MONTHLY Review

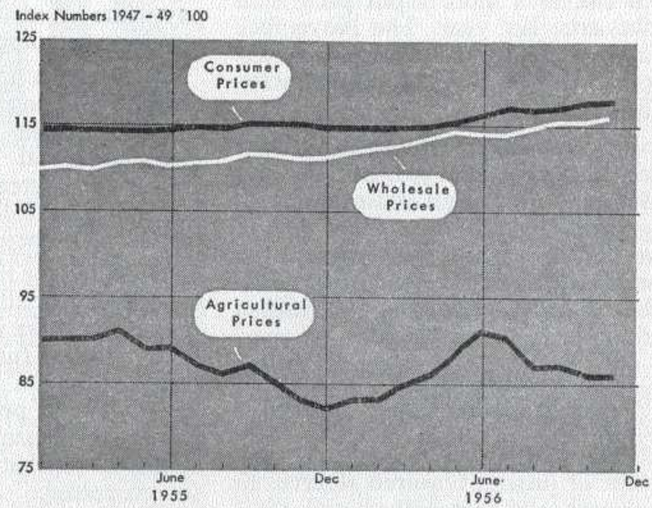
FEDERAL RESERVE BANK OF MINNEAPOLIS

SERIAL NO. 24 DECEMBER 31, 1956 VOL. 12

Current conditions . . . .

Economic prospects bright at new year's beginning

PRICE TRENDS—STILL UPWARD



A GOOD START into the new year is indicated by favorable district economic trends at the end of 1956. Even district farmers were optimistic at the year's end—more so than at any time since the early fifties.

Farmers have reason to be hopeful as production prospects improved during the growing season and as prices advanced, even though somewhat timidly. This change in price trend, the first since 1951, does not necessarily mean that farmers as a group are 'out of the woods,' economically speaking, or that agriculture's problems are now solved. It simply means farmers now are more hopeful that economic (and government) machinery is grinding out a better balance between production and both current and prospective demand. For example, it is expected the soil bank program in 1957 will take out of production a significant number of acres. Both domestic and foreign demand for farm products is currently strong, and the immediate outlook is favorable.

Although the district's economy is currently one of strength as measured by record levels in bank debits, department store sales, electric energy output, employment, wages, nonresidential construction, and bank deposits, there do exist some restraints and some uncertainties which temper or moderate the strong bullish factors.

One of these moderating forces is found in the important residential construction field, which, although not in the doldrums, is below year-ago levels. Another district industry, associated with residential building, is lumbering and millwork, which also is moderately down at the end of 1956.

As prices have risen elsewhere, so have prices in the district tended upward throughout 1956. To curb this inflationary trend and to maintain the dollar's purchasing power, the Federal Reserve's monetary policy of restraint continues unabated at the year's end.

That credit restraint is currently desirable and necessary is a logical conclusion when it is observed that most plants and equipment, as well as the labor force, are at or near maximum use. Too much money and credit at this time would operate only to push prices even higher and, conversely, to further cheapen dollar purchasing power.

Another indication of the pressure on capital and labor resources is the strong demand for bank loans that continues at the year's end. This pressure for loans continues in spite of the rising cost of money (interest rates) to the highest level in over 23 years.

Following are summaries that highlight the current economic scene in the Ninth district:

November banking developments

District member bank deposits during November continued to rise at a more rapid pace than was true last year. The November increase shattered the previous deposit high which had been established in November of 1954.

In November, deposits and loans respectively rose $61 million and $15 million in contrast to respective gains of $16 million and $11 million in November last year. Between the end of June and the end of November deposits grew by $308 million this year and $177 million last year.

The rapid inflow of deposits has been accompanied by a continued decline in the level of borrowings at the Fed. After falling to 5 percent of district required reserves in August and September and to 3 percent in October, borrowings fell further to approximately 1.5 percent of required reserves in November.

Maximum rates raised for time and savings deposits

The Federal Reserve Board of Governors and the FDIC have authorized insured commercial banks to raise interest rates on savings deposits and on certain types of time deposits. This marks the first increase in *maximum* rates on such deposits since 1936. The new higher rates are effective as of January 1, 1957.

Thus, insured commercial banks *may* increase interest rates on savings accounts (and on time deposits and certificates of deposit of more than six-months duration) up to a maximum figure of 3 percent. On time deposits and certificates which mature in 90 days to six months, the current 2 percent maximum has been raised to 2½ percent. The *maximum* rate of 1 percent on deposits and certificates of less than 90 days was left unchanged. (Banking legislation *prohibits* interest payments on demand deposits, i.e. checking accounts.)

Most banks in the district are currently paying less than the present 2½ percent ceiling on savings deposits. Local competitive situations will determine whether or not banks actually raise rates as a result of the new maximums.

