

# FEDERAL RESERVE BANK OF NEW YORK



## MONTHLY REVIEW

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## The Business Situation

Business activity has continued to decline this spring, but at a pace that may have slowed somewhat since the earlier months of the recession. Factory output and employment are still being reduced but not quite so rapidly as during the winter, while construction activity, helped by the better weather, now appears to be experiencing some seasonal upturn. In March and April sales of new cars, though remaining far below year-earlier levels, at least declined no further, while department store sales improved (when allowance is made for seasonal factors such as the early date of Easter this year). Military ordering apparently has begun to advance somewhat, and a few industries outside the defense sector also have reported that sales and orders seem to be leveling out for the present. After allowing for seasonal variations, total new orders received by manufacturers of durable goods declined only slightly in February and March.

The steadying in demand has not been sufficiently strong or widespread, however, to stave off further cuts in production. In most capital goods industries order backlogs are still shrinking, with the volume of incoming business failing by a considerable margin to close the gaps in work schedules which are developing as delivery is made on orders dating back to last year. In many lines, moreover, the slowing-down in the sales decline has apparently been matched by a speed-up in the liquidation of inventories, and has provided relatively little stimulus to current production. As a result, layoffs of industrial workers have continued at a very rapid rate, and unemployment in industrial areas has increased further. Total unemployment did fall slightly in April to 5.1 million persons, as increased seasonal hiring in construction and agriculture offset the layoffs in manufacturing and related industries, but the reduction was much smaller than the usual March-to-April decline; the seasonally adjusted unemployment rate (unemployment as a proportion of the labor force) rose to 7.5 per cent, from 7.0 per cent in March.

In all the business cycles since World War I, the period of actual decline has exceeded eighteen months only once—during the depression of the early thirties—and in most other cases has lasted only about a year. With the present contraction already well into its third quarter, therefore, the tentative signs of a bottoming out that have recently begun to appear have been interpreted by some observers as conforming to the usual pattern. Whether a leveling-off in business activity does actually come soon evidently depends in considerable degree upon whether the current

steadying of demand is firmly enough based to withstand the continued downward pressures from declining employment and incomes in some major industries. But paralleling the question whether aggregate effective demand will be maintained is another question of increasingly critical importance as the recession continues. Will price and cost rigidities prevent the flexible change and adaptation which a market economy must have if it is to restore that kind of balance between the composition of output and the composition of demand which will engender a resumption of sustained over-all expansion? How these questions will be resolved over the next few months no one can predict with assurance.

Several important forces will be at work, however, to slow the momentum of the recession. Among these are important official actions such as the prospective rise in military and other Government spending, the steady advance of State and local government outlays, and the vigorous steps to ease credit taken by the Federal Reserve System. Partly as a result of these actions, moreover, both business and consumers appear to have remained confident that the deterioration will not proceed much further. Notwithstanding sharp declines in sales, most industries have only moderately curtailed the investment plans they held at the onset of the recession, while consumers on the whole have reduced their spending relatively little except on automobiles and other "big-ticket" items. Moreover, if manufacturers and distributors are to have the stocks needed to support present sales, or even somewhat lower rates of sales, they cannot continue the recent pace of inventory liquidation for many months longer.

There are some grounds for hoping that consumer willingness and ability to buy may soon be bolstered by a leveling off and ultimately a reduction in the cost of living. Retail prices of manufactured consumer goods other than food have already been edging lower for several months, and it seems only a matter of time until the recent spurt in food prices, which has largely reflected unusually bad weather and delayed cattle marketings, will be at least partly reversed. Meanwhile, the "cost of living" may be easing for business firms as well. Strong upward pressures on costs undoubtedly persist as hourly wage rates rise, and because many firms are forced to run their plants at substantially less than the production rates for which they are designed. On the other hand, industrial materials prices have been tending lower, and some equipment and similar items are becoming available below list prices.

Furthermore, recent data suggest that wage costs (per unit of output) also may have turned downward, reflecting such factors as the installation of new machinery, the sharp reduction in overtime work at premium pay, and, quite probably, the greater efficiency to which the recession has spurred both management and labor.

### THE SCOPE OF THE RECESSION

The recession has made sizable inroads into production, employment, and profits in most nonfarm industries. (Farm income, on the other hand, has actually expanded by about 5 per cent since last August.) Unemployment rates have risen in all lines of work, even including the service industries and government, while output has contracted by at least 5 per cent in all but a handful (food, tobacco, chemicals, and printing and publishing) of the major industry groups included in the Federal Reserve's industrial production index.

The breadth of the recession reflects the substantial declines that have occurred, over a relatively short span of time, in most of the major sources of demand (see

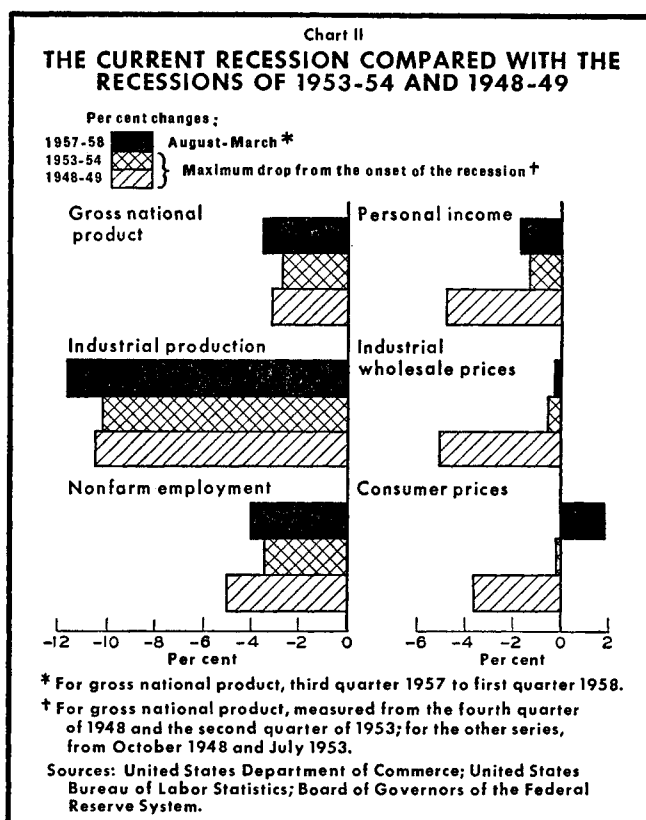
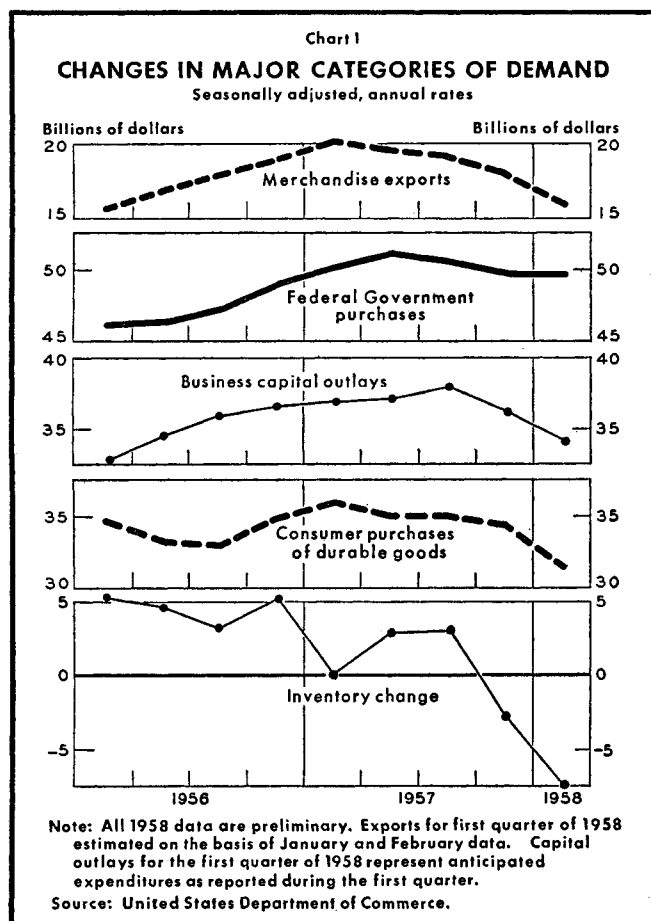


Chart I). In the second quarter of 1957, exports of merchandise began to recede from the unsustainable post-Suez peak. Federal purchases of goods and services started to fall in the third quarter of 1957. Business capital outlays turned downward in the fourth quarter, and consumer purchases of durable goods, which had been more or less steady during 1957, dropped sharply in the first quarter of 1958. Moreover, as usually happens at turning points in demand, these declines have been accompanied by an abrupt shift from inventory accumulation to rapid liquidation, which, in effect, has been equivalent to a reduction of 10 billion dollars in the annual rate of current demand.

