FEDERAL RESERVE BANK OF RICHMOND

MONTHLY REVIEW

Regional Interest Rate Differentials
Consumer Credit
Commercial Paper Since 1966
The Fifth District

MARCH 1969

Regional Interest Rate Differentials

At one time the cost of borrowed money differed substantially, often dramatically, from one section of the country to another. In 1857, for example, the City of Los Angeles sold 20-year public improvement bonds which paid 12% a year. The average yield on New England municipal bonds that year was only 4.81%. In 1860, savings banks in California were reportedly paying 15% interest to their depositors. At the same time the Bowery Savings Bank of New York paid only 5%.[1]

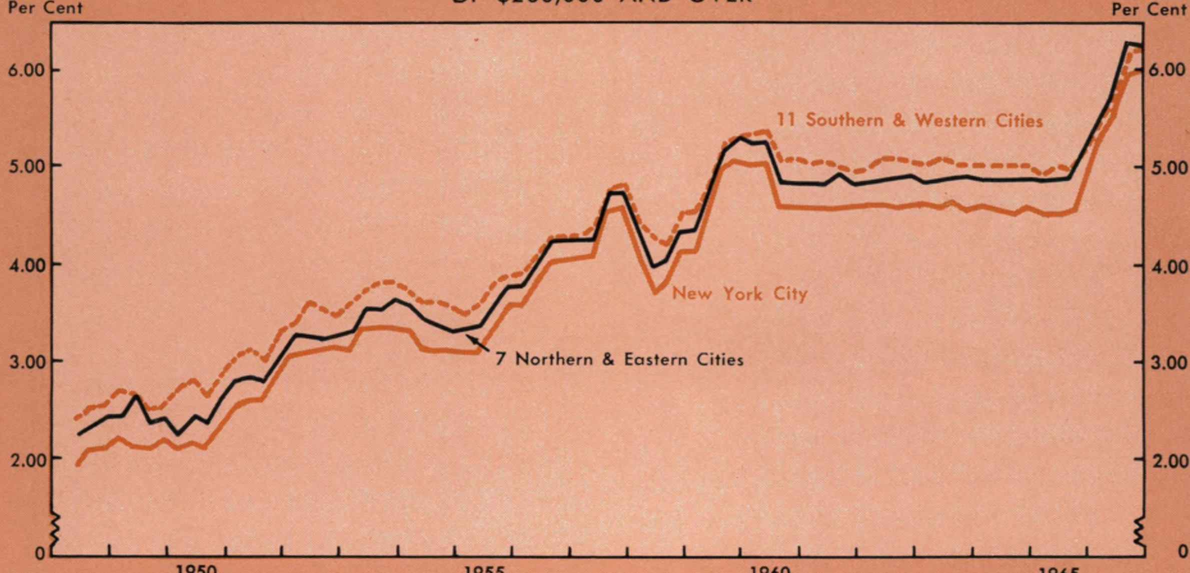
While a number of factors were responsible for such large differentials, the most important was the vast expanse of the country with its poor communication and transportation facilities. This impeded the flow of money from one section of the country to another, and as a result, interest rates tended to reflect local supply and demand conditions. In the sparsely settled areas of the South and West, the relative scarcity of loanable funds reflected underdeveloped local credit markets and limited access to the money markets of Europe and the East Coast. Demands for credit, on the other hand, were often strong as the return on invested capital was likely to be great. In such cases, businessmen and individuals were willing to pay high rates of interest. Sidney Homer writes that "In 1854, J. R. Yarba mortgaged 17,000 acres in southern California for $5,500 at 60% annual interest." That same year "Jose Sepulveda owed $7,000 at rates varying between 48% and 84% a year. . . . In 1879, a Montana banker pointed out that '18% was the lowest rate known in Montana.' "

Since that era, steady improvements in communication and transportation facilities have made it possible for borrowers in areas of unusually strong credit demand to tap distant sources of funds. Simultaneously, lenders in low interest rate areas have become able to shift their funds to sections where yields are higher. This arbitraging has gradually narrowed sectional differentials.

Working toward the same end was the development of essentially uniform banking and other financial facilities throughout the country, with effective interlinkage among the several sections pro-

[1] These examples are taken from: Sidney Homer, *A History of Interest Rates* (New Brunswick: Rutgers University Press, 1963).

BANK RATES ON SHORT-TERM BUSINESS LOANS OF $200,000 AND OVER



Source: Board of Governors of the Federal Reserve System.

vided through correspondent banking and a variety of financial agency services. This trend was accelerated by the establishment of the Federal Reserve System in 1914.

The 1920's and 1930's By the early 1920's regional interest rate differentials had been markedly reduced. In his book, *Money Rates and Money Markets in the United States,* Winfield Riefler calculated for four geographic regions average interest rates charged by member banks in cities under 15,000 on customers' paper rediscounted with the Federal Reserve Banks. He found average interest rates of 6.00% in the East, 7.45% in the Middle West, 8.25% in the South, and 8.49% in the Far West. While these spreads are substantial compared to today's markets, they were far smaller than the differentials of the 19th century.

Additional regional information is provided in the Federal Reserve's series on rates charged on customer loans. This series, begun in 1919, originally included both commercial loans and time and demand loans on securities. For the period 1919 to 1928 it shows average rates of 5.24% in New York, 5.60% in other selected cities in the North and East, and 6.10% in selected cities in the South and West. The spreads are considerably smaller than those indicated in Riefler's study.

Beginning in 1928, the Federal Reserve regional interest rate series was revised to include only short-term commercial and industrial loans and the number of reporting centers was standardized at 19. This revised series shows average rates during the period 1928-1939 of 3.17% in New York, 4.00% in the North and East, and 4.45% in the South and West. These spreads are greater than those shown for the 1919-1928 period, due in part perhaps to statistical differences in the series, but more importantly to the disruption of financial markets occasioned by the Great Depression. The revised series shows a steady narrowing of the spreads after 1939 when business conditions began to improve. For the period 1940-1947, the average spread between the highest and lowest rates was only 66 basis points, roughly half that of the preceding period. (A basis point is one-hundredth of one per cent.)