These higher rates may stimulate savings, especially by individuals. Currently, there is a strong demand for long-term funds to be used for plant expansion and construction. Inflationary pressures resulting from such demands will be reduced to the extent that additional savings are generated.

Retail sales turn upward

District department store sales recovered from a brief slump in October. The index, adjusted for seasonal variation, in November rose to 122 percent of the 1947-49 base period. This is 19 percent above October of this year and 11 percent above November of a year ago. Merchants have expressed disappointment in the sale of gift items, but, in the aggregate, sales have risen decidedly more than the rise in prices over the past year.

Sales in all retail stores in the nation were up in November according to the U. S. Department of Commerce report. The preliminary figure, adjusted for seasonal factors and trading day differences, was 3 percent above October of this year and 5 percent above November of last year. In only two types of businesses, the lumber, building and hardware group and the automotive group, were November sales down from a year ago.

In the first two weeks of December, department store sales in the four large district cities were 4 percent above the corresponding weeks of last year. This percentage change may reflect a downward bias (as an indicator of 1956 Christmas trade) since at the end of the first two weeks of this December the remaining pre-Christmas shopping period was two shopping days longer than last year.

Farm interest rates firming

Interest rates on loans to farmers at district banks, have been notably stable the past two or three years, but now are showing signs of some adjustment upwards.

At least a few country banks have found it necessary to strengthen rates being charged on some of their farm loans. For the most part, this appears limited primarily to banks whose charges have been low in relation to their competition, and to those loans which have been made at the low end of the range of interest rates charged.

The main reason is the higher cost of money, as many banks have raised their rates paid on savings and as the general interest rate structure has gone up. Though there is not any evidence of any general increase in interest rates, the strengthening trend has been indicated at enough scattered banks around the area to be significant. The amount of the change is perhaps not as important as the fact that it does indicate the first upward adjustments in interest rates for farmers resulting from the relatively tight credit situation that has existed for the past 18 months. The majority of country banks have not changed their rates on farm loans.

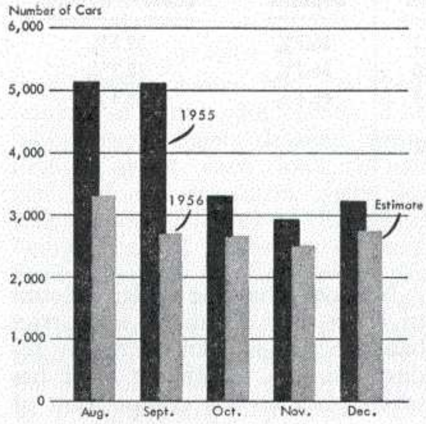
Sales of 1957-model automobiles

THE 1957 car models were introduced during October and early November 1956—in most makes of cars this was a few weeks later than for the 1956 models. Announcements of the new models resulted in a fairly heavy accumulation of early orders which were slow in being filled because of production difficulties and other delays.

Sufficient new cars were delivered to dealers in the Minneapolis-St. Paul metropolitan area to enable them to maintain sales at slightly below year-ago levels. New passenger car registrations during the first 11 business days of December were down somewhat more than that. The success of the 1957 automobiles will not become evident until March 1957 or later.

An informal survey of major auto dealers and automobile financing institutions in the Twin Cities was made in mid-December. Although registration figures indicate that sales are slightly under a year ago, the experience of individual dealers surveyed varies widely with the number reporting higher sales than a year ago about equal to the number reporting lower sales. Those in the latter category attributed depressed sales in some cases to a scarcity of new models and in other cases to a scarcity of credit.

NEW PASSENGER CAR REGISTRATIONS in the Minneapolis-St. Paul Area



Comments by major dealers and financing institutions in the Minneapolis-St. Paul market indicate that both are striving for more conservative terms. Despite this, automobile buyers, faced with the purchase of more expensive cars, are pressing for smaller down payments and longer maturities. The available statistics indicate that the buyers are succeeding in their efforts. The proportion of automobile contracts with maturities in excess of 30 months is increasing slightly, and down payments of one-third of selling price are not quite as frequent as was true a year ago.

In view of the demand for more liberal credit terms, it is interesting to note that many dealers report buyers are more interested in the higher-priced models and in expensive accessories.

Farm machinery prospects

PROSPECTS for farm machinery sales this winter and spring are taking a turn for the better, most farm equipment companies report. Many firms are expecting somewhat better sales of farm equipment during 1957 than they experienced during the past year. Sales this fall have improved, and new orders show an encouraging trend.

Prospects are closely geared to crop conditions throughout the area, however. As a result, areas hit by drouth this season are not expected to increase machinery purchases very much, if at all. Relatively good crop production throughout most of the area, however, along with improvement in prices of most farm products—notably hogs – have brightened the farm income prospects and thus the outlook for farm machinery sales. Such sales, which have been notably slow for the past year or two, are a fairly sensitive indicator of changes in the spending attitude of farmers.