Some weakening of demand in most of these key sources also occurred in 1948-49 and 1953-54, but during neither of these earlier periods was there a comparable bunching of declines. Exports, in particular, were a source of strength in both the previous recessions, and the declines in consumer spending were relatively transient and mild, probably in part due to the tax cuts that took effect in mid-1948 and at the beginning of 1954. It is not surprising, therefore, that over the first seven months (August-March) of the current recession, most of the comprehensive measures of business activity (see Chart II), such as gross national product, nonfarm employment, and indus-

trial production have declined faster than during the corresponding periods of the earlier recessions. Indeed, measured in percentage terms, the declines in these indicators have already carried beyond those recorded for the full period of decline in 1953-54 and, generally speaking, about as far as in 1948-49.

Despite the more rapid contraction in business activity in the current recession, neither wholesale nor retail prices have responded to nearly the same extent as in the previous postwar contractions. A considerable part of this difference in price behavior is attributable to the recent rise in farm and food prices, which contrasts with a steep drop in 1948-49 and a more gentle decline in 1953-54. Unquestionably, however, nonfarm prices also have been "stickier" than during the earlier recessions. The reasons for the growing degree of cost and price inflexibility are probably many and complex; whatever they may be, however, the current experience once again underscores the importance of policies to restrain general price rises during periods of prosperity, if the price level is to be kept from creeping progressively higher. As already suggested, there is basis for concern over whether the downward rigidity of some costs and prices may not, in effect, be prolonging the recession by delaying the corrective readjustments needed to overcome it.

#### THE CAPITAL GOODS SECTOR

One important contractionary force in the recession has been the drop in business outlays for new plant and equipment. Output in the capital goods industries has already been reduced by about 15 per cent since the peak reached about a year ago, but even so, shipments probably are still running ahead of new orders, and backlogs of unfilled orders are still falling. With the exception of work on public utility projects, which has remained at peak rates, roughly comparable declines have occurred in business construction and in contract awards for new construction.

The decline in capital investment reflects in part the sizable margins of unused capacity that have appeared in most major industries. On the basis of the recent McGraw-Hill survey, output in manufacturing is currently averaging only about 75 per cent of capacity, compared with over 90 per cent at the crest of the boom, and, while more difficult to measure, underutilization of facilities undoubtedly also prevails in many segments of other industries such as transport and retail trade. Of course, much of the present gap between consumption and potential output reflects the temporarily reduced sales rates and the liquidation of inventories associated with the recession, but some part of the margin probably represents capacity

built to meet future demand increases expected to accompany the secular growth in population and incomes. It is possible that a higher proportion of the heavy capital outlays in 1955-57 may have gone into expansion of capacity, and less into programs for raising productivity through the modernization of existing plant, than was generally thought at the time.

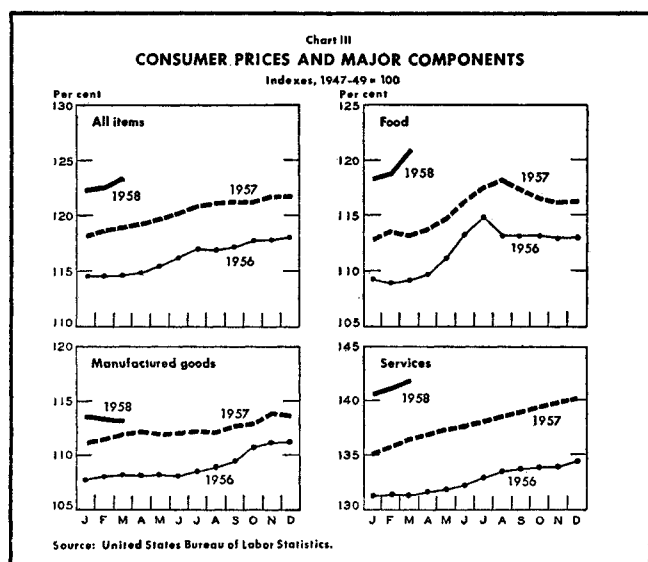
According to the United States Department of Commerce-Securities and Exchange Commission survey released in March, businessmen expect to reduce their capital outlays for 1958 by about 5 billion dollars, or 13 per cent, from 1957. Particularly sharp curtailments, ranging upward of 25 per cent, are anticipated by such industries as the railroads, primary metals, and autos, but almost all groups plan substantial reductions. The public utilities, which have scheduled a 4 per cent increase, are the only sizable sector in which plans are running counter to the general trend.

The retrenchment in outlays is to be accomplished, the results of the survey imply, by successive reductions in spending as the year progresses. By the end of the year, the drop in the outlay rate from the peak reached in the third quarter last year may approximately match the 20 per cent decline which occurred in 1948-49.

#### CONSUMER DEMAND

While the decline in the output of consumer goods set in later than in the producer goods area, it has been more rapid; as a result, the drop in the two sectors is now roughly equal in magnitude. The deepest cutbacks have occurred in automobile assemblies, which in April were running 40 per cent below a year ago, but appreciable reductions have also been recorded in many other consumer goods lines. Total consumer spending in the first quarter was about 1 per cent below the summer 1957 peak, but expenditures on food and services increased, perhaps to some extent at the expense of other, more postponable purchases, such as cars, other consumer durables, and clothing; spending on these latter items contracted by 8 per cent from the third quarter of 1957 through the first quarter of this year.

The increase in outlays on food and services largely reflects the rapid rise in the prices of these categories. An increase of 1 per cent in the price of food and essential services may be said to cost the public on the order of 1½ billion dollars annually; and these prices have advanced by some 5 per cent since last year (see Chart III). It must be kept in mind, however, that the official consumer price index overstates the rise in living expenses to the extent that people can—and do—avoid the higher



prices by rearranging their purchasing patterns. This applies particularly to foods; for example, consumers probably have reacted to the sharp rise in the prices of fresh fruits and vegetables by switching to canned or frozen foods. In contrast to food and service costs, retail prices of durable goods have been drifting lower—new car prices, for example, were reported by the United States Bureau of Labor Statistics to have been less than 2 per cent higher in March than a year earlier, compared with a margin at model introduction time of over 4 per cent. There is also some evidence that the sharp and well-publicized price cuts on previously “fair-traded” appliances may have boosted total sales in these lines.

The fact that the decline in total consumer outlays has been so moderate is explained at least in part by a large increase in social security payments as more older persons file for retirement (probably because of the reduced availability of jobs) and by the sharp rise in unemployment insurance and other public as well as private payments (such as the “supplementary unemployment benefits” provided by the labor contracts in the auto, steel, and some other industries). Since last August, the annual rate of government “transfer payments”, which most recipients presumably spend quickly, has increased by 3 billion dollars, offsetting a third of the 9 billion drop (through March) in other sources of personal income.

