

STAFF REPORT

working paper

SAVINGS AND LOAN ASSOCIATIONS

IN THE NINTH DISTRICT

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1/72



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SAVINGS AND LOAN ASSOCIATIONS IN THE NINTH DISTRICT

I. INTRODUCTION

In the past ten years, savings and loan associations (S&Ls) have played a very important role in the district's financial world. They ranked first in the district's mortgage lending activities -- followed by commercial banks and life insurance companies -- and second in their share of district consumer savings -- only surpassed by commercial banks. The purpose of this paper is to explore savings and loan associations in detail -- particularly those in the Ninth Federal Reserve District -- in order to discover their main functions, their general locations, and their market share among major financial intermediaries.

II. THE SAVINGS AND LOAN INDUSTRY

Before analyzing district savings and loan associations a brief description of the characteristics of savings and loans and the relation with their supervisory agency, the Federal Home Loan Bank (FHLB) System, is presented.

A savings and loan association is a private financial corporation which like a commercial bank serves as a financial intermediary by accepting savings from and making loans to the public. It does, however, differ from a commercial bank because it is required by law to provide funds for residential construction and home financing and has to carry at least three-fourths of its assets as residential mortgage loans.

Most of the nation's S&Ls are members of the FHLB System and are regulated by the Federal Home Loan Bank Board (FHLBB). The FHLB System was created under the Federal Home Loan Bank Act in 1932. It is designed to

provide a central credit agency to supplement the funds of its member institutions and therefore to stabilize the nation's residential construction. The FHLBB is a one-industry regulatory agency. It regulates twelve regional home loan banks which serve as central banks to supply funds in the form of advances to member associations. The Board, through its regional banks, charters federal savings and loan associations and regulates and supervises its member associations and a few savings banks under its jurisdiction. It directly regulates interest rates paid on savings accounts and member's liquidity and indirectly regulates other member activities through its power to restrict advances. Although regional banks supervise their members' activities, they are wholly owned by member associations. The Board, besides governing members, also regulates the Federal Savings and Loan Insurance Corporation (FSLIC) -- an agency which insures each savings account at member associations up to \$20,000.

Savings and loan associations consist of two main types. Federal savings and loan associations are chartered under the provisions of the Home Owner's Loan Act of 1933 and are supervised by the FHLBB. They are required by law to belong to the FHLB System and to have their savings accounts insured by the FSLIC. In addition, the associations are mutually owned by their members -- both savings account holders and borrowers. State savings and loan associations are chartered under state statutes and are supervised by their respective state savings and loan departments. Membership in the FHLB System is open on a voluntary basis to qualified state associations, as is the insurance of their accounts, and more than half of the state-chartered associations take both options. State associations are either mutually owned or have some form of permanent stock ownership which is similar to an ownership of ordinary corporation stocks.

III. THE STRUCTURE OF DISTRICT SAVINGS AND LOAN ASSOCIATIONS

In the Ninth Federal Reserve District, there were 141 savings and loan associations at the end of 1969. This represented 2.4 percent of all S&Ls in the nation. Figure 1 shows the location of district FHLB member associations by charter as of year-end 1969 and whether or not they had branches. The largest associations were clustered around the Minneapolis-St. Paul area and played a leading role in the district's savings and loan business. In recent years, S&Ls have been rapidly expanding their branch operations. There were 72 branches in the district in 1969, half of which were maintained by leading Twin Cities S&Ls.

Table 1 shows the number and assets of these associations by state, charter, FHLB membership, and FSLIC insurance. As shown in the table, most district associations are chartered by the Federal Government, are members of the FHLB, and are insured by the FSLIC.