Many farm operators have delayed machinery purchases over the past two years due to lower income, it is believed. END

District bank liquidity declines

THE ASSETS of Ninth district member banks have declined significantly in liquidity since the beginning of the current economic advance which began late in 1954. The 18-month period preceding June 30, 1956 witnessed demands by business and consumers for additional loans on a vast scale. A loan expansion of $326 million resulted (see table 1). During this period deposits actually decreased by $156 million; funds for this loan expansion were secured by sales of $352 million of U. S. government securities plus borrowings from the Federal Reserve and elsewhere. These developments were responsible for an increase in the so-called risk ratio (the ratio of loans to deposits) from 37 to 46 percent. This change corresponds closely to the pattern set by all member banks in the country since the aggregate risk ratio moved from 38 to 48 percent.

How does this mid-year liquidity position of district banks compare with their liquidity under the somewhat similar economic conditions

TABLE 1

Assets and Deposits of Ninth District Member Banks

(In millions of dollars)

	U.S. Gov't Securities	Loans	Deposits	Loans ÷ Deposits	All Member Banks (U.S.) Loans ÷ Deposits
June 30, '53	$1,391	$1,347	$3,672	36.7%	39.5%
Dec. 31, '54	1,620	1,512	4,120	36.7%	38.2%
June 30, '56	1,268	1,838	3,964	46.4%	48.4%
Change Since June 30, '53	—123	+491	+292		
Change Since Dec. 31, '54	—352	+326	—156		

that prevailed in June of 1953? At that time economic activity was also at a very high level and credit conditions were tight. Ninth district banks then had a much lower risk ratio (37 percent) and they held $123 million more in 'Governments' than was true as of June 1956, indicating a more liquid position existed.

An analysis of the government bond portfolio on the basis of its maturity schedules provides another measure of liquidity. In periods of restrictive credit policies interest rates tend to rise and bond prices fall, with the price decline corresponding directly to the amount of time before the maturity of the security. Since, under such circumstances, long-term bonds can often be sold only at a large discount from par, banks must actually rely on shortly-maturing securities for additional liquid reserves (to meet depositors' claims or to make additional loans).

Short-term holdings have been reduced

District banks' holdings of 'Governments' maturing within one year have declined drastically since June 1953 and December 1954; these declines amount to 40 percent and 49 percent respectively (table 2). Corresponding declines of 34 and 8.4 percent have occurred in holdings of securities redeemable in one to five years. Thus the future ability of district banks to obtain reserves without liquidating government securities below par has been severely reduced.

Not only has the dollar amount of short-term securities in district bank portfolios been materially reduced, but a significant shift has taken place in the composition of government bond portfolios over the last three years. Securities maturing within one year have declined from 33 percent to 21 percent of the entire portfolio, while those maturing in five years or more have increased from 13 percent to 39 percent of the total (table 2).

In summary

In summary, it is evident that the liquidity of district member banks declined substantially between the two comparable dates—June 1953 and June 1956. The trend is visible both in terms of a greater ratio of risk assets to deposits and with regard to the lengthening of the maturity distribution of government security holdings.

This is not to be construed as inferring that a high degree of risk exists in district banks' present liquidity, especially if high levels of economic activity continue. Even if a severe business recession should occur, the Fed could aid in providing bank assets with the necessary liquidity by making loans to banks and by purchasing securities in the open market.

However, the capability of member banks to expand loans further has been restricted as a result of the decline in holdings of securities near maturity. Thus, sizable new reserves cannot be obtained by district banks through the 'run-off' of short-term securities; nor can they be obtained from the sale of 'long-terms' except at the lowered prices in today's market.

Under these conditions, further substantial loan expansion in the Ninth district is unlikely.

END

TABLE 2

Ninth District Member Bank Holdings of U.S. Government Securities by Maturity

(In millions of dollars)

	June 30 1953	Dec. 31 1954	June 30 1956	% Change between June '53 and June '56	% Change between Dec. '54 and June '56	% Distribution by Maturity June 1953	% Distribution by Maturity Dec. 1954	% Distribution by Maturity June 1956
Due in one year*	$ 452	$ 525	$ 270	—40.3%	—48.6%	32.5%	32.4%	21.3%
Due in 1-5 years	761	548	502	—34.0%	—8.4%	54.7%	33.8%	39.6%
Bonds due in more than 5 years	178	547	496	+178.6%	—9.3%	12.8%	33.8%	39.1%
Total U.S. Gov't Securities	$1,391	$1,620	$1,268	—8.8%	—21.7%	100.0%	100.0%	100.0%

*Estimates of Treasury Notes maturing within one year are based upon samples of investment portfolios of 269 member banks as of June 30, 1955 and 1956.