In the past, sales of consumer durable goods have frequently tended to parallel fluctuations in the buying of new homes, and they may again. Private housing starts declined 17 per cent from the 1957 peak of 1,056,000 units (annual rate) reached last August, to only 880,000

units in March 1958. In the last few months, however, there has been an unusually rapid increase in the availability of mortgage funds, reflecting the easing of Federal Reserve credit policies, the reduction in the competing demands for credit on the part of businesses, as well as to some extent the raising of the maximum interest rates on Veterans Administration-guaranteed mortgages by the Emergency Housing Act. In addition, Federal Housing Administration and VA regulations have recently been liberalized in several important respects, including the removal of the downpayment requirements on VA mortgages and the lowering of such requirements on FHA-insured mortgages to the extent authorized by the Act. In March and early April applications for approvals for new building under these programs increased. The data for housing starts in April, not available at this writing, may indicate to what extent this gain reflects a shift from conventional financing, and to what extent a net addition to the total volume of building.

One major area of demand that has continued to expand in the face of the recession has been State and local government spending, aided by the credit ease that has promoted the flotation of a record volume of municipal securities issues during the opening months of this year.

#### THE INVENTORY SITUATION

While there have been sizable declines in the production of most types of finished goods, some of the deepest cut-backs have occurred in the production of materials and parts involved in the manufacture of a broad range of finished products—for example, steel, building materials, and fuels. Demand for these “general purpose” materials has been curtailed not only by the reduced demand for finished goods, but by rapid inventory liquidation on the part of both users and producers. In the first quarter, manufacturers’ inventories were being drawn down at an annual rate of close to 6 billion dollars, the fastest rate of liquidation recorded during the postwar period. Most of the reduction has taken place in the volume of goods-in-process, paralleling the drop in industrial output. Manufacturers’ stocks of raw materials and of goods ready for sale (which usually account for two thirds of the total) have decreased only slightly, and still appear high in relation to current output and sales rates—especially in view of the quick delivery now generally obtainable, and the “soft” price situation prevailing for a number of important products.

Through March (the latest month for which data are available) manufacturers’ sales were still falling faster than their inventories, so that inventory/sales ratios—probably



one of the chief measures that influence inventory policies—have continued to rise. On the basis of past experience, some leveling-off in sales will probably be required to bring about the initial reduction in inventory/sales ratios. While a downturn in these ratios would not necessarily signal an immediate end to the decline in inventories, it would suggest that the point of most rapid liquidation had been passed.

#### IN CONCLUSION

The information now available concerning March and April developments suggests some lessening in the downward thrust of the recession. The contraction in total sales and orders has slowed down but, allowing for the effects of seasonal influences, output and employment are still falling. So far, business and consumer confidence appears

to have been well-maintained, but there is justifiable concern that this confidence might be undermined by heavy and prolonged unemployment with its attendant hardships and social strains.

In view of these considerations, with business activity still declining, and with only rather tentative indications of a leveling off yet apparent, recent Federal Reserve actions have been designed to assure a monetary environment that will foster recovery. The machinery of finance cannot produce the changes needed to overcome the underlying causes of the recession nor assure the resumption of production. But, when the competitive forces of the market are bringing about the correctives, and the energy of government is providing a new stimulus, there should be an ample supply of credit—out in front of the economic needs—to help in fulfilling those needs.

### Money Market In April

Federal Reserve Bank discount rates and member bank reserve requirements were both lowered in April, for the third reduction in each since the beginning of the year. Reflecting these moves and other market influences, average free reserves rose to 536 million dollars, the highest monthly average since late in 1954, and most market interest rates adjusted downward to lower levels. The capital markets were particularly active, with a large volume of new offerings successfully floated at generally declining yields, including a 3.9 billion dollar intermediate-term cash borrowing by the Treasury which was heavily oversubscribed and soon quoted at a premium bid.

On April 17 discount rate reductions from  $2\frac{1}{4}$  per cent to  $1\frac{3}{4}$  per cent, effective on the following day, were announced by the Federal Reserve Banks of New York, Philadelphia, Chicago, St. Louis, and Minneapolis. Six other Reserve Banks made similar cuts during the following two weeks, with the new  $1\frac{3}{4}$  per cent rate taking effect on April 22 at the Reserve Banks of Boston and Atlanta, on April 25 at the Reserve Banks of Cleveland, Richmond, and Kansas City, and on May 1 at the Reserve Bank of San Francisco. At the end of the month only the Federal Reserve Bank of Dallas remained at  $2\frac{1}{4}$  per cent.

The Board of Governors also announced on April 17 that member bank reserve requirements against net demand deposits would be lowered by  $\frac{1}{2}$  of 1 percentage point at reserve city banks (effective on April 24) and by 1 percentage point at central reserve city banks ( $\frac{1}{2}$  of 1 percentage point effective on April 17 and the other  $\frac{1}{2}$  of

1 percentage point effective on April 24). Reserve requirements against net demand deposits at country banks remained unchanged, as did requirements against time deposits at all member banks. The new reserve requirements against demand deposits are thus 18 per cent for central reserve city banks,  $16\frac{1}{2}$  per cent for reserve city banks, and 11 per cent for country banks; against time deposits they remain at 5 per cent for all member banks. About 450 million dollars of reserve balances were released by this reduction, making a total of close to 1.5 billion freed in this manner thus far this year.

The decline in market interest rates extended over a broad front. After having fallen almost steadily since last October, Treasury bill yields held relatively close to the  $1\frac{1}{8}$  per cent level during most of the month, but rates on commercial paper and bankers' acceptances both declined—by  $\frac{3}{8}$  per cent and  $\frac{1}{4}$  per cent, respectively—partly in adjustment to the prior declines in bill yields. And in the wake of the cut in the discount rate, the principal banks in New York City and the other financial centers lowered their lending rates to prime customers from 4 to  $3\frac{1}{2}$  per cent, the second  $\frac{1}{2}$  per cent reduction during the year thus far. Bond yields also declined on balance over the course of the month, with average yields on outstanding long-term Treasury and seasoned high-grade corporate and municipal securities all falling by about  $\frac{1}{8}$  of 1 per cent. The effective rate for Federal funds fluctuated considerably from day to day, but at all times remained below the discount rate.

## MEMBER BANK RESERVE POSITIONS

Average member bank free reserves rose to 536 million dollars over the five weeks ended in April, about 50 million dollars above the average for the four statement weeks ended in the previous month, despite a sizable increase in member bank loans and investments and deposits. Excess reserves rose to 670 million dollars from 619 million, while average member bank borrowing from the Reserve Banks remained virtually unchanged at 134 million. In addition to the expansion in primary reserves, member banks continued to rebuild their liquidity positions, with the weekly reporting banks acquiring almost 1.9 billion dollars of Government securities in the five-week period ended April 23.

In the last two weeks of the month free reserves averaged 568 million dollars as the above-mentioned reduction in central reserve city and reserve city member bank reserve requirements went into effect. Over much of the month there was moderate pressure upon the reserve positions of the New York and Chicago central reserve city banks, despite the availability of reserve balances in the banking system as a whole, since the bulk of the free reserves was lodged in the country banks. However, the differential adjustment in reserve requirements eased the reserve position of the central reserve city banks, both in New York and Chicago, by freeing an estimated 130 million dollars of their average reserve balances in each of the weeks ended April 23 and 30.

Gold outflows and related foreign account transactions drained reserve balances steadily over the period, as has been the case in recent months, reversing the inflow of funds through such transactions that had taken place during most of last year. About 450 million dollars of reserves were absorbed by this factor during the five statement weeks ended in April. Since mid-February this drain has amounted to about 750 million dollars, as several foreign nations have converted additions to dollar holdings into gold in line with their traditional practices in the holding of reserves. However, as has also been the case in recent months, the impact upon reserve positions was offset by the lowering of reserve requirements and by counteracting open market operations designed—in conjunction with movements in other factors affecting the reserve base—to replace the funds thus absorbed. System outright holdings of short-term Treasury securities increased by 156 million dollars between March 26 and April 30, and a sizable volume of repurchase agreements was written with Government securities dealers from time to time during the period, although none of these was outstanding at the close of the month.

