Growth of S & L associations slackens as savers redirect funds

The currently depressed condition of the housing sector within the context of a relatively healthy economy has been a source of widespread concern. The extent of the recent slowdown in the construction industry, of which residential building represents an integral part, has been graphically documented in a previous article in the *Monthly Review*.[1]

For the most part, the blame for the sharp drop in home building has been placed not so much on a reduction in the demand for housing services as on an increase in interest rates on home mortgage loans — an increase in discounts which home owners must absorb — and, in particular, on a contraction in the availability of credit. The average secondary market yield on FHA insured mortgages on new homes rose from 5.46 per cent in September 1965 to 6.63 per cent in September of the current year. The rise in interest rates on conventional mortgage loans during this interval, while not as pronounced, was still substantial when viewed against the trend of recent years.

At the same time credit has become scarcer. One reason for this is that savings and loan associations and savings banks — institutions whose investment portfolios consist primarily of home mortgage loans — have seen their rate of deposit inflow slip badly in the last two years, victim of the increasingly attractive yields available at commercial banks and in open market securities. In addition, commercial banks and life insurance companies, which also participate in home mortgage financing, but are primarily oriented toward the business community, have had to meet the increased demands for credit emanating from that sector; and in the most recent period their total resources available to meet these demands have also been under pressure.

Among the suppliers of credit to home builders and home buyers, savings and loan associations are by far the largest. At the end of 1965 they held 44 per cent of the outstanding mortgage loans on one-to-four family nonfarm homes. Commercial banks, savings banks, and life insurance companies, as a group, held 43 per cent, but none held as much as 15 per cent.[2]

Growth in the United States

Savings and loan associations (S&Ls) in the United States have undergone a rapid and relatively steady growth since the end of World War II. They have doubled total assets on the average of nearly once every five years, growing from a $9 billion industry in 1945 to one of $129 billion at the end of 1965 (Table 1). During this same 20-year span, savings accounts rose from $7 billion to $110 billion, an increase essentially matched by mortgage loans.

TABLE 1 — TOTAL ASSETS, SAVINGS AND LOAN ASSOCIATIONS, UNITED STATES

End of Year	Amount ($ billions)	5-year Increase (Per cent)
1945	8.7	
1950	16.9	94
1955	37.7	123
1960	71.5	90
1965	129.4	81

Source: U.S. Savings and Loan League, **Fact Book.**

Since 1965, however, a noticeable slowdown in growth has taken place. The net addition to savings accounts during 1965 was 20 per cent below that recorded in the preceding year (Table 2). In

[1] "Construction industry reacts to restrictive monetary policy," **Monthly Review**, Federal Reserve Bank of Minneapolis, October 1966.

[2] U.S. Savings and Loan League, **Savings and Loan Fact Book**, 1966, p. 33.

TABLE 2 — INCREASE IN NET SAVINGS AND MORTGAGE LOANS MADE, SAVINGS AND LOAN ASSOCIATIONS, UNITED STATES
(billions of dollars)

	1964	1965	1966
Net Savings			
Year	10.6	8.4	
Jan.-Sept.	7.2	5.3	1.4
Mortgage Loans Made			
Year	24.5	23.8	
Jan.-Sept.	18.7	18.1	14.0

Source: Federal Home Loan Bank Board.

the first nine months of 1966, moreover, the increase in net savings was only one-fourth as large as that recorded during the comparable period in 1965. Mortgage loans made (which differ from changes in mortgage loans outstanding by the amount of loan repayments and sales) also showed a smaller rise in 1965, but the drop was not quite as sharp as that of net savings. The decline from 1964 was only on the order of 3 per cent. During the first three quarters of 1966 the pace of mortgage loans made was about 25 per cent under that of the similar period in 1965.