Rates on Business Loans in the Postwar Period Prior to 1948, it was impossible to tell the extent to which observed regional differences in interest rates were due to location or simply to regional differences in the distribution of loans by size. Accordingly, in 1948 the series on business loans was revised to break out data on four loan-size classifications, as well as by region. Data on the largest of the loan classifications for the period 1948-1966 appear in the chart.

The series was revised again in 1967 to improve the homogeneity of the loans reported so as to isolate more effectively the impact of region on the interest rate averages. To this end, the number of loan-size classifications was increased from four to five, business instalment loans and loans to foreign businesses were excluded, and revolving credits were reported separately. In addition, the number of financial centers reporting was increased from 19 to 35 and the number of respondent banks raised from 66 to 126.

Business Loan Rates in New York Perhaps the most obvious fact which emerges from an examination of regional differences is the systematic tendency for interest rates to be lower in New York than elsewhere. This should not be surprising since New York is the financial center of the country and of the world. The apparatus for transferring funds from lenders to borrowers is more highly developed there than any place on the globe. Business borrowers have access to many bank and nonbank financial institutions, and large corporate borrowers, in addition to the financial institutions, can tap the bond market, the commercial paper market, or borrow from abroad or directly from other nonfinancial corporations. Strong competition and the existence of a number of sophisticated traders who arbitrage across various markets and various maturities within markets tend to keep bank rates at the lower end of the regional scale.

As the chart indicates, from 1948 through 1966 rates on loans of $200,000 and over were generally lowest in New York and highest in the South and West. This was also true in the other three smaller loan classifications with only minor exceptions. For the period as a whole, average interest rates by size class of loan are shown in Table I.

Differences in the Two Series A comparison of Tables I and II suggests that regional variations may have been obscured in the statistics prior to the 1967 revision. For one thing, the regional differentials in the revised series are generally somewhat larger. Also, according to the new series, interest rates on large loans are slightly lower in New York than in the Southeast, but on smaller loans this situation is reversed. Actually the differences between the two regions are surprisingly small.

A striking feature of the two series is the sharp change in rate levels in cities of the North and East relative to other areas. Whereas in the pre-1967 data these rates were constantly below those in the South and West, in the revised series this order is sharply reversed. Part of the seeming inconsistency between the two series may be due to fairly major changes in the statistical composition of the newer series.

The post-1967 data show a marked tendency for regional differences in interest rates to diminish as the loan size increases. As can be seen from Table II, differences between highest and lowest regional rates narrowed from 73 basis points for loans in the smallest size class to 38 basis points for loans in the largest size class. This is to be expected as firms borrowing large amounts are generally not limited to the local market but are in a position to shop around for the most attractive terms.

Table I

Interest Rates on Short-Term Business Loans
Average for 2nd Quarter through 4th Quarter 1966
By Size Class of Loan
(1948 revision of series)

Size Class	New York City	North and East	South and West
$1,000 to 10,000	5.12	5.38 (.26)	5.47 (.35)
$10,000 to 100,000	4.47	4.86 (.39)	4.94 (.47)
$100,000 to 200,000	4.27	4.44 (.17)	4.56 (.29)
$200,000 and over	3.85	4.05 (.20)	4.25 (.40)
All size classes combined	3.98	4.21 (.23)	4.52 (.54)

Note: Figures in parentheses show spreads over New York rates.
Source: Board of Governors of the Federal Reserve System.

Movement of Rates over Time It is clear from an examination of the chart that bank rates in all sections of the country tend to move together. Generally speaking, rate movements follow a marked cyclical pattern which is discernible in every region and for every size class of loan. Because of the concentration of money and capital market machinery in New York, rate movements there might be expected to lead rate movements in other regions. But close examination of the quarterly data reveals no systematic tendency for this to occur. If rates in New York do in fact respond first to changes in monetary and credit conditions, the lead time is apparently less than a quarter.

Table II

Interest Rates on Short-Term Business Loans
Average for 1st Quarter 1967 through 2nd Quarter 1968
By Size Class of Loan
(1967 revision of series)

Size Class	New York City	South-east	South-west	North Central	West Coast	North-east	Spread Between Lowest and Highest
$ 1,000 to $ 9,999	6.58	6.55*	6.72	6.84	7.28	6.77*	.73
10,000 to 99,999	6.49	6.37*	6.52	6.68	6.96	6.90*	.53
100,000 to 499,999	6.17	6.14*	6.30	6.42	6.52	6.68	.54
500,000 to 999,999	5.96	5.97	6.17	6.18	6.21	6.41	.45
1,000,000 and over	5.86	5.89	6.11	6.02*	5.98*	6.24	.38
All size classes combined	5.94	6.11	6.26	6.18*	6.24*	6.54	.60

*Figure is out of order from lowest to highest as one reads from left to right.
Source: Board of Governors of the Federal Reserve System.

There are, however, slight differences among regions in the amplitude of cyclical fluctuations in bank rates on business loans. Almost invariably changes in New York are greater than elsewhere, both during downswings and upswings. The evidence using data from the 1948 revision is presented in Table III. The changes in the table were computed using the specific turning points of the respective series. Data since the 1967 revision, which cover a single period of rising rates—from roughly mid-1967 to mid-1968—confirm the conclusion of greater cyclical volatility of rates in New York.

Table III also suggests that rates are more cyclically volatile the larger the size of loan, regardless of location. This is to be expected since the market for large loans tends to be nationwide. Bankers throughout the country must compete both with market instruments and with the banks in New York. Consequently, rate changes on large loans in one section of the country tend to spread across the land.