During the year thus far—from the end of December

Table I  
Changes in Factors Tending to Increase or Decrease Member Bank Reserves, April 1958  
(In millions of dollars; (+) denotes increase, (—) decrease in excess reserves)

Factor	Daily averages—week ended					Net changes
	Apr. 2	Apr. 9	Apr. 16	Apr. 23	Apr. 30	
<i>Operating transactions</i>						
Treasury operations*	+ 125	+ 44	+ 25	+ 51	— 195	+ 50
Federal Reserve float	— 207	+ 103	— 50	+ 161	— 213	— 206
Currency in circulation	— 112	— 108	+ 11	+ 116	+ 99	+ 6
Gold and foreign account	— 123	— 92	— 145	— 41	— 50	— 451
Other deposits, etc.	+ 66	— 122	+ 114	+ 7	+ 30	+ 95
Total	— 250	— 175	— 44	+ 293	— 330	— 506
<i>Direct Federal Reserve credit transactions</i>						
Government securities:						
Direct market purchases or sales	+ 107	+ 3	— 17	+ 93	— 92	+ 94
Held under repurchase agreements	— 34	—	+ 22	— 14	+ 6	— 20
Loans, discounts, and advances:						
Member bank borrowings	— 20	— 54	+ 109	— 87	+ 13	— 39
Other	— 2	— 1	—	—	—	— 3
Bankers' acceptances:						
Bought outright	—	— 1	+ 1	— 1	— 1	— 2
Under repurchase agreements	—	—	—	—	—	—
Total	+ 51	— 51	+ 113	— 8	— 75	+ 30
Total reserves	— 199	— 226	+ 69	+ 285	— 405	— 476
Effect of change in required reserves†	+ 210	+ 163	— 48	— 223	+ 347	+ 449
Excess reserves†	+ 11	— 63	+ 21	+ 62	— 58	— 27
Daily average level of member bank:						
Borrowings from Reserve Banks	144	90	199	112	125	134‡
Excess reserves†	695	632	653	715	657	670‡

Note: Because of rounding, figures do not necessarily add to totals.

\* Includes changes in Treasury currency and cash.

† These figures are estimated.

‡ Average for five weeks ended April 30.

to the end of April—System outright holdings of Treasury securities have decreased by 38 million dollars as compared with declines of 1.4 billion in the corresponding period in 1957, 1.1 billion in 1956, 1.3 billion in 1955, and 685 million in 1954. Furthermore, the three reductions in reserve requirements during the year thus far, the first reductions since mid-1954, have freed about 1.5 billion dollars of additional reserve balances. As a result of these influences and of the many other factors that affect reserve positions, total member bank reserve balances at the end of April were only about 780 million dollars below the end-of-December level, while required reserves were 1.5 billion dollars lower. Partly reflecting the substantial net gain of usable reserves, total loans and investments adjusted at the weekly reporting banks have increased by 3.1 billion dollars through the first sixteen weeks of 1958 (see Table II), compared with a contraction of 918 million in the corresponding period last year and contractions of 1.2 billion dollars in 1956, 1.6 billion dollars in 1955, and 2.4 billion in 1954.

## GOVERNMENT SECURITIES MARKET

The prices of Treasury notes and bonds rose almost steadily in active trading until the last week of April,

when a rather sharp break occurred over a few days. Investment demand remained fairly strong, in large part due to market anticipations of continued credit ease. To a large extent trading consisted of switching transactions designed to lengthen investor portfolios and acquire higher coupon issues, but prices of shorter term securities were maintained by buying attributable primarily to banks rebuilding liquidity positions.

Activity early in the month centered around the Treasury's cash offering of 2½ per cent notes due February 15, 1963, announced on April 2. The subscription books were open only on April 7. Commercial banks were permitted to pay for their own and their customers' allotments by credit to Treasury Tax and Loan Accounts, with payment required by April 15. The offering was heavily oversubscribed, with total subscriptions amounting to 15.7 billion dollars. Subscriptions for over \$25,000 were allotted on a 24 per cent basis, but not less than \$25,000, and those for \$25,000 or less were allotted in full. A total of 4.0 billion dollars of the notes was issued, including 100 million dollars that went to Government Investment Accounts.

The new notes quickly moved to a premium bid of about ½ of a point in "when-issued" trading and then moved higher over the course of the month. At the close of the month the new issue was quoted at 100¾<sub>32</sub> (bid).

Over the month as a whole, issues maturing before 1962 generally gained from ¾<sub>32</sub> to 1½<sub>32</sub> of a point, while those in the 1962-72 range gained up to about 1½ points. The 3's of 1995 closed at 97¾<sub>32</sub>, up 30<sub>32</sub>; the 3½'s of 1990 closed at 105¾<sub>32</sub>, up 129<sub>32</sub> points; and the 3¼'s of 1978-83 closed at 102¾<sub>32</sub>, up 20<sub>32</sub> of a point.

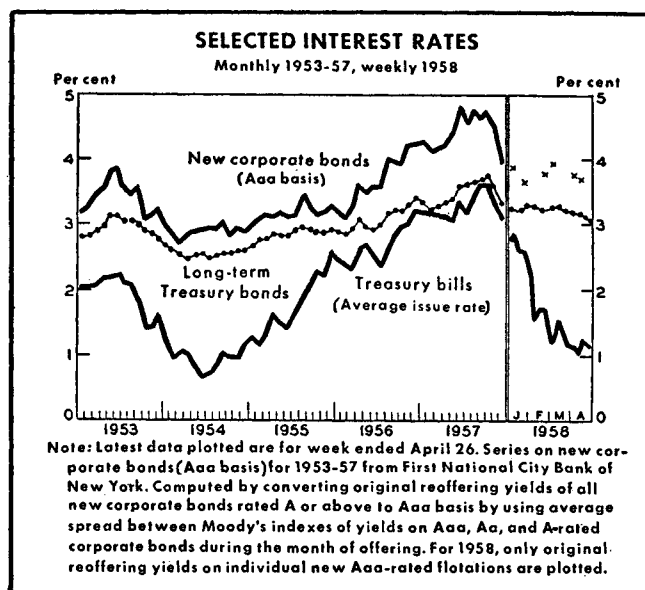
Treasury bill yields moved within a fairly narrow range over most of the month. Longer bills traded at about 1½ per cent during the first half of the period, dropped to about 1 per cent shortly after the announcement was made of the changes in reserve requirements and the discount rate, and then rose somewhat near the end of the month. Occasional pressures in the central money market resulted in offerings of bills from commercial banks adjusting reserve positions, but the yield rise was moderate. The average issuing rate in the regular Monday auction fell to 1.074 per cent on April 7 from 1.148 per cent the preceding week, rose to 1.225 per cent on April 14, and then declined again to 1.055 per cent in the auction held on April 21, the lowest level since January 1955. In the final auction of the month, held on April 28 for bills maturing on July 31, the average issuing rate rose to 1.367 per cent, but these bills were quoted at 1.20 per cent bid by the close on April 30.

## OTHER SECURITIES MARKETS

The tone of the corporate and municipal bond markets improved during April and most new offerings moved fairly well at declining yields, despite a continued heavy volume of flotations. An estimated 700 million dollars of municipal bonds were marketed, 250 million more than in the previous month but about the same as in the corresponding month last year, while 760 million dollars of corporate bonds for new capital purposes were floated, 320 million greater than in March and 510 million more than in April 1957. Nevertheless reoffering rates on new issues generally moved lower over the month. Moody's index of seasoned Aaa-rated corporate bonds fell 9 basis points to 3.55 per cent and the index for similarly rated municipals declined 15 basis points to 2.64 per cent.

As the accompanying chart indicates, the yield decline in the capital markets during April reversed the trend toward a widening spread between short and long-term yields that had been taking place during the past few months. During the first quarter of the year short-term rates had fallen rather sharply, while long-term yields had held relatively stable or—as during February and March—even moved higher. By early April the differential between short and long rates had thus increased to the widest point since the early 1940's. However, this differential narrowed somewhat during the month, although near the close some new issues were moving slowly at the lower rate levels and yields on longer Governments were rising.