Ninth district growth

The growth of S&Ls in the Ninth Federal Reserve district has closely paralleled the vigorous expansion of S&Ls throughout the nation (Table 3). Between 1950 and 1955 total assets increased by $550 million, a rise of 116 per cent compared to a 123 per cent advance at all S&Ls in the United States. A slightly slower but still robust 87 per cent rise occurred between 1955 and 1960,

TABLE 3 — TOTAL ASSETS, SAVINGS AND LOAN ASSOCIATIONS, NINTH DISTRICT[1]

End of Year	Amount ($ millions)	5-year Increase (Per cent)
1950	477	
1955	1030	116
1960	1929	87
1965	3160 (est.)	64

[1] Excludes Michigan and Wisconsin

Sources: U.S. Savings and Loan League, Annals; statistical reports of Federal Home Loan district banks.

representing a dollar advance of $900 million. This was not essentially different from the 90 per cent rise scored by all S&Ls during this same 5-year span. A much sharper contraction in the growth rate of total assets at the district level occurred between 1960 and 1965. While the rise in total assets at all S&Ls slipped to 81 per cent during this period, the increase at district S&Ls dropped to 64 per cent.

Growth in district states

An examination of the record of growth in total assets for the 10-year period between 1955 and 1965 at S&Ls in the four states which are situated within the Ninth Federal Reserve district indicates that North Dakota and South Dakota posted much higher growth rates than did the district as a whole (Table 4). Montana and Minnesota in most comparisons trailed the district growth rate. In every state, however, the growth rate slackened in the second half of this 10-year period.

South Dakota recorded the strongest advance between 1955 and 1965, a 343 per cent increase and an expansion of more than four-fold. In North Dakota total assets of S&Ls more than tripled during the 10-year span. S&L growth in Minnesota closely followed the district pattern, not surprising since the state accounts for 80 per cent of the combined total assets. Montana followed closely behind Minnesota.

Comparison to district commercial banks

Ninth district S&Ls grew much faster than did district commercial banks during the decade 1955-65 (Table 4). While S&Ls in the four states were more than tripling total assets, commercial banks fell short of doubling their size. This observation with respect to the district was generally true in each of the four states. It can also be seen, however, that in each of the four states commercial banks grew faster in the second 5-year period than in the first — exactly the reverse of the S&L experience.

TABLE 4 — GROWTH IN TOTAL ASSETS, SAVINGS AND LOAN ASSOCIATIONS AND COMMERCIAL BANKS, NINTH DISTRICT

	End of Year Balances ($ millions)			Percentage increase		
	1955	1960	1965	1956-60	1961-65	1956-65
District (4 States)						
S&Ls	1030	1929	3160e	87	64	207
Banks	5843	7204	10325	23	43	77
Minnesota						
S&Ls	822	1520	2434e	85	60	196
Banks	3787	4636	6752	22	46	78
Montana						
S&Ls	72	128	211e	78	65	193
Banks	747	907	1233	21	36	65
North Dakota						
S&Ls	99	198	351e	100	77	255
Banks	671	839	1176	25	40	75
South Dakota						
S&Ls	37	83	164e	124	98	343
Banks	638	822	1164	29	42	82

e = Estimate

Sources: U.S. Savings and Loan League, **Annals**; statistical reports of Federal Home Loan district banks; Federal Deposit Insurance Corporation, **Assets and Liabilities of Operating Banks.**

A clearer picture of the relative strength of district S&Ls is presented in Table 5 which shows the percentage of total assets of S&Ls to the combined total assets of S&Ls and commercial banks. S&Ls in the 4-state area increased their share in the combined total assets of commercial banks and S&Ls from less than 15 per cent at the end of 1955 to over 23 per cent ten years later. The rate at which this ratio increased, however, declined between the first half and the second half of the decade, reflecting the combination of a slowdown in S&L growth and a speeding up in commercial bank expansion.