Bank loans
to Ninth district farmers

THE EXTENT and nature of bank lending to farmers in the Ninth district is revealed by a special survey made as of June 30, 1956. District banks on that date had loans outstanding to some 277,000 farm borrowers, out of about 375,000 farms listed for this district by the 1954 Census. In other words, banks were lending to roughly three out of every four farm operators in the district.

Through a systematic sampling of farm loans at 140 district banks, detailed information on some 10,000 individual loans made to some 6000 individual farm borrowers was obtained. The average debt per borrower was $1,694; the average amount per loan was $965.

District banks on this date were extending about $470 million in farm loans (not including CCC loans). Of this total, $78 million were loans secured by farm real estate and $391 million were various types of non-real-estate loans. Since banks provide approximately 85 percent of the short-term production credit loaned to district agriculture by major lenders (not including CCC loans or loans made by the Farmers Home Administration) the information obtained by this survey is significant as to both the quantity and kinds of non-real-estate credit extended to agriculture.

Banks provide a much smaller proportion of *real estate credit* used by agriculture. Thus, while the survey information on real estate loans is important as a measure of bank lending in this field, it may only partially represent the characteristics of real estate loans made by other lending institutions.

Survey reveals characteristics

What the survey shows amounts to a 'photograph' of the farm loans that district banks had on their books on June 30, 1956. The 'photograph' shows detailed information about each loan. When classified and tabulated, these details provide profiles of the credit being extended to district farmers. Studying these profiles reveals the major characteristics of this credit —not only in the sense of a debt obligation, but also as the contribution being made to agriculture by borrowed capital and the ways this capital is being used by district farms. They also reveal much about the procedures used in extending that credit, and the kinds of services provided.

Results of the survey show that a very substantial amount of the loans made to farmers in the Ninth district are for the purpose of financing intermediate-term investments in agriculture. A large number of farm loans are also made on an unsecured basis, although the typical farm chattel was the most common collateral for a loan. The survey also showed that a large proportion of farm loans are renewed each year on the basis of a previous understanding between borrower and lender. Loans acquired from dealers and other sources have become an important part of the total lending of banks. The bulk of farm loans are made by small, local banks which deal directly with their customers; but larger banks occasionally 'participate' by taking part of a loan that is too large for the local bank to handle alone.

Why credit is important

Both the amount and the terms of credit used by farmers in their business are important. The amount of debt a farmer owes represents a fixed obligation against his business: it must ultimately be repaid out of income—or, assets must be liquidated in order to repay the loan. In the same way, the amount of credit extended to agriculture at any particular time represents a financial obligation of the industry.

In another way, the amount of credit extended to agriculture is important because it represents borrowed or 'hired' capital. To the

Sampling procedures for this nationwide survey of bank loans to farmers were designed to provide statistically reliable information for various Federal Reserve districts and for the nation as a whole. We are pleased to note that out of 140 banks selected as a sample of banks representative of the Ninth district, all except one cooperated in the survey.

By providing detailed information on individual loans and individual borrowers, these banks have provided a great amount of valuable information about the characteristics of bank loans to agriculture in this district and throughout the nation.

The survey was made with the cooperation of the Federal Deposit Insurance Corporation and the American Bankers Association. Both member and non-member banks are included in the survey, so that a complete and accurate cross-section of bank lending to farmers could be obtained.

TABLE I

Purpose of Farm Loans—Ninth District Banks, June 30, 1956

(Thousands of dollars)

Purpose of Loan	Real Estate Loans Amount Outstanding	Real Estate Loans Percent	Non-real-estate Loans Amount Outstanding	Non-real-estate Loans Percent
Current Operting Expenses:				
Feeder livestock	$ 538	0.7	$ 29,330	7.5
Other current operating expenses	2,418	3.1	106,663	27.3
Total Current	**2,956**	**3.8**	**135,993**	**34.8**
Intermediate-term Investments:				
Other livestock	1,218	1.6	48,591	12.4
Machinery and equipment	4,546	5.8	117,108	30.0
Automobile and other consumer durables	568	0.7	18,710	5.0
Improve land and buildings	15,240	19.8	11,937	3.1
Total Intermediate	**21,572**	**27.9**	**196,346**	**50.5**
Buy Farm Real Estate	38,529	49.5	11,238	2.9
Consolidate and pay other debts	12,388	15.9	33,750	8.6
Other Purposes	2,455	3.7	13,590	3.2
Total, All Purposes	**$77,900**	**100.0**	**$390,917**	**100.0**

extent that individual farmers can finance part of their business operations with this 'hired' capital, they are able to operate with more capital and resources at their disposal than would otherwise be possible. This larger capital structure usually means a larger business, larger output and, presumably, a more efficient and profitable scale of farm operation.

In addition to the total amount of credit used by agriculture, the terms on which it is extended are also important. These define the basis on which capital may be borrowed and thus, indirectly, tend to regulate its use.

The various credit profiles obtained from this survey describe the following major characteristics:

(1) The purpose for which credit is being used by farmers.