As mentioned earlier, rates on bankers' acceptances and commercial paper moved lower during the month. On April 7, April 14, and again on April 21 commercial paper dealers reduced their rates by ⅛ of 1 percentage





point, to bring the offered rate on prime 4 to 6-month paper down to  $1\frac{3}{4}$  per cent. On April 10 the major finance companies that place their paper directly with investors announced a rate reduction of  $\frac{1}{8}$  of 1 percentage point on all maturities, and followed with a cut of  $\frac{1}{4}$  of 1 percentage point on April 21, to bring the offered rate on 30 to 89-day directly placed paper to  $1\frac{1}{4}$  per cent. Bankers' acceptance dealers also announced a rate reduction, of  $\frac{1}{4}$  of 1 percentage point across the board on April 18, thus lowering bid and asked rates on 90-day acceptances to  $1\frac{1}{2}$  per cent and  $1\frac{3}{8}$  per cent, respectively.

#### MEMBER BANK CREDIT

Total loans and investments of the weekly reporting member banks increased by 1.6 billion dollars during the five weeks ended April 23, as a 2.1 billion dollar expansion in investments more than offset a 515 million dollar decline in loans. Business loans decreased by 801 million dollars, but securities loans increased by 219 million.

The 801 million dollar drop in outstanding business loans was spread throughout most of the industry categories. It included a contraction of 328 million dollars in bank borrowings by sales finance companies, 158 million in takings by food, liquor, and tobacco concerns, and 138 million in loans to metals and metal products firms. During the corresponding five weeks last year business loans had fallen 221 million dollars. For the sixteen weeks of 1958 elapsed through April 23, business loans have fallen by 2.0 billion dollars and total loans by 1.6 billion at the weekly reporting banks; in the first sixteen weeks of 1957, business loans had increased by 247 million dollars but total loans had declined by 303 million.

The expansion in investments primarily reflected bank acquisition of the new 2½ per cent Treasury notes of 1963, which were subscribed for on April 7 and dis-

Table II  
Changes in Principal Assets and Liabilities of the  
Weekly Reporting Member Banks  
(In millions of dollars)

Item	Statement week ended					Change from Dec. 31, 1957 to Apr. 23, 1958
	Mar. 26	Apr. 2	Apr. 9	Apr. 16	Apr. 23	
<b>Assets</b>						
Loans and investments:						
Loans:						
Commercial and industrial loans	- 15	- 186	- 182	- 2	- 416	- 2,009
Agricultural loans	-	+ 2	+ 8	- 4	+ 6	+ 24
Securities loans	- 517	- 97	+ 441	+ 513	- 121	+ 746
Real estate loans	+ 24	- 39	+ 17	+ 17	+ 6	- 26
All other loans (largely consumer)	- 39	+ 19	- 21	+ 91	- 15	- 337
Total loans adjusted*	- 545	- 307	+ 263	+ 613	- 539	- 1,622
Investments:						
U. S. Government securities:						
Treasury bills	- 127	- 63	- 112	+ 147	- 174	+ 30
Other	- 20	+ 68	+ 54	+ 1,962	+ 117	+ 3,654
Total	- 147	+ 5	- 58	+ 2,109	- 57	+ 3,684
Other securities	+ 31	+ 39	+ 88	+ 157	- 65	+ 1,003
Total investments	- 116	+ 35	+ 30	+ 2,266	- 122	+ 4,687
Total loans and investments adjusted*	- 661	- 272	+ 293	+ 2,879	- 661	+ 3,065
Loans to banks	- 179	- 26	+ 336	+ 26	- 116	+ 744
Loans adjusted* and "other" securities	- 514	- 277	+ 351	+ 770	- 604	- 619
<b>Liabilities</b>						
Demand deposits adjusted	- 736	- 388	+ 1,132	+ 1,240	- 130	- 526
Time deposits except Government	+ 217	+ 58	+ 190	+ 149	+ 139	+ 2,835
U. S. Government deposits	+ 236	- 842	- 1,380	+ 1,762	- 341	+ 647
Interbank demand deposits:						
Domestic	- 250	+ 1,020	- 320	+ 291	- 744	- 1,559
Foreign	- 38	+ 41	+ 8	+ 3	+ 8	- 180

\* Exclusive of loans to banks and after deduction of valuation reserves; figures for the individual loan classifications are shown gross and may not, therefore, add to the totals shown.

tributed on April 15. Thus far this year investment holdings of the reporting banks have expanded by 4.7 billion dollars, while in the corresponding period a year ago they had declined by 615 million. Total loans and investments adjusted are therefore up by 3.1 billion dollars thus far this year as compared with a contraction of 918 million in the corresponding period last year.

## International Monetary Developments

#### MONETARY TRENDS AND POLICIES

**UNITED KINGDOM.** In presenting the 1958-59 budget to the House of Commons on April 15, the British Chancellor of the Exchequer reiterated the government's intention to "win the battle against inflation". While the chancellor saw no need to intensify the existing disinflationary measures, he nevertheless felt that the time was not ripe for any general relaxation of credit policy. It was still necessary, he stated, for the banks to hold

down their lending, for hire-purchase restrictions to be maintained, and for the Capital Issues Committee to preserve a critical attitude toward all applications for new capital issues. The only exceptions to this policy concern localities of high unemployment which are to be given preferential treatment with respect to bank loans and approved capital issues, and major capital goods exports which are to be assisted by increased export-credit guarantees. The chancellor declared subsequently that "having

set our hand to this business of safeguarding the value of our currency and stabilizing the cost of living, we must see it through to a firm and successful conclusion before we embark on other tasks. This budget, I am confident, is in keeping with these aims."

The budget consequently provides only for certain rather cautious and limited changes. The most noteworthy of these are: (1) the consolidation of the 30 per cent tax on distributed profits and the 3 per cent tax on undistributed profits into a single 10 per cent tax on all profits; (2) a 25 per cent increase in the initial depreciation allowance on new investment; and (3) standardization of purchase taxes, including a cut from 60 per cent to 30 on household appliances. The budget speech also stressed the authorities' continued determination to attract funds from nonbank sources, especially small savings, and to control the money supply better through "vigorous funding" and a "tight hold on public expenditure". Thus, the limit on individual holdings of 4¼ per cent seven-year tax-exempt National Savings Certificates was raised to £750 from £450, and a new 5 per cent seven-year Defense Bond was introduced, which compares with the current 4½ per cent ten-year bond.<sup>1</sup> In addition, the authorities decided to retain, "at any rate for another year", the practice first adopted in fiscal 1956-57 of making the Treasury the sole source for the long-term capital needs of the nationalized industries.

The latter decision is likely to help keep down the pressure on bank advances, although these rose by 47 million pounds in the four statement weeks ended April 16, as against a 17 million increase in the corresponding period of 1957; the clearing banks' average liquidity ratio stood at 33.1 per cent in mid-April. The yield of 2½ per cent Consols declined from 5.07 per cent at the end of March to 4.87 on April 10, but then rose slightly to 4.96 on April 30. The market continued to bid up the price of Treasury bills; the average Treasury bill tender rate, which had stood at 5.52 per cent at the final March tender, fell to 5.18 at the last tender in April.

**CANADA.** The Canadian Government on April 14 announced two new loan issues, the proceeds of which are to be used to refund May 1, 1958 maturities and "for general purposes". The two new loans consist of, first, an 800 million dollar issue, available in fourteen-month, three-year, and twelve-year maturities, priced to yield 2.94, 3.35, and 3.71 per cent, respectively, and, secondly, a 3¾ per cent issue, maturing on January 15, 1978 and priced to yield 4.01 per cent, of which 150 million dollars was

sold. The two issues (which will leave the government, after the May refunding, with 350 million dollars for impending expenditures) were floated against the background of a relatively stable bond market. Yields of long-term government bonds in mid-April were slightly above end-of-1957 levels, while those of medium-term issues had fallen by about 0.3 percentage point. At the short end of the market, however, a substantial decline has taken place, with the average Treasury bill tender rate plummeting to 1.37 per cent on April 24—a drop of over 2 percentage points in three months that left the rate the lowest since June 1955.