The relative growth of district S&Ls vis-à-vis their commercial banking competitors during 1955-65 obscures underlying trends. Time deposits (including passbook savings accounts) of commercial banks grew much faster than did net savings at S&Ls during 1955-65. In part this probably reflected a narrowing differential in yields available at the two institutions. Interest rates paid on time and savings deposits at commercial banks in the U. S. (district data are not available) after a long period of lethargy started a sharp upward climb in 1957, seven years after yields on savings at S&Ls had started their gradual rise. The interest rate differential narrowed from 1.4 per cent in 1956 to less than 0.5 per cent in 1965. Periodic raises of interest rate ceilings by banking regulatory bodies have, no doubt, helped speed the decline in rate differential. That commercial banks did not grow faster than S&Ls during this period given the more rapid growth in time deposits reflects the fact that part of the gain in time deposits was at the expense of growth in demand deposits.

TABLE 5 — TOTAL ASSETS AT SAVINGS AND LOAN ASSOCIATIONS AS A PER CENT OF TOTAL ASSETS AT SAVINGS AND LOAN ASSOCIATIONS AND COMMERCIAL BANKS, NINTH DISTRICT

	Per Cent, End of Year		
	1955	1960	1965
Minnesota	17.8	24.7	26.5
Montana	8.8	12.4	14.6
North Dakota	12.8	19.1	23.0
South Dakota	5.5	9.2	12.3
Total District	14.9	21.1	23.4

Recent slowdown

Mirroring the record of S&Ls in the nation, district S&Ls since 1965 have experienced a sharp cutback in the inflow of net savings and this has been accompanied, although to a lesser degree, by a contraction in mortgage loans made.

During 1965, the increase in net savings fell to $164 million from $206 million in 1964 (Table 6), a drop of 20 per cent. The rate of inflow has declined even further in 1966. From January to September net savings inflow totaled $73 million, down 33 per cent from that recorded in the comparable period of 1965. On the other hand, time deposit inflow at district member banks was up 10 per cent in 1965 over the year before, and during the first three quarters of 1966 inflow was up 15 per cent over the similar period in 1965.

Mortgage loans made have undergone a much more gradual decline. During 1965 they totaled $536 million, down 7 per cent from 1964. They have eased another 6 per cent in the first three quarters of 1966 from that of the January-September period the year before.

Factors in savings slowdown

Why has the rate of savings at S&Ls declined in the past two years and where have savings gone? The second part of this question is somewhat easier to answer than the first, although some factors already mentioned may help clarify the reasons for decline.

First of all, there has been a redirection of individual savings flow toward commercial banks and away from savings institutions of which S&Ls are the most prominent. As Table 7 shows, in 1964 savings inflow at savings institutions was nearly double that at commercial banks. This advantage diminished in 1965 to the point where net savings inflow at both institutions was about equal. Savings institutions have continued to lose ground in their battle for savings during 1966. During the first half of this year the net inflow of savings at savings institutions was only 70 per cent as large as net savings inflow at commercial banks. A further look at the table, however, suggests that

TABLE 6 — INCREASE IN NET SAVINGS AND MORTGAGE LOANS MADE, SAVINGS AND LOAN ASSOCIATIONS, NINTH DISTRICT

(millions of dollars)

	1964	1965	1966
Net Savings			
Year	206	164	
Jan.-Sept.	145	109	73
Mortgage Loans Made			
Year	578	536	
Jan.-Sept.	427	384	360

Note: Figures are for S&Ls that are members of the Federal Home Loan Bank System. Member associations in the Ninth district account for 99 per cent of total assets of all associations.

Source: Statistical reports of Federal Home Loan district banks.

the increased share of savings at commercial banks during the first six months of 1966 was gained at the expense of demand deposits. Consequently the increase in total deposits at commercial banks was not materially different from that of savings institutions.

The contraction in the yield advantage of savings deposits at S&Ls over time and savings deposits at commercial banks has been cited as a factor in the relative decline of savings at S&Ls. Between 1964 and 1965 the average differential in favor of S&Ls narrowed from 0.71 to 0.47 per cent. While yields on both types of deposits rose during 1965, the increase in S&L savings deposit yield was quite small. This stems in part from the nature of S&L asset portfolios. The average rate of return on the mortgage portfolio of a savings institution cannot rise rapidly because the average life of a home mortgage loan, which ordinarily carries a fixed rate of interest, is relatively long. Consequently, S&Ls, in the short run, are limited in the size of the increase in yields they are able to offer on savings accounts if they do not wish to impair their reserve and surplus positions.

