CONFIDENTIAL (FR)

AGGRESSIVE BANK CONTACTS:

FOLLOW-UP

July 12, 1973

SUMMARY*

A reexamination of the 64 aggressive lending banks that were contacted by the Reserve Bank Presidents reveals that most of these banks have become more restrictive in their credit policies in recent weeks. Almost all of the banks reported a reduction in their rate of credit extension in the five weeks ended July 4, compared with the previous nine weeks ended May 30. Despite strong seasonal demand, most of the banks also reported a decline in the rate of growth of business loans over the recent period.

Overall growth in large certificates of deposit also slowed substantially in the recent five-week period, and many of the banks reported a decline in large CD's outstanding between May 30 and June 4. Moreover, the banks generally did not significantly alter their use of major nondeposit sources in the recent period.

Tighter current and expected money market conditions are causing a number of banks to further intensify their credit restraint programs. The largest banks in Philadelphia, for example, expressed increasing concern about a possible credit crunch, as their deposits have declined more than usual this summer while money market rates have continued to rise. So far, however, only large business loans have been constrained, as conditions for other loans have not been tightened.

Efforts to restrict the growth in business loans, however, are still being hindered by outstanding commitments and by the greater use of these commitments. A bank in the Richmond District, for example, experienced unexpectedly large takedowns in June and early July that caused its business loans to rise substantially. In an attempt to hold

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*Prepared at the Federal Reserve Bank of Dallas down future business loan expansion, this bank has established a central management committee to closely screen all new lines and all applications for sizable loans. Most of the growth of business loans in the Atlanta District since May 30 has also resulted from takedowns, as two of the largest banks among the four contacted indicated that they are refusing to take on any new commitments. In addition, the banks are generally cutting back their real estate and security loans to help meet business loan commitments.

Seasonal factors will operate to reduce loan pressures in July and August. And these downward pressures should combine with the generally restrictive loan attitudes of the banks to cause the rate of credit extension to decline further in the weeks immediately ahead.

FIRST DISTRICT -- BOSTON

With regard to the aggressive banks survey, the following data indicates a decline both in the rate of loan expansion and in the tapping of open market funds by the eight leading banks in New England.

During the period March 28 through May 30, total loans by these banks were expanding at a 24 percent annual rate. During the period May 30 through June 27, their loans were expanding at a 16 percent annual rate.

With respect to the acquisition of open market funds (all nondeposit sources of funds, net of Fed funds sold, plus large CD's), they were acquiring such funds at a 114 percent annual rate during the period March 28 through May 30. During the period May 30 through June 27, these open market funds contracted at an annual rate of 20 percent. At a meeting with the heads of the eight large banks today, they indicated that the sharp increase in the cost of these marginal funds was a factor in their reduced usage.

In discussing the competitive forces pushing them in the direction of increased loan volume, they stressed the greatly intensified competition in the New England market coming from two large Chicago banks.

SECOND DISTRICT -- NEW YORK

The total loans of two banks that had loan records indicating substantial growth earlier this year continued to advance during the first three weeks of June but showed signs of steadying in the two weeks ended July 4. One of these banks has total deposits in excess of $10 billion, and the other bank's deposits are in the range of $1-5 billion.

Business loans at these two banks generally continued to expand during the five weeks ended July 4. The growth of business loans extended by the large bank showed signs of slowing compared to the average growth during the first half of the year and loans appeared to be steadying during the two weeks ended July 4. The growth of business loans extended by the smaller bank slowed somewhat, but continued to suggest an upward bias through the end of the period. We estimate that the growth of business loans at both banks is being strongly affected by seasonal demand during the month of June. We anticipate that this demand will ease during July and August.

Total loans and total business loans of a third New York City bank with deposits in excess of $10 billion are holding close to or below levels reached in the latter part of March.

On or about July 14, we will have conducted individual meetings emphasizing credit restraint with a total of eleven leading New York City banks with widely varying loans and commitment patterns. We will continue to review current developments in the growth of bank lending and related matters in the context of encouraging credit restraint.

THIRD DISTRICT -- PHILADELPHIA

We have talked again with the six large member banks in Philadelphia. All of the banks are increasingly concerned about a credit crunch in the near future so they have intensified their efforts at restraint. Most banks cited high interest rates and greater than usual decline in deposits to date this summer as the basis for their concern. So far, only large commercial and industrial loans have been constrained. Conditions for loans to small business, real estate, etc. have not been tightened as yet. The rate of growth for loans continues to decline at Philadelphia banks, and all banks indicated a readiness to cooperate with the Fed in restraining credit.