Mortgage Rates Until a few years ago when the Federal Home Loan Bank Board began to collect regional mortgage rate data on a systematic basis, such information was scattered and fragmentary. Consequently, valid historical comparisons are difficult. The chart shows the effective rate on conventional first mortgages by major geographic region. The effective rate consists of the contract rate of interest plus initial fees and charges. While the regions on the chart are labeled the same as for short-term business loans in the 1967 revision, they are not composed of precisely the same financial

Table III

Cyclical Changes in Bank Rates
Measured in Basis Points
(1948 revision of series)

From Peak to Trough

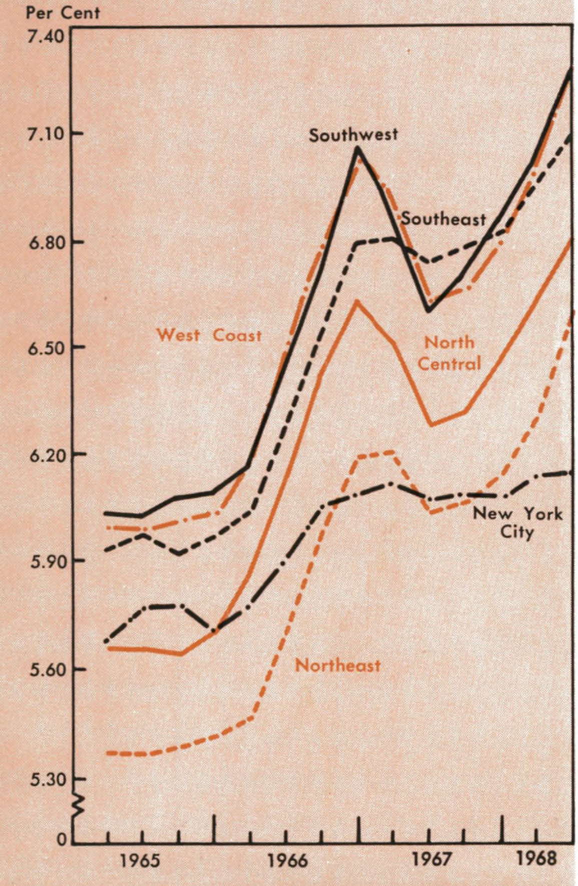
Size Class of Loan	New York City 1953-1954	New York City 1957-1958	New York City 1960-1961	North and East 1953-1954	North and East 1957-1958	North and East 1960-1961	South and West 1953-1954	South and West 1957-1958	South and West 1960-1961
$ 1,000 to $ 10,000	—15	—36	—23	—11	—21	—14	—12	—20	—21
10,000 to 100,000	—13	—52	—31	—16	—48	—32	—12	—32	—23
100,000 to 200,000	—25	—81	—42	—19	—63	—37	—18	—48	—36
200,000 and over	—27	—88	—51	—30	—75	—49	—32	—64	—42

From Trough to Peak

Size Class of Loan	New York City 1950-1953	New York City 1954-1957	New York City 1958-1960	New York City 1961-1966	North and East 1950-1953	North and East 1954-1957	North and East 1958-1960	North and East 1961-1966	South and West 1950-1953	South and West 1954-1957	South and West 1958-1960	South and West 1961-1966
$ 1,000 to $ 10,000	96	88	64	101	52	72	47	85	46	75	59	100
10,000 to 100,000	105	110	92	124	86	104	92	136	75	97	85	112
100,000 to 200,000	115	140	129	140	115	124	113	145	97	114	107	124
200,000 and over	127	149	138	148	135	141	131	150	130	133	118	130

Source: Board of Governors of the Federal Reserve System.

EFFECTIVE RATES ON CONVENTIONAL FIRST MORTGAGES ON NEW HOMES



Source: Federal Home Loan Bank Board.

centers. These differences limit the comparability of the mortgage series with the business loan series.

The chart shows mortgage rates to be lowest in New York City and the Northeast and highest in the West and Southwest. This order is considerably different from that for short-term business loans. Part of the explanation may lie in the existence of significant regional differences in the nonprice terms of mortgage contracts. Other data indicate that non-price terms tend to be most liberal in those areas with the highest interest rates. Thus, if the cost element implicit in the nonprice terms were included in some sort of weighted average cost of mortgage credit, the regional ordering of this weighted cost might be different from that of average effective rates.

With respect to timing of mortgage rate changes, the series for the various regions move closely together, with major turning points in the respective series coinciding almost exactly. This suggests some geographic mobility of mortgage money but, more importantly, it reflects the dependence of the mortgage market on general credit conditions.

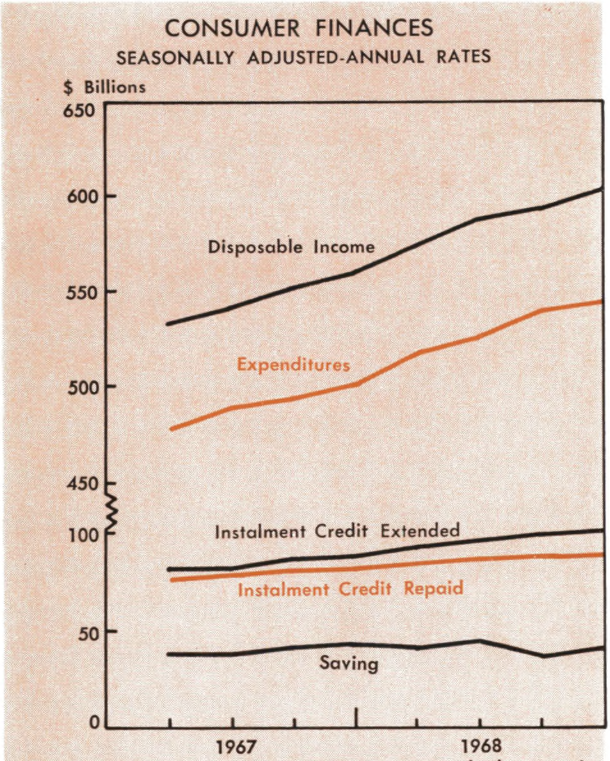
Conclusion Improvements in communications have tied the country's credit markets together so that changes in one sector of the market or section of the country tend to be transmitted fairly promptly to other sectors and sections. But despite the ease with which funds flow geographically, regional interest rate differentials have not been entirely eliminated. This is evident even on the basis of data which have been averaged over large geographic areas.