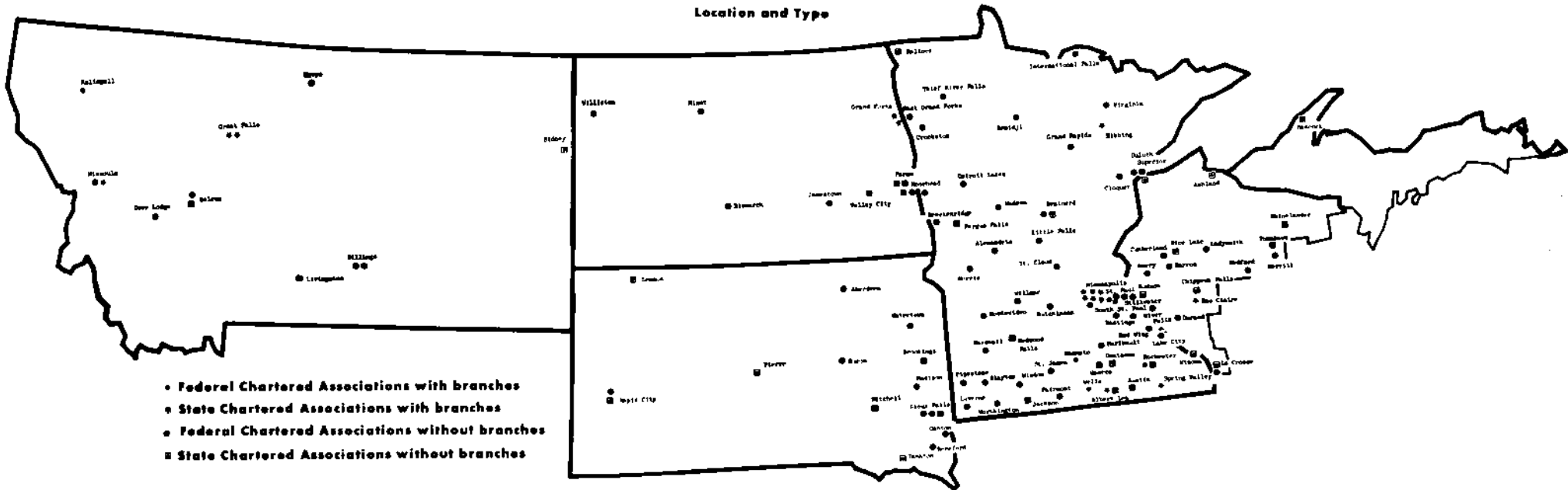
TABLE 1 Number and Assets of Savings and Loan Associations,
Ninth District - December 31, 1969

State	Members of Federal Home Loan Bank System						Nonmembers		Total			
	Total		Insured by FSLIC				Noninsured		Noninsured		Total	
			Federally Chartered		State-Chartered		State-Chartered		State-Chartered			
#	\$Mill	#	\$Mill	#	\$Mill	#	\$Mill	#	\$Mill	#	\$Mill	
Minnesota	64	3,064	53	1,939	11	125	0	0	13	15	77	3,079
North Dakota	11	449	7	213	4	236	0	0	1	1	12	450
South Dakota	16	225	9	187	6*	38	1	**	1	1	17	226
Montana	13	253	10	221	2	30	1	2	3	**	16	253
NW Wisconsin	18	282	10	214	8	68	0	0	0	0	18	282
Upper Michigan	1	226	0	0	1	226	0	0	0	0	1	226
District	123	4,499	89	3,774	32	723	2	2	18	17	141	4,516

* Including four permanent stock associations

** Less than \$0.5 million.

Figure 1. Savings and Loan Associations of Federal Home Loan Bank System in the Ninth District



As of December 31, 1969, total assets of district S&Ls amounted to \$4.5 billion, about 2.8 percent of the national total. Almost all of the district assets were held at member associations of the FHLB System, with half of the total at Twin Cities S&Ls.

Asset holdings of individual associations in the district ranged from one with \$200,000 in South Dakota to an association with \$750 million in Minnesota. The average size of a savings association in the district was \$32 million, slightly higher than the national average. The asset distribution among district S&Ls is skewed like that of many other industries in the nation: a large number of small savings institutions hold a small portion of the total assets while the bulk of the resources is concentrated in a few large associations.

Savings and loan associations play an important role in the Ninth District financial world. Table 2 presents a comparison of major characteristics of this industry with the district's other selected types of financial intermediaries -- commercial banks, credit unions, and mutual savings banks.