(2) The stated maturity; repayment method; the planned and the actual pattern of renewals.

(3) The security or collateral—that is, the assets that farmers are required to pledge as collateral for the credit they receive.

(4) Interest rates—the price borrowers pay for the use of credit.

(5) Where credit is acquired.

The survey also shows important characteristics about the borrower —such as how long he has been in debt, type of farm, his age and net worth.

Purpose of farm loans

The 'photograph' of farm loans outstanding at district banks on June 30, 1956 shows the purpose for which these loans were made, and thus indicates the uses being made of this credit by farmers. Table 1 shows the amounts outstanding for both real estate and non-real-estate loans according to purpose. Half of the non-real-estate credit and slightly more than one-fourth of the real estate credit loaned to farmers in this district was for purposes classified as 'intermediate-term' investments. These include loans for such purposes as the purchase of dairy or breeding livestock, purchase of machinery and equipment, purchase of automobiles and some other consumer durables, and loans to improve land and buildings. Altogether, lending for intermediate-term investments made up 46 percent of all loans outstanding at district banks on June 30.

Considerable interest has been shown in the problem of intermediate-term credit in recent years, partly because of increased operating costs and investments in agriculture which have emphasized the needs for this kind of credit. This survey now provides some real measure of the extent to which such credit is being provided.

The survey results (table 1) also indicate that loans secured by farm real estate are used to finance a variety of farm business needs—including production expenses, the refinancing of other debts, and the improvement of land and buildings. These are the purposes for which real estate loans were originally made, and where the credit has been 'on the books' for two or three years or more, they may not represent today's use of borrowed capital.

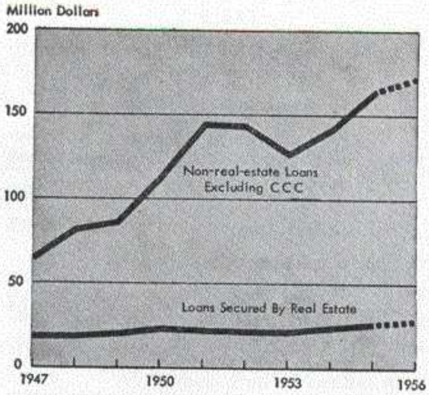
Maturity, repayment, renewal

Table 2 shows the terms of maturity, repayment provisions and renewal status of the non-real-estate loans that were outstanding at district banks on June 30, 1956. These figures represent a wide variety of loans, including instalment loans made directly by banks and also those acquired from dealers and other sources.

Instalment lending for purchase of durables and other equipment items probably accounts for the substantial amount of loans made for terms of two years or over. The bulk of other non-real-estate loans are made for maturities of 15 months or less. This undoubtedly reflects the practice of many banks to make loans for maturities of one year or less, with the understanding that the loans may be renewed, a common practice among banks in most areas of the country. The practice is favored by many lenders because it provides for a periodic review of the loan, including at least partial repayment and a complete review of the borrower's financial circumstances and possible continuing need for credit.

In classifying maturity and repayment terms, all notes were listed as 'demand' loans when they were legally defined as such, and all demand notes listed as 'single payment.' It should be noted, therefore, that a large number of the loans written as demand loans are actually repaid in regular or irregular instalments over an extended period with interest charged only on the balance outstanding. A substantial portion of the loans in the 'demand' classification are clearly of this type.

Some real estate loans are also written on a 'demand' basis and some are written for relatively short periods of from two to five years. This again reflects the variety of practices used by individual banks. Repayment figures as well as direct contact with lenders indicate that most of the real estate loans listed as 'demand' were actually being repaid on a regular instalment basis and were, in practice, normal real estate loans. Some real estate loans written for maturities of two to five years were also made with the understanding that repayment would be over a longer period, lenders indicated. Some of these loans, however, were to finance intermediate-term investments or production expenses which would normally be repaid within the period indicated.



FARM LOAN TRENDS at district member banks are shown above. Although both real estate and non-real-estate farm loans have been rising steadily, the debt outstanding remains fairly low relative to the value of assets represented.

1956 figures are estimated.

It should be emphasized that the maturities listed may not always represent the actual repayment commitment of the borrower. The 'normal practice' of a bank in making such loans is probably a better measure of the actual rate of repayment and loan liquidation in such cases. Many of these differences reflected the kind of credit being extended. Instalment loans for machinery, automobiles and consumer durables are frequently written for terms longer than one year; thus the terms of such loans largely represent the expected repayment. The bulk of farm chattel lines, on the other hand, are probably written for shorter periods (a year or less) and may be frequently renewed. Such lines of credit are somewhat more flexible in serving the needs of borrowers. The renewal method provides for periodic review and adjustment of the borrower's credit needs and helps to make this flexibility possible.