**DENMARK.** The National Bank of Denmark reduced its discount rate to 5 per cent from 5½, effective April 19, thus becoming the sixth Western European central bank to lower its rate since the beginning of this year. The reduction—which, according to the governor of the bank, marked a long-needed easing of monetary policy—came at a time of some lessening of the external and internal pressures which the Danish economy has faced in the past two years. On the external side, there has been a considerable strengthening of the country's reserve position, making possible the repayment to the International Monetary Fund in March of 10 million dollars of the 34 million that Denmark had drawn at the height of its foreign exchange crisis last June. Internally, prices and wages (the latter are linked to the cost of living) have tended to become stabilized, and unemployment has reached a relatively high level. The government's financial position has been improving as a result of fiscal measures taken in mid-1957; and the prospect of a reduction in or temporary elimination of the government's borrowing needs already has imparted a somewhat easier tone to the capital market.

**FRANCE.** The Bank of France on April 17 increased the penalty rates on discounts in excess of the ceilings set for each individual credit institution. The rates were raised to 8 per cent from 7 for discounts between 100 and 110 per cent of a bank's ceiling, and to 12 per cent from 10 for discounts in excess of 110 per cent of that ceiling. The previous rates had been in effect since August 12, when they had been raised by 1 per cent simultaneously with the 1 per cent increase to 5 per cent in the Bank of France's discount rate. The latest move serves to supplement a series of anti-inflationary measures taken since mid-1957, including the imposition in February of ceilings on the amount of short and medium-term credit extended by the banks to the private sector. These ceilings reportedly have been strictly maintained this year so far; the penalty rates, according to the Bank of France, were increased primarily as a precautionary and alerting measure.

<sup>1</sup> Both issues are nonmarketable; the former is sold on a discount basis similar to our Series E Savings bond, while the latter is a current-income bond corresponding to our Series H Savings bond.

**EXCHANGE RATES**

American-account sterling was generally firm during April. A somewhat easier tendency developed from time to time in expectation of a further reduction in the British bank rate. The announcement of a substantial increase during March in the United Kingdom's gold and dollar reserves was well received in the market. Commercial demand, principally from oil companies, and short covering firmed the quotation to  $\$2.81\frac{3}{32}$ , the highest level since May 1954. During the latter part of the month, the undertone was affected by the threat of a British rail strike and, for a few days, by an unusually heavy demand for dollars in London, which caused the rate to move lower to  $\$2.81\frac{1}{16}$ . Renewed commercial demand subsequently stimulated the market, and the rate recovered to  $\$2.81\frac{3}{16}$  at the month end.

Commercial activity in the forward market was on a rather small scale. However, the discounts on future deliveries, responding to changing market sentiment concerning a possible British bank rate change, tended to widen and narrow accordingly. At the end of the month,

the discounts on three and six months' sterling stood at  $2\frac{1}{16}$  and  $4\frac{3}{4}$  cents, respectively, equivalent to 3.82 per cent and 3.38 per cent per annum.

Continental and sugar interests provided the principal demand for transferable sterling during April. After touching  $\$2.79\frac{5}{8}$  in the earlier part of the month, the quotation moved downward to  $\$2.79\frac{9}{32}$ , mainly on Continental offerings. Toward the end of the month, however, the rate strengthened to  $\$2.79\frac{19}{32}$ . The quotation for securities sterling ranged between  $\$2.77$  and  $\$2.79\frac{1}{2}$  during the month, with some investor interest developing in the latter part in British Government bonds and in a British oil company security. At the month end, the quotation was at the higher level.

The Canadian dollar quotations during the month reflected primarily the pressure of offerings of United States dollars resulting from the proceeds of sales of Canadian securities and also from sales by Canadian commercial interests. The rate rose from a low of  $\$1.02\frac{21}{32}$  on April 1 to a high of  $\$1.03\frac{5}{16}$  on April 10. During the latter part of the month, the quotations moved erratically within a narrow range, and closed at  $\$1.03\frac{13}{64}$ .

### **The Financing of Small Business: Survey of Second District Commercial Banks**

In the latter half of 1957 the Federal Reserve System undertook a multipronged nation-wide study of the financing facilities available to small business. This study represented an attempt to evaluate the functioning of these facilities during and after a prolonged period of monetary restraint, and to evaluate the impact of that restraint upon small as compared with large business firms.

The study was divided into three major parts. The first part consisted of a broad review and evaluation of the information relating to small business financing which was available at the time the project was undertaken. A second part was a new survey of current policies and practices of lenders, conducted through interviews with representative lenders throughout the country, including commercial banks, commercial finance companies, factors, and larger corporations that provide the "downstream" supply of trade credit to smaller customers and suppliers; in addition, a special survey was made of suppliers of equity capital for small business ventures. In conjunction with the commercial bank interviews, the System also undertook a statistical survey of business loans outstanding at member banks on October 16, 1957, which was de-

signed to be broadly comparable to a previous study made on October 5, 1955. The third part of the over-all study is to be a new inquiry into the financing problems of small business firms as seen from the viewpoint of the borrowers themselves; this will entail both interviews and a detailed analysis of financial records. The first two parts of the study have been completed and the results were submitted to the Congress in March, but the final part is still in an exploratory stage.

The present article, the first of a series, is primarily concerned with the role of Second District commercial banks in financing small business firms during the past few years, as revealed by the exceptionally wide range of new information that the System study has made available through both interviews and statistical surveys. While the analysis is principally in terms of developments within the Second Federal Reserve District, the general conclusions parallel the findings for the country as a whole, unless special mention is made to the contrary. The over-all nation-wide results were summarized in "Financing Small Business", published as committee prints by the Committees on Banking and Currency and the Select

Committees on Small Business of the United States Congress, and further detail at the national level is being published by the Board of Governors in the *Federal Reserve Bulletin*.

### THE PRINCIPAL FINDINGS

Among the principal findings of the statistical survey of commercial bank lending in the Second District were the following. The total volume of business loans outstanding at Second District member banks increased by 3.8 billion dollars, or 36 per cent, between October 5, 1955 and October 16, 1957. As Table I indicates, the largest increase (72 per cent) occurred in loans to the largest borrowers, those of asset size 100 million dollars and over. On the other hand, bank borrowings of firms with assets under 5 million dollars rose only slightly between 1955 and 1957, and borrowings by the smallest group—firms of asset size under \$50,000—actually declined slightly.

The industry groups which experienced the greatest relative increases in loans were the metals and metal products group, the petroleum, coal, chemicals, and rubber group, and the transportation and public utility group. The outstanding amount of loans to the latter groups increased between 50 and 60 per cent, and loans to the metals companies were up by 103 per cent.

The largest banks showed the largest relative increase in the amount of outstanding business loans. By contrast, banks with deposits of less than 10 million dollars, which numerically represent a large percentage of the banking population in the Second District, expanded their business loan portfolios only slightly. Loans to newly organized borrowers (defined as firms established after October 15, 1955) represented 5 per cent of the total amount of loans outstanding in October 1957 and 7 per cent of the total number of loans; since this type of information had not

been available previously, however, no comparison with earlier years is possible.

While it is clear from the results of these surveys that bank lending to smaller firms has risen less markedly in this District during recent years than loans to larger companies, it would be misleading to infer on the basis of the above statistics alone that the bank financing needs of small businesses were not adequately met over this period. For one thing, the differential changes in lending volume to firms of varying sizes were closely related to basic shifts in the composition of final product demand in the economy as a whole between 1955 and 1957, which in turn were reflected in the pattern of demand for bank loans. Secondly, it is important to note that, while commercial banks occupy a key position in the financing of small business, they are only one of a number of financial intermediaries supplying funds to such firms. Commercial finance companies and factors, both of which offer specialized financial services to small firms, have shown considerable growth in recent years, and there has also been a rapid increase in the volume of trade (or "inter-business") credit which currently actually exceeds commercial bank credit to small business in dollar volume. Thus, the adequacy of financing facilities for small business firms cannot be judged on the basis of bank credit extensions alone. Third, an over-all classification of borrowing firms by asset size may not always provide a meaningful identification of "small" businesses, since the appropriate definition of "smallness" tends to vary from one industry to another. The results of the interviews conducted with bankers in the Second Federal Reserve District, finally, suggest that the great majority of District banks did not consciously or deliberately discriminate against small business firms as money conditions became tighter. In fact, they seem to have made special efforts to assure that the credit needs of smaller firms would be met to the extent that this was possible, given the limited total resources available for loans.

