1964	152.7	26.7	17.5	16.2	12.8	9.0	6.7	8.1	6.0	5.8	5.6
1965	165.4	27.5	16.6	17.9	13.7	10.1	8.5	8.5	7.2	6.4	6.4
1966	181.3	30.4	16.8	20.1	14.7	10.9	9.8	10.0	8.0	6.8	6.8
1967	190.6	31.6	16.6	21.7	14.4	11.4	10.4	11.0	8.7	7.3	7.0
1968	212.9	34.6	16.3	24.8	15.3	12.7	13.0	13.2	10.2	8.3	8.2
1969	243.0	38.0	15.6	29.0	17.5	15.0	16.0	14.4	11.9	10.0	10.0
Average Annual Rate of Increase‡											
1960-1969	8.8%	7.0%	—	10.9%	5.7%	9.0%	16.3%	10.6%	14.2%	10.7%	11.4%
1960-1964	7.7	6.7	—	9.2	4.8	6.9	13.1	8.7	13.6	9.7	10.2
1965-1969	10.1	8.4	—	12.8	6.3	10.4	17.1	14.1	13.4	11.8	11.8

* Valued on free on board basis.

† Excludes Soviet sphere countries and Cuba.

‡ Compounded.

Source: International Monetary Fund

TABLE IV

**United States Merchandise Trade
1960–1969
(Bil. of \$)**

Year	Agricultural		Nonagricultural	
	Exports	Imports	Exports	Imports
1960	\$4.8	\$3.8	\$15.5	\$11.2
1961	5.0	3.7	15.7	10.9
1962	5.0	3.9	16.4	12.4
1963	5.6	4.0	17.5	13.0
1964	6.3	4.1	19.8	14.5
1965	6.2	4.1	20.9	17.3
1966	6.9	4.5	23.0	21.0
1967	6.4	4.5	24.8	22.3
1968	6.2	5.2	27.8	28.1
1969	5.9	5.0	31.5	31.1

Source: U. S. Department of Commerce

export of total goods and services, compared with 16.1 percent in 1969.

The deterioration in the merchandise trade balance largely explains the increase in the deficit in the United States balance of payments, as measured on the liquidity basis,¹ since the mid-1960's (see chart). Other factors, do, however, affect the United States balance of payments position, including United States Government grants and capital flows and short- and long-term private capital flows. For example, the temporary shift to a small surplus in the balance of payments in 1968 was the result of massive inflows of foreign funds into the stock market in the United States and into U. S. Government securities.

DIRECTION OF TRADE

During the 1960's, significant changes occurred in the composition and flow of international trade.

¹The liquidity measure of the balance of payments equals changes in liquid liabilities to foreign official holders, other foreign holders, and changes in official reserve assets.

Some nations developed new trade outlets, while others experienced difficulties in adjusting to the changes taking place in international markets. Lower production costs abroad often resulted in price differentials in favor of selected foreign products. Improved production methods and higher quality broadened the market for foreign goods, particularly European and Japanese goods. As a result, domestically produced goods faced greater competition in the United States as well as in foreign markets. Changes in consumer tastes and preferences also affected the mix of United States exports and imports. Tariff and nontariff barriers adversely affected the growth of United States exports to the European Economic Community (EEC)² and to Japan. Expanded agricultural production in the world, a drive toward agricultural self-sufficiency in the developing nations, and the protective farm policies of the EEC have influenced United States agricultural exports.

United States manufacturers made substantial investments in production facilities abroad in an effort to overcome foreign trade barriers and to take advantage of rapidly expanding foreign markets. Although these direct investments created some additional outlets for United States exports, particularly capital goods, they also displaced United States exports, such as electrical apparatus.

Major Trading Partners. United States international trade is concentrated among relatively few countries. In 1969, 13 nations each purchased in excess of \$500 million of United States exports and, as a group, accounted for 68.8 percent of merchandise exports from the United States (see Tables VI and VII). These countries also supplied

²The European Economic Community includes West Germany, the Netherlands, Italy, France, Belgium, and Luxembourg.

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TABLE V

United States Foreign Trade
1960–1969
(Bil. of \$)

Year	Total Goods and Services*		Total Merchandise (Goods)		Merchandise Trade as Percent of Total Goods and Services	
	Exports†	Imports	Exports†	Imports	Exports	Imports
1960	\$27.5	\$23.4	\$19.6	\$15.0	71.3%	64.1%
1961	28.8	23.1	20.2	14.7	70.1	63.6
1962	30.5	25.4	21.0	16.4	68.9	64.6
1963	32.6	26.6	22.4	17.1	68.7	64.3
1964	37.3	28.7	25.7	18.7	68.9	65.2
1965	39.4	32.3	26.7	21.4	67.8	66.3
1966	43.4	38.1	29.4	25.5	67.7	66.9
1967	46.2	41.0	31.0	26.8	67.1	65.4
1968	50.6	48.1	34.0	33.2	67.2	69.0
1969	55.4	53.3	37.3	36.1	67.3	67.7

* Includes merchandise, military sales, transportation, travel, investment income, and other services.

† Excluding military grants and aid.

Source: U. S. Department of Commerce

the bulk of United States merchandise imports—74.1 percent in 1969. The top four buyers of United States exports were also the leading suppliers of United States imports, purchasing 45 percent of total merchandise exports and supplying 55.5 percent of total merchandise imports in 1969. Canada was the most important trading partner of the United States in the 1962-1969 period. In 1969, Canada accounted for 24 percent of the exports from and 28.8 percent of the imports to the United States.

During 1962-1969, United States exports and imports tended to become more concentrated with these 13 trading partners. Most of the leading trading partners of the United States are major industrialized countries. The increasing proportion of export and import trade with these countries would tend to imply that United States international trade with the developed countries of the

world has grown faster than trade with the less-developed countries. In fact, United States exports and imports of industrial and consumer goods increased at a faster pace than total exports and imports (see Table VIII). As would be expected, trade in these types of commodities tends to be concentrated among the industrialized nations where per capita income has been rising and there has been a growing demand for more sophisticated goods. In contrast, the developing nations of the world generally have low per capita incomes and slow growth rates in per capita income and thus have less demand for United States exports. The exports of the developing countries are largely primary products and foodstuffs, and the demand for these commodities by the industrialized countries, including the United States, has not grown as rapidly as the demand for manufactured goods.

TABLE VI

United States Merchandise Exports and Imports by Country of
Destination and Origin
Selected Years