Jimmie R. Monhollon

Consumer Credit

Consumer credit outstanding has grown rapidly since World War II, expanding from about $8.4 billion in 1946 to about $102.1 billion in 1967. Exemplifying the dramatic growth and importance of such credit, instalment credit, which has accounted for the bulk of consumer credit since World War II, financed 17% of consumer purchases in 1967 as compared to 6% in 1946. Thus, consumer credit is not only an important indicator of economic activity but also a measure of demands being placed on credit markets. Over the years consumer credit has played a significant part in the growth of the market for consumer durable goods although more recently it has increasingly financed purchases of nondurables and services as well.

Consumer credit includes short- and intermediate-term credit extended to individuals through commercial banks, sales finance companies, retail outlets, and other financial institutions such as credit unions and consumer finance companies. It does not include real estate mortgages and insurance policy loans.



Source: Department of Commerce, and the Board of Governors of the Federal Reserve System.

There are two basic divisions in consumer credit, instalment and noninstalment. Noninstalment credit includes all consumer credit scheduled to be repaid in a lump sum, such as, single-payment loans, charge accounts, and service credit. Instalment credit, which currently makes up about 80% of consumer credit outstanding, covers all credit that is scheduled to be repaid in two or more payments. This category includes revolving credit and budget and coupon accounts. Its four classifications are automobile paper, other goods paper, home repair and modernization loans, and personal loans.

The rate of growth of consumer credit outstanding tends to be greater in periods of rapid business expansion and slower during slowdowns or declines in business activity. The growth of consumer credit is determined by the amount of extensions of new credit and repayments of outstanding credit. Typically, the greater the rate of increase in the economy the more rapidly new credit is extended. Repayments are governed primarily by past extensions although current economic conditions may be reflected in delinquencies or prepayments. Typically, as extensions increase in a period of business expansion repayments do also but at a slower rate. In a business slowdown both extensions and repayments fall off, but the decline in repayments is less pronounced.

In the past two years consumer credit outstanding has grown at an average annual rate of 7.5%. This growth rate closely parallels that of GNP (7.5%), personal disposable income (7.1%) and consumer spending (7.4%). A closer look at the two year period conforms to the typical pattern, although exceptions have occurred.

The first half of 1967 found the economy in what has been called a "mini-" recession. GNP grew at a greatly reduced rate. Growth in personal income slackened and consumer spending, which had been slow in 1966 remained weak. Instalment credit had likewise grown rather slowly in 1966 when credit markets had been tight. In 1967 consumer credit grew even more slowly though credit was readily available. Also, consumers tended to make rather large repayments on previously incurred debt. Extensions and repayments were of about the same size and total consumer credit outstanding grew at an average annual rate of only 1.7%. Automobile paper, which accounted for 30% of credit outstanding, was the weakest sector, actually falling at an average annual rate of 8.0%.

AVERAGE CONSUMER CREDIT OUTSTANDING*

Billions of Dollars

	1967				1968			
	I	II	III	IV	I	II	III	IV
Total Consumer Credit	95.6	96.5	98.2	100.2	100.9	103.4	106.8	110.6
Noninstalment Credit	19.2	19.6	19.8	20.4	20.6	21.1	21.4	22.3
Instalment Credit	76.4	76.9	78.4	79.8	80.4	82.4	85.4	88.3
Automobile Paper	30.1	30.0	30.8	30.7	30.7	31.8	33.2	33.9

* Not seasonally adjusted.
Source: Board of Governors of the Federal Reserve System.

The second half of 1967 saw some acceleration in overall economic growth, with a step-up in the rate of increase in disposable personal income; but, the growth of consumer spending was even slower than it had been. The counterpart of this sluggishness in consumer spending was a substantial increase in the saving rate. New consumer credit was being extended at a rapid rate while repayments increased only slightly with the result that consumer credit outstanding grew at an average annual rate of 7.8%.

The first half of 1968 was marked by renewed strength in the economy. Business was expanding at a substantially faster rate in real as well as in money terms. Disposable income, likewise, took a big leap forward. The increase was more than matched by the rate of increase in consumer spending. The resurgence in spending was associated with a slight reduction in the rate at which people were saving and by a substantial increase in the rate at which consumers were taking on new credit. All areas of consumer credit were strong. Automobile paper was, however, the strongest factor in the turnabout, accounting for 34.4% of the increase in consumer credit activity which took place in early 1968. In spite of the strong business expansion and the rapid rate of increase in new consumer credit the rate of repayment on previously incurred credit fell slightly in early 1968, and total consumer credit outstanding grew at an annual rate of 6.5%.

With the imposition of the surtax in July 1968, the rate of increase in consumer disposable income fell. The reduced rate of growth in disposable income was also a reflection of a slight decline in the rate of business expansion. Consumer spending, however, advanced sharply in the third quarter. This vigor was effected by a drastic decline in the saving rate and a rapid increase in the rate at which new credit was being extended, which were in turn prompted in large part by consumers' attitude that they should "buy now while it's cheap."