Loans made by commercial banks, on the other hand, ordinarily carry relatively shorter maturities and thus the rates on loans can be adjusted more rapidly. In addition, the vigorous demand for loans which has existed in the last two years has supported a substantial increase in loan rates and the gross rate of return of earning assets. On the

TABLE 7 — NET ACQUISITION OF FINANCIAL ASSETS BY HOUSEHOLDS, UNITED STATES
(billions of dollars: seasonally adjusted at annual rates)

	1964		1965		1966[1]	
	Amount	Per cent of total	Amount	Per cent of total	Amount	Per cent of total
Net acquisition of financial assets	$47.6	100.0	$51.6	100.0	$46.0	100.0
Demand deposits and currency	6.7	14.1	7.2	14.0	—3.8	—8.3
Savings accounts	23.9	50.2	26.4	51.2	16.8	36.5
Commercial banks	8.2	17.2	13.3	25.8	10.0	21.7
Savings institutions	15.8	33.2	13.1	25.4	6.8	14.8
Insurance and pension reserves	15.5	32.6	15.7	30.4	16.3	35.4
Credit market instruments	3.3	6.9	2.7	5.2	17.0	37.0
Net investment in noncorporate business	—2.9	—6.1	—1.9	—3.7	—2.2	—4.8
Net acquisition of financial assets as a per cent of disposable personal income		10.9		11.0		9.2

[1]Average of first and second quarters.
Source: **Federal Reserve Bulletin**, October 1966, p. 1529.

other side of the balance sheet, the barrier to further increases in interest rates payable on bank time deposits, Regulation Q, has been increased twice since the third quarter of 1964, allowing a larger increase in yields than would have been possible otherwise.

Secondly, there has occurred a redirection of household savings flow away from savings institutions toward credit market instruments (e.g., U. S. Government securities, corporate stocks and bonds, local and state government obligations). This relative change has been substantially a 1966 phenomenon. Between 1964 and 1965 the share of net financial asset acquisition represented by net increases in savings accounts at savings institutions and in credit market instruments owned by individuals declined in about the same proportion. During the first two quarters of 1966, however, credit market instruments increased their share of net financial assets acquired by individuals to 37 per cent from 5 per cent in 1965. During this same period savings institutions saw their share diminish from 25 per cent to 15 per cent. It should also be noted, however, that the increase in acquisitions of credit market instruments was partly at the expense of commercial bank savings accounts. The share of net financial assets acquired represented by bank savings accounts during the first half of 1966 declined to 22 per cent from 26 per cent in 1965.

The movements of yield differentials in favor of credit market instruments appear to have had an impact on the relative decline in savings accounts. Substantial increases in yield did occur on a broad spectrum of open market securities between November 1965 and June 1966. During this period 3-month Treasury bills rose from 4.08 to 4.50 per cent; 4- to 6-month prime commercial paper from 4.38 to 5.51 per cent; 9- to 12-month U.S. Government securities from 4.29 to 4.94 per cent. Although the increase in yields on savings accounts is not available for this period, it is quite likely that it was much smaller.

The rate of saving inflow at S&Ls might also be expected to fall with a decline in the share of income individuals desire to save for the purpose of acquiring financial assets. This share, expressed as the percentage of net acquisition of financial assets to disposable personal income (income after taxes, but before spending for consumption goods and services and spending on durable goods), amounted to 10.9 per cent in 1964. It remained about the same in 1965, but slipped to 9.2 per cent in the first half of 1966.

—STANLEY L. GRAHAM

Current conditions . . .