Country†				Percent Change			Annual Rate of Change*		
	1962 (mil. of \$)	1965 (mil. of \$)	1969 (mil. of \$)	1962-1965	1965-1969	1962-1969	1962-1965	1965-1969	1962-1969
Exports									
Canada	\$ 3,830	\$ 5,587	\$ 9,138	45.9%	63.6%	138.6%	13.4%	13.1%	13.2%
Japan	1,414	2,058	3,490	45.5	69.6	146.8	13.3	14.1	13.8
United Kingdom	1,075	1,565	2,335	45.6	49.2	117.2	13.3	10.5	11.7
West Germany	1,076	1,502	2,118	39.6	41.0	96.8	11.8	9.0	10.2
Mexico	790	1,105	1,449	39.8	31.1	83.4	11.8	7.0	9.1
Netherlands	818	1,088	1,447	33.0	33.0	76.9	10.0	7.4	8.5
Italy	767	864	1,262	12.6	46.1	64.5	4.0	10.0	7.4
France	585	902	1,195	54.2	32.5	104.3	15.5	7.3	10.7
Belgium-Luxembourg	526	650	960	23.6	47.7	82.5	7.3	10.2	9.0
Australia	402	701	855	74.8	22.0	113.2	20.0	5.1	11.4
Brazil	425	328	672	-22.8	104.9	58.1	- 7.1	19.6	6.8
Venezuela	468	624	708	33.3	13.5	51.3	10.0	3.2	6.1
India	669	928	517	38.7	- 44.3	- 22.7	11.5	- 9.6	- 3.0
EEC‡	3,772	4,904	6,981	30.0	42.4	85.1	9.2	9.2	9.2
Total World	\$20,901	\$26,225	\$37,988	25.5%	44.9%	81.8%	7.9%	9.7%	8.9%
Imports									
Canada	\$ 3,661	\$ 4,832	\$10,390	32.0%	115.0%	183.8%	9.7%	21.1%	16.1%
Japan	1,358	2,414	4,888	77.8	102.5	260.0	21.2	19.3	20.0
United Kingdom	1,004	1,405	2,121	39.9	51.0	111.2	11.8	10.9	11.3
West Germany	962	1,342	2,603	39.5	94.0	170.6	11.7	18.0	15.3
Mexico	580	638	1,029	10.0	61.3	77.4	3.3	12.7	8.5
Netherlands	221	251	466	13.6	85.7	110.9	4.4	16.7	11.2
Italy	452	620	1,204	37.2	94.2	166.4	11.1	18.0	15.0
France	428	615	842	43.7	36.9	96.7	12.8	8.2	10.1
Belgium-Luxembourg	380	494	684	30.0	38.5	80.0	9.1	8.5	8.8
Australia	292	314	588	7.5	87.3	101.4	2.5	17.0	10.5
Brazil	541	512	616	- 5.4	20.3	13.9	- 1.8	4.7	1.9
Venezuela	977	1,021	940	4.5	- 7.9	- 3.8	1.5	- 1.9	- 0.5
India	255	348	344	36.5	- 1.2	34.9	10.9	- 0.3	4.4
EEC‡	2,443	3,322	5,800	36.0	74.6	137.4	10.8	15.0	13.1
Total World	\$16,397	\$21,366	\$36,052	30.3%	68.7%	119.9%	9.2%	14.0%	11.3%

* Compounded.

† Countries in order with respect to value of 1969 exports.

‡ EEC—European Economic Community consisting of West Germany, Netherlands, Italy, France, Belgium, and Luxembourg.

Source: U. S. Department of Commerce

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TABLE VII

Proportion of United States Trade with
Leading Trading Partners
Selected Years

Leading Partner	Leading Partners' Trade as Percent of Total United States Trade					
	Exports to			Imports from		
	1962	1965	1969	1962	1965	1969
Canada	18.3%	21.3%	24.0%	22.3%	22.6%	28.8%
Canada, Japan, United Kingdom, and West Germany	35.4	40.8	45.0	42.6	46.8	55.5
Leading 13 countries	61.5	68.3	68.8	67.8	69.3	74.1

Source: U. S. Department of Commerce

In general, exports to the major trading partners of the United States grew more rapidly during 1962-1965 than during 1965-1969. In contrast, United States imports from its major trading partners increased faster during 1965-1969 than during 1962-1965 (see Table VI). These contrasting patterns largely reflect the factors discussed earlier and partially explain the deterioration in the merchandise trade surplus in the United States balance of payments.

Canada, the largest single market for United States merchandise exports, also supplies the bulk of United States imports (see Table VI). The close proximity, similarity of markets, and relative freedom of trade between Canada and the United States account for this large volume of trade. Both exports to and imports from Canada have grown faster than United States total world trade. During the 1962-1965 period, the United States had a surplus in its trade account with Canada; however, from 1965 to 1969, imports from Canada grew at a faster pace than exports to Canada. As a result, by 1969, United States trade with Canada was in deficit by about \$1.2 billion. The sharp increase in

trade of automotive vehicles and parts, stimulated by the 1965 United States-Canadian Auto Products Trade Agreement, contributed to the shift in the United States-Canadian trade balance. Under the Agreement, Canadian autos and parts can be shipped to the United States free of duty, while similar United States exports to Canada are exempt from duty only when prescribed rules for the use of Canadian goods and services are met in the manufacture and sale of the automobiles. Although United States and Canadian exports of automotive vehicles and parts increased rapidly as a result of this agreement, there was a net loss to the United States trade balance. Automotive product imports from Canada grew from less than \$100 million in 1964 to about \$2.9 billion in 1969. During the same period, United States exports of automotive products to Canada rose from about \$600 million to about \$2.6 billion.

In 1962, the United States also had a surplus in its trade account with both Japan and West Germany. However, between 1962 and 1969, the growth of imports from these two countries far outpaced the growth of exports to them, and by

TABLE VIII

United States Merchandise Exports and Imports by Commodity Group
Selected Years

Commodity Group	1962 (mil. of \$)	1965 (mil. of \$)	1969 (mil. of \$)	Percent Change			Annual Rate of Change*		
				1962-1965	1965-1969	1962-1969	1962-1965	1965-1969	1962-1969
Exports									
Food and live animals	\$ 3,245	\$ 3,003	\$ 3,733	23.4%	- 6.8%	15.0%	7.3%	- 1.7%	2.0%
Beverage and tobacco	498	517	713	3.8	37.9	43.2	1.3	8.4	5.3
Crude materials, inedible excluding fuels	2,227	2,856	3,570	28.2	25.0	60.3	8.6	5.8	7.0
Mineral fuels and related products	828	947	1,130	14.4	19.3	36.5	4.6	4.5	4.5
Animal and vegetable oils and fats	301	472	307	56.8	- 35.0	2.0	16.2	- 7.8	0.3
Chemicals	1,876	2,402	3,383	28.0	40.8	80.3	8.6	8.9	8.8
Nonelectrical machinery	4,087	5,274	7,188	29.0	36.3	75.9	8.9	8.0	8.4
Electrical apparatus	1,361	1,600	2,677	22.0	61.3	96.7	6.9	12.7	10.1
Transportation equipment	2,579	3,214	6,515	24.6	102.7	152.6	7.6	19.3	14.2
Metals and manufacturers	1,372	1,787	2,387	30.2	33.6	74.0	9.2	7.5	8.2
Textiles and clothing	613	671	785	9.5	17.0	28.1	3.1	4.0	3.6
Other manufactured goods	1,781	2,432	3,827	36.6	57.4	114.9	11.0	12.0	11.3
Total	\$20,901	\$26,225	\$37,988	25.5%	44.9%	81.8%	7.9%	9.7%	8.9%
Imports									
Food and live animals	\$ 3,243	\$ 3,460	\$ 4,531	6.7%	31.0%	39.7%	2.2%	7.0%	4.9%
Beverage and tobacco	431	553	778	28.3	40.7	80.5	8.7	8.9	8.8
Crude materials, inedible excluding fuels	2,706	3,103	3,460	14.7	11.5	27.9	4.7	3.6	3.6
Mineral fuels and related products	1,887	2,221	2,794	17.7	25.8	48.1	5.6	5.9	5.8
Animal and vegetable oils and fats	98	116	137	18.4	18.1	39.8	5.8	4.3	4.9
Chemicals	760	769	1,232	1.2	60.2	62.1	0.4	12.5	7.1
Nonelectrical machinery	540	1,160	2,542	114.8	119.1	370.7	29.0	21.7	24.8
Electrical apparatus	415	640	1,947	54.2	204.2	369.2	15.6	32.1	24.7
Transportation equipment	720	1,148	5,279	59.4	359.8	633.2	16.8	46.4	32.9
Metals and manufacturers	1,722	2,875	4,036	67.0	40.4	134.4	18.7	8.9	12.9
Textiles and clothing	1,031	1,343	2,025	30.3	50.8	96.4	9.2	10.8	10.1
Other manufactured goods	2,462	3,310	5,960	34.4	80.1	142.1	10.4	15.8	13.5
Total	\$16,397	\$21,366	\$36,052	30.3%	68.7%	119.9%	9.2%	14.0%	11.3%

* Compounded.