Although these intermediaries are located throughout the district, most of the information for the Upper Peninsula of Michigan and Northwestern Wisconsin is not readily available. As of December 31, 1969, in the four complete states of the district, commercial banks surpassed substantially all the other three types of financial institutions in terms of number, assets, total loans outstanding, and time and savings deposits. Although savings and loan associations placed second in the above mentioned areas, they ranked first in making mortgage loans due to their specially assigned functions. Mutual savings banks serve similar functions as S&Ls, but since there is only one in the district its share of district loans and saving deposits, as shown in Table 2, was relatively small.

TABLE 2 A Comparison of Selected Types of District Financial Institutions - 4 States, December 31, 1969
(Millions of Dollars)

	<u>Number</u>	<u>Assets</u>	<u>Total Loans</u>	<u>Mortgage Loans</u>	<u>Residential Loans</u>	<u>Time & Savings Deposits</u>
Commercial Banks	1,185	14,522	7,577	2,173	1,496	4,067
Savings and Loans	102	3,989	3,515*	3,466	3,466	3,371
Credit Unions	827	428	349	--	--	372
Mutual Savings Banks	1	606	450	450	450	554

*Estimated from the FHLB of Des Moines' ratio of mortgage loans to total loans (98.6 percent).

Sources: Assets and Liabilities, Commercial and Mutual Savings Banks, December 31, 1969; 1969 Annual Statistical Report of Members, Federal Home Loan Bank of Des Moines; Monthly Report, February 1970, Federal Home Loan Bank of Seattle; The F&M Annual Reporter, The Farmers & Mechanics Savings Bank of Minneapolis; and International Credit Union Yearbook 1970, Credit Union National Association International, Inc.

IV. SAVINGS AND LOAN ASSOCIATIONS AS SAVINGS DEPOSITORIES

As mentioned previously, savings and loan associations are one type of financial intermediary, the third largest in terms of assets in the nation, following only commercial banks and life insurance companies. They serve as depositories by accepting consumer savings from the public and as money lenders by lending those savings to home builders and buyers. There were over 46 million savers with an average account balance of \$2,898 at the nation's savings and loan associations in 1969. Funds were lent to 10.8 million borrowers, and the average loan balance was \$13,043. Thus, S&Ls served as intermediaries between a little more than four savers for every borrower.

Normally, savings inflow is the main source of funds for expanding loan portfolios at savings and loan associations. The other principal sources -- advances from the FHLB, borrowings from commercial banks, retained