In late 1968, expansion in consumer spending slowed considerably, with little change in expenditures for goods. Growth in consumer credit, though still high, was tapering off.

Wynnelle Wilson

CONSUMER FINANCIAL RELATIONSHIPS

Based on Figures Seasonally Adjusted at an Annual Rate

	1967				1968			
	I	II	III	IV	I	II	III	IV
Personal Consumption as a % of Disposable Income	90.02	90.54	90.09	89.74	90.43	90.03	91.29	90.67
Personal Saving as a % of Disposable Income	7.43	7.20	7.36	7.75	7.10	7.50	6.25	6.87
Consumer Credit Extended as a % of Disposable Income	15.22	15.30	15.72	15.66	16.16	16.30	16.77	16.66
Consumer Credit Repaid as a % of Disposable Income	14.80	14.86	15.01	14.90	14.93	14.88	15.08	14.97
Repayments/Extensions	.97	.97	.96	.95	.92	.91	.90	.90
Extensions/Instalment Credit Outstanding*	.24	.28	.28	.29	.26	.30	.29	.29
Repayments/Instalment Credit Outstanding*	.26	.26	.26	.26	.27	.26	.26	.25
Annual Percentage Rate of Increase in Extensions	−24.52	7.77	18.43	5.76	25.68	12.54	16.89	4.10
Annual Percentage Rate of Increase in Repayments	4.04	7.07	10.90	4.07	11.97	6.96	10.16	3.55

* Not seasonally adjusted.
Source: Department of Commerce and Board of Governors of the Federal Reserve System.

Commercial Paper Since 1966

Although the tight money episode of 1966 has faded into economic history, a number of its effects remain as a testimonial to its impact. Many businessmen changed or modified their usual practices in response to the drying up of credit and the resulting strain on their own liquid resources. One such change was to increase their use of commercial paper as a source of short-term funds. From the start of 1966 through 1968 commercial paper outstanding rose \$11.4 billion to a total of \$20.5 billion, an average annual increase of 33%. This compares with an average annual increase of 15% for the previous three-year period. This article discusses changes in the commercial paper market since 1966.

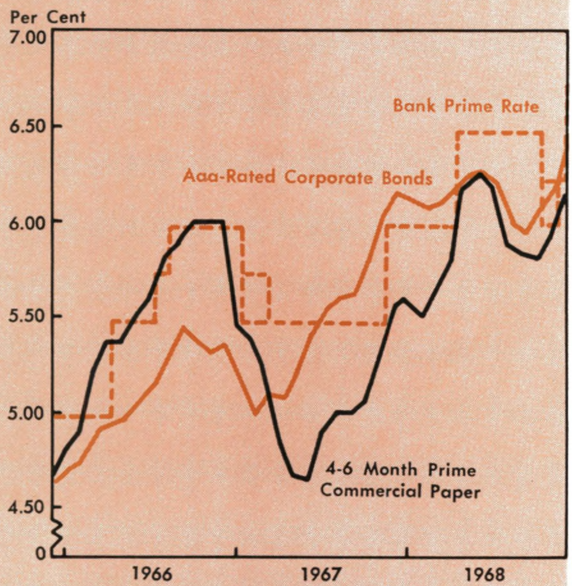
What Is Commercial Paper? Commercial paper is a short-term, unsecured promissory note sold by a corporation either to a dealer or directly to an investor. Maturities vary from a few days to nine months and may be tailored to the investor's specifications. Paper maturing beyond 270 days must be registered with the Securities and Exchange Commission and largely because of this requirement only \$79 million of such paper is outstanding. The SEC has ruled that proceeds from the sale of unregistered paper may be used only for "current transactions." Like Treasury bills, commercial paper is sold at a discount, the effective interest rate being determined by the difference between the price and par. Commercial paper differs from other major money market instruments in having no formal secondary market.

Commercial paper is marketed in two ways. The larger volume of paper is placed directly with investors by about 20 large finance companies, such as General Motors Acceptance Corporation and CIT Financial Corporation. These companies must continually raise funds to relend and short-term borrowings are essential between sales of long-term debentures. For these large finance companies, bank borrowing is a less important source of funds than commercial paper. A large concern may have over \$1 billion of commercial paper notes outstanding at any time, although several hundred million dollars is average. However, the maintenance of the large separate sales force necessary to place paper directly is justified not so much by the total value of the notes outstanding as by their almost daily issuance. Investors in directly placed paper, primarily industrial corporations and utilities, accept a lower interest rate than on dealer paper in return for the assurance of a steady supply. While directly placed paper is still the backbone of the market, its share has fallen from almost 80% in 1965 to 65% in 1968.

The second type of commercial paper is sold to dealers who resell it to investors, often other corporations. The principal issuers of dealer paper are nonfinancial corporations although roughly 100 smaller finance companies also use the dealer market. The dealer's commission is ⅛ of 1% per annum on prime paper. Generally speaking, these corporations do not sell paper on a continuous basis but use it to help finance seasonal or special needs, such as inventory accumulation. For most of these issuers, the commercial paper market is a less important source of funds than bank borrowing. Dealer paper may bear any maturity between one and nine months, but most maturities fall between three and six months. There are currently seven national dealers in commercial paper, all leading New York investment houses. There are perhaps another half dozen smaller dealers across the country serving regional markets only.

