Prefatory Note

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[1] In some cases, original copies needed to be photocopied before being scanned into electronic format. All scanned images were deskewed (to remove the effects of printer- and scanner-introduced tilting) and lightly cleaned (to remove dark spots caused by staple holes, hole punches, and other blemishes caused after initial printing).

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CONFIDENTIAL (FR)

SUPPLEMENT

CURRENT ECONOMIC AND FINANCIAL CONDITIONS

Prepared for the
Federal Open Market Committee

By the Staff
Board of Governors
of the Federal Reserve System

October 16, 1964.

The Domestic Economy

Gross national product increased $9 billion in the third quarter to a seasonally adjusted annual rate of $627.5 billion, according to the Department of Commerce preliminary estimate. The total was 6.9 per cent above a year earlier; in constant dollars the increase over the year amounted to 4.8 per cent.

A large increase in final sales in the third quarter was partly offset by a decline in inventory investment, now estimated on the basis of incomplete data at an annual rate of $1.7 billion, as compared with $3.7 billion in the second quarter.

The rise in final purchases reflected substantial increases in personal consumption expenditures, net exports, business fixed investment, and State and local government purchases. Federal purchases and nonfarm residential construction activity were down from the second quarter totals.

The rise in consumption expenditures, nearly $8.5 billion (annual rate), was greater than the increase in disposable income and reflected strength in both durable and nondurable goods, as well as in services. Consumer after-tax income was up $6 billion, and the ratio of personal saving to disposable income declined to 7.4 per cent from 8.2 per cent in the second quarter.

Personal income before taxes increased $2 billion in September to a seasonally adjusted annual rate of $497 billion, a level 6 per cent higher than a year earlier. The September increase was in line with the average in earlier months this year. Most of the September increase was in wages and salaries. A gain of $800 million in manufacturing payrolls has been exceeded this year only in April and matched only in August.

Seasonally adjusted retail sales, based on data through October 10, appear to be off slightly from September. With automotive outlets registering decreasing sales, total durables may decline from their record September level, although sales at furniture and appliance stores have been very strong. Nondurable goods sales appear to be remaining at their slightly reduced September level.

The Domestic Financial Situation

On the basis of preliminary and incomplete data, the money supply is estimated to have increased $600 million further in the first half of October. Seasonally adjusted time and savings deposits are estimated to have increased $700 million in this period, reflecting in part the rapid rebuilding of CD balances at New York, Chicago, and certain outside banks.

Common stock prices broke sharply on Thursday in response to news of various political developments including reports that Premier Krushchev was being replaced in Russia. While trading in the decline was active, the market remained orderly, and losses were much smaller than during the decline following President Kennedy's assassination. By 1 p.m. Friday three-fourths of the loss had been recovered. Standard and Poor's composite index of 500 stock was quoted at 84.66, less than 1 per cent below the record high reached on Monday.

Total customer credit in the stock market rose $41 million during September, a month in which the Standard and Poor index rose nearly 3 per cent. This was the first month-to-month increase in stock market credit since the expansion of subscription accounts at the time of the A. T. & T. offering in April. Most of the gain in credit in September was attributable to a rise of $33 million in customers' debit balances on non-Government securities.

Preliminary data on net savings flows to mutual savings banks indicate a September expansion of $480 million. While this inflow was one-eighth larger than in September 1963, the year-over-year increase was smaller than monthly gains posted during the summer, when several large New York City banks were conducting intensive campaigns to attract funds. Adjusting roughly for seasonal influences, the September inflow was the smallest since May.

The following paragraphs summarize the results of the first quarterly survey of changes in bank lending practices, which was conducted as of September 30. This survey covers the respondents in the Quarterly Survey of Interest Rates on Loans to Businesses. (Reports received for a number of smaller banks in a few Districts are not included.)

About three-fifths, or 47 of the 78 reporting banks, indicated that demand for commercial and industrial loans had strengthened during the third quarter, while only one felt that it had weakened (item 1). Most of the banks at which demand strengthened over the quarter had not changed their policies with respect to solicitation of new loans, although an appreciable proportion of them had become less aggressive in seeking such business and a few more aggressive. Among all respondents taken together, 14 banks claimed to have become more aggressive in seeking new business, one more than had become less aggressive (item 2).