Source: U. S. Department of Commerce

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1969, the United States trade balance with Japan was in deficit by nearly \$1.4 billion and by about \$0.5 billion with West Germany. United States exports to Japan have been hampered by Japanese import restrictions, the dynamic growth of Japanese productive capacity, and sharp competition from other Asian nations for the market for agricultural products in Japan. In contrast, the improved quality of Japanese manufactured products made these goods highly acceptable in the United States. Lower comparative prices and low United States duties also supported the growth of Japanese exports to the United States, particularly for such products as small automobiles, radios, television sets, tape recorders, cameras, and textile products. During the 1962-1969 period, the rate of increase in United States imports from Japan was almost double the rate of increase in United States exports to Japan.

United States imports from West Germany also increased nearly twice as fast as exports to West Germany during 1962-1969. The difference in the rate of increase of exports to and imports from West Germany became more pronounced in the 1965-1969 period, partly in response to price differentials that resulted from inflation in the United States as well as increased sales of small automobiles to the United States. In 1965, automobile imports from West Germany commanded about 5 percent of the American market for new cars. By 1969, West Germany's share of the United States new car market had increased to about 7 percent; the increase represents some 275,000 cars. Both West Germany and Japan have experienced rapid economic growth and have become large suppliers to the United States as well as strong competitors of the United States in other world markets.

Although export and import trade with the United Kingdom increased in the 1962-1969 period, the relative balance between the two countries remained fairly stable, with the United States maintaining a slight trade surplus. The rate of inflation in the United Kingdom was more rapid than that in the United States and thus offset any potential price advantage on the part of the United Kingdom. This tended to hold down United States imports from the United Kingdom. In order to slow the rate of inflation and improve its balance of payments position, the United Kingdom periodically implemented various restrictive monetary and fiscal policies and other domestic austerity measures during the period; eventually, the pound sterling was devalued late in 1967. Some of these measures were designed to discourage imports and to stimulate exports. These programs, however, tended to hold down United States exports to the United Kingdom.

The remaining industrialized countries among the 13 leading trading partners of the United States are all members of the European Economic Community (the Netherlands, Italy, France, and Belgium-Luxembourg). Although United States exports to the EEC increased at a slightly faster rate than total exports, the United States did not maintain its share of the growing EEC market. As the EEC countries continued their efforts toward complete integration of their economies, trade barriers among the member nations were lowered, and preferential trade agreements were established with associated nations (mainly the former French colonies in Africa). Trade between the EEC countries increased greatly, partly at the expense of nonmember countries, including the United States. In 1966, the EEC also formed a common agricultural policy that established a system of variable levies on the imports of many agricultural

products and a system of subsidy payments to EEC farmers. As a result of the subsidies that stimulated domestic farm production and high import levies, the demand for many United States agricultural products was reduced. United States exports of agricultural products to the EEC reached a peak of about \$1.6 billion in 1966, but dropped to \$1.3 billion in 1969. Shipments of agricultural commodities on which variable levies are applied fell from \$737 million in 1966 to \$441 million in 1969, while EEC imports of United States agricultural commodities not covered by variable levies rose fractionally, from \$857 million in 1966 to \$860 million in 1969.

United States imports from the EEC increased at a faster rate than total imports during 1962-1969. As mentioned previously, West Germany contributed to a large share of the growth. However, imports from Italy were also strong, especially in the 1965-1969 period. As was the case for West Germany, United States imports of automobiles from Italy increased sharply during the period under review. Imports of footwear also rose markedly. Approximately 25 percent of all non-rubber footwear sold in the United States is imported, and a large share is imported from Italy. Legislation is presently pending that would impose quotas on footwear imports into the United States, limiting such imports to a level equal to the average of imports in 1967-1969.

Economic activity has been expanding rapidly in Australia, and the country has become an important customer for United States products. However, in recent years, exports to Australia have not grown as rapidly as the growth in total United States exports. In the past, Australia was very dependent on the United Kingdom and the United States as sources of supplies and as markets for its products; however, in recent years, Australia has

turned toward its Asian neighbors as trading partners.

United States trade with Brazil, Venezuela, and India tends to fluctuate with swings in the domestic economies of those countries and with the level of production of their major exports. For example, the level of United States imports from Brazil is greatly influenced by the level of production and prices of coffee. Imports from Venezuela have been influenced by a reduced demand for Venezuelan oil, which has a higher sulfur content than crude oil from other parts of the world and, therefore, emits more pollutants when it is used. Exports to India have been reduced sharply since 1965 because of improvements in output of India's food products and the subsequent reduction of United States grain shipments to India.

Pattern of Merchandise Trade. The major shifts in the pattern of United States merchandise export and import trade during the 1962-1969 period reflect the slower growth of agricultural exports and the increased rate of growth in imports of manufactured goods (see Table VIII). The value of agricultural exports, represented by the two commodity groups "food and live animals" and "animal and vegetable oils and fats," rose at a slower pace than total merchandise exports during 1962-1969 and actually declined during 1965-1969. These were the only commodity groups to show such a pattern. The decrease in exports of animal and vegetable oils and fats was particularly sharp and resulted from a slight downward trend in world imports of animal fats and a huge world supply of low-priced vegetable oils, particularly palm oil. Palm oil production has increased greatly in the developing countries of Africa, South America, and Asia and has almost completely replaced lard in the manufacture of margarine and compound edible fats.

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Three major factors contributed to the decline in exports of "food and live animals" during the 1965-1969 period: the EEC agricultural policy, reductions in food-aid program shipments to India and Pakistan, and overall improvements in world food production. Japan is the largest market for United States farm products, but the United States has faced increasing competition in that market, particularly from Australia. After reaching a peak in 1966, cereal grain exports to Japan have decreased, and because of improved domestic production, Japan is now a net exporter of rice.

The rate of increase in exports of textiles and clothing was also extremely low during the period under review. Many developing nations establish a textile industry in their early efforts toward industrialization, both for the purpose of import substitution and for export. Textile exports increased from the low-labor cost countries, such as Japan, Hong Kong, India, and other Asian countries. As a result, the competition for United States textile exports is stronger, and United States imports of low-priced foreign textiles have risen. Although United States imports of textiles and clothing did not increase as fast as total United States merchandise imports during the 1962-1969 period, the volume of textile imports reached such proportions that some hardships existed in the domestic textile industry. Voluntary import restrictions did not improve the situation, and legislation has been proposed that would impose quota restrictions on textile imports into the United States, with the proposed quota base being the average import volume for 1967-1969.

The growth of both United States exports and imports of mineral fuels and related products were slower than the total growth in merchandise trade. Exports of coking coal, however, grew rapidly in response to demand for high-quality coal from

foreign steel producers. The relatively slow growth in mineral fuel imports is related to the United States domestic oil quota system.

United States exports of electrical apparatus, transportation equipment, and other manufactured goods all increased at a faster pace than total United States merchandise exports during 1962-1969, while United States imports of these commodity groups, plus nonelectrical machinery, also increased rapidly. The increases in imports of these commodities have been sharp since 1965. The strength in imports of transportation equipment reflects the sharp rise in imports of automobiles from Canada, West Germany, and Japan, while the surge in imports of electrical apparatus is due in part to large shipments of television sets, radios, and other consumer electrical products from Japan.

CONCLUDING COMMENTS

Total United States trade increased rapidly during the 1962-1969 period; however, merchandise imports rose at a faster pace than merchandise exports, resulting in a deterioration of the United States trade balance. Many factors contributed to these growth patterns in United States international trade, including inflation and the rapid expansion of economic activity in the United States. Inflation in the United States widened price differentials between domestic goods and foreign goods and made foreign goods relatively cheaper than domestic goods. Consequently, sharp increases were recorded in imports of manufactured goods, particularly transportation equipment.

International trade between the United States and its major trading partners has grown faster than trade with the rest of the world. In 1962, the

United States exchange of goods was approximately in balance, or in slight surplus, with its four major markets; namely, Canada, Japan, the United Kingdom, and West Germany. By 1969, the United States had developed a trade deficit with Canada, Japan, and West Germany and had only a

small trade surplus with the United Kingdom.

The rapid growth of imports and the deterioration in the long-standing United States trade surplus has contributed importantly to the recent problem of large and persistent deficits in the United States balance of payments.