Ratings No company undertakes the sale of commercial paper in the national market, either through dealers or direct placement, without first receiving a rating from the National Credit Office, a division of Dun & Bradstreet. The five ratings, which range from *prime* to *not recommended,* are valuable to investors who may not be familiar with the details of the issuing firm's operations and finances. In deciding upon a rating for a corporation, the National Credit Office considers such factors as the corporation's net worth, its performance and financial position compared to that of its industry, its record over the previous ten years, its prospects for growth and future earnings, and the quality of its management. A corporation's banking relationships are closely scrutinized, and in most cases a firm must maintain a bank line of credit equal to its commercial paper notes outstanding to receive a top rating. The prime rating is generally accorded a firm with a net worth of \$25 million or more if all other standards are met satisfactorily. A company with a net worth of at least \$5 million is eligible for the next highest rating of *desirable,* and firms with a net worth of \$1.2 million or more can qualify for a rating of *satisfactory.* There is no national market for paper rated below desirable, and desirable paper is increasingly confined to regional markets. A firm's rating largely determines the interest rate it has to

THE COST OF PRIME COMMERCIAL PAPER AND SELECTED ALTERNATIVES



Source: Board of Governors of the Federal Reserve System.

pay and the acceptability of its paper to investors.

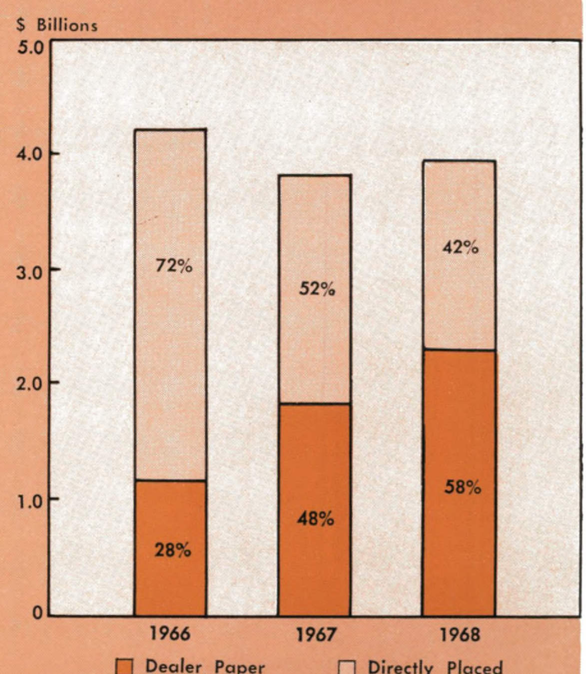
Recent Expansion Two of the most striking aspects of the recent boom in commercial paper are the rise in the relative importance of dealer paper and the phasing out of nonprime issuers. In 1966, commercial paper outstanding jumped $4.2 billion, an increase of almost 50% from the previous year. As in past years the greater part of this increase was accounted for by directly placed paper. The stringent credit conditions which prevailed in 1966, however, provided the impetus for the expansion of the dealer market. Beginning roughly in the second quarter of 1966, corporations which were unable to secure requisite amounts of funds from banks searched for other sources and many qualified companies turned to the commercial paper market.

The actual net increase in the number of firms selling commercial paper in 1966 was 15, bringing the total to 350. However, the number of new firms which entered the market was far larger. The bulk of the entrants were large, prime-rated corporations. Paper sold by these corporations was eagerly sought by investors, often in preference to paper sold by smaller companies which had been in the market for some time. Many large corporations adopted the policy of purchasing only prime-rated paper. Also, several state legislatures stipulated that only prime name paper could be purchased by state controlled funds, and in several states this restriction extended to state chartered savings banks. In the face of such competition, a number of smaller firms, principally regional finance companies, were forced to withdraw from the national market.

Despite the easier credit conditions which prevailed in 1967, the number of firms issuing paper climbed to 391, a net gain of 41. Of the several factors which contributed to this increase perhaps the most important was a legacy of the previous year's credit scarcity: a new awareness by corporate treasurers of the desirability of having alternative sources of funds. Firms were impressed with the dependability of the commercial paper market throughout 1966 and many of those eligible to tap it wished to establish contacts as insurance against another possible squeeze. Companies which had entered the market on a more or less emergency basis remained active in order to maintain contacts and to preserve a desirable flexibility in their financial programs.

Another factor which attracted issuers in 1967 was the widening of the spread between commercial paper rates and other sources of credit available to corporations. As shown in the chart, the cost of borrowing through sales of long-term bonds exceeded the cost of prime commercial paper for the first time since 1965. While bank rates declined in early 1967 and

INCREASE IN COMMERCIAL PAPER BY TYPE



Source: Federal Reserve Bank of New York.

then leveled off, commercial paper rates continued to plunge through the first half. The spread between the four- to six-month prime commercial paper rate and the prime rate climbed to 85 basis points in June, compared to a high of 21 basis points in 1966.

While dealer paper had constituted an expanding share of the total growth in commercial paper since 1965, not until 1968 did it account for more than half of the total increase in outstandings. The surge in dealer paper, which is illustrated in the bar chart, reflected the continued high cost of long-term borrowing, the maintenance of unusually large yield spreads favoring commercial paper over bank loans, and the rising tide of publicity concerning the market. In addition, the recent expansion of several prominent investment houses into the commercial paper field spurred competition and resulted in a more active solicitation of business. Many companies were first induced to issue paper by dealers. By October 1968, the number of issuers had jumped to 477, compared to 391 in all of 1967.