Any meaningful assessment of the statistical survey of Second District loans, particularly as it relates to small business, must take account of all of the considerations just outlined, as well as of various others. The following sections will consider the statistical findings with respect to loan trends in the light of some of the relevant factors mentioned—notably the changing nature of the demand structure since 1955. Exploration of other facets of the problem, such as changes in interest rate and maturity patterns, the availability of bank credit for new firms as contrasted with existing ones, and the relationship between the statistical findings and the results of the various interview surveys will be left to later articles.

Table I  
Commercial Loans Made by Second District Member Banks  
to Borrowers of Various Sizes, Outstanding on  
October 5, 1955 and October 16, 1957

Asset size of borrower (In thousands of dollars)	Number of loans		Amount of loans	
	Percentage distribution 1957	Percentage change 1955-57	Percentage distribution 1957	Percentage change 1955-57
Under 50.....	42.2	8.1	1.9	- 3.9
50 to 250.....	35.4	18.1	6.3	7.0
250 to 1,000.....	10.1	16.6	7.6	5.4
1,000 to 5,000.....	3.3	16.3	10.4	3.2
5,000 to 25,000.....	1.6	38.8	16.4	29.8
25,000 to 100,000.....	0.8	58.6	17.4	51.3
100,000 and over.....	1.0	17.2	35.6	71.6
Not ascertained.....	5.5	- 60.5	4.4	22.9
Total—all borrowers..	100.0	3.0	100.0	35.8

Note: Because of rounding, the figures do not necessarily add to the totals shown.

## THE CHANGING PATTERN OF LOAN DEMANDS

The economic setting in which the nation-wide commercial loan survey of October 1957 was undertaken differed strikingly, in a number of respects, from the setting of the survey conducted two years earlier. The October 1955 study came near the end of a period of extraordinarily rapid increases in the volume of consumer purchases, particularly of automobiles and other types of durable goods that are to a large extent bought on credit. Residential construction activity similarly had risen to an all-time high and business firms were stepping up their outlays for new plant and equipment substantially and

were also generally building up inventories to meet the expanded demands. In the following two years, on the other hand, the rate of increase in consumer outlays fell off markedly—total expenditures for durable consumer goods actually failed to register a net gain—and residential construction outlays declined. The inventory build-up, moreover, tended to level off, and by October 1957 had given way to net inventory liquidation. Plant and equipment expenditures, however, continued on a rapid upward trend throughout 1956 and into 1957, leading to record levels of activity in metal production and other heavy industries through much of this period.

Table II  
Commercial Loans Made by Second District Member Banks, Classified by Business and Asset Size  
of Borrower, Outstanding on October 5, 1955 and October 16, 1957

Business of borrower*	Asset size of borrower (in thousands of dollars)							
	Under 50	50 to 250	250 to 1,000	1,000 to 5,000	5,000 to 25,000	25,000 to 100,000	100,000 and over	All borrowers†
Amount outstanding on October 16, 1957 (in millions of dollars)								
<b>Manufacturing and mining—total</b> .....	39	228	416	654	1,075	1,356	2,879	6,822
Food, liquor, and tobacco.....	4	17	36	69	67	164	439	801
Textiles, apparel, and leather.....	12	81	181	215	177	111	187	976
Metals and metal products.....	10	61	87	163	340	431	1,151	2,262
Petroleum, coal, chemicals, and rubber.....	2	11	23	65	298	495	958	1,974
All other manufacturing and mining.....	12	58	89	142	193	156	144	809
<b>Trade—total</b> .....	103	326	292	232	208	164	209	1,571
Wholesale.....	15	119	189	158	132	78	51	756
Retail.....	88	207	104	74	76	85	158	815
<b>Other—total</b> .....	129	347	380	600	1,069	977	2,011	5,935
Commodity dealers.....	1	3	9	36	69	43	102	269
Sales finance companies.....	1	8	27	72	157	285	594	1,145
Transportation, communication, and other public utilities.....	11	26	43	143	431	403	1,178	2,345
Construction.....	19	80	70	90	95	40	23	447
Real estate.....	14	90	104	129	182	53	27	785
Service firms.....	63	121	70	69	51	82	59	558
All other nonfinancial borrowers.....	21	38	56	62	85	72	29	386
<b>Total—all borrowers</b> .....	271	901	1,088	1,487	2,352	2,497	5,099	14,328
Percentage change in amount outstanding, 1955-57								
<b>Manufacturing and mining—total</b> .....	- 23.5	- 10.4	9.9	1.7	22.3	46.9	122.6	48.7
Food, liquor, and tobacco.....	- 4.8	11.2	- 7.3	19.4	- 39.8	- 1.8	85.9	26.1
Textiles, apparel, and leather.....	- 41.3	- 32.4	2.1	- 11.0	- 0.8	- 2.5	28.2	- 4.3
Metals and metal products.....	1.8	16.5	28.3	27.5	45.9	179.2	154.2	103.0
Petroleum, coal, chemicals, and rubber.....	- 62.5	68.6	- 4.9	- 15.6	19.5	25.5	152.9	58.3
All other manufacturing and mining.....	- 6.3	- 4.4	26.3	2.1	81.2	65.8	80.7	41.1
<b>Trade—total</b> .....	- 1.9	18.0	4.6	- 9.6	35.4	59.9	54.4	17.2
Wholesale.....	- 31.8	2.7	- 3.7	- 13.6	76.5	113.5	187.6	15.1
Retail.....	5.8	29.1	23.8	‡	- 3.5	29.9	34.1	19.2
<b>Other—total</b> .....	2.5	11.4	1.3	11.1	37.1	56.4	30.3	28.5
Commodity dealers.....	- 30.8	- 39.9	- 63.0	- 4.2	- 22.8	72.7	- 17.4	- 14.9
Sales finance companies.....	41.8	- 8.6	27.3	- 6.7	36.6	66.7	17.9	27.0
Transportation, communication, and other public utilities.....	53.8	29.7	8.1	71.3	59.8	74.5	42.8	53.2
Construction.....	- 12.1	1.3	- 2.2	8.7	29.1	112.5	958.4	23.7
Real estate.....	- 24.1	2.6	- 12.9	- 18.7	58.1	126.3	17.2	16.2
Service firms.....	4.1	34.7	28.8	94.8	53.1	27.7	17.7	29.9
All other nonfinancial borrowers.....	24.4	- 5.6	29.5	- 9.9	0.1	- 22.1	86.8	- 4.3
<b>Total—all borrowers</b> .....	- 3.9	7.0	5.4	3.2	29.8	51.3	71.6	35.8

Note: Because of rounding, the figures do not necessarily add to the totals shown.

\* The industry classifications shown in this and the subsequent table were based on the *Standard Industrial Classification Manual* published by the United States Bureau of the Budget.

† Includes borrowers whose asset-size was not ascertained.

‡ Less than 0.05 per cent.

The growing importance of business capital outlays in the over-all demand structure was clearly reflected in a changing pattern of loan demands between the two survey dates. Since the investment boom had led to strong pressures on the capital markets and a significant rise in long-term interest rates, many of the firms that were embarking on new capital spending programs sought to finance these programs initially through intermediate-term credit from the commercial banks, expecting to refinance such loans in the capital markets as soon as long-term rates became more favorable. Such "capital loan" demands converged with particular force on the larger banks, both because the firms that were undertaking the more important expansion programs normally were themselves large and tended to be customers of the bigger banks, and because smaller banking institutions usually do not have the resources for handling large-scale transactions. These developments helped to explain why, between the two survey dates, there was a relatively greater increase in loans to large businesses than to smaller firms, why the loan increase was more pronounced for firms in heavy industries (which provided the primary support for the capital boom and in which large firms tend to predominate) than in retail trade and other service industries which include a larger number of small firms, and why the largest banks showed the greatest expansion in their loan portfolios.