DIRECT PLACEMENT OF CORPORATE DEBT

Corporations can obtain capital funds from two basic sources: internal generation and external acquisition. When capital is generated internally, a portion of corporate cash flow (net profits and depreciation charges) must be retained. When capital is acquired from external sources, a corporation may choose from several alternatives, including the sale of equity issues and borrowing. Borrowed funds, in turn, may be obtained either through loans or through the sale of debt instruments. When the sale of equities or debt obligations is used, there is the further option of making a public offering or of placing securities directly with large institutional investors.

Corporations frequently raise long-term external capital through a public offering of securities (debt or equity). The offering is handled by an underwriting syndicate that purchases securities from the issuing company either by competitive bidding or through negotiation and, in turn, sells the securities to individual and institutional investors. Underwriters assume all of the marketing risk

in return for a profit, which is represented by the difference between the price paid to the issuing corporation and the price paid by the investor minus underwriting expenses.

The alternative to a public offering is the direct placement of securities with large institutional investors, usually private and public pension funds and life insurance companies. Private or direct placement involves direct negotiation between issuer and purchaser and eliminates the underwriting function. In a direct placement, a prospective issuer investigates, often with the aid of an agent, the possible sale of securities to one investor or to a small group of institutional investors.¹ The seller and buyer negotiate the terms and conditions of the offering, and the exchange of funds and securities takes place directly.

¹An agent (usually a securities underwriter) will often bring borrower and lender together and assist in negotiating terms and conditions of the offering. The agent receives a fee for these services (usually paid by the borrower).

Within the context of total corporate external financing, this article examines the use of direct placement of corporate debt and the advantages and disadvantages of this form of corporate financing.

CORPORATE EXTERNAL FINANCING, 1949–1969

During the last half of the 1960's corporate demand for external capital rose sharply, surpassing \$10 billion per year (see Chart 1). This resurgence in the demand for external capital countered the tendency apparent during the second half of the 1950's and early 1960's for net corporate funds raised externally to account for a progressively smaller share of total net demands for funds in capital markets.² For example, during 1952-1955, the annual average ratio of corporate capital funds raised to total capital funds raised was 35 percent, compared with 11 percent during 1962-1965. In 1966-1969, the ratio rebounded to 26 percent.

Although total corporate borrowing increased substantially in the late 1960's, the volume of funds raised by direct placement of debt issues actually declined from the record level reached in 1965 (see Table I). This recent downturn reversed an upward trend that began in the 1930's.³ The volume of direct placements of debt issues fell from a high of 66.7 percent of all debt issues in 1964 to a low of 30.6 percent in 1969. For the

1953-1969 period, direct placements accounted, on average, for 44.5 percent of all debt issues.

The decline in the importance of privately placed corporate debt may also be observed in Chart 2. As the chart shows, the spread between public and private placements has increased recently, following a number of years when private borrowings exceeded public offerings.

The long-term popularity of direct placements as well as the shorter run fluctuations in the growth pattern of this form of finance can be explained in terms of the nature of a private placement. As part of this explanation, attention is given to the characteristics of recent directly placed debt issues.

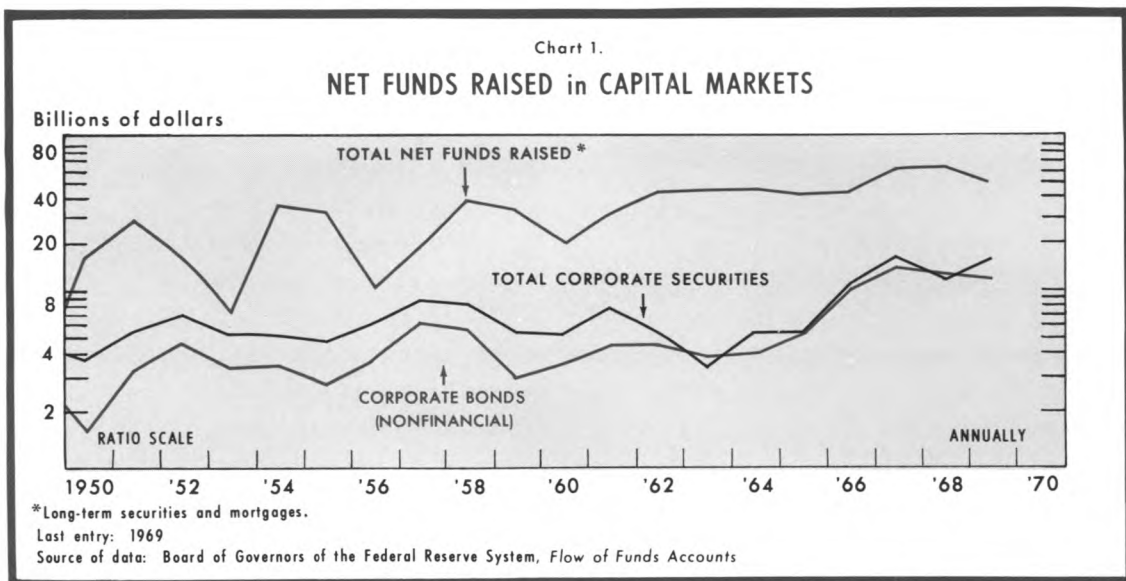
Before discussing recent direct placements, however, the limitations of the data on private placements must be noted. A *private* placement of debt is just that: a private arrangement between borrower and lender. The parties to the arrangement have no obligation to publicize their dealings and, in fact, some strongly prefer not to have these transactions made public. Of course, a desire for secrecy does not imply wrongdoing; the parties involved may prefer concealment for competitive or strategic reasons; but, as a result, the published data on private placements are incomplete.

FACTORS AFFECTING THE USE OF DIRECT PLACEMENTS

Initial Costs. Lower distribution costs to borrowers is perhaps the most frequently mentioned advantage of direct placements. Although supporting data are limited, there is evidence that the costs involved in negotiating direct placements are significantly less than the costs of floating a registered public offering (see Table II). The cost differential is particularly large for smaller issues (under \$2 million) and gradually diminishes as the

²Net funds raised in capital markets include net long-term borrowing by the U. S. Government, state and local governments, nonfinancial corporations, foreigners, and net new mortgage debt.

³See Paul M. Van Arsdell, *Corporation Finance, Policy, Planning, Administration* (New York: Ronald Press, 1968), p. 861.



size of the issue increases. The relatively high underwriting cost (underwriting spread) of public offerings accounts for a large part of the wide differential in total distribution costs. With the exception of modest fees paid to agents or "finders," nearly all distribution costs are avoided in direct placements. The saving is even larger when the services of an agent are not required.

A tabulation of underwriting spreads on public offerings of debt issues in 1963 indicates that there had been only minor changes in this expense since the earlier Securities and Exchange Commission survey (see Table II). In four of the seven issue size classes, underwriting spreads were higher in 1963 than in the earlier period, while in three size classes some reduction occurred. If expenses of direct placements and other expenses of public

offerings are essentially unchanged, distribution cost comparisons probably continue to favor direct sales, particularly for smaller issues.

A recent estimate of the expenses involved in raising \$1 million through a public offering suggests that the cost of flotation may approach 20 percent of the principal sum. These expenses include \$100,000 for the underwriter, \$25,000 in finder's fees, \$15,000 in legal fees, \$7,500 for a certified audit of the borrower, \$10,000 in printing expenses, \$15,000 for public relations, and another \$15,000 in "unaccountables" for a total of \$187,500 *excluding interest*.⁴ In this example

⁴Arlene Hershman, "Private Placement: The 'New' Money Game," *Dun's Review*, 93, 2 (February 1969), p. 81.