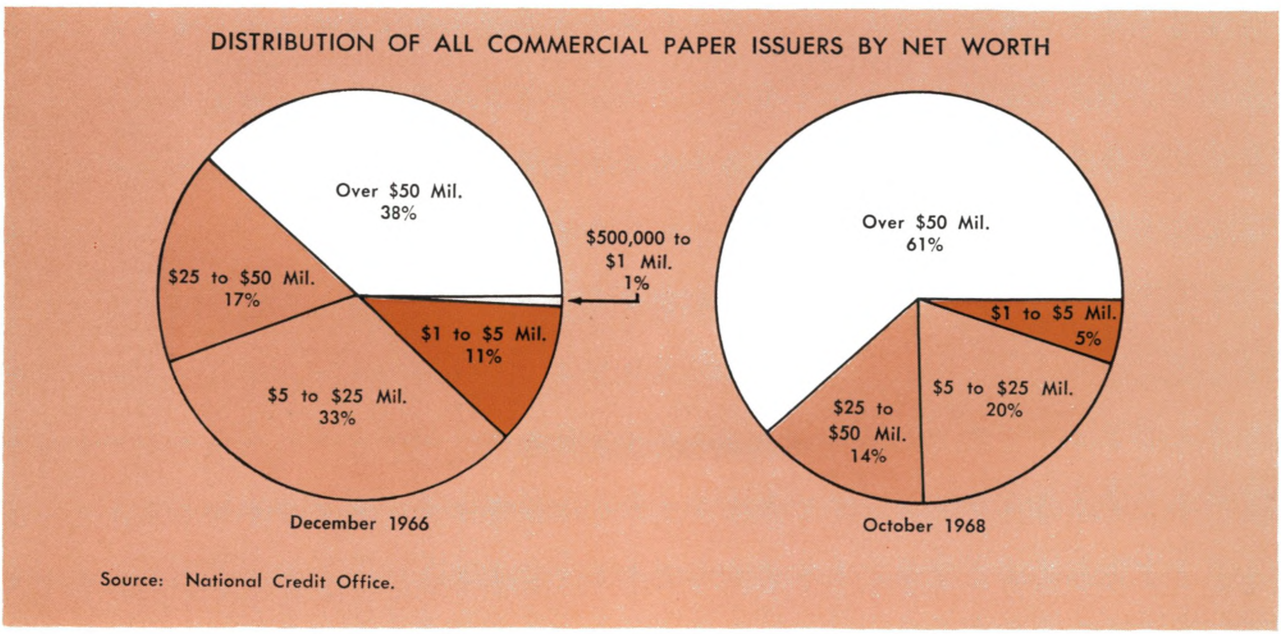
Changing Composition of Issuers Over the years, the commercial paper market has become progressively more exclusive even as the volume outstanding has soared. While the number of issuers has risen steadily in the last three years, there are still far fewer than in the past. In 1920, for example, over 4,000 issuers accounted for about $1.3 billion of paper outstanding. On the eve of World War II, about 750 firms were selling paper although three large finance companies dominated the market. The pie chart illustrates the increasing domination of the national market by the nation's largest corporations.

Since 1966 the number of finance companies issuing paper has declined from 134 to 122. The withdrawal from the national market of smaller nonprime finance companies has been partially offset by the establishment of captive finance companies by large manufacturing and retailing concerns.

Of the approximately 200 manufacturing firms selling paper in 1968, around 40 entered the market in the last two years. Aerospace and electronics firms have become much more active while manufacturers of grain, flour, fertilizer, and seed, which used to be prominent issuers, have largely faded from the market. After declining steadily as issuers of commercial paper, the number of wholesalers and retailers has increased gradually since 1966 and together totaled about 11% of all issuers in 1968.

The most interesting development has been the emergence of utilities as major issuers. Ten years ago there were no utilities in the market; two years ago, only eight. Today nearly 100 utilities are active in the market. Utilities have always depended heavily on sales of long-term bonds and flotations of stock to finance capital improvement and expansion. Bank loans have been the chief source of interim funds. As members of a regulated industry, these companies are extremely cost-conscious and have been especially sensitive to the escalation of interest rates since 1965. Quite naturally, therefore, utilities have been attracted by the relatively lower cost of commercial paper.

Jane F. Nelson



The Fifth District

Personal Income

Total personal income and per capita personal income have more than doubled, both nationally and in the District, during the past twenty years. Personal income, the total income received by individuals from all sources before personal taxes, is a major component in the national income accounts which, among other uses, are a measure of economic growth. Per capita personal income, total personal income divided by the population, is an indicator of the economic well-being of the individual, and the economic conditions of various regions can be compared by looking at these figures. Only a partial comparison can be made on this basis, however, because taxes and the cost of living also vary from area to area.

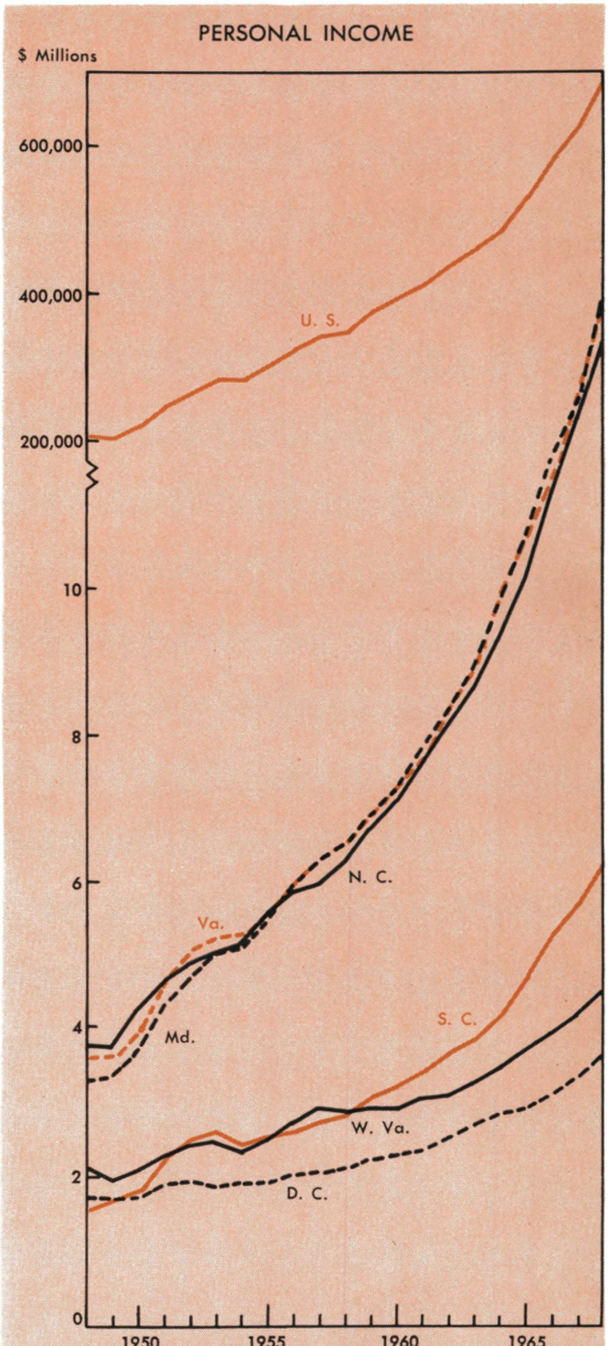
State rankings in total personal income tend, quite naturally, to follow population rankings, with the most populous states running ahead. Accordingly, in the Fifth District, Virginia led all states, followed by Maryland, North Carolina, South Carolina, West Virginia, and the District of Columbia in that order. These rankings were the same as the total population ranking with the exception of North Carolina which ranks first in population but third in total personal income. On a per capita basis, however, the District of Columbia ranked first last year, followed by Maryland. Both were well ahead of the national