More than a third of the farm chattel loans outstanding on June 30 had been renewed at least once as a result of previous understanding between borrower and lender. Instalment loans are renewed less frequently since the initial terms of the loan extend over the full period of expected repayment.

Security and collateral

The security listed for farm loans suggests to some extent the kinds of assets that may be pledged as collateral for a loan. While the specific collateral often represents the purpose for which the money is borrowed—such as a conditional sales contract for an automobile—in many cases this is not true. Often the collateral includes much more than the item for which credit was advanced, or the collateral may be different entirely. For instance, many banks in the western areas of the Ninth district emphasize livestock in their collateral require-

TABLE 2

Selected Characteristics of Non-real-estate Loans at District Banks—June 30, 1956

(Thousands of dollars)

Maturity:	Amount Outstanding	Percent
Demand	$ 33,112	8.5
6 mos. and less	36,218	9.3
6 mos. to 1 year	177,563	45.4
1 to 2 years	112,340	28.7
2 to 5 years	30,553	7.8
Over 5 years	1,131	.3
Total	$390,917	100.0

Repayment Method:	Amount Outstanding	Percent
Single payment (including demand loans)	$323,807	82.8
Instalments with interest charged on unpaid balance	50,505	12.9
Instalments with interest charged on original amount	16,598	4.2
Unknown	7	.1
Total	$390,917	100.0

Renewal Status:	Amount Outstanding	Percent
Note has not been renewed	$220,202	56.4
Note renewed because of understanding when note was made part or all of note would be renewed	139,279	35.6
Note renewed for other reasons	31,271	8.0
Total	$390,752	100.0

ments even when extending credit for other purposes such as purchase of farm machinery.

Table 3 shows the forms of security used as a basis for advancing the credit to farmers as of June 30, 1956. A substantial part of this credit—20 percent of all loans—was loaned on an unsecured basis. This is common in cases where the borrower has a sound financial record and is known to be reliable. In most cases he has probably been doing business with his particular banker for a number of years.

In interpreting these figures it should be recognized that security may be required for several different reasons. Mainly, it is to provide the necessary protection for depositors whose funds the bank is lending, and to meet the requirements of bank supervisory authorities. The security itself provides some guarantee that the loan can be repaid, if necessary, out of the liquidation of pledged assets—although this is seldom the expectation at the time the loan is made.

Another important reason for collateral is to protect the assets of the borrower from attachment or lien by subsequent creditors with whom a borrower might become involved. This prevents other obligations from undermining the soundness of the credit already extended.

TABLE 3

Security Required for Farm Loans at Ninth District Banks—June 30, 1956

(Thousands of dollars)

Major Security:	Amount Outstanding	Per-cent
Unsecured	$ 93,719	20.0
Endorsed or Co-maker	16,371	3.5
Chattel mortgage, Chattel deed of trust or conditional sales contract	277,205	59.1
Farm real estate (except Govt. guaranteed or insured to be included under code 5)	72,103	15.4
Govt. guaranteed or insured (excl. loans directly guaranteed by CCC)	5,798	1.2
Other	3,435	.7
Unknown	188	.1
Total	$468,818	100.0
How Acquired:		
Loan made direct to customer	$409,505	87.4
Loan acquired from dealer	59,313	12.6
Total	$468,818	100.0

Interest rates

Interest rates on farm loans represent the cost of credit to the borrower. From the lender's standpoint they reflect not only the cost of funds loaned but also the risk element in making loans and the services that may be provided by the lender.

Rates paid by farmers on loans for intermediate-term investment were shown by this survey to be somewhat higher than credit for other purposes. One of the reasons for this difference is the practice of charging interest on a discount basis for many instalment loans. On this basis, interest is figured on the original amount of the loan even though it may be paid off in regular instalments over a period of time. Over the life of the loan the effective rate of interest paid on the amount of the loan actually outstanding is roughly twice the stated interest rate.

Since most instalment loans of this type represent intermediate-term investments, they help to raise the interest rate average for loans in this category. On about one-fourth of the non-real-estate loans paid in instalments the interest charged was figured in this way. But these amounted to only 4 percent of all non-real-estate loans.

This is a common practice in instalment lending. When a bank accepts such paper from farm equipment dealers or other dealers in farm supplies, only part of the amount charged to the farmer by the dealer is paid to the bank. In most cases it amounts to about half of the total interest charged.

Although interest charges are an important cost consideration in using credit, the significance of a particular interest rate may be tempered by other important considerations such as the 'risk' involved and the other services provided. Probably most important of all considerations is the profitable use of the additional capital within the farm business itself.

Based on the great amount of detailed information given about individual loans and individual borrowers, the survey makes it possible to describe accurately the main characteristics of credit being extended to agriculture by district banks—the amounts, the variety of purposes and, to some extent, the procedures employed.

Neither the 'profiles' of these characteristics nor the details from which they are compiled, however, can describe the full range of uses made of 'borrowed capital' by individual farmers. Nor can they fully describe the variety of means by which lenders make credit available to individual farmers under varying circumstances.