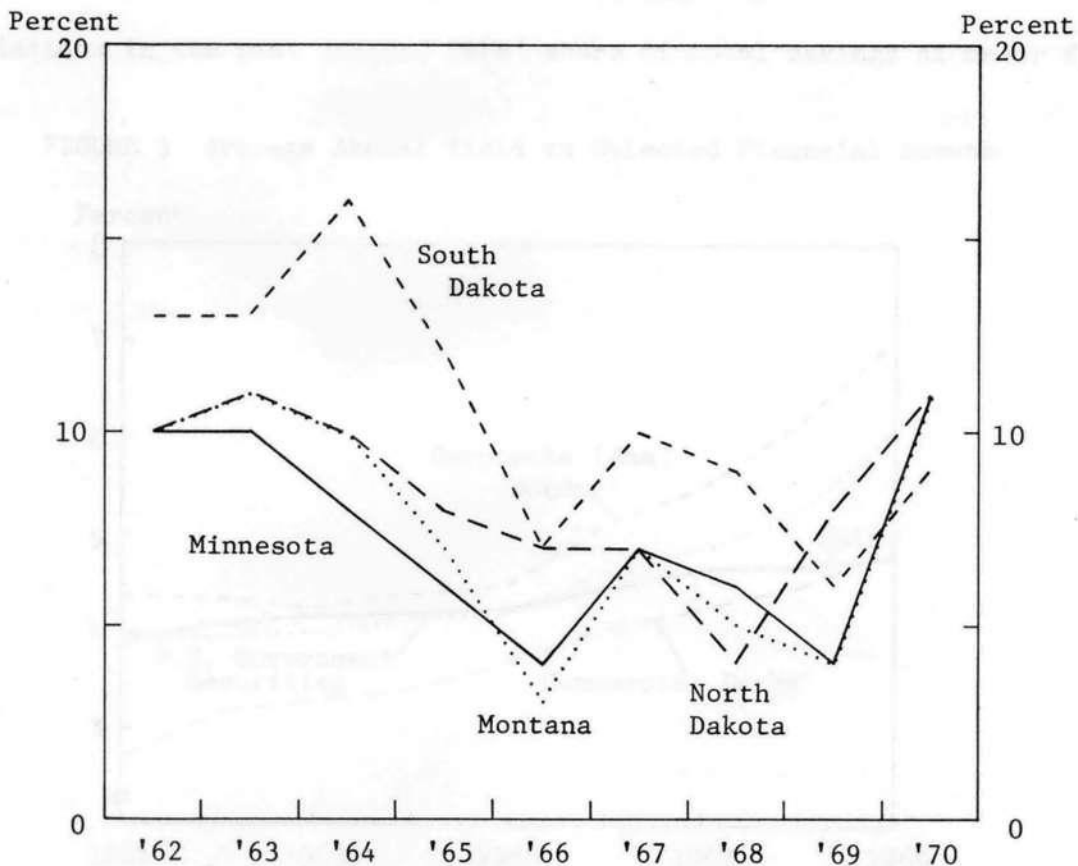
earnings, and selling of security holdings -- account for a very small portion of the funds available. Advances from the FHLB, however, play an important part when the major source of funds -- savings inflow -- is low, such as in 1969. During that year, a period of tight money policy, when market rates of interest were higher than the maximum rates S&Ls were permitted to pay on savings deposits, savers reduced their savings accounts and invested in higher yield market instruments, such as corporate bonds and Treasury bills. As a result, S&Ls suffered a substantial slowdown in the inflow of savings while demand for mortgage loans remained strong. In order to accommodate the strong loan demand, S&Ls stepped up their borrowings from their regional home loan banks. In 1969 advances from the Des Moines FHLB, which regulates S&Ls in three district states, accounted for about one-third of members' funds available while savings inflow provided slightly over one-half of the total. This is in contrast to the case in 1968, a year of less restrictive monetary policy, when savings inflow accounted for nine-tenths of total funds at member associations and outstanding borrowings from the Des Moines FHLB, in fact, declined.

Savings and loan associations primarily serve the household sector of the economy by issuing various types of savings accounts to the general public, mainly to individuals. Individuals, either alone or jointly, held 94.4 percent of the total deposits at S&Ls in May, 1968.

Due to the liberalization in the FHLB Board's regulations in early 1970, S&Ls now issue up to twenty-one different types of savings accounts, which can be classified into two major categories: passbook and certificate. These accounts differ with respect to maximum interest rates payable to depositors, maturity, and minimum balances authorized by the Federal Home Loan Bank Board. According to the FHLBB, most savings at insured associations are passbook savings.

In the past ten years, total savings capital held at district member associations of the FHLB increased each year -- on the average, about 8 percent annually.* The growth rate, however, slowed in the period 1964-69 (Figure 2) reflecting partly the increased bank competition for funds and partly the disintermediation out of savings institutions generally occurring in 1966 and 1969 as a result of tight monetary policy. The bank competition factors can be illustrated by both Figures 3 and 4. Figure 3 shows that during the 1960s banks enhanced their competitive position for savings

FIGURE 2 Annual Rate of Savings Growth at Ninth District Savings and Loan Associations - 4 States