TABLE I

New Issues of Corporate Securities
1953-1969

Year	Public Offerings and Direct Placements			Direct Placements of Debt Issues		
	Equity and Debt	Debt Issues*		Volume (mil. of \$)	As Percent of All Debt Issues	As Percent of Equity and Debt
	Volume (mil. of \$)	Volume (mil. of \$)	As Percent of Equity and Debt			
1953	\$ 8,898	\$ 7,083	79.6%	\$3,228	45.6%	36.3%
1954	9,516	7,488	78.7	3,484	46.5	36.6
1955	10,240	7,420	72.5	3,301	44.5	32.2
1956	10,939	8,002	73.2	3,777	47.2	34.5
1957	12,884	9,957	77.3	3,839	38.6	29.8
1958	11,558	9,653	83.5	3,320	34.4	28.7
1959	9,748	7,190	73.8	3,632	50.5	37.3
1960	10,154	8,081	79.6	3,275	40.5	32.3
1961	13,165	9,420	71.6	4,720	50.1	35.9
1962	10,705	8,969	83.8	4,529	50.5	42.3
1963	12,211	10,856	88.9	6,143	56.6	50.3
1964	13,957	10,865	77.8	7,243	66.7	51.9
1965	15,992	13,720	85.8	8,150	59.4	51.0
1966	18,074	15,561	86.1	7,542	48.5	41.7
1967	24,798	21,954	88.5	6,964	31.7	28.1
1968	21,966	17,383	79.1	6,651	38.3	30.3
1969	26,744	18,347	68.6	5,613	30.6	21.0
Average 1953-1969	—	—	79.5%	—	44.5%	35.4%

* Debt issues include mortgage bonds, unsecured notes and debentures, and convertible bonds, notes and debentures.

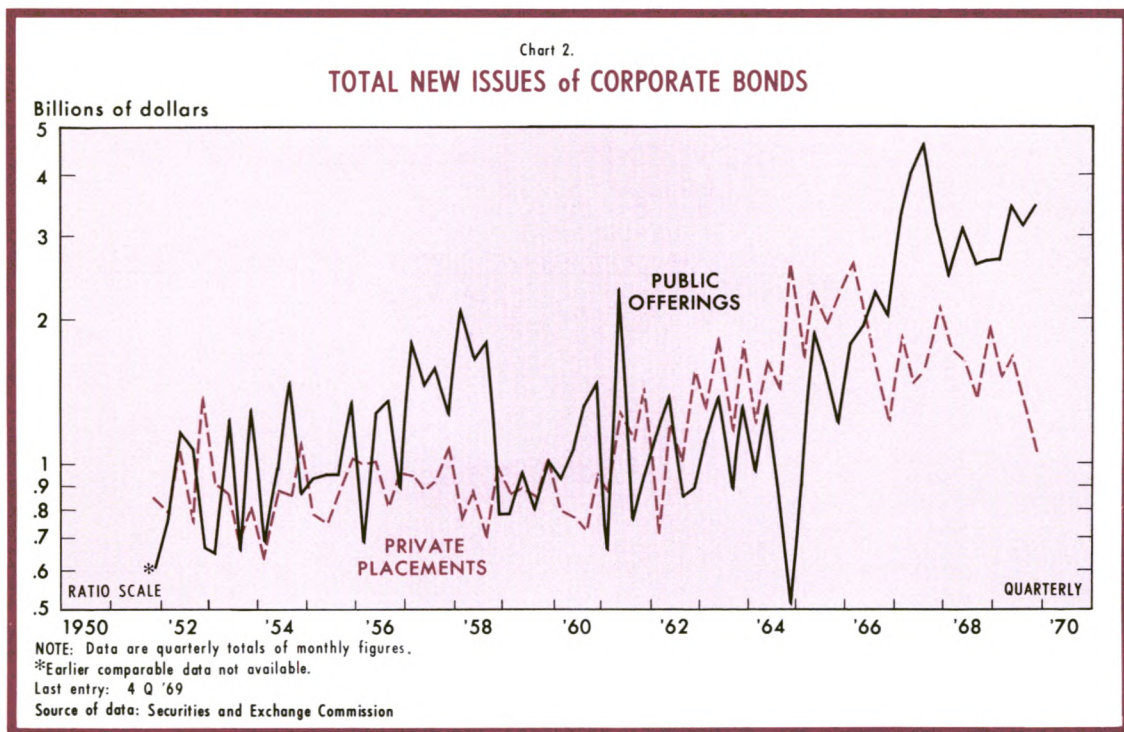
Source: Securities and Exchange Commission

of a relatively small borrowing, a private placement would probably be very attractive to the borrower, because it would eliminate the underwriting expense and result in other distribution cost savings.

Interest Rates. Although issuing costs tend to be lower for private placements than for public offerings, it is generally assumed that interest rates are somewhat higher on direct placements than on public offerings. Although reliable data are scarce, a comparison of the average of yields on all directly placed industrial bonds and Moody's Baa

Industrial bond yields tends to confirm this relationship (see Table III). The annual average spread between the yields shown in the table has a mean value of 80 basis points in favor of the Moody's series. The largest spread for the period was 110 basis points and occurred in 1952, while the smallest spread amounted to 42 basis points and occurred in 1957. Although this comparison is only an approximation because of the absence of homogeneity in such determinants of yield as quality, maturity, seasoning, size, and time of offering—it indicates the existence of the expected yield differential.

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A recent analysis, however, points out that it is an oversimplification to generalize that interest rates are higher in the private placement market than in the public market.⁵ It was found that yields on direct placements are relatively higher on issues of larger, well-known companies, but for smaller firms, yields on direct placements are about the same or somewhat lower than these companies would pay on a public offering. Thus, despite the initial cost advantage of a private placement, it is not surprising that large issues by major corporations tend to be placed in the public market.

Flexibility. Direct placements possess a convenience and flexibility that may benefit both

⁵Avery B. Cohan, *Yields on Corporate Debt Directly Placed* (New York: National Bureau of Economic Research, 1967), Ch. 6.

borrower and lender. This adaptability is essentially due to the limited number of investors involved that permits the terms and conditions of the loan to be tailored to the preferences of all parties involved.

Moreover, by paying a small commitment fee, a borrowing corporation can arrange in advance for some future capital requirements. An advance commitment protects the issuer from market uncertainties, while granting the option of canceling the issue if the need for funds does not materialize. At the same time, an investor can earmark funds for future investment and receive an immediate return from the commitment fee. Final negotiations to formulate the terms and conditions can take place at the time of actual takedown.

TABLE II

Comparative Costs of Public Offerings and Direct Placements of Corporate Debt Securities

Size of Issue (mil. of \$)	1951-1953-1955						1963	
	Public Offerings			Direct Placements			Cost Differential Between Public Offerings and Direct Placements	Underwriting Spread on Public Offerings As Percent of Proceeds
	Underwriting Spread As Percent of Proceeds	Other Expenses As Percent of Proceeds	Total Expenses As Percent of Proceeds	Fees As Percent of Proceeds	Expenses As Percent of Proceeds	Total As Percent of Proceeds		
							(percentage points)	
Under \$0.3	—	—	—	1.86%	1.49%	3.35%	—	—
\$ 0.3 - \$ 0.4	—	—	—	1.60	1.06	2.66	—	—
\$ 0.5 - \$ 0.9	7.53%	3.96%	11.49%	1.31	0.83	2.14	9.35%	4.73%
\$ 1.0 - \$ 1.9	5.80	2.37	8.17	0.97	0.59	1.56	6.61	7.89
\$ 2.0 - \$ 4.9	2.37	1.41	3.78	0.69	0.43	1.12	2.66	3.87
\$ 5.0 - \$ 9.9	1.01	0.82	1.83	0.49	0.34	0.83	1.00	1.61
\$10.0 - \$19.9	0.88	0.64	1.52	0.31	0.32	0.63	0.89	0.89
\$20.0 - \$49.9	0.85	0.48	1.33	0.22*	0.22	0.44	0.89	0.80
\$50.0 and over	0.88	0.32	1.19	—	—	—	—	0.79

NOTE: The data for 1951, 1953, and 1955 are from *Cost of Flotation Corporate Securities 1951-55*, Securities and Exchange Commission, U. S. Government Printing Office, Washington, D. C., June 1957. Total costs of public offerings include underwriters' compensation and all other fees and expenses incident to the offering; e.g., legal, printing, accounting, and engineering expenses. Total costs of direct offerings include the fees paid agents or finders and other expenses of the offering. Data for 1963 on public offerings are from a special study of underwriting spreads on 123 issues of debt securities. See *Statistical Bulletin*, Investment Bankers Association of America, Washington, D. C., June 1964.