One of the largest banks in Philadelphia continues to be the most aggressive lender. This bank's annual loan growth of 29 percent is the highest among city banks despite a steady drop since March (42 percent). Likewise, business loan growth has declined since March from 26 percent to 21 percent at present. Deposits have weakened since the last report despite increased reliance on CD's and has forced this bank to increase its reliance on nondeposit sources of funds. The bank reported increased loan demand during June. However, this increase was substantially less than that experienced in the first quarter of 1973. Most of the current gain was reported to be concentrated in real estate and consumer loans rather than in commercial and industrial loans, due to an internal policy of restraint and the nonprofitability of large commercial and industrial loans. Deposits are considered very disappointing by management. Net demand deposits are currently at the same level as a year ago. This bank is attempting to moderate loan expansion but expressed some bitterness over the high cost of money and resultant effects on profitability.

Another of the largest banks in Philadelphia was contacted on July 5. The annual rate of growth for loans has consistently dropped from 30 percent in January to 14 percent at present. Similarly, business loan growth has declined sharply and consistently since the start of the year. Although the growth rate of deposits is weaker than loan growth, deposit growth seems to have leveled off at around a 9 percent annual rate after declining consistently since last February. The official contacted said that controls were continuing to tighten because management was considerably more fearful of a credit crunch than in June. Most of the cutback was concentrated in loans to finance companies and other prime rate borrowers. There was no indication that demand for credit by small business, etc. would not be met. Dependence on nondeposit sources of funds has declined slightly since the June discussions. Although this bank would generally be considered an aggressive bank, the overall trend since March is compatible with Chairman Burns' guidelines of restraint.

We also spoke with a third large Philadelphia bank. The annual rate of loan expansion at this bank has trended modestly downward since February to a 20 percent annual rate, which is in line with other Philadelphia banks. However, commercial and industrial loan growth has increased sharply during this same period, after lagging other banks for most of the year. Deposit growth has dropped to a 4 percent annual rate, the lowest rate among city banks. Bank officials are concerned about their very poor deposit position. The decline in deposits so far this summer is considerably greater than usual. Because of the drop in deposits and inability to turn over more than one third of their CD's which matured in June, management experienced more tightness in June than in the previous reporting period. This resulted in increased borrowing mainly in the Federal funds market. The bank initiated a policy to restrain loan growth in March, and no further tightening is expected at this time. Bank officials believe that their loan position now has stabilized, and a relatively good liquidity position can be maintained because of securities maturing during the summer months. The bank seems most willing to cooperate with the Fed in moderating loan expansion.

We talked with another large bank in Philadelphia on July 5. Their loan growth (9.5 percent annual rate) remains substantially lower than other city banks but has trended upward since March. However, annual growth of business loans (4 percent) has declined since the meeting in June. The bank is experiencing a stronger than usual seasonal decline in deposits that is blamed on the overall economic climate. According to officials at this bank, there has been no change in overall policy since June. Terms and conditions for loans should continue to tighten. The bank has been reluctant to acquire Federal funds because of high rates. The bank does not intend to expand the volume of CD's in the future. At present, this bank would not be considered aggressive, and its policies for the future are in line with an attitude of moderation in loan expansion.

A fifth large Philadelphia bank that we had discussions with is not considered an aggressive bank. However, the annual rate of growth in loans has increased from 20 percent in April to 24 percent in June. Business loan expansion is slower than any other Philadelphia bank (under 5 percent annual rate). Deposit growth has increased to an annual rate of 12 percent in June, highest among city banks. This bank was least concerned about a credit squeeze at the meeting in June. However, their attitude has changed since then. The bank is more concerned about availability of funds, especially on a short-term basis. As a result, large commercial and industrial loans are coming under more intense scrutiny, although it was noted that the effect on their volume of loans would not be realized for several months. There has been no attempt to curtail real estate, small business, or construction loans. The bank has lessened its dependence on nondeposit sources of funds in accordance with the attempt to moderate expansion.

The final large Philadelphia bank we contacted is a moderately aggressive bank. Pressure has eased considerably since March. Loan growth has declined from an annual rate of 25 percent in March to 16 percent in June. At the same time, deposit growth has picked up to 11 percent. As liquidity improved, nondeposit sources of funds have declined from an April peak. Officials of this bank reported that they have been trying to hold down their loans across the board. However, they expect to lose future business because of these actions. The bank has been actively reducing all nondeposit sources of funds, especially Federal funds. Holdings of government and municipal securities now are considered to be at a minimum level. Reluctantly, specific programs of restraint have been initiated since our June meeting when this particular bank was critical of being asked to slow down. Loan trends show stronger declines than officials reported.

FOURTH DISTRICT -- CLEVELAND

Eight of the banks have reduced the rate of total loan expansion compared to behavior in the five months ending May 30, 1973. One Cleveland bank would appear to have been more aggressive in the period after May 30, but this reflects instability in the commercial and industrial loan volume which declined from March 28 to May 30 and then increased rapidly.