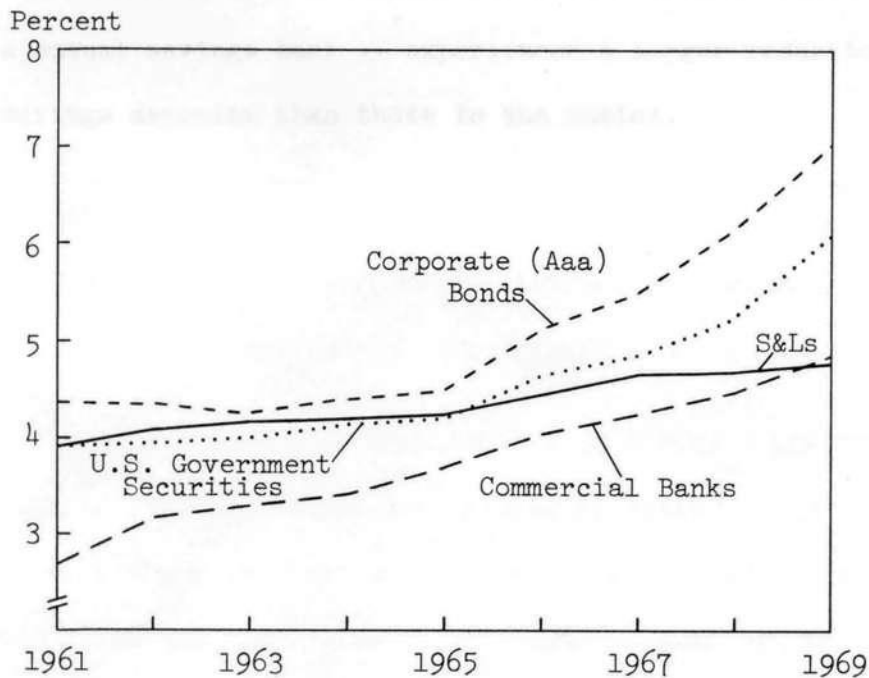
*Data on savings associations published by Federal Home Loan Banks are available only at the state level and for some large cities. Statistics used, therefore, will only reflect the figures for four full states in the district, i.e., Minnesota, North Dakota, South Dakota, and Montana.

deposits as their offering rate rose faster than that of S&Ls, thus narrowing the gap between the two rates and luring more funds. The result was that commercial banks attracted a greater portion of the consumers' savings in the district. This phenomenon will be analyzed in detail later.

The low rates of savings growth in 1966 and 1969 correspond with periods of monetary restraint. During those years, soaring interest rates on corporate bonds and government securities prompted savers to bypass savings institutions and invest directly in securities markets. However, as market rates eased gradually in the spring of 1970 this disintermediation diminished, and savings inflow at district associations subsequently strengthened.

Despite the continued growth in savings capital at all district associations in the past decade, S&Ls' share of total savings at major financial

FIGURE 3 Average Annual Yield on Selected Financial Assets



Source: Savings and Loan Fact Book '70, United States Savings and Loan League.

institutions has steadily declined. As mentioned before, savings and loan associations are only one of several types of financial intermediaries in the nation. They compete with commercial banks, mutual savings banks, credit unions, and other financial organizations for private, primarily over-the-counter savings.

Figure 4 shows the share of over-the-counter savings by major types of financial institutions in the district. Data were taken from 1961-1969 year-end call reports on time and savings deposits of individuals, partnerships, and corporations at all insured commercial and mutual savings banks, savings capital at FHLB member S&Ls, and savings deposits at all federally and state-chartered credit unions in the district's four full states. District insured commercial banks held over half of the consumer savings deposits in the district, but their share also grew at the expense of other thrift institutions. Between 1961 and 1969, district thrift institutions -- the S&Ls and a mutual savings bank -- experienced a larger reduction in their share of savings deposits than those in the nation.