* \$20.0 million and over.

Sources: Securities and Exchange Commission and Investment Bankers Association of America

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TABLE III

Average Yields on Directly Placed Industrial Bonds and Moody's Baa Industrial Series 1951-1965

<u>Year</u>	<u>Directly Placed</u>	<u>Moody's Baa* Industrials</u>	<u>Difference</u> (percentage points)
1951	3.84%	3.04%	0.80%
1952	4.30	3.20	1.10
1953	4.43	3.55	0.88
1954	4.44	3.40	1.04
1955	4.35	3.47	0.88
1956	4.78	3.84	0.94
1957	5.21	4.79	0.42
1958	5.31	4.59	0.72
1959	5.58	4.91	0.67
1960	5.98	5.11	0.87
1961	5.76	5.10	0.66
1962	5.81	4.98	0.83
1963	5.65	4.90	0.75
1964	5.64	4.87	0.77
1965	5.67	4.92	0.75

* Selected as a proxy for the yield on middle quality, publicly offered corporate debt.

Sources: A. B. Cohan, *Yields on Corporate Debt Directly Placed*, National Bureau of Economic Research, New York, 1967 and Moody's Investor Service

SEC Registration. Because a private placement does not involve a public offering, such securities do not have to be registered with the Securities and Exchange Commission. By foregoing SEC registration, a borrower can attempt to convince a potential lender of the soundness of the investment by referring to projected developments involving the corporation that the SEC does not permit to be included in a prospectus for a public offering. Further, SEC registration may involve a waiting period of 20 days. In contrast, private placements have been arranged and consummated in as few as four days. On the other hand, since an unregistered security cannot be traded in public markets, there is no opportunity for the borrower

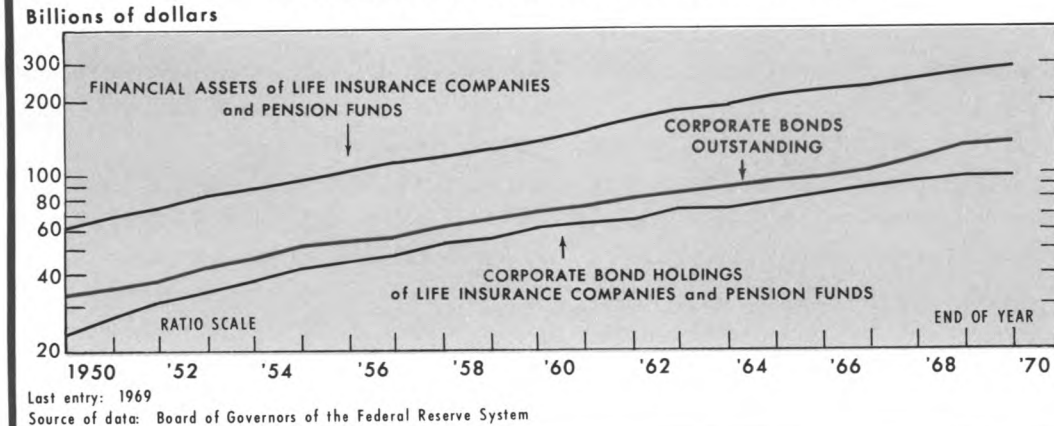
to repurchase his own debt if interest rates decline. From the lender's viewpoint, an unregistered security does not possess the liquidity of a marketable security. Thus, if a borrower expects a drop in interest rate levels, he may substitute public offerings for private placements, or insist on a call option in a loan agreement (the lender is likely to grant such an option only in exchange for a higher pre-call yield).

Institutional Demand. Until 1966, a frequently mentioned reason for the growth in direct placements was the increasing demand for corporate debt securities by insurance companies and pension funds, a demand that was not accompanied by a corresponding increase in the publicly offered supply. Institutional holdings of corporate bonds more than tripled between 1950 and 1965, while the total volume of corporate debt outstanding rose by about 175 percent (see Chart 3). The continued growth of life insurance and pension fund assets at a rate that was in excess of the rate of increase in corporate bonds outstanding was also considered to be evidence of the influence of strong institutional demand on the increase in the volume of outstanding debt in general and private placements in particular. Presumably, to the extent that this demand pull was effective, investor preferences were transmitted to borrowers in terms of very attractive (low) interest rates on corporate debt.

Whatever the merits of this argument, it is no longer true that institutional holdings of corporate bonds are increasing faster than the volume of outstanding corporate bonds. Nor is it true that life insurance and pension fund assets are growing at a faster pace than the amount of corporate bonds outstanding. From 1965 to 1969, the dollar

Chart 3.

FINANCIAL ASSETS of SELECTED FINANCIAL INSTITUTIONS and CORPORATE BONDS OUTSTANDING



amount of outstanding corporate debt issues has increased by 50 percent, while institutional holdings of these securities have risen by only 20 percent. Meanwhile, the financial assets of life insurance companies and pension funds have increased by only 30 percent as a result of the large increase in policy loans and a general slowing in the rate of growth of contractual savings institutions. The absolute amounts of these increases are: corporate bonds, \$50 billion; institutional assets, \$70 billion; and institutional holdings of corporate bonds, \$16 billion. These figures suggest that although corporate debt is still an important component of institutional assets, life insurance companies and pension funds have lost some of their enthusiasm for corporate bonds recently.

INFLATION AND PRIVATE PLACEMENTS

When prices are rising rapidly, fixed income assets, such as corporate bonds, become less

attractive investments because of greater uncertainty about their *real* yield (nominal yield adjusted downward for the reduction in the purchasing power of money) and because of capital loss associated with rising market rates of interest. In such times, investors frequently turn to equity instead of debt to hedge against inflation. Such a switch in investor preferences, especially among institutions, appears to have taken place in the United States during the last half of the 1960's, when the rate of inflation accelerated.⁶ It was recently estimated that, during 1970, non-insured pension funds will place 85 percent of their new funds in common stock, up sharply from 45 percent five years earlier; similarly, life insurance companies are expected to increase the share of their net new funds going into common stock to 16 percent in 1970, compared with 8 percent in

⁶See, for example, "The New Fashions in Financing," *Business Week*, February 7, 1970, pp. 21-22.

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1965.⁷ Much of this increase may, however, be due to stock purchases by pension programs administered by life insurance companies. The growing equity role played by life insurance companies in real estate financing is also a significant reflection of the changing investment attitude of these companies.⁸

Although money managers substantially reduced their cash holdings in previous years, there were reports in 1969 and early in 1970 of growing concern over portfolio liquidity. Because of a cautious outlook regarding cash flow prospects and demands on that cash, funds managers have become more interested in adding cash and *marketable* securities to their holdings. Thus, the preferences of institutional investors seem to have swung away from privately placed debt toward registered debt and equity shares.

As institutional investors reduce their activity in the bond market, corporate borrowers must either depend more on large numbers of individual investors, who can be reached only through public debt offerings, or increase share offerings, or both. The recent rise in publicly offered common stock and the decline in privately placed corporate bonds parallels the acceleration in the rate of inflation, as measured by the implicit GNP price deflator (see Chart 4).

In summary, the decline in the importance of direct placements of corporate debt since 1965 can be attributed in large part to the direct and indirect effects of inflation on institutional

demand for corporate debt in general and private placements in particular. As institutional lenders became more interested in equity participations, borrowers were induced to substitute public debt and equity offerings for direct placements. Similarly, equity participations and convertible issues were often used to increase the attractiveness of private placements to lenders.