PERSONAL INCOME

	Total			Per Capita		
	1948	1968*	Average Annual Growth 1948-'68	1948	1968*	Average Annual Growth 1948-'68
	$ mil.	$ mil.	per cent	dollars		per cent
Md.	3,331	13,912	7.4	1,467	3,703	4.7
D. C.	1,644	3,661	4.1	1,957	4,525	4.3
Va.	3,624	13,977	7.0	1,130	3,040	5.1
W. Va.	2,126	4,503	3.8	1,120	2,495	4.1
N. C.	3,732	13,375	6.6	973	2,605	5.1
S. C.	1,779	6,324	6.5	891	2,349	5.0
5th Dist.	16,236	55,751	6.4	1,156	2,966	4.8
U. S.	208,878	682,772	6.1	1,430	3,416	4.5

* 1968 figures are estimated.

Source: U. S. Department of Commerce.

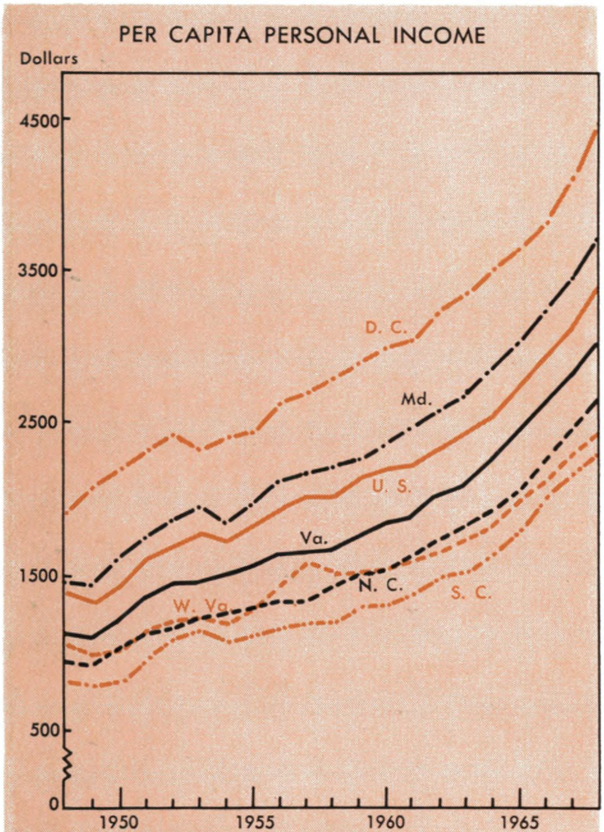


Note: 1968 figures estimated.
Source: Department of Commerce.

average. Virginia, North Carolina, West Virginia, and South Carolina followed in descending order.

The average annual growth rate of total personal income and per capita personal income may be a better measure of economic growth than the total amounts. With respect to total personal income, Maryland led the District with an increase of more than 7% per year over the twenty-year period from 1948 to 1968. The national average was slightly more than 6% for the same period, and only West Virginia and the District of Columbia in the Fifth District had growth rates less than the national average.

Virginia and North Carolina were the District leaders in growth in per capita income with an average annual rate slightly over 5% since 1948. The United States average over the same period was 4.5%. West Virginia and the District of Columbia again were below the national average, but the other Fifth District states surpassed it.



Note: 1968 figures estimated.
Source: Department of Commerce.

The 1968 rise in total personal income nationwide, according to the Department of Commerce, was the largest on record in absolute terms and the largest percentage gain since 1951. The increase was primarily attributable to payroll expansions. Gains were also made in transfer payments which are Government payments to individuals which do not involve payment for goods and services received by the Government. An example of this is Social Security benefits which increased in March 1968. Nonwage income, such as personal interest income and dividend payments, also increased. In the Fifth District, the gain was held down by a lag in agricultural income. Nationwide personal income increased 9.2% in 1968. In the Fifth District the increase in personal income was somewhat higher at 9.6%. Maryland led the District with a growth rate of 10.5% followed by Virginia and South Carolina at 9.9%, the District of Columbia at 9.7%, North Carolina at 9.0%, and West Virginia at 7.3%.

The growth in total per capita income in the District in 1968, however, lagged behind the United States average with the national figure at 8.1% and the Fifth District reaching only 7.6%. The District of Columbia led the District with an increase of 9.8% followed by Virginia at 8.4% and Maryland at 8.2%. Below the national average in per capita income gains were West Virginia with a 6.9% increase, North Carolina at 6.8%, and South Carolina at 6.2%.

Katherine M. Chambers