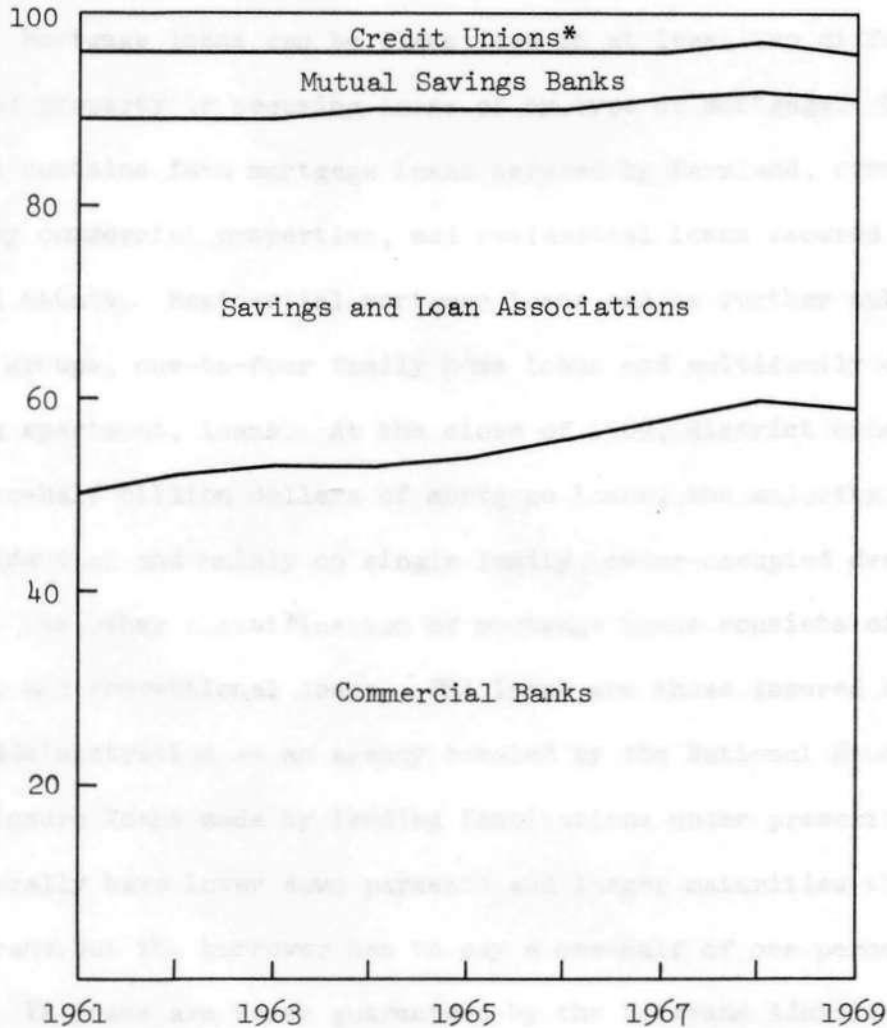


Estimated as a percentage of district savings for 1961 to 1969.

V. SAVINGS AND LOAN ASSOCIATIONS AS MORTGAGE LENDERS

While other financial intermediaries which have a wide range of assets to loan, savings and loan associations are limited by law to making mortgage loans to home buyers and business. They are especially designed to provide the credit and housing needs of the economy. Mortgage loans, therefore, are the largest asset category of S&Ls. As of year-end 1969, mortgage loans in district S&Ls amounted for 75 percent of total

FIGURE 4 Shares of Ninth District Savings by Major Financial Institutions - 4 States (percent)



*Estimated at 4 percent of district savings for 1961 to 1963.

V. SAVINGS AND LOAN ASSOCIATIONS AS MORTGAGE LENDERS

Unlike other financial intermediaries which have a wide range of loans to make, savings and loan associations are limited by law to making only mortgage loans to home builders and buyers: they are especially designed to finance the construction and housing sectors of the economy. Mortgage loans, therefore, are the largest asset category at S&Ls. As of year-end 1970, mortgage loans at district S&Ls accounted for 85 percent of total

assets, while cash, U.S. government securities, and other assets, including FHLB stocks, shared the remaining portion of the total.

Mortgage loans can be classified in at least two different ways: by type of property in securing loans or by type of mortgage. The first breakdown contains farm mortgage loans secured by farmland, commercial loans secured by commercial properties, and residential loans secured by residential real estate. Residential mortgage loans can be further subdivided into two groups, one-to-four family home loans and multifamily dwelling, including apartment, loans. At the close of 1969, district S&Ls held nearly one-half billion dollars of mortgage loans, the majority of which were residential and mainly on single family, owner-occupied dwellings.