PRIVATE PLACEMENTS IN 1969

During 1969, commitments for and takedowns of direct placement securities by domestic corporations totaled \$7,034 billion and consisted of 1,235 issues.⁹ Some characteristics of a portion of those transactions (\$5,615.7 billion), as reported in the *Investment Dealers' Digest*, are summarized in Table IV. Manufacturing industries accounted for the largest share of direct placements in 1969 in both the number of issues and the dollar volume, while companies in finance and real estate were second. These two categories of borrowers accounted for more than one-half of the number and dollar volume of direct placements in 1969.¹⁰ Although transportation accounted for less than 7 percent of the number of issues, these issues tended to be large and, as a result, nearly 18 percent of the dollar volume of private funding consisted of issues by the transportation industry.

⁹See "Corporate Financing Directory," *Investment Dealers' Digest*, Section II, March 3, 1970 and September 9, 1969. These figures are somewhat larger than those reported by the Securities and Exchange Commission. This discrepancy results from the *Investment Dealers' Digest* practice of reporting placements as they are contracted for, whereas SEC figures reflect takedowns.

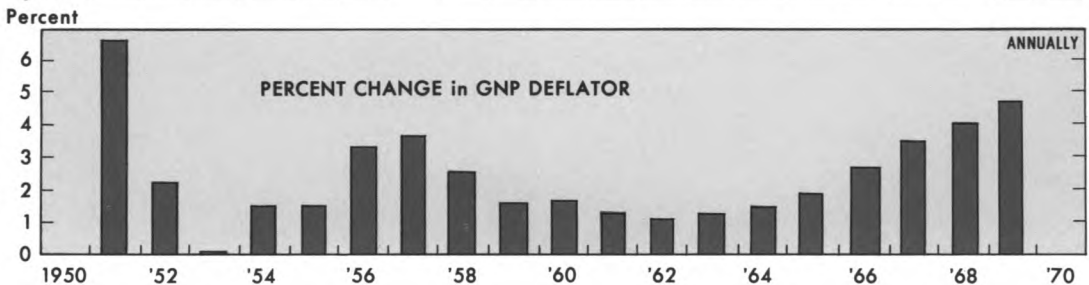
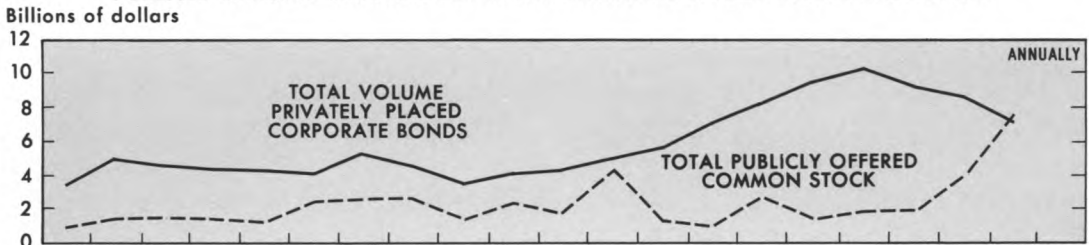
¹⁰For comparative figures from 1963, see "Direct Placement of Corporate Debt," *Economic Review*, Federal Reserve Bank of Cleveland, March 1965, pp. 13-16.

⁷Henry Kaufman, "The New Supply and Demand Dimensions in the Stock Market," Speech to the New York Society of Security Analysts, March 6, 1970.

⁸See, for example, Sanford Rose, "The Future Largest Landlords in America," *Fortune*, July 1970, pp. 90-93.

Chart 4.

PUBLICLY OFFERED COMMON STOCK and PRIVATELY PLACED CORPORATE BONDS



Last entry: 1969

Sources of data: *Investment Dealer's Digest*; Securities and Exchange Commission; U. S. Department of Commerce

Public utilities' offerings represented the smallest amount of funds raised in the private placement market.

The pattern of direct placements was much different from the pattern of public offerings during 1969. Public utilities' issues accounted for nearly 50 percent of the dollar volume of underwritings, compared with only 8 percent of private placements.¹¹ The relatively heavy use of public offerings by utilities is due in part to legal constraints; that is, in many instances, public utilities are not permitted to make private placements. In addition, the Securities and Exchange Commission study of flotation costs during

1951-1955 found that the costs of an underwritten offering of utility debt may be considerably less than the flotation costs for other industries; e.g., manufacturing.¹²

In 1969, nonconvertible debt dominated both the number and dollar volume of total privately placed debt (see Table IV). Nevertheless, nearly one-third of the issues carried carry some form of privilege to convert the securities involved into equities. In 1963, convertibles accounted for less than 3 percent of all privately placed issues. The addition of an equity feature to debt financing is a

¹¹ *Investment Dealers' Digest*, Section II, March 3, 1970, p. 14.

¹² Securities and Exchange Commission, *Cost of Flotation of Corporate Securities 1951-55*, (Washington, D. C.: Government Printing Office, 1957).

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TABLE IV

Distribution by Type of Borrower, Type of Security, and Size of Issue of Direct Placements of Corporate Debt Securities 1969

<u>Type of Borrower</u>	<u>Number of Issues</u>	<u>Percent Distribution</u>	<u>Volume of Issues</u> (mil. of \$)	<u>Percent Distribution</u>
Manufacturing*	391	34.2%	\$1,928.9	34.3%
Finance and real estate	205	17.9	1,122.6	20.0
Transportation	77	6.7	986.3	17.6
Public utilities†	97	8.4	476.9	8.5
All other	373	32.6	1,101.0	19.6
Total	1,143	100.0%	\$5,615.7	100.0%
<u>Type of Security</u>				
Mortgage bonds	48	4.2%	\$ 205.8	3.7
Nonconvertible bonds, notes, and debentures	723	63.3	3,610.7	64.3
Convertible bonds, notes, and debentures	372	32.5	1,799.2	32.0
Total	1,143	100.0%	\$5,615.7	100.0%
<u>Size of Issue</u>				
(mil. of \$)				
Under \$0.5	217	19.0%	\$ 54.5	1.0%
\$ 0.5 - \$ 0.9	178	15.6	116.9	2.1
\$ 1.0 - \$ 2.9	320	28.0	537.1	9.6
\$ 3.0 - \$ 4.9	123	10.8	441.4	7.9
\$ 5.0 - \$ 9.9	137	12.0	870.5	15.5
\$10.0 - \$24.9	123	10.8	1,774.7	31.6
\$25.0 and over	45	3.9	1,820.6	32.4
Total	1,143	100.0%	\$5,615.7	100.0%

NOTE: Details may not add to totals because of rounding.

* Includes mining and extractive companies.

† Includes electric, gas, water, and communication companies.

Source: *Investment Dealers' Digest*

logical consequence of the inflation-induced change in preferences of institutional investors.

Relatively small issues accounted for the majority of private placements, but a few large placements accounted for a major share of the dollar volume. Transactions of \$10 million or more contributed only 15 percent of the number, but nearly two-thirds of the dollar volume. In contrast,

placements of less than \$3 million accounted for more than 60 percent of the number, but only 13 percent of the dollar volume.