As the financial needs of agriculture continue to grow, both in amount and complexity, the use of credit by farmers will undoubtedly grow also. As it does, the information provided by banks cooperating in this survey will prove a valuable guide in making this needed credit available and will be helpful in interpreting the changes that take place.

END

Construction and mortgage activity in the district

THE VOLUME of nonresidential construction — industrial, commercial, educational, public and heavy engineering—set another record in 1956. In fact, the activity in this type of construction was an important source of strength in the district's economy when other factors (home building, automobile sales, steel and ore boat strikes) were acting adversely.

Expansion in nonresidential construction in 1956 more than offset the contraction in home building. The value of non-home construction in the nation totaled about $28.7 billion, an increase of $2.5 billion from 1955, according to the most recent estimate prepared jointly by U. S. Departments of Labor and Commerce. Expenditures for residential building totaled about $15.5 billion, a decrease of $1.4 billion from 1955. Expenditures for new construction in 1956 will rise to the unprecedented figure of over $44 billion.

The current expansion in construction has been centered on production capacities, distribution outlets and service facilities. Information on the amount of contracts awarded[1] by projects provides an insight into the type of construction put in place in this district.

Educational facilities are being expanded at a rapid pace. Of the amount of contracts awarded for nonresidential construction in the first 11 months of this year, 18 percent was for educational buildings. The construction in this field reflects the pressing need for additional classrooms in elementary, secondary and higher education. The contracts awarded totaled 10 percent more than in the comparable period of 1955, although some expansion programs were held off due to the rise in interest rates.

Commercial building comprised 12 percent of the total according to value of contracts awarded. In this district, as in other areas of the nation, distribution is not only expanding but is undergoing a structural change. In the food industry supermarkets are replacing small grocery stores. Shopping centers are replacing some of the small neighborhood retail outlets in every line of merchandise. This structural change has been reflected in the rise in business failures and involuntary liquidations of some of these small proprietorships, although the number of small business firms, in the aggregate, has increased.

Industrial building in this district in 1956 was not as strong as in the more industrialized areas. Except for one taconite plant, the large, low-grade iron-ore and copper beneficiating plants under construction in recent years have been completed. For instance, in the first 11 months of the year, only 5 percent of the nonresidential building contract awards were issued for this type of building, whereas in the same period of 1955 the proportion was 9 percent.

More funds were invested in social, hospital, religious, public and miscellaneous buildings in 1956 than in the former year. Buildings in these categories comprised 22 percent of the total awards, a larger percentage than in 1955.

In addition to all the nonresidential building categories listed above, an impressive volume of contracts were awarded for public works, which include highways, streets, bridges, municipal sewerage systems, and dams and reservoirs. The amount of such contracts awarded in the first 11 months of 1956 was nearly 33 percent of the total issued in the nonresidential building.

Public utilities increased their expansion programs in 1956. The amount of contracts awarded in the first 11 months aggregated 35 percent more than in the comparable period of 1955 and account for almost a tenth of nonresidential construction contracts.

During the course of the year, supplies of building materials became less tight and, in general, are now ample.

The volume of construction undertaken, and the emphasis on heavy construction, however, placed a strain on the production capacities for some building materials. In both structural steel and cement, shortages developed periodically, even though producers had increased their capacities. The output of paints, clay and gypsum products has been larger than in 1955. On the other hand, the output of lumber and millwork declined noticeably during the year, which reflects the cutback in residential building. In the western part of the district, saw and planing mill operators have reduced their crews because of high lumber stocks.

Contractors also drew heavily on available manpower when employment already was at a high level. In all district states, with the exception of Upper Michigan, construction undertaken provided an opportunity for more employment. For the first 10 months of the year, the monthly average number of workers employed was 2000 above the same period in 1955.

As was anticipated in economic forecasts at the beginning of 1956, this was an 'off year' for homebuilding. New housing starts in 1956 as a whole, however, compare favorably with any other year except the extraordinary ones of 1950 and 1955.

In the Ninth district home building was cut back by one-fifth from a year ago. In the first 11 months of 1956 the number of new housekeeping units authorized by build-

[1] The F. W. Dodge Corporation figures do not include Montana in this district.

ing permits was down 18 percent from the same period of a year ago. When the number of demolitions and conversions of units is taken into account, the net addition made to the stock of housing was 20 percent less than in 1955.

Rising construction costs in 1956, reflected in higher prices, were a factor in the smaller market for low-priced houses. In the annual survey made on prices of houses in the Minneapolis metropolitan area[2] it was observed that the prices of new houses in the low-priced bracket (below $14,000) rose faster than on old houses. In the latter half of 1954 the average price was $11,700, and in the first half of 1956, $12,600, an increase of $900 in one and one-half years. In this district, the average valuation on contracts awarded for one family dwellings in the first 11 months was $1,200 above the average for the comparable 1955 period. The pronounced rise in average price and contract valuation, in part, reflects the trend toward larger houses.

