

# NORTHWESTERN Banker Newsletter

Vol. 6 No. 36

Des Moines, Iowa

January 2, 1978

## Prospects for the Credit Markets in 1978

"American credit markets in 1978 will face their most difficult challenge since the current economic expansion began in early 1975."

This is the conclusion reached by Henry Kaufman, general partner and economist, and James McKeon, vice president and senior capital market analyst, Salomon Brothers, New York, who believes that credit demands will move toward \$350 billion compared with \$323 billion in 1977.

"Needs for funds in three key sectors — household, business, and the Federal government — will intensify the credit creation explosion already evident this year. Financial capacity will be strained somewhat more than in 1977, increasing market pressures and resulting in a disappointment among some would-be borrowers.

"Short-term interest rates will rise irregularly to levels about 1.25 to 1.75 percentage points over current rates. Long-term yields, as measured by high-grade utility bonds, should approach or exceed 9%. Quality yield spreads should widen again."

The report noted that real savings formation will not match the rise in demand, so that

somewhat greater monetary accommodation will be needed.

However, these developments should not hamper economic growth next year even though more adverse conditions will prevail at the close.

Real economic growth is expected to be in the 4½% to 5% range while the inflation rate is projected to rise to 6½%. These assumptions are based on only a modest decline in the high rate of personal consumption, higher residential construction, larger capital spending than now envisaged, and bigger governmental expenditures.

Kaufman and McKeon make these major points in their analysis of the credit market outlook:

—The external financing needs of business corporations will soar to over \$100 billion, a record that will be 21% higher than this year's estimated \$84 billion and 2.6 times greater than the 1975 cyclical low. The biggest change will be in net new borrowings from commercial banks, at \$28 billion compared with \$18 billion this year. Borrowings by non-financial businesses from the commercial paper market and at finance companies will also remain extremely large. Total short-term borrowings by non-financial busi-

ness corporations will reach \$42 billion compared with \$33.3 billion in 1977. These businesses are expected to increase their net issuance of corporate bonds to \$27 billion this year. Internal cash generation will rise only marginally despite an anticipated increase in pre-tax profits of about 8%. Liquidity building will slow; four-fifths of external financing will be for capital goods and inventory expenditures.

—The household sector will continue to provide the bulk of new spending. Consumer instalment borrowing will rise at a slower rate than in 1977 this year, but nevertheless will reach a new record of \$36.5 billion, which is not an unsustainable rate.

The housing market will become increasingly tight. Housing starts will decline moderately to 1.9 million in 1977, but completions will continue to rise sharply. Residential and other mortgage demands are anticipated to increase from \$116 billion in 1977 to \$123 billion next year, with Federal credit agency programs providing \$26 billion compared with \$22 billion this year. This will leave \$97 billion to be financed in the private market which will be noticeably less

CREDIT MARKETS.....  
(Turn to page 3, please)

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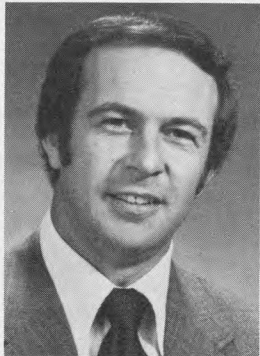
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### New Fed Chairman

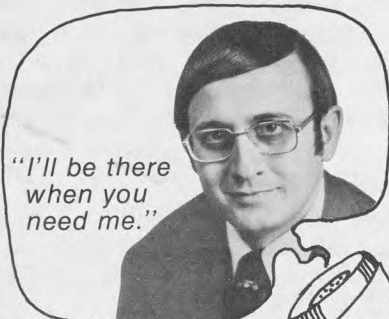
G. William Miller has been named chairman of the Federal Reserve Board by President Carter. Mr. Miller is chairman and chief executive office of Textron, Inc., Providence, R.I. He will succeed Arthur Burns, who will continue on the board.

### FDIC To Notify Directors Of Problem Bank Status

Chairman George A. LeMaistre of the Federal Deposit Insurance Corporation (FDIC) has announced that after January 1, 1978, the members of the board of directors of an insured state nonmember bank will be formally notified if their bank is considered to warrant inclusion on the FDIC list of problem banks.

Initiation of the notification procedure does not change the Corporation's policy of maintaining the confidentiality of an individual bank's problem status.

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### Iowa News

**DES MOINES:** The SBA farm drought disaster office has extended the filing deadline to February 23, 1978. Also the office has moved to Third and Keo Way. To date 4,200 applications for \$174 million have been received and the SBA has approved 800 loans totaling \$26 million. The largest was for \$400,000, the smallest for \$2,000.

**FAYETTE:** William B. Dohrmann of Miami, Okla., and Albert C. Duroe of Jesup, have purchased controlling interest in the State Bank of Fayette. Mr. Dohrmann will join the bank as president and Mr. Duroe will become chairman. Mr. Dohrmann is originally from Hampton, and is an agriculture graduate of Iowa State University, Ames. He has been with Hormel for the past 14 years.

**MINEOLA:** Wilbert C. Kruse has been promoted to vice president of Mineola State Bank. He has been with the bank since June of 1971.

**OTTUMWA:** The name of the Market Street office of the First National Bank has been changed to the Burgason Office in honor of one of the bank's employees, Rosetta M. Burgason. Ms. Burgason, assistant vice president and manager of the office, joined the bank in 1947.