The other classification of mortgage loans consists of FHA loans, VA loans, and conventional loans. FHA loans are those insured by the Federal Housing Administration -- an agency created by the National Housing Act of 1934 to insure loans made by lending institutions under prescribed conditions. They generally have lower down payments and longer maturities than conventional loans, but the borrower has to pay a one-half of one percent insurance premium. VA loans are those guaranteed by the Veterans Administration for returning veterans in acquiring homes. Besides other benefits, this type of loan has low or no down payment, longer amortization, a maximum guarantee of a home loan of up to 60 percent of the loan amount, or \$12,500, whichever is less. The interest rate ceiling on VA-guaranteed loans usually is the same as the ceiling rate of FHA loans. Conventional loans are those made by financial institutions without FHA insurance or VA guarantee. They conform to accepted standards, modified within legal bounds by mutual consent of the borrower and the lender. At the end of 1970, conventional loans accounted for over two-thirds of the total mortgage loans

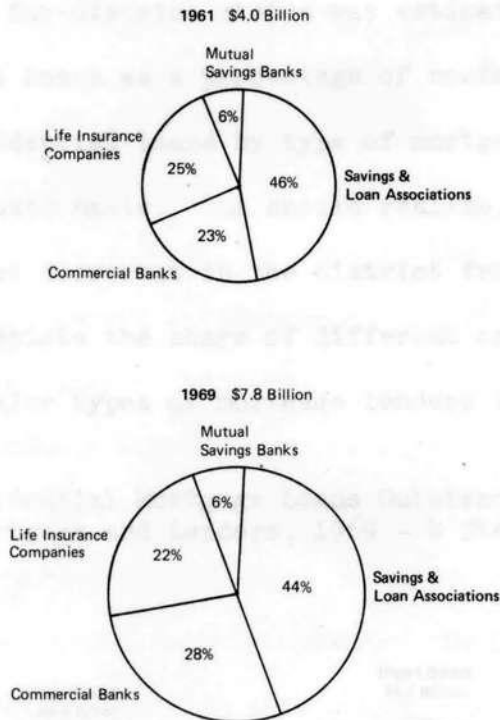
held by savings associations in the district, a proportion much lower than that for S&Ls in the nation as a whole.

In the past ten years, total mortgage loans held by FHLB member associations in the Ninth District have doubled. Like the growth in savings, the increase slowed during the tight money periods of 1966 and 1969 when there was a shortage of mortgage funds.

Savings and loan associations are not alone in mortgage lending. This function is shared with many other types of organizations: private institutions, such as commercial banks, life insurance companies, mutual savings banks, pension funds, nonprofit institutions, credit unions, real estate companies, and individuals and public agencies, mainly consisting of the Federal National Mortgage Association (FNMA), the Government National Mortgage Association (GNMA), and the Federal Home Loan Bank System. However, the bulk of mortgage credit outstanding is provided by only four of these organizations: savings and loan associations, life insurance companies, commercial banks, and mutual savings banks. At year-end 1969, they constituted four-fifths of the national total. According to the United States Savings and Loan League, savings associations currently provide two-fifths of all home mortgage credit in the United States and surpass all other financial institutions in both the total amount of their home loans outstanding and the dollar volume of their portfolios represented by owner-occupied homes.

Although detailed district mortgage loan data by all types of lenders are not available, the overall district picture seems to have followed the national pattern. Among the four major lending institutions, total mortgage loans outstanding at district savings associations have dominated the amount of the district's total mortgage loans outstanding during the past decade. However, as Figure 5 shows, their share at the end of the 8-year period was slightly lower than at the beginning. Similarly, the share of

FIGURE 5 Total Mortgage Loans Outstanding By Major Lending Institutions - 4 States



Sources: Federal Home Loan Banks of Des Moines and Seattle; Federal Deposit Insurance Corporation; Institute of Life Insurance.