There is a tendency for dollar volume to be concentrated in the big issues in all borrowing groups (see Table V). In 1969, more than 60 percent of the dollar volume was in the two largest issue size classes for manufacturing, finance and

TABLE V

Distribution of the Number and Dollar Volume of Direct Placements of
Corporate Debt Securities
By Size of Issue and Type of Borrower
1969

Size of Issue (mil. of \$)	Manufacturing		Finance and Real Estate		Transportation		Public Utilities		All Other	
	Number	Volume	Number	Volume	Number	Volume	Number	Volume	Number	Volume
Under \$0.5	21.0%	1.0%	11.2%	0.5%	1.3%	*	14.4%	0.6%	26.0%	2.3%
\$ 0.5 - \$ 0.9	18.2	2.4	10.7	1.3	3.9	0.2	18.5	2.2	17.2	4.0
\$ 1.0 - \$ 2.9	25.1	8.4	32.2	10.5	20.8	3.0	29.9	9.6	29.8	16.5
\$ 3.0 - \$ 4.9	10.5	7.6	14.6	9.5	11.7	3.6	11.3	7.7	8.6	10.6
\$ 5.0 - \$ 9.9	11.8	15.3	14.2	15.5	19.5	10.9	10.3	12.5	9.9	21.2
\$10.0 - \$14.9	8.4	25.6	14.2	36.5	27.3	33.2	12.4	34.7	7.5	34.4
\$25.0 and over	5.1	39.7	2.9	26.1	15.6	49.1	3.1	32.8	1.1	11.0
Total	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%
Total Number	391		205		77		97		373	
Total Volume (mil. of \$)		\$1,928.9		\$1,122.6		\$986.3		\$476.9		\$1,101.0

NOTE: Details may not add to totals because of rounding.

* Less than 0.05 percent.

Source: *Investment Dealers' Digest*

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TABLE VI

**Distribution by Maturity and Coupon Rates of Direct Placements
of Corporate Debt Securities
1969**

<u>Maturity Class</u>	<u>Number of Issues</u>	<u>Percent Distribution</u>	<u>Volume of Issues</u> (mil. of \$)	<u>Percent Distribution</u>
No maturity reported	79	6.9%	\$ 228.8	4.1%
Under 5 years	62	5.4	237.8	4.2
5 to less than 10 years	120	10.5	298.3	5.3
10 to less than 15 years	258	22.6	791.1	14.1
15 to less than 20 years	362	31.7	1,717.6	30.6
20 years and over	262	22.9	2,342.3	41.7
Total	1,143	100.0%	\$5,615.7	100.0%
<u>Coupon Rates</u>				
No coupon reported	107	9.4%	\$ 390.0	6.9%
Under 5.00%	8	0.7	3.2	0.1
5.00% - 5.49%	14	1.2	189.4	3.4
5.50% - 5.99%	31	2.7	285.3	5.1
6.00% - 6.49%	81	7.1	415.4	7.4
6.50% - 6.99%	79	6.9	444.4	7.9
7.00% - 7.49%	157	13.7	821.1	14.6
7.50% - 7.99%	215	18.8	1,236.2	22.0
8.00% - 8.49%	185	16.2	801.4	14.3
8.50% - 8.99%	158	13.8	596.4	10.6
9.00% - 9.49%	51	4.5	279.3	5.0
9.50% - 9.99%	32	2.8	72.5	1.3
10.00% and over	25	2.2	81.8	1.5
Total	1,143	100.0%	\$5,615.7	100.0%

NOTE: Details may not add to totals because of rounding.

Source: *Investment Dealers' Digest*

real estate, and public utilities. In transportation, more than 80 percent of the dollar volume was in the two largest size classes.

Maturities of directly placed issues were heavily concentrated in the three longest maturity classes (see Table VI). Three-fourths of the number and dollar volume of all issues were due to mature in more than 10 years from the date of issue. In terms of dollar volume, more than 40 percent of the issues were due to mature in 20 years or longer. However, given the very high interest rates

prevalent in 1969, it is not surprising that maturities of privately placed issues tended to be somewhat shorter, compared with earlier years. In 1963, for example, private placements of bonds with a maturity of 20 years or more accounted for 50 percent of the dollar volume.

Although net interest costs of direct placements cannot be evaluated because of lack of data, the distribution of reported coupon rates provides an approximation of the range of borrowing costs in 1969 (see Table VI). More than 75 percent of the

TABLE VII

**Distribution of the Number and Dollar Volume of Direct Placements of
Corporate Debt Securities
By Maturity and Coupon Rate and Type of Borrower
1969**

Maturity Class	Manufacturing		Finance and Real Estate		Transportation		Public Utilities		All Other	
	Number	Volume	Number	Volume	Number	Volume	Number	Volume	Number	Volume
No maturity reported	5.4%	2.7%	5.9%	3.5%	9.1%	1.5%	8.2%	9.6%	8.3%	7.0%
Under 5 years	6.6	6.9	4.4	3.1	1.3	1.5	6.2	5.5	5.4	2.6
5 to less than 10 years	13.3	4.4	7.8	4.7	6.5	3.4	4.1	10.5	11.5	7.1
10 to less than 15 years	24.8	15.3	22.4	17.5	22.1	13.4	3.1	0.3	25.5	15.0
15 to less than 20 years	35.8	27.4	25.4	21.6	48.1	56.9	9.3	7.3	33.2	31.8
20 years and over	14.1	43.3	34.1	49.6	13.0	23.3	69.1	66.7	16.1	36.5
Total	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%
Coupon Rates										
No Coupon reported	10.2%	4.9%	7.8%	7.9%	6.5%	2.8%	3.1%	8.1%	11.5%	12.6%
Under 5.00%	0.3	*	1.0	0.1	-0-	-0-	-0-	-0-	1.3	0.2
5.00% - 5.49%	1.8	4.1	1.5	8.6	-0-	-0-	-0-	-0-	1.1	1.2
5.50% - 5.99%	2.8	6.0	3.9	5.1	2.6	3.5	1.0	0.6	2.4	6.8
6.00% - 6.49%	7.7	9.3	5.4	6.6	5.2	3.8	3.1	2.4	8.8	10.3
6.50% - 6.99%	7.2	9.7	8.3	7.7	3.9	5.1	2.1	0.3	7.8	10.8
7.00% - 7.49%	13.0	18.2	15.1	12.2	13.0	5.6	17.5	14.2	12.9	19.1
7.50% - 7.99%	17.6	19.6	20.0	22.2	20.8	31.3	29.9	30.7	16.1	13.8
8.00% - 8.49%	15.1	11.6	18.0	17.2	20.8	23.8	19.6	16.4	14.5	6.6
8.50% - 8.99%	13.3	7.8	12.2	8.9	15.6	9.5	11.3	16.5	15.5	15.6
9.00% - 9.49%	4.6	6.4	2.4	2.0	7.8	7.7	9.3	8.1	3.5	1.7
9.50% - 9.99%	3.3	0.6	2.4	0.5	2.6	3.7	2.1	2.5	2.7	0.6
10.00% and over	3.1	1.8	2.0	0.9	1.3	3.1	1.0	*	1.9	0.6
Total	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%

NOTE: Details may not add to totals because of rounding.

* Less than 0.05 percent.

Source: *Investment Dealers' Digest*

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number and dollar volume of placements carried coupon rates ranging between 6 percent and 9 percent. Placements with rates of 7 1/2 to 8 percent accounted for the largest share of volume (22 percent) and the heaviest concentration in number of issues (nearly 19 percent).

Data on maturity and coupon rates by type of borrower reveal considerable variation in the distribution of direct placements among industry groups (see Table VII). For example, public utility borrowing was concentrated in the long end of the maturity spectrum (over 20 years), while transportation was heavy in the intermediate maturities (10 to 20 years). Although manufacturing, real estate, and finance companies placed over one-fourth of their debt with a coupon rate of less than 7 percent, only about 4 percent of the dollar volume of public utilities placements and 12 percent of transportation issues were placed at such favorable rates. The relatively high coupon rates on utility debt is a reversal of previous

patterns, where public utility obligations were generally accorded low coupons in recognition of their high quality. Transportation companies had the largest share of the dollar volume of debt placed at rates above 9 1/2 percent.

CONCLUDING COMMENTS

Private placements frequently provide the small, little-known firm with a relatively low-cost and highly flexible external source of capital funds. The private placement market is also attractive to a firm that must depend on projected developments to successfully market its debt and to a firm that must raise capital quickly, perhaps to finance merger activity. During periods of inflation and liquidity squeeze, however, investor demand for nonmarketable debt securities tends to decline. Nevertheless, the advantages of a direct placement are such that when the price level stabilizes, the private placement market will probably regain its prominence as a source of external corporate financing.



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