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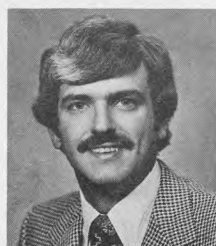


has announced the following three promotions: Kent Wigg to assistant vice president and manager, soon-to-be completed Plaza Office at 2900 Hamilton Boulevard, Mary E. Petty to assistant manager, Plaza Office; and Stephen Sargent to assistant manager, Morningside Office at 4608 Morningside Avenue. Mr. Wigg formerly was assistant manager, Morningside Office; and Ms. Petty and Mr. Sargent were family banking officers, main bank.

**WATKINS:** Funeral services were held recently for Alfred Joseph Schmuecker, 75, retired Watkins banker. From 1929-69 Mr. Schmuecker was cashier of the Watkins Savings Bank, retiring as executive cashier.

### Nebraska News

**LINCOLN:** Gateway Bank & Trust has announced the following promotions and elections: James A. Kruger, executive vice president; Mike Fosdick, loan division, and John McLaughlin, operations, vice presidents; Dennis Beranek, assistant vice president, loan division; Alan Austin, assistant cashier, and James Melton, loan officer.



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**Illinois News**

About 600 Illinois bankers will examine current credit and installment loans issues at the Illinois Bankers Association 30th annual Consumer Credit Conference, January 12-13 at the Hyatt Regency O'Hare in Chicago.

The conference will extend information in such issues as the "Risks and Pitfalls of Regulations B & Z, The Compliance Officer, New Collection Procedures, and Federal and State Legislative Update.

**CHICAGO:** H. Peter DeRosier has been advanced to vice president by the National Boulevard Bank. He joined the bank's correspondent department in 1969.

**CHICAGO:** Merchandise National Bank has announced the elections of Joseph F. Henmueller to vice president and James G. Sauer to assistant vice president. The bank also announced the opening of its new facility in Chicago's Apparel Center.

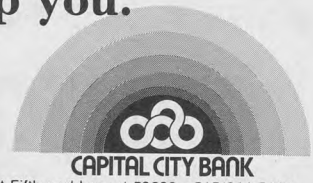
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has increased its capital from \$60,000 to \$120,000.

**Minnesota News**

**MAPLEWOOD:** Carol A. Kennedy has been elected cashier of the Maplewood State Bank.

**WILLMAR:** Eight women employees of Citizens National Bank have been on strike since before Christmas. Several months ago they organized independently as Willmar Bank Employees Association and have been certified by the NLRB. They claim sex discrimination and also demand higher base pay levels.

**Colorado**

**DENVER:** The Colorado Bankers Association has filed a petition with the Colorado Banking Board asking it to restrain Merrill Lynch investment firm and City National Bank of Columbus, O., from continuing to operate their Cash Management Account that has been offered since last September. The CBA maintains they are conducting a banking business in Colorado illegally.

**South Dakota News**

**ARMOUR:** First State Bank has increased its capital from \$125,000 to \$250,000.

**ARTESIAN:** Live Stock State Bank has changed its location from Artesian to 100 East Havens and Main Street in Mitchell.

**LAKE ANDES:** Andes State Bank

**CREDIT MARKETS.....**  
(Continued from page 1)

able to extend credit freely.

—Federal expenditures are expected to increase sharply, an extraordinary development for the fourth year of a business recovery, when revenues usually accelerate while the rise in expenditures slows. This will provide a boost to economic activity. The combination of Treasury and Federal credit agency borrowings, net of Federal Reserve takedowns, will grow from this year's \$72.6 billion to an estimated \$84.2 billion in 1978.

However, because of the sharp upsurge in private credit demands, the Federal needs for funds will be only 26% of total taxable credit market financing compared with 54% in 1975. Taxable credit demands are estimated at \$327

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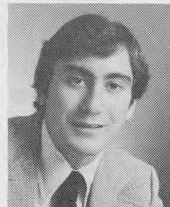
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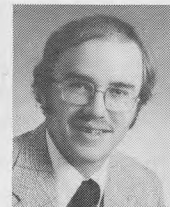
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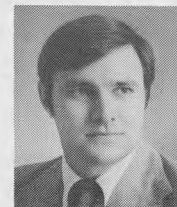
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billion in 1978, twice the 1975 level.

Because of the enlarged loan demands by business, mortgage borrowers and consumers, the burden of financing Federal needs will fall on two groups. Foreign central banks are expected to provide \$29 billion compared with \$28 billion this year, while individual investors will need to take a stupendous \$32 billion compared with \$11 billion in 1977.

—State and local government bond issuance is expected to fall sharply to \$38 billion from this year's record \$43.6 billion. Net of maturities, state and municipal debt will rise by about \$21 billion, or 7.7% next year, compared with \$30 billion or 12.2% in 1977.

While commercial banks, faced with larger loan demand, may not be as large a buyer of tax-exempt issues in 1978, fire and casualty insurance and tax-exempt bond funds may very well expand their buying. Within the tax-exempt category, issues to finance industrial aid and pollution control facilities, are projected to rise to a new high of \$4 billion as against \$3.4 billion in 1977. An important assumption is that tax-exempt yield levels will not advance next year as much as taxable levels.

Among institutional investors, thrift institutions will face a slowdown in the inflow of funds, long-term institutional investors such as insurance companies and

pension and retirement funds, will continue to move away from equity investments and further into corporate and foreign bonds and commercial mortgages, and commercial banks will finance rising loan demands through increased borrowing in the open market.

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