The largest numerical indication that banks were moving in the direction of firmer lending policies was the increased importance attached to the applicant's value to the bank as a depositor or source of collateral business in deciding whether to approve credit requests (item 3). Forty-three of the 78 banks indicated that this consideration was more important than 3 months earlier, and 26 indicated that more attention was being given to applicant's intended use of the loan proceeds.

The proportion of banks indicating firmer policies with respect to credit lines of new and nonlocal customers also was quite high, being about one-third of the total in each case (item 4). Only 3-4 banks had applied firmer policies in reviewing credit lines for established and local customers.

Moving next to the specific terms and conditions of lending, such as interest rates, and balance requirements, which might be expected to respond more slowly to changes in policy than the factors just discussed, the proportion of banks reporting firmer policies is generally much lower (item 5). But some tendency toward firmness in such credit terms was nonetheless quite pervasive. About one-sixth of the respondents, for example, had moved toward firmer requirements on interest rates and type and amount of collateral, three-tenths on compensating balances, and two-fifths on standards of credit worthiness. Morover, these tendencies toward firmness were widely distributed geographically, although banks in the San Francisco District showed the most widespread trend in this direction and banks in the St. Louis District and in New York City showed the least impact.

Banks have made the least change so far in loan maturity terms, with only 6 banks showing any general firming here. As regards willingness to make term loans, nearly one-fifth of the respondents had become firmer and one-tenth easier (item 6). However, 7 of the banks had moved toward longer term loan maturities and only 3 to shorter ones. The average of the reported maximum maturities that banks now generally will approve on term loans was about 6 years, but 5 years was the most commonly reported figure and 7 years the next highest.

Lending policies with respect to finance companies also firmed in the third quarter, but to a less extent than for nonfinancial businesses. Only a few banks had tightened with respect to interest rates and size of compensating balances, but appreciable numbers had stepped up enforcement of balance requirements and become firmer in establishing new or larger credit lines.

An appreciable number of banks that reported changes in policies also commented about the reasons for their action. For the most part, banks pursuing firmer policies referred to tighter money positions, high loan/deposit ratios, and growing concern about the quality of credit. Those seeking loans more aggressively or easing terms and conditions attributed this development to such factors as increased competitive pressure, the decision that a higher loan/deposit ratio would be appropriate, or a weakening of loan demand.

Reported Changes in Bank Lending Practices
June - September 1964
(Numbers of banks)

Lending to Nonfinancial Businesses

	Stronger	Weaker	Unchanged
1. Strength of loan demand	47	1	30
	Greater	**Less**	**Unchanged**
2. Aggressiveness of bank in seeking new loans	14	13	51

3. Factors considered in deciding whether to approve credit requests:

	More important	Less important	Essentially unchanged
Applicant's value to the bank as a depositor or source of collateral business	43		35
Applicant's intended use of loan proceeds	26	1	51

4. Practices with respect to reviewing lines of credit or loan applications:

Type of customer	Firmer	Easier	Essentially unchanged
Established customers	3	1	74
New customers	27	2	49
Local service area customers	4		74
Nonlocal service area customers	26		51

5. Terms and conditions of loans:

	Firmer	Easier	Essentially unchanged
Interest rates	13	1	64
Compensating or supporting balances	23	2	53
Standards of credit worthiness	30	1	47
Type and amount of collateral	14	3	61
Maturity	6		65

6. Term loans	More willing	Less willing	Unchanged
Willingness to make	8	15	55
	Longer	Shorter	Unchanged
Maximum maturity bank will approve	7	3	66

Years	Number of banks
3	10
5	35
6	3
7	15
8	6
10	4
n. a.	5

Lending to Finance Companies

	Firmer	Easier	Essentially unchanged
Type of requirement:			
Interest rates	5	2	71
Size of compensating or supporting balances required	2	2	73
Enforcement of balance requirements	13	2	62
Establishing new or larger credit lines	20	3	54

Source: Survey of Lending Practices at Large Banks in the Quarterly Interest Rate Survey.

International Developments

Revised figures for September show a small over-all deficit for the U.S. balance of payments; earlier and more tentative data had suggested a surplus for the month. The third quarter deficit now appears to have totaled about $1 billion, or approximately $2-1/4 billion at a seasonally adjusted annual rate. This total excludes the $200 million of special U. S. Government securities purchased by the Canadian Government in connection with the Columbia River project transaction.

Note: On page I-2 of Current Economic and Financial Conditions, the third line from the bottom should read "late September", rather than "mid-September."