Another Cleveland bank shows a more rapid expansion of commercial and industrial loans and real estate loans after May 30 than before. However, security loan growth has slowed. Issues of large CD's have financed less than 10 percent of this recent loan growth, while sales of securities have financed about 30 percent, and other money market sources (reductions in net Federal funds sales and purchases of securities with agreements to resell) have financed about 60 percent.

FIFTH DISTRICT -- RICHMOND

Total loans of large banks in the Fifth District rose in the May 30 to July 4 period about in line with increases in the comparable period of each of the last two years. For weekly reporting banks, total loans were up 2.9 percent in the May 30-July 4 period compared with 3.4 percent in the like period of 1972 and 3.0 percent in the comparable 1971 period. Business loans in this year's period, however, are up 4.3 percent compared with 2.8 percent in the 1972 period and 1.7 percent in the same weeks of 1971. For real estate loans, this year's 2.5 percent gain compares with 1.4 percent and 1.6 percent in the comparable period of 1972 and 1971, respectively. Consumer loans in this year's period rose 2.7 percent, about in line with the increase in the same period of each of the last two years. Security loans dropped off 11.4 percent between May 30 and July 4, this year. For the comparable weeks of each of the last two years, they had recorded substantial increases. Weekly reporters reduced outstanding large CD's by 5.6 percent in the May 30-July 4 period. For the same period last year, such CD's rose 0.2 percent and for the 1971 period they increased 1.7 percent.

We feel that none of our large banks can be accurately characterized as aggressive lenders. The one bank ($1.2 billion deposits) that we thought might bear that characterization in our last report continues to experience some loan expansion but at a considerably more moderate pace than in the March 28-May 30 period. Business loans at this bank changed very little through June, but takedowns in the first week of July total 3 percent above the May 30 level. Real estate and consumer loans are also up 3 percent over the period but security loans are down 6 percent. Large CD's are also down about 8 percent for the May 30 level. This bank, which had been an overly frequent visitor at the discount window earlier in the year, is now out of the window and has recently reduced its total investments by a substantial amount. Its total investments fell 12 percent between May 20 and July 4. It has also borrowed heavily in the Federal funds market.

Of the other banks that we reported on last time, one ($555 million total deposits) experienced heavy takedowns in June and early July with the result that its business loans rose 15 percent over that period. For the same period, its consumer loans rose 3 percent, its real estate loans dropped 1 percent, its security loans declined 70 percent, and its loans to nonbank financial institutions were down 66 percent. Its total loans for the period rose 4 percent. We contacted this bank and were told that their takedowns in the period, primarily by national accounts, were unexpectedly large. Their line usage rose in this period from 31 percent to slightly over 33 percent. This bank has financed its recent loan expansion by increasing its outstanding large CD's, which rose 20 percent in the May 30-July 4 period, and through increasing its Federal funds purchases. The bank's investments were reduced 3 percent in the period. New CD issues have been mainly in 60-89 day maturities. The bank considers the takedown experience of the past six weeks to be abnormal and expressed serious concern over the sharpness of the recent rise in line usage. It has taken what it considers to be the extreme step of establishing a central management committee to screen closely all new lines and all applications for sizable loans. They hope to hold business loans at about current levels over the next month or so anyway.

SIXTH DISTRICT -- ATLANTA

Four of the previously contacted banks were recontacted, and they reported an overall tightening in credit expansion. Two of the banks indicated that no new commitments were being taken, and most of the banks anticipate little or no credit expansion for the next 30 to 60 days. New tighter credit policies were in effect as of July, 1973 for three of the four banks contacted.

Business loan expansion was down to 1.0 percent during May 30, 1973 to July 4, 1973, compared with a 3.8 percent expansion from March 28 to May 30. Real estate loans expanded at a 4.8 percent slower rate in the latest period than in the earlier one. Security loans dropped off 12.4 percent from the earlier period, resulting in a 10.0 percent decline for the period ending July 4, 1973. While consumer loans expanded at a 3.2-percent rate in the latest period, this represented a slowdown of 1.6 percent from the earlier growth rate.

Net Federal funds purchased were down 29.2 percent from the previous period, with nondeposit sources of funds up 2.0 percent for the current period. In general, a much tighter situation exists than was reported four weeks earlier.

SEVENTH DISTRICT -- CHICAGO

Three of the four banks that were contacted in June continued to expand their commercial and industrial loans in the period between May 30 and July 4, but at a slower rate than in the period between March 28 and May 30. Growth in real estate loans at the four banks picked up in the latest period, but security loans declined.