Economic indicators for the beginning of the fourth quarter characterize business activity in the Ninth district as strong, but lacking some of the ebullience of the year's earlier months. Cash flows into the district farm sector continued at record high levels, but with prices at lower levels. Total construction contracts awarded were up, but the residential component continued a sharp downtrend.

On a seasonally adjusted basis district wage and salary employment indicators in the early part of the fourth quarter were little changed from late third-quarter levels. Industrial output, as measured by the district indices of industrial use of electric power and production worker man-hours, also remained at an essentially static but high level.

The district in general and Minnesota in particular have benefited from the receipt of prime contracts issued by the U.S. Department of Defense. During the first half of the year Minnesota was one of the few states of the nation where dollar value of prime contract receipts was about 50 per cent above that of 1965.

During October total construction contracts were about 5 per cent above the year-earlier level. This increase represented a drop over the first nine months of the year of 9 per cent in residential building contracts let and an increase of about 23 per cent in nonresidential and nonbuilding contracts.

The housing construction slowdown has not had a very severe impact on the lumber and timber products industry in Montana — at least through the month of October. During that month employment in the lumber industry was about 7 per cent above the year-earlier level.

The most recent *Business Week* estimates of personal income (first eight months of the year) indicate that the district's rate of growth was somewhat above the national average of 8.2 per cent. Although Montana's rate was slightly below the national average, North Dakota, South Dakota, and Minnesota all experienced above-average personal income growth. The faster income growth rate resulted in a slightly higher rate of growth in retail sales within the district relative to the nation.

In November total credit at so-called "city" banks fell $26 million, in sharp contrast to the $7 million average rise that has occurred in recent years during this month and the $30 million rise during November 1965. Investments followed the seasonal pattern; but loans dropped $25 million. Loans to nonbank financial institutions plunged $20 million; "all other" loans, $10 million, both far below their normal pattern. Business loans increased a seasonal $4 million.

Daily average deposit inflow at district banks during November was about 20 per cent below that of the average inflow for comparable months in the preceding five years, the entire slowdown occurring at country banks.

The decline in outstanding loans at city banks served to dampen the loan-to-deposit ratio for these banks: it fell to 63.3 per cent at the end of November, its lowest level since January.

The following selected topics describe particular aspects of the district's current economic scene:

Bank debits continue higher

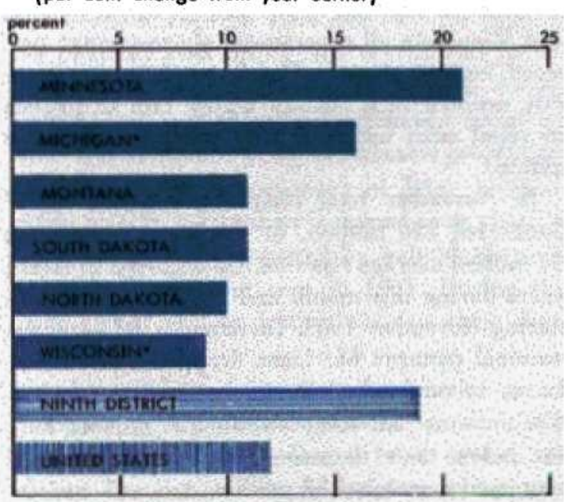
Over the first ten months of 1966, Ninth district bank debits — the amount of checks drawn on banks — have consistently registered higher levels than in 1965. The volume of bank debits reported by the total sample of Ninth Federal Reserve district cities was 18 per cent above the comparable 1965 period.

For Minnesota the volume of bank debits for reporting cities for the first ten months increased 21 per cent from the same period in 1965. Registering substantial increases were Minneapolis and adjoining cities to the north, west, and south; and several cities on the Mesabi Iron range including Hibbing, Virginia, Hoyt Lakes, and Eveleth.

Bank debit volume in Upper Michigan increased 16 per cent during the January-October period. The principal push came from such reporting cities as Marquette, Escanaba, and Ishpeming.

Bank debits as reported by the Federal Reserve System for the most part are checks against depositors' accounts and thus represent payments for goods, services, and debts. They also include transfers of funds which of themselves have no business significance. Bank debits mainly include all debits against checking accounts of individuals, partnerships and corporations, and of states and political subdivisions. They do not include debits to the accounts of other banks, to the United States government, or to savings accounts.

Bank debits for first 10 months of 1966
(per cent change from year earlier)



*Includes only ninth district portion of state

Iron ore shipments ahead of 1965

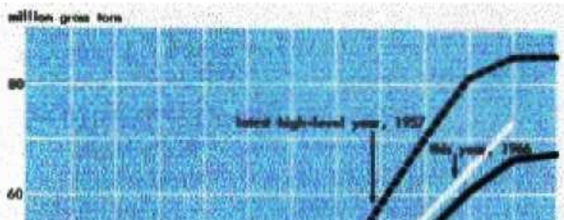
Great Lakes shipments of iron ore from U.S. and Canadian ports during November totaled about 5.9 million gross tons, according to the monthly report of the American Iron Ore association. The November shipments brought total shipments to more than 70 million tons for the 1966 season, an increase of 4 million gross tons over the first 11 months of 1965.

Tonnage shipped from U.S. ports increased generally over those of the previous year with Taconite Harbor, Minnesota, showing a substantial increase.

The 11-month cumulative total is the highest since 1960 when more than 69 million tons of ore were hauled out of Great Lakes ports to make up for tonnage lost in the 1959 steel strike.

The heavy shipments run slightly counter to steel mill production records for the year. Output at U.S. steel mills has been running behind that of last year; but in early November, for the first time this year, the output record raced ahead of 1965's pace.

Cumulative iron ore shipments



Source: American Iron Ore Association

With ore shipments running higher and mill output running lower, ore stockpiles at mills are up. Total inventories at iron and steel plants at the close of September amounted to 57.5 million tons, up 2.2 million tons over that of the year earlier. The inventory consisted of almost 34 million tons of U. S. Great Lakes ores, 2.5 million tons of other U. S. ores, 1.5 million tons of ore from Canadian Great Lakes sources, and 9.6 million tons of foreign ores.

Recent sales reports from the automobile industry indicate a national sales dropoff of about 5 per cent (summer and fall of 1966 as compared to the same periods 1965). One major company, General Motors, noted the market softening when it announced "schedule changes" for 11 of its 23 assembly plants during December and January.

But although some nervousness as to market potential has cropped up in the steel industry because of setbacks in buying for automobile manufacture, many mills report the receipt of substantial orders from other industrial segments. Over-all strength of the economy, particularly in the steel consuming industries, thus seems to indicate a strong continuing demand for steel at least into the early part of 1967.

Of 249 blast furnaces available in the U.S. and Canada, 194 were operating the last day of September. This compares with 166 in operation at the close of September 1965 out of 251 available.

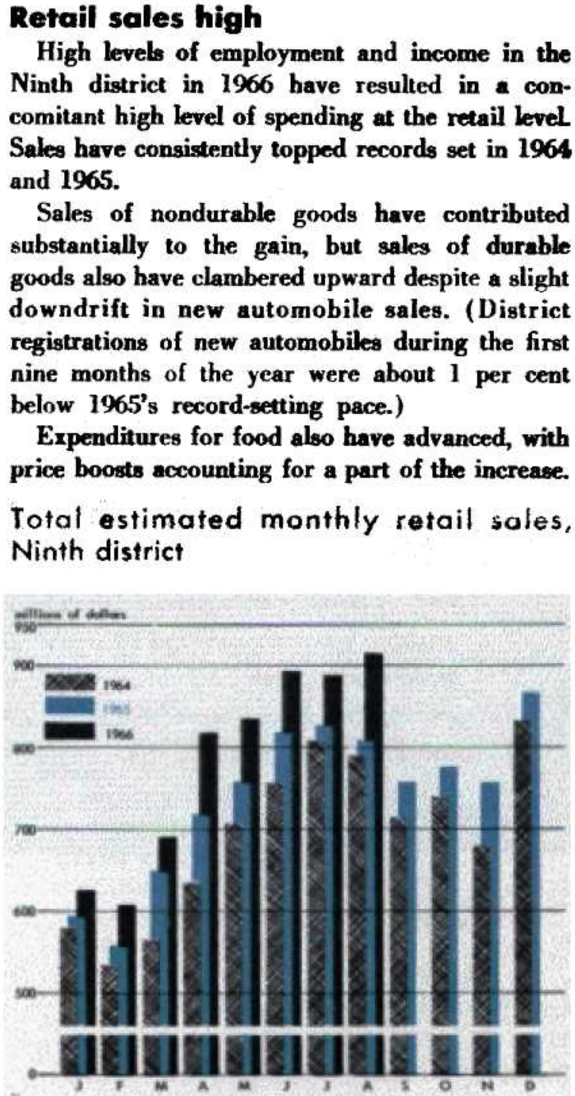
Retail sales high

High levels of employment and income in the Ninth district in 1966 have resulted in a concomitant high level of spending at the retail level. Sales have consistently topped records set in 1964 and 1965.

Sales of nondurable goods have contributed substantially to the gain, but sales of durable goods also have clambered upward despite a slight downdrift in new automobile sales. (District registrations of new automobiles during the first nine months of the year were about 1 per cent below 1965's record-setting pace.)

Expenditures for food also have advanced, with price boosts accounting for a part of the increase.

Total estimated monthly retail sales, Ninth district



Source: "Estimated Monthly Retail Sales for All Stores by Federal Reserve Districts" Board of Governors of the Federal Reserve System.

Notice to readers:

Effective with this issue, publication of the **Monthly Review** of the Federal Reserve Bank of Minneapolis will be discontinued. This change is part of a program aimed at developing a more flexible and timely system of special purpose publications.

Beginning in January 1967, current Ninth district statistical data plus a brief narrative summary of Ninth district economic conditions will be issued monthly in a newly designed release to be called **Ninth District Conditions.** Results of longer term studies completed by the Bank's research staff will be published in occasional special reports by the Bank or in other media. Notices of studies as and when published will appear in **Ninth District Conditions** and notices will also be sent to a supplementary mailing list to be maintained for the purpose. The annual operating statement of the Federal Reserve Bank of Minneapolis formerly carried in the January **Monthly Review** will be issued as a separate release for those interested. All current subscribers to the **Monthly Review** have been notified of the change in publication policy through a special mailing, and have been asked to indicate by return postcard their mailing list preferences for future releases.

Index for the Year 1966

Economic Briefs

1. Call due for huge Montana dam

A bid call for the prime contract on Libby dam on the Kootenai river in northwestern Montana is due this winter. The 440-ft. high, concrete gravity dam will cost about $350 million. Its 90-mi. reservoir will extend 42 miles into Canada. Already underway is construction of a 7-mi., $50 million railroad tunnel to carry Great Northern tracks west from Whitefish, Montana. The present roadbed will be flooded by reservoir water.

2. Important oil discovery

Texaco, Inc., has brought in an important wildcat well in southeastern Stark county in North Dakota. Oil flow is up to 47 barrels per hour from Red River Ordovician formation. The well's location is 25 miles from any other oil production.

3. Refinery to boost premium production

A $3 million expansion program has been announced by Northwestern Refining Company, St. Paul Park, Minnesota. The primary unit in the construction plan will be a catalytic reformer to convert refinery naphtha into premium grade gasoline through use of a platinum catalyst. According to company officials, the reforming unit is made necessary by increased demand for high octane gasoline resulting from the greater use of high-compression automobile engines.

4. Trane expansion scheduled

Construction on the first unit of a planned $6 million administration and office building of the Trane Company, LaCrosse, Wisconsin, is scheduled to start early in 1967. Primarily an air conditioning and heating equipment manufacturer, Trane is LaCrosse's major industry.