#### **LOAN INCREASES BY INDUSTRY**

These changes in the pattern of final demand between 1955 and 1957 are reflected in the commercial loan surveys taken in the Second District in those two years. Significant shifts occurred in the relative importance of the major industry groups borrowing from Second District member banks, partially reversing the changes that had occurred between a similar 1946 survey and the 1955 survey. In the earlier period, the relative importance of manufacturing and commercial concerns as borrowers had declined, while the importance of public utilities, construction contractors, and the service industries as borrowers had in general increased substantially. The most significant feature of the 1955-57 period, however, as Table II indicates, was a high rate of growth in business borrowing by metals and metal products firms, petroleum, coal, chemicals, and rubber concerns, and the transportation and public utilities group, with a lower rate of growth in borrowing by commercial establishments and service industries.

Manufacturing and mining industries increased their business borrowings during the two-year period ended October 1957 by nearly 50 per cent in dollar amount, accounting for about 2.2 billion dollars or three fifths of the total net rise in business borrowings at Second Dis-

trict member banks. The increase in the number of loans outstanding was strikingly lower—only 2 per cent. On the other hand, between 1955 and 1957 business firms engaged in service industries, real estate, and the closely allied "all other nonfinancial business" group showed a generally less rapid growth in both the dollar amount and the number of outstanding loans at Second District member banks. This was in contrast to a rather sharp and striking growth for these groups in the period of 1946 to 1955. As far as the distribution by asset size of loans to service firms is concerned, no concentration among large companies is discernible and all the size groups appear to have participated evenly in the aggregate growth of loans to this sector between 1955 and 1957.

#### **BUSINESS OF BORROWER AND SIZE OF BANK**

Small banks in general tend to lend to small business, while larger banks lend to all sizes of businesses, although the larger firms predominate at least in terms of dollar amount. It is not surprising therefore that, according to the 1957 survey, the bulk of the loans extended by the large banks, in dollar terms, tended to accommodate customers in industries where large firms predominate—such as manufacturing and mining, public utilities, and sales finance companies, while small banks primarily served relatively small business firms in trade and service industries (see Table III).

The distribution of loans outstanding on the 1957 survey date at the largest banks in the Second District (those with deposits of 1 billion dollars or more) indicates that manufacturing and mining firms accounted for slightly more than half of the total dollar amount of loans outstanding, while in 1955 they had accounted for slightly less than half. Transportation, communication, and other public utility firms absorbed nearly 20 per cent of the total, also a slightly higher share than in 1955. On the other hand, loans to the business firms engaged in trade, real estate, construction, and service industries, most of which are of relatively small size, declined as a proportion of the aggregate commercial loans of these banks.

In number of loans outstanding, the predominance of manufacturing and mining borrowers at large banks is not so pronounced; in 1957 they accounted for only 25 per cent of the total number of loans, slightly less than their share in 1955. Retail and wholesale trade concerns, many of which are relatively small in size, accounted for nearly one third of the total number of loans extended by large banks. The distribution of the number of loans at small banks with deposits of less than 10 million dollars indicates a heavy concentration of loans to retail trade concerns (38 per cent) and to concerns engaged in serv-



**Table III**  
**Commercial Loans Made by Second District Member Banks, Classified by Business**  
**of Borrower and Size of Bank, Outstanding on October 16, 1957**

Business of borrower*	Amount of loans (in millions of dollars)							Number of loans						
	Banks with total deposits of (in millions of dollars)						All member banks	Banks with total deposits of (in millions of dollars)						All member banks
	Under 10	10 to 50	50 to 100	100 to 500	500 to 1,000	1,000 and over		Under 10	10 to 50	50 to 100	100 to 500	500 to 1,000	1,000 and over	
<b>Manufacturing and mining—total</b>	20	105	110	516	425	5,645	6,822	3,172	7,349	4,790	8,597	1,732	17,072	42,712
Food, liquor, and tobacco.....	2	14	4	68	65	648	801	446	1,254	385	1,086	273	1,547	4,990
Textiles, apparel, and leather.....	3	21	33	84	33	802	976	308	1,474	1,291	1,749	193	6,206	11,220
Metals and metal products.....	5	39	42	211	178	1,787	2,262	763	2,258	1,428	3,000	671	3,521	11,640
Petroleum, coal, chemicals, and rubber.....	1	8	5	41	112	1,806	1,974	208	528	321	643	240	1,303	3,244
All other manufacturing and mining	9	23	26	112	37	602	809	1,447	1,836	1,364	2,120	355	4,496	11,618
<b>Trade—total</b> .....	70	173	88	298	70	872	1,571	15,090	22,156	7,188	15,905	2,387	21,452	84,178
Wholesale.....	8	47	34	126	19	522	756	1,084	3,642	1,568	3,948	424	8,118	18,783
Retail.....	62	126	54	173	51	350	815	14,007	18,514	5,620	11,957	1,963	13,334	65,395
<b>Other—total</b> .....	90	232	177	689	296	4,451	5,935	18,371	22,240	11,101	22,888	2,903	30,747	108,250
Commodity dealers.....	1	1	5	25	10	227	269	204	136	85	237	21	473	1,156
Sales finance companies.....	†	19	11	122	65	928	1,145	8	344	130	334	46	694	1,556
Transportation, communications, and other public utilities.....	6	19	12	118	127	2,063	2,345	1,341	1,577	441	1,946	231	4,046	9,582
Construction.....	15	31	32	128	34	208	447	3,379	3,880	2,025	5,804	646	1,611	17,346
Real estate.....	13	67	54	139	29	485	785	1,533	3,712	1,660	3,476	421	8,202	19,004
Service firms.....	47	71	38	110	21	270	558	9,820	9,780	5,192	8,081	1,114	8,830	42,816
All other borrowers.....	7	26	26	48	10	270	386	2,085	2,812	1,569	3,011	423	6,892	16,791
<b>Total—all borrowers</b> .....	179	511	375	1,503	791	10,968	14,328	36,633	51,745	23,079	47,390	7,022	69,271	235,140
Number of banks.....	316	186	26	32	3	8	571	316	186	26	32	3	8	571

Note: Because of rounding, the figures do not necessarily add to the totals shown.

\* See footnote to Table II.

† Less than 0.5 million.

ice industries (27 per cent), but a relatively small proportion of loans going to manufacturing and mining firms (9 per cent).

#### BANK SIZE AND BORROWER SIZE

As mentioned above, small banks generally tend to lend primarily to small business, while the larger banks lend to all sizes of business. Between 1955 and 1957 few changes took place in this general pattern. In the Second District, the proportion of total loans to the largest borrowers made by the biggest banks increased somewhat, and the proportion of loans to the middle asset-size groups of borrowers made by these largest banks declined moderately. On October 16, 1957 the billion-dollar banks accounted for 90 per cent of the dollar amount of loans on the books of Second District banks to businesses with assets of 100 million dollars or more. This proportion ranged down to 66 per cent for businesses with assets of 1-5 million dollars, and to 23 per cent for concerns with assets of less than \$50,000. In terms of the number of loans, these proportions were 71, 49, and 32 per cent, respectively. Between 1955 and 1957 the share of these big banks in the number of loans to the smallest and largest asset groups showed a marked increase.

Banks with total deposits of less than 10 million dollars supplied a significant proportion of the total bank loans only for firms with assets of less than \$250,000. These banks accounted for 19 per cent and 10 per cent, respectively, of the amount of loans to firms with assets of less than \$50,000, and those of assets between \$50,000 and \$250,000. The operations of banks in the 10-50 million dollar deposit range extended somewhat farther up the business asset range. They accounted for a significant proportion of the number of loans to firms with assets of up to 5 million and for a minor proportion of the number of loans to all larger borrower groups.

In 1955 the two smallest size-groups of banks, those with deposits of less than 50 million dollars, accounted for 19 per cent of the total number of loans to companies with assets of 100 million dollars or more. By 1957 this proportion had dropped to about 2 per cent. This change is probably in part a reflection of the prevailing restrictive credit conditions. With credit tight, many of the smaller banks may have given priority in the use of their scarce reserves to meeting the local needs with which they were more familiar.

As already indicated, these and other findings will be explored further in subsequent issues of this *Review*.