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CONFIDENTIAL (FR)

SUPPLEMENT

CURRENT ECONOMIC AND FINANCIAL CONDITIONS

Prepared for the
Federal Open Market Committee

By the Staff
Board of Governors
of the Federal Reserve System

July 12, 1974

SUPPLEMENTAL NOTES

The Domestic Economy

Retail sales. Retail sales in June were down .7 percent from May, according to the Census advance report, with all important groupings of stores--except gasoline stations--reporting lower purchases. Outlays for durable goods exhibited the greatest weakness, with sales of the automotive group down 2.1 percent, and furniture and appliance sales off 1.1 percent. Sales of nondurable goods were .3 percent lower than in May.

Average sales in the second quarter were 2.5 percent above the first quarter and, at best, this probably meant a slight increase in real terms. In current dollars, a 4.5 percent recovery in the automotive group was significant, following two successive quarters of lower sales. Total sales less autos and nonconsumer items were up 2.3 percent in the quarter.

RETAIL SALES
(Seasonally adjusted, percentage change from previous quarter)

	1973	1974				
	Q IV	Q I	Q II	April	May	June
Total sales	.3	1.5	2.5	.9	.7	-.7
Durable	-3.4	-2.8	3.9	2.1	1.8	-1.5
Auto	-6.6	-8.1	4.5	3.3	2.3	-2.1
Furniture & appliance	-1.0	4.2	4.2	-1.3	1.8	-1.1
Nondurable	2.2	3.5	1.9	.4	.3	-.3
Food	1.9	4.3	1.2	1.0	.6	-.4
General merchandise	1.2	3.8	1.8	-1.4	1.1	-.7
Gasoline	2.3	3.9	8.1	2.6	2.4	1.3
Total, less auto and nonconsumption items	2.0	3.6	2.3	.5	.4	-.3
GAF	.7	3.8	1.6	-2.3	1.6	-.8
Real*	-2.0	-2.1	n.a.	.4	-.4	n.a.

*Deflated by all commodities CPI, seasonally adjusted.

Industrial production. Industrial production was estimated to be unchanged in June and at 125.5 percent of the 1967 average was virtually the same as the 125.6 percent of a year earlier. Declines in output of consumer goods and business equipment were offset by increases in production of intermediate products and industrial materials. On the basis of preliminary data, the second quarter average was .3 percent above the first quarter level.

Auto assemblies in June were at an annual rate of 7.7 percent, the same as in May. Auto production schedules for the third quarter have been revised upwards to an 8.7 million unit rate, reflecting a decision to produce a larger number of 1974 models in July.

Output of household appliances continued strong but production of other durable consumer goods declined, as did output of nondurable consumer goods reflecting, in part, a strike in the men's clothing industry. Production of business equipment declined about nearly one percent in June but it was still 4-1/2 percent above a year earlier. Output of intermediate products rose further.

Production of durable goods materials rose as output of steel and consumer durable materials increased. Production of nondurable goods materials was unchanged as was output of the textile, paper, and chemical group. (Confidential until release June 16, afternoon.)

INDUSTRIAL PRODUCTION
(1967=100, seasonally adjusted)

	1973	1974			Percent change from	
	June	April	pMay	eJune	Month ago	A year ago
Total index	125.6	124.9	125.5	125.5	0	- .1
Consumer goods	131.9	128.7	129.5	128.7	- .6	-2.4
Business equip.	122.5	128.3	129.1	128.0	- .9	4.5
Defense equip.	80.1	80.6	81.7	81.4	- .4	1.6
Materials	129.0	128.5	129.0	129.4	.3	.3
steel	119.9	116.4	117.5	118.3	.7	-1.3
Autos*	10.2	7.5	7.7	7.7	0	-24.5

*Seasonally adjusted annual rate, millions of units.

Note: For release Tuesday, July 16, 1974.

Real estate. Merchant builder sales of new single-family homes rose in May to the highest rate in almost a year, but were still well below the peak in October 1972. Even at the higher sales rate, however, the stock of unsold homes equaled nearly 9 months' supply. While the median price of new units sold showed little change, it continued above the rising median price of unsold homes. Sales of used homes in May were above a year earlier, although by a smaller margin than in April. The median price of such units increased to \$32,130, almost 12 percent above May 1973.