Overall, the four banks expanded their sales of large CD's, with only one bank reporting a decline since May 30. However, the recent growth rates in CD sales are significantly smaller than were reported for the period ending May 30, 1973.

The data were difficult to evaluate because of seasonal characteristics. However, no personal recontacts are thought necessary at this time.

NINTH DISTRICT -- MINNEAPOLIS

We have reviewed changes from May 30 through July 4 in the several categories of loans and in large CD's for the five banks previously reported on. We have also compared these changes with those for the two previous periods covered in our report of June 8. The results of our analysis do not tend to discount the banks' assurances of cooperation in the credit restriction program, nor do they provide evidence of any drastic reductions in the rate of loan increase. The most significant figures noted on the surface appear to be in the business loans category where the five banks showed an increase of $33 million to totals of $1.4 billion. More than half of this occurred in one bank which showed a business loan increase for the period since May 30 of slightly over 4 percent. We have again contacted this bank, which has assured us that it is attempting to fully cooperate with the program and is being selective in loan extensions. However, it is under extreme seasonal pressures from regular customers.

TENTH DISTRICT -- KANSAS CITY

A follow-up check was made on eleven aggressive lending banks in the Tenth District. These banks increased their total loans (excluding Federal funds sold) 2.5 percent from May 30 to July 4, while real estate loans increased 2.3 percent and commercial and industrial loans, 1.8 percent. In sharp contrast with the 16.5-percent increase in CD sales during the period ended May 30, the eleven banks reduced their CD sales by 2.0 percent in the latest period.

In evaluating whether these banks have reduced their rate of credit extension relative to the period March 28 to May 30, consideration was given to the shorter length of the most recent period and to the very marked seasonal strength of loans in the Tenth District during June relative to April/May. On the basis of this evaluation, all of the eleven banks appear to have moderated their rate of credit extension. Therefore, we have not recontacted these banks.

ELEVENTH DISTRICT -- DALLAS

Continuous monitoring of the seven large aggressive lending banks over the past five weeks reveals a further growth of total loans but at a rate nearly 20 percent slower than was evident in the previous nine weeks between March 28 and May 30. In the recent period of May 30 to July 4, total loans at these seven banks rose $71 million, compared with an increase of $160 million between March 28 and May 30.

Business loans of the seven banks increased at an even slower pace relative to the earlier period. Business loans increased by nearly $69 million in the past month compared with a rise of almost $161 million in the previous nine weeks. Real estate loans actually declined by $26 million, compared to an increase of $75 million in the earlier period, and security loans declined about $36 million as opposed to the $16-million advance from March 28 to May 30. However, consumer loans, rising $7 million in the past five weeks, showed a faster weekly pace than the equivalent increase in the nine-week period.

The level of large certificates of deposit outstanding declined in all but one of these banks, but the total was $3 million more than on May 30. However, in the previous period such CD's rose by $110 million. Guaranteed paper, ineligible acceptances, and loans sold to related organizations all rose less than $20 million in the latest five-week period as opposed to an increase of $87 million in the previous nine weeks.

Discussions with three of the largest banks brought out a willingness to restrain total loans but a recognition of the outstanding commitments which appear to limit the flexibility of the banks. No overt resistance was encountered, but in at least two instances loan growth exceeded the pace of the earlier period and some outright sales of loans were accomplished as a means of limiting the loan buildup on the banks' books.

As indicated in the first report of these contacts with aggressive lending banks, it is probably too early to expect a marked change in performance. The commitments outstanding and the higher rate of use of such commitments almost guarantee an increase in loans in the near future. However, it is already apparent that the banks are using reductions in real estate and security loans to satisfy some of the commitments. Consumer loan increases, somewhat less controllable, will probably continue to reflect consumer purchasing trends.

In summary, we are reasonably well satisfied that the banks have our admonition continuously in mind, and we expect that future performance regarding the rate of credit extension will be even better than that experienced over the past month.

TWELFTH DISTRICT -- SAN FRANCISCO

Follow-up check of six aggressive lending banks in the Twelfth District discloses on balance a moderate reduction in rate of credit extensions during the current period compared to the earlier period ended May 30.

Commercial loans have continued to increase moderately at four of the six banks, while two banks have posted moderate declines. Real estate loans have increased slightly at five of the six banks, as have consumer loans. The only category reflecting an overall decline is security loans. Changes in large CD's outstanding are somewhat mixed, with four banks reporting declines during the current period and two banks reporting larger totals.

We were informed during our contacts several weeks ago that the change in lending practices endorsed by bank management would take some period of time before being reflected in reported figures, owing to their widespread branch systems. Consequently, we have had no personal recontacts at this time; however, we will continue to follow trends closely.