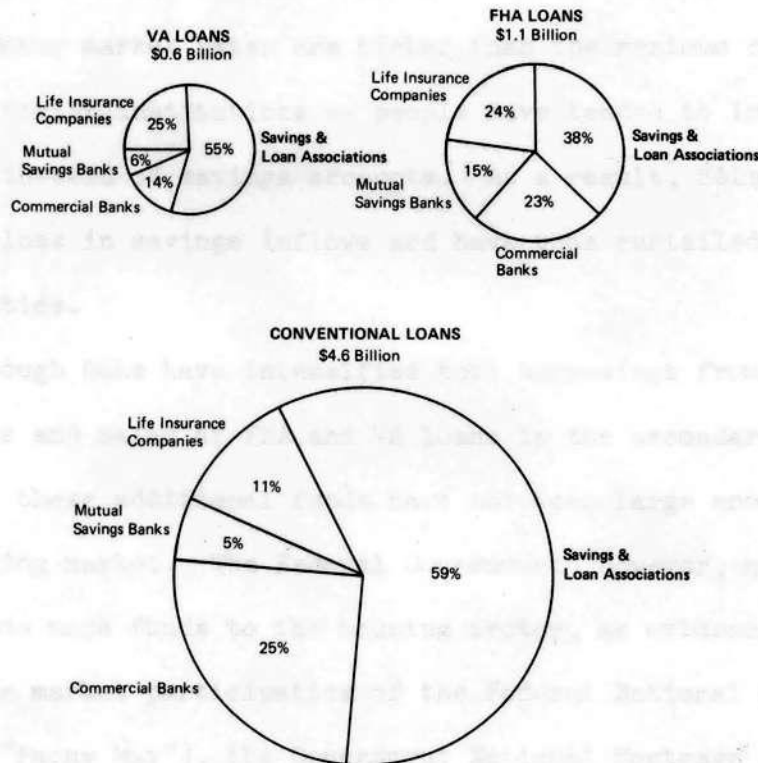
total mortgage loans at insurance companies also shrank somewhat over that period. Commercial banks, on the other hand, rose from third place in 1961 to second place in 1969, thus recording the greatest relative growth in real estate loans in that period. Of course, unlike savings and loan associations which had almost all of their portfolios in residential loans, commercial banks' and insurance companies' mortgage loans also included nonresidential loans, such as farm and commercial property mortgages.

It would be appropriate to compare each lender's market share of residential loans in particular. It would also be interesting to compare their market shares by types of mortgage, that is, by conventional, FHA, and VA loans, if possible. District loan data used for this type of comparison

included total mortgage loans at savings and loan associations and mutual savings banks and residential loans at commercial banks and insurance companies. The last set of data for district states was estimated according to a national figure of residential loans as a percentage of nonfarm mortgages at insurance companies, since residential loans by type of mortgages at these companies are not available on a state basis. One should realize, however, that the proportion might be somewhat different in the district from that in the nation.

Figure 6 depicts the share of different categories of residential loans held by four major types of mortgage lenders in the Ninth District. At

FIGURE 6 Residential Mortgage Loans Outstanding by Type of Mortgage and Lenders, 1969 - 4 States



Sources: The F&M Annual Reporter, the Farmers & Mechanics Savings Bank of Minneapolis; Federal Home Loan Bank of Des Moines and Seattle; Summary Report of Conditions, FDIC; The Tally of Life Insurance Statistics, August, 1970.

year-end 1969, total residential mortgage loans outstanding at these institutions amounted to over \$6 billion, and savings and loan associations were the largest holder of all three types of mortgage loans.

VI. CONCLUDING REMARKS

There is little doubt that mortgage lending activities at savings and loan associations will continue to grow in the future. To what extent they expand will mainly depend on general money and credit conditions and the Federal Government's actions to help the housing sector of the economy.

According to past experiences, savings inflows have been the major source of funds at savings and loan associations. The growth of mortgage loans has therefore been highly dependent upon the growth of savings deposits at these institutions. Unfortunately, however, at times of tight money -- periods when money market rates are higher than the maximum rates which can be offered by thrift institutions -- people have tended to invest their money in securities instead of savings accounts. As a result, S&Ls have suffered a substantial loss in savings inflows and have thus curtailed their mortgage lending activities.

Although S&Ls have intensified both borrowings from their regional home loan banks and sales of FHA and VA loans in the secondary market in these periods, these additional funds have not been large enough to lift the depressed housing market. The Federal Government, however, now appears determined to provide more funds to the housing sector, as evidenced by the recent active mortgage market participation of the Federal National Mortgage Association (FNMA or "Fanny May"), the Government National Mortgage Association (GNMA or "Ginny May"), and the FHLBB, including the recently established Federal Home Loan Mortgage Corporation. These agencies have played an increasingly important role in supplying mortgage funds to the housing sector in the

past and are expected to provide even greater support in the coming years. Housing construction, therefore, seems destined to become less dependent on swings in savings flows at thrift institutions and, thus, less volatile in the future.

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