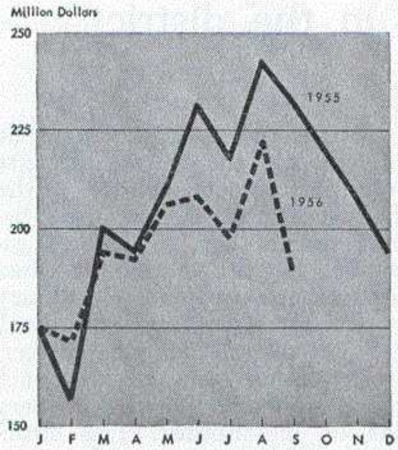
More important than the rise in construction costs in reducing the effective demand for new houses have been the lessened availability of mortgage funds on the liberal terms offered earlier and the rise in interest rates. A tightening in mortgage credit grew largely out of a rapidly growing demand for long-term funds in the business and municipal government sectors of the economy.

The market for new houses has become noticeably saturated in only a few isolated communities. The number of vacant units increased in 1956, but most of the increase apparently occurred in the 'for rent' group. Despite this national trend, vacant dwelling units available for rent or sale in the third quarter were only 2.8 percent of total year-round dwelling units according to the results of a survey conducted by the United States Bureau of the Census.

The new increase in mortgage debt outstanding in the first nine

AMOUNT OF NINTH DISTRICT NONFARM MORTGAGES

$20,000 or less—January 1955-September 1956



months was $11.4 billion. This amount compares with an increase of $12.5 billion in the same period of 1955 and, to some extent, reflects a larger volume of repayments in 1956. Despite larger down payments required and shorter maturities on loans, it is quite clear that the amount of new loans made in 1956 will be the second largest on record – only about 5 percent below the 1955 all-time high.

The increase in mortagage debt on multi-family and commercial structures has been larger in 1956 than last year. In the first nine months the debt increased by $2.3 billion as compared with $2.1 billion in the comparable period in 1955.

The decline that has occurred has been concentrated in financing single family units. Even in this segment of the mortgage market, lending has held up better than anticipated. Mortgage debt outstanding on 1- to 4-family houses rose by $8.5 billion in the first nine months as compared with a $9.8 billion rise in the same period of last year. On the basis of these figures, nationally the increase in the mortgage debt on 1- to 4-family houses was 13 percent less than in 1955.

In the Ninth district, credit extended on mortgage loans has declined only slightly more than nationally. The number of nonfarm mortgages of $20,000 or less recorded was down 9 percent in the first nine months from the same period in 1955, while nationally it was down 8 percent. The amount of credit extended on these mortgages in the district was down about 6 percent and in the nation, 4.5 percent. By and large, local financial institutions have continued to serve the real estate credit needs of their own customers, but many mortgage brokers have lost their outlets for mortgage loans, and others have been limited in the number they can accept for their correspondents.

With the maximum rate of interest on VA-guaranteed loans and on FHA-insured loans held at 4½ percent,[3] lenders have shifted to conventional loans where the rate is set by market forces. A decrease of about 22 percent occurred in the number of VA-guaranteed loans closed in the four states wholly in this district in the first nine months of 1956 as compared with the same period last year. The amount of credit granted on these loans was down *less*, 18 percent, which indicates that larger loans were closed. In Montana and Minnesota, where data are available on FHA-insured loans, the number closed was down over 20 percent and the amount of credit granted was down somewhat less. On the other hand, the number of conventional loans closed and the amount of credit granted on them rose sharply.

In this district home building declined to a low ebb in the fourth quarter. In the large cities relatively few houses were roughed in during the fall to be finished during the winter. Furthermore, the inventory of unsold new houses was down as compared with the number on the market a year ago. This information leads to the conclusion that a relatively small number of new houses will be offered for sale this winter and early next spring.

END

[2] The results of the survey were published in the August issue.

[3] On December 4, 1956, a maximum rate of 5 percent became effective on F.H.A. loans.

Special Supplements Issued during 1956

PULP AND PAPER IN THE UPPER LAKES REGION
July 1956, 32 pages

HOUSING AND MORTGAGE MARKETS
September 1956, 32 pages

These publications are available free upon request from the Research Department, Federal Reserve Bank of Minneapolis, Minneapolis 2, Minnesota.

Index for the Year 1956

Each month's Current Events section has been introduced with a discussion which gives a composite picture of the Ninth district economic outlook. Since the summary of the month discusses that month's current situation, reported in the topics, these summaries have not been indexed. The entries below indicate for each article the month of issue and the page on which it appeared. For example, Ja: 2 refers to the January issue, page 2. Capital letters in titles denote feature articles.

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