SALES, STOCKS AND PRICES OF NEW SINGLE FAMILY HOMES

	Homes sold <u>1/</u>	Homes for sale <u>2/</u>	Months' Supply	Median price of:	
	(thousands of units)			Homes sold	Homes for sale
				(thousands of dollars)	
<u>1973</u>					
QI	726	426	7.0	30.4	29.4
QII	680	436	7.7	32.7	31.2
QIII	566	453	9.6	33.5	32.1
QIV	483	446	11.1	34.0	32.9
<u>1974</u>					
QI(r)	527	453	10.3	35.0	34.0
January	474	450	11.4	34.2	33.4
February(r)	516	459	10.7	34.9	33.5
March	590	453	9.2	36.0	34.0
April(r)	582	449	9.3	35.7	34.3
May(p)	601	440	8.7	35.8	34.7

1/ Seasonally adjusted annual rate.

2/ Seasonally adjusted, end of period.

Wholesale prices. The wholesale price index rose between May and June by 0.5 percent, seasonally adjusted (not at an annual rate), to a level 14-1/2 percent above a year earlier. The increase reflected another sharp rise in the index of industrial commodities and a further decline in the index of farm products and foods.

The index of industrial commodities increased 2.2 percent, seasonally adjusted, to a level 22 percent above the year-earlier level. Increases were widespread and large with those for metals and metal products, fuels and power, machinery and equipment, and chemicals especially important. This was the sixth consecutive monthly increase of 2 percent or more.

The index of farm products and foods declined, for the fourth consecutive month, by 4 percent, seasonally adjusted. Lower prices for livestock, meats, fluid milk, and fresh vegetables accounted for most of the decline. This index for June was slightly (1.2 percent) below a year ago.

WHOLESALE PRICES
(Percent changes at seasonally adjusted compound annual rates)^{1/}

	June 1973 to June 1974	Dec. 1972 to June 1973	June 1973 to Dec. 1973	Dec. 1973 to Mar. 1974	Mar. 1974 to June 1974	May 1974 to June 1974
All commodities	14.5	20.2	10.9	24.5	12.2	5.7
Farm products	- 1.2	45.8	10.4	10.8	-29.3	-47.6
Industrial commodities	21.9	10.6	10.9	32.3	35.7	26.9
Crude materials	42.3	23.0	40.4	88.7	10.4	14.0
Intermediate materials	24.1	12.2	11.7	32.6	43.7	28.5
Finished goods	15.5	6.3	7.1	23.1	25.9	25.0
Producer	12.4	5.4	5.3	13.2	27.2	25.6
Consumer	17.1	6.7	8.1	28.3	25.3	24.8
Nondurable, excl. foods	22.9	8.5	11.3	40.4	30.9	26.6
Durable	7.9	4.5	2.8	11.3	15.0	13.6
Consumer finished foods	8.3	27.0	18.5	17.3	-16.7	-45.0

Note: Farm products include farm products and processed foods and feeds.

^{1/} Not compounded for one-month changes.

Capacity utilization. In the second quarter, overall major materials utilization remained essentially unchanged from the first quarter. This apparent stability masks a significant upswing in petroleum refining utilization offset by a downward movement in most of the remaining series.

(Confidential until release July 16, afternoon.)

MAJOR MATERIALS UTILIZATION
(Seasonally adjusted, percent)

	1973			1974	
	II	III	IV	I	II
Textiles (yarn, fibers, woven fabric)	94.0	93.5	92.9	92.5	90.3
Paper, pulp, board	95.6	98.0	96.4	95.1	96.4
Petroleum refining	97.5	95.3	92.8	84.7	89.5
Basic iron and steel	93.4	94.3	94.7	92.9	91.8
Metals*	91.3	92.3	92.6	91.3	91.0
Chemicals and petroleum	93.5	92.7	91.1	87.2	87.5
<u>MAJOR MATERIALS</u>	<u>93.4</u>	<u>93.5</u>	<u>92.3</u>	<u>90.2</u>	<u>90.1</u>

*Consists of basic iron and steel, aluminum, and copper.

Retail trade inventories. Book value of retail trade inventories rose at a \$9.1 billion annual rate in May (p), following an upward-revised \$1.3 billion rate in April. All of the May increase was in the non-durable category (especially general merchandise) as a \$1.9 billion decline in auto stocks and a smaller drop in lumber and building materials offset increases in furniture and jewelry. Excluding autos, retail inventories rose at an \$11.0 billion rate in May and the April rise was \$3.9 billion. The retail trade inventory-sales ratio edged up to 1.47 from 1.46 in April.

For total manufacturing and trade, the May book value increase was \$44.5 billion, annual rate, up sharply from the \$24.0 billion April rate and from the \$36.9 billion first quarter rate. The total manufacturing and trade inventory-sales ratio edged up in May. (Confidential until release, Tuesday, July 16.)

The following tables supercede those in the July 10 Greenbook.

Table 1

BUSINESS INVENTORIES
(Change at annual rates in seasonally adjusted
book values, \$ billions)

	1973		1974	
	QIII	QIV	QI	May (p)
Manufacturing and trade	21.1	36.5	36.9	44.5
Manufacturing, total	12.4	19.0	22.5	27.9
Durable	9.8	12.8	14.3	17.2
Nondurable	2.6	6.3	8.2	10.7
Trade, total	8.7	17.5	14.4	16.6
Wholesale	4.5	6.6	9.7	7.5
Retail	4.2	10.9	4.7	9.1
Auto	1.2	4.4	-2.5	-1.9

Table II

INVENTORY RATIOS

	1973		1974	
	April	May	April	May (p)
<u>Inventories to sales:</u>				
Manufacturing and trade	1.44	1.44	1.44	1.45
Manufacturing, total	1.59	1.59	1.62	1.62
Durable	1.91	1.90	2.04	2.02
Nondurable	1.21	1.21	1.17	1.18
Trade, total	1.30	1.30	1.27	1.30
Wholesale	1.13	1.15	1.04	1.08
Retail	1.42	1.41	1.46	1.47
<u>Inventories to unfilled orders:</u>				
Durable manufacturing	.806	.786	.714	.700

CORRECTIONS:

Table I-7, footnote 2/ should read as follows: Excluding Federal pay increases, rates of change in the GNP implicit deflator are: 1974-I, 11.4 percent; 1974-IV, 7.6 percent; 1975-I, 6.6 percent.

INTEREST RATES

	1974			
	Highs	Lows	June 17	July 11
<u>Short-Term Rates</u>				
Federal funds (wkly. avg.)	13.55(7/3)	8.81(2/27)	11.60(6/12)	13.34(7/10)
3-month				
Treasury bills (bid)	8.90(4/30)	6.93(2/6)	8.17	7.32
Comm. paper (90-119 day)	12.25(7/11)	7.75(2/22)	11.25	12.25
Bankers' acceptances	12.75(7/11)	8.13(2/25)	11.00	12.75
Euro-dollars	14.06(7/9)	8.25(2/18)	11.88	13.75
CD's (NYC) 90-119 day				
Most often quoted new	12.00(7/10)	7.88(2/20)	10.50(6/12)	12.00(7/10)
6-month				
Treasury bills (bid)	8.86(5/6)	6.80(2/19)	8.17	7.89
Comm. paper (4-6 mo.)	12.13(7/10)	7.50(2/22)	11.00	12.00
Federal agencies	9.95(7/8)	7.16(2/19)	9.44	9.90
CD's (NYC) 180-269 day				
Most often quoted new	10.75(7/10)	7.50(2/27)	10.00(6/12)	10.75(7/10)
1-year				
Treasury bills (bid)	8.65(5/3)	6.37(2/15)	8.04	8.06
Federal agencies	9.59(7/10)	7.01(2/19)	9.08	9.57
CD's (NYC)				
Most often quoted new	9.75(7/10)	7.00(2/27)	9.00(6/12)	9.75(7/10)
Prime municipals	6.50(7/12)	3.70(2/15)	5.40(6/19)	6.50(7/12)
<u>Intermediate and Long-Term</u>				
Treasury coupon issues				
5-years	8.56(5/7)	6.72(2/14)	8.01	8.54
20-years	8.34(7/11)	7.40(1/4)	8.09	8.34
Corporate				
Seasoned Aaa	8.67(7/11)	7.73(1/2)	8.45	8.67
Baa	9.50(7/11)	8.54(1/2)	9.33	9.50
New Issue Aaa Utility	10.25(7/10)	8.05(2/13)	9.49(6/19)	10.25p(7/10)
Municipal				
Bond Buyer Index	6.95(7/10)	5.16(2/6)	6.13(6/19)	6.95(7/10)
Mortgage--average yield				
in FNMA auction	9.65(7/1)	8.43(2/25)	9.54	9.65(7/1)

SUPPLEMENTAL APPENDIX A*
THE INDUSTRIAL COMPOSITION OF BUSINESS LOAN GROWTH
AT LARGE BANKS IN THE FIRST HALF OF 1974

Business loans at all commercial banks grew at a 23 per cent seasonally adjusted annual rate in the first half of 1974. While data are not available on the breakdown of loans by industry for all banks, the industrial composition of loans at 150 large Weekly Reporting Banks that account for about 60 per cent of all business loans indicates that a substantial part of the not seasonally adjusted growth of business loans was to manufacturing firms, both durable and nondurable. See Table 1. Business loan growth, however, was broadly based by industry category, as it was over the same period in 1973 when CID constraints on advances in the prime rate sharply increased the relative attractiveness of bank loans.

Business borrowing at banks was large in the first half of 1974 in part because corporate profits after inventory valuation adjustment and taxes were declining in most major industry sectors. Further, there was rapid accumulation of inventories that required financing; some of the inventory growth was unintended, as consumer sales slowed in the first part of the year, but some could also be traced to voluntary stockpiling of materials and finished goods in reflection of fears of future scarcity and higher prices. Working capital needs were also inflated by rising prices, particularly for energy, as the adjustment of prices of final output to the surge of oil and coal prices was delayed in many industries by regulatory processes.

While in the entire first half of 1973 business loans were inflated by rate-induced shifts from the commercial paper markets, in 1974 shifts between the commercial paper market and bank loans occurred intermittently and were induced by both rate and nonrate factors. For example, in March-April, as the increase in market rates outstripped the rising prime rate, borrowers shifted from the commercial paper market to bank loans in large volume. In the May-June period, however, increasing quality consciousness in the commercial paper market made it virtually impossible for nonprime borrowers to issue paper, and bank

* Prepared by Paul W. Boltz, Economist, Banking Section, Division of Research and Statistics.

loan demands were increased as such borrowers were forced to draw on their bank lines--despite a relatively high prime rate. And, throughout the first half of 1974, bank loan demands reflected some borrower unwillingness to pay high capital market rates, and most recently unsettled conditions in money and capital markets have resulted in large shifts of credit demands to New York City and Chicago banks, as postponements, reductions, and cancellations of scheduled bond and stock issues became widespread.

Table 2 shows the growth of business loans in two-month intervals which roughly coincide with the changing character of business loan growth in the first half of 1974. In the first two months of the year business loan growth was sustained by heavy borrowing by trade concerns (wholesale and retail firms and commodity dealers). At that time, commodity dealer financing needs rose sharply in response to the speculative surge in commodity markets, the delayed marketing of 1973 farm crops, which had been postponed until after the turn of the year for tax and price reasons, and interruptions to the flow of farm commodity exports due to transportation difficulties. Firms in wholesale and retail trade required financing for what appeared to be unintended inventory accumulation as consumer sales, especially of durable goods, slumped early in the year. In addition, mining companies (the category that includes oil extraction firms) stepped up their borrowing at banks in January and February, in part related to financing of payments to the Federal Government for oil leases.

The composition of loan growth changed in March and April, and in these two months business loans at all commercial banks rose far more rapidly than in January and February. Loans to commodity dealers declined and those to mining companies slowed, though wholesale and retail trade firms accelerated their borrowing for inventory purposes. Durable manufacturing firms began to borrow very heavily in this period and have continued to expand their bank loans into the present period. This likely reflects financing needs arising from increased capital expenditures in nominal terms and the accumulation of raw materials and goods in process; firms which manufacture machinery have been consistently large borrowers throughout the first half.

While the higher cost of energy was adding to working capital needs of virtually all nonfinancial businesses, the impact on transportation companies and public utilities was acute, and in March and April many of these companies turned to bank loans to finance increased costs until rate adjustments could be made. In addition, some of the capital financing of utilities was being diverted to banks from the bond market where rates were becoming unattractive and buyers of bonds were becoming skeptical of the ability of utilities to pass through their rising costs.

In May and June public utilities and manufacturers of durables continued their rapid pace of borrowing. Construction loans rose sharply in this period as cost overruns and lagging sales of completed residential units increased the size and term of financing needs.

Overall the rate of growth of business borrowing has been decelerating gradually since March. By June the seasonally adjusted monthly rate of business loan growth at commercial banks was less than a third of the March rate, but in the last week of June and in early July business loan growth accelerated in New York and Chicago. With the outstanding volume of commercial paper declining sharply in early July, it appears that not only was the lagging adjustment of the prime rate to rising market rates encouraging the growth of business loans at banks, but also that increasingly unsettled money and capital market conditions were augmenting bank loan demand.

Table 1
NET CHANGE IN COMMERCIAL AND INDUSTRIAL LOANS AT LARGE COMMERCIAL BANKS, BY INDUSTRY
(In millions of dollars, not seasonally adjusted)

Business of borrower	<u>1971</u>	<u>1972</u>	<u>1973</u>	<u>1974</u>	Loans outstanding 12/26/74
	Dec. 30- June 23	Dec. 29- June 28	Dec. 27- June 27	Dec. 26- June 26	
Total trade	343	-98	1,178	1,642	13,336
Total manufacturing	-634	-250	5,079	5,416	30,474
Durable	276	-68	2,946	3,842	17,095
Metals	45	-408	2,074	2,933	13,394
Other durable	231	340	872	909	3,701
Nondurable	-910	-182	2,133	1,574	13,379
Mining	-206	-203	331	373	3,818
Public utilities, communication and transportation	-110	28	1,630	1,670	13,819
Construction	379	444	838	632	5,563
Foreign business concerns	265	213	554	632	4,073
All other	-257	-262	2,701	1,627	20,956
Total commercial and industrial loans	-220	-128	12,311	11,992	92,039

Table 2

NET CHANGE IN COMMERCIAL AND INDUSTRIAL LOANS AT LARGE COMMERCIAL BANKS, BY INDUSTRY
1974

(In millions of dollars, not seasonally adjusted)

Business of borrower	Dec. 26- Feb. 27	Feb. 27- Apr. 24	Apr. 24- June 26	Dec. 26- June 26
Total trade	782	896	-36	1,642
Total manufacturing	190	4,283	943	5,416
Durable	308	2,744	790	3,842
Metals	273	2,154	506	2,933
Other durables	35	590	284	909
Nondurable	-118	1,539	153	1,574
Mining	248	195	-70	373
Public utilities, communication and transportation	-372	1,022	1,020	1,670
Construction	-75	232	475	632
Foreign business concerns	-56	329	359	632
All other	-491	1,223	895	1,627
Total commercial and industrial loans	226	8,180	3,586	11,992

SUPPLEMENTAL APPENDIX B*
MONTHLY SURVEY OF BANK LOAN COMMITMENTS
MAY 1974

In May, growth in loans made under commitments at the 137 banks reporting on the Monthly Survey of Loan Commitments slowed from the accelerated rates in February, March, and April (Table 2), and this slowdown matched the deceleration of growth of loans at all commercial banks in that month. Smaller takedowns appear to have resulted in faster growth of unused commitments, which typically accelerate when the volume of takedowns falls (Table 1), total unused commitments rose more rapidly in May than in any of the four previous months. Almost all the growth of unused commitments in May was for commercial and industrial loans. Unused commitments to nonbank financial institutions showed negligible growth, and commitments for real estate mortgages declined.

New commitments took a decided downturn in May, although they remained at a higher level than in any other month in 1974 except April. However, this series has moved erratically since the inception of the monthly survey in the summer of last year, 1/ and the contraction is not necessarily indicative of the posture of banks' commitment policies.

The trend of utilization ratios has been upward this year, but in May utilization ratios generally fell, reflecting the slower pace of takedowns and the advance of unused commitments (Table 3). However, banks continued to restrain mortgage commitments, and the utilization ratios of real estate commitments advanced further in May.

* Prepared by Paul W. Boltz, Economist, Banking Section, Division of Research and Statistics.

1/ Many banks on the panel were unable to provide complete information on commitments in the early months of the survey. To provide a consistent profile of commitments with the largest possible panel, only data since November are included in the tables.

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MONTHLY SURVEY OF BANK LOAN COMMITMENTS
AT SELECTED LARGE U.S. BANKS 1/
(AS OF MAY. 31, 1974)

TABLE 1 - UNUSED COMMITMENTS

(DOLLAR AMOUNTS IN BILLIONS)

	(1) C & I FIRMS TOTAL		(2) C & I TERM LOANS		(3) C & I REVOLVING CREDITS		(4) C & I TERM LOANS & REV. CREDITS		(5) C & I CONFIRMED LINES		(6) C & I OTHER COMMITMENTS		(7) NON-BANK FINANCIAL INSTITUTIONS		(8) REAL ESTATE MORTGAGES		(9) TOTAL COMMITMENTS	
	AMT	% CHG	AMT	% CHG	AMT	% CHG	AMT	% CHG	AMT	% CHG	AMT	% CHG	AMT	% CHG	AMT	% CHG	AMT	% CHG
NOVEMBER 30	83.6	0.0	5.3	0.0	19.0	0.0	24.3	0.0	54.9	0.0	4.4	0.0	27.7	0.0	6.8	0.0	120.1	0.0
DECEMBER 31	83.0	-0.7	5.5	3.7	18.6	-2.1	24.1	-0.8	54.6	-0.5	4.3	-1.7	27.0	-2.5	8.8	0.3	118.9	-0.9
JANUARY 31	85.0	2.4	5.2	-4.8	18.3	-1.6	23.5	-2.3	56.8	4.1	4.6	7.1	28.0	3.7	8.6	-2.6	121.6	2.3
FEBRUARY 28	85.7	0.9	5.5	4.8	18.5	1.3	24.0	2.1	57.0	0.3	4.7	1.8	28.3	1.1	8.5	-0.9	122.6	0.8
MARCH 31	85.2	-0.7	5.7	4.5	18.4	-0.5	24.2	0.7	56.2	-1.5	4.8	2.4	28.0	-1.3	8.2	-3.9	121.3	-1.0
APRIL 30	85.3	0.1	6.4	10.8	18.6	1.1	25.0	3.4	55.5	-1.3	4.8	-0.3	26.9	-3.9	8.2	0.2	120.3	-0.8
MAY 31	86.5	1.5	6.2	-2.5	18.8	1.1	25.0	0.2	56.9	2.6	4.6	-4.2	26.9	0.2	8.1	-1.5	121.5	1.0
NOV 73 - MAY 74 AVERAGE	84.9	0.6	5.7	2.8	18.6	-0.1	24.3	0.5	56.0	0.6	4.6	0.9	27.5	-0.5	8.5	-1.4	120.9	0.2

NUMBER OF BANKS 137

1/ BANKS PARTICIPATING IN THE MONTHLY LOAN COMMITMENT SURVEY ARE SELECTED WEEKLY REPORTING BANKS WITH TOTAL DEPOSITS OF \$100 MILLION OR MORE.

** NOTE: MINOR INCONSISTENCIES MAY OCCUR DUE TO ROUNDING. **

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MONTHLY SURVEY OF BANK LOAN COMMITMENTS
AT SELECTED LARGE U.S. BANKS 1/
(AS OF MAY. 31, 1974)

TABLE 2 - LOANS UNDER COMMITMENTS 2/

(DOLLAR AMOUNTS IN BILLIONS)

	(1) C & I FIRMS TOTAL		(2) C & I TERM LOANS		(3) C & I REVOLVING CREDITS		(4) C & I TERM LOANS & REV. CREDITS		(5) C & I CONFIRMED LINES		(6) C & I OTHER COMMITMENTS		(7) NON-BANK FINANCIAL INSTITUTIONS		(8) REAL ESTATE MORTGAGES		(9) TOTAL COMMITMENTS	
	AMT	% CHG	AMT	% CHG	AMT	% CHG	AMT	% CHG	AMT	% CHG	AMT	% CHG	AMT	% CHG	AMT	% CHG	AMT	% CHG
NOVEMBER 30	70.6	0.0	18.6	0.0	19.7	0.0	38.3	0.0	25.9	0.0	6.4	0.0	18.1	0.0	18.0	0.0	106.7	0.0
DECEMBER 31	72.1	2.1	19.1	2.7	19.6	-0.2	38.8	1.2	26.7	3.3	6.6	3.0	19.8	9.6	18.2	1.4	110.2	3.2
JANUARY 31	71.2	-1.3	19.0	-0.5	19.8	0.7	38.7	-0.1	25.6	-4.0	6.7	1.3	18.4	-7.1	18.2	0.0	107.8	-2.1
FEBRUARY 28	72.6	2.0	19.3	1.2	20.3	2.4	39.5	2.1	26.6	3.7	6.5	-2.9	18.4	-0.4	18.3	0.2	109.3	1.3
MARCH 31	77.3	6.5	19.5	1.3	21.2	4.7	40.7	3.0	29.9	12.4	6.7	3.7	19.4	5.6	18.4	0.6	115.1	5.3
APRIL 30	79.5	2.8	20.6	5.5	21.4	1.0	42.0	3.2	31.0	3.6	6.5	-3.2	20.6	6.3	18.6	1.4	118.8	3.1
MAY 31	80.1	0.8	20.8	0.9	21.8	1.7	42.6	1.3	30.5	-1.5	7.0	7.9	20.5	-0.6	18.7	0.2	119.3	0.4
NOV 73 - MAY 74 AVERAGE	75.5	2.2	19.7	1.9	20.7	1.7	40.4	1.8	28.4	2.9	6.7	1.6	19.5	2.2	18.4	0.6	113.4	1.9

NUMBER OF BANKS 137

1/ BANKS PARTICIPATING IN THE MONTHLY LOAN COMMITMENT SURVEY ARE SELECTED WEEKLY REPORTING BANKS WITH TOTAL DEPOSITS OF \$100 MILLION OR MORE.

2/ LOANS UNDER COMMITMENTS ARE DEFINED AS ALL LOANS UNDER COMMITMENTS CURRENTLY OR PREVIOUSLY IN FORCE, LESS REPAYMENTS OF THE PRINCIPAL. THE REPORTED DATA ARE DISTORTED BY TAKE-DOWNS OF LOAN COMMITMENTS BY OVERSEAS BRANCHES OF US BANKS AND LOAN SALES.

** NOTE: MINOR INCONSISTENCIES MAY OCCUR DUE TO ROUNDING. **

NOT FOR
QUOTATION OR
PUBLICATION

MONTHLY SURVEY OF BANK LOAN COMMITMENTS
AT SELECTED LARGE U.S. BANKS 1/
(AS OF MAY. 31, 1974)

TABLE 3 - UTILIZATION RATIO 2/

(PERCENTAGES)

	(1) C & I FIRMS TOTAL	(2) C & I TERM LOANS	(3) C & I REVOLVING CREDITS	(4) C & I TERM + REV.	(5) C & I CONFIRMED LINES	(6) C & I OTHER COMMITMENTS	(7) NON-BANK FINANCIAL INSTS.	(8) REAL ESTATE MORTGAGES	(9) TOTAL	(10) SHORT -TERM TOTAL ^{3/}
NOVEMBER 30	45.8	77.8	50.9	61.2	32.0	59.4	39.5	67.2	47.1	39.8
DECEMBER 31	46.5	77.7	51.4	61.7	32.9	60.5	42.3	67.4	48.1	41.1
JANUARY 31	45.6	78.4	52.0	62.1	31.1	59.2	39.7	68.0	47.0	39.6
FEBRUARY 28	45.9	77.8	52.2	62.2	31.8	58.0	39.3	68.2	47.1	39.8
MARCH 31	47.6	77.3	53.5	62.8	34.7	58.3	41.0	69.2	48.7	41.8
APRIL 30	48.3	76.4	53.5	62.7	35.8	57.6	43.4	69.5	49.7	42.9
MAY 31	48.1	77.0	53.6	63.0	34.9	60.5	43.2	69.8	49.5	42.7
NOV 73 - MAY 74 AVERAGE	46.8	77.5	52.4	62.2	33.3	59.1	41.2	68.5	48.2	41.1
NUMBER OF BANKS	137									

1/ BANKS PARTICIPATING IN THE MONTHLY LOAN COMMITMENT SURVEY ARE SELECTED WEEKLY REPORTING BANKS WITH TOTAL DEPOSITS OF \$100 MILLION OR MORE.

2/ THE UTILIZATION RATIO IS THE RATIO, EXPRESSED AS A PERCENTAGE, OF LOANS UNDER COMMITMENTS TO THE SUM OF UNUSED COMMITMENTS AND LOANS UNDER COMMITMENTS

3/ EXCLUDES REAL ESTATE LOANS AND TERM LOANS.

** NOTE: MINOR INCONSISTENCIES MAY OCCUR DUE TO ROUNDING. **

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MONTHLY SURVEY OF BANK LOAN COMMITMENTS
AT SELECTED LARGE U.S. BANKS 1/
(AS OF MAY. 31, 1974)

TABLE 4 - NEW COMMITMENTS

(DOLLAR AMOUNTS IN BILLIONS)

	(1)		(2)		(3)		(4)		(5)		(6)		(7)		(8)		(9)	
	AMT	% CHG	AMT	% CHG	AMT	% CHG	AMT	% CHG	AMT	% CHG	AMT	% CHG	AMT	% CHG	AMT	% CHG	AMT	% CHG
NOVEMBER 30	4.9	0.0	1.1	0.0	1.2	0.0	2.3	0.0	1.8	0.0	0.8	0.0	0.9	0.0	0.8	0.0	6.6	0.0
DECEMBER 31	5.0	1.4	1.3	22.2	1.1	-5.4	2.4	8.0	1.8	-1.3	0.7	-10.8	1.1	21.1	1.1	35.5	7.1	8.0
JANUARY 31	4.8	-2.8	0.8	-39.5	0.9	-22.4	1.7	-31.8	2.2	23.3	0.8	21.0	0.9	-11.8	0.9	-15.4	6.7	-6.0
FEBRUARY 28	4.5	-6.7	0.8	2.1	0.9	5.7	1.7	3.9	2.1	-4.0	0.6	-29.3	0.7	-22.8	0.8	-7.8	6.1	-9.0
MARCH 31	6.3	38.7	1.3	59.6	1.3	41.8	2.6	50.3	2.8	32.4	0.6	10.6	0.9	26.3	0.9	11.8	8.1	33.5
APRIL 30	7.0	11.0	1.2	-8.7	1.6	28.6	2.9	9.6	3.0	8.2	0.6	-1.0	1.1	19.4	0.9	2.3	9.0	10.9
MAY 31	6.5	-6.1	1.2	-0.3	1.5	-6.6	2.7	-4.0	2.8	-6.1	0.7	9.8	1.4	26.4	0.9	-2.3	8.8	-1.7
NOV 73 - MAY 74 AVERAGE	5.6	5.9	1.1	5.9	1.2	7.0	2.3	6.0	2.3	8.7	0.7	0.1	1.0	9.8	0.9	4.0	7.5	6.0

NUMBER OF BANKS 137

1/ BANKS PARTICIPATING IN THE MONTHLY LOAN COMMITMENT SURVEY ARE SELECTED WEEKLY REPORTING BANKS WITH TOTAL DEPOSITS OF \$100 MILLION OR MORE.

** NOTE: MINOR INCONSISTENCIES MAY OCCUR DUE TO ROUNDING. **

SUPPLEMENTAL APPENDIX C*
TREASURY STUDY OF TAX AND LOAN ACCOUNTS

The Treasury has just published a report on its study of the tax and loan account system. The purpose of the study was to evaluate the desirability of maintaining, eliminating, or modifying the current system. The basic issue under investigation was whether, or to what extent, the Government incurred a net monetary cost under the current arrangement, taking into account the implicit value of services provided by the banks to the Government on the one hand and the Government's loss of income from holding its funds in non-interest bearing deposits on the other. Critical data bearing on this issue were gathered from a sample of 600 banks (300 banks with the largest tax and loan accounts and a sampling of 300 other banks). Summarized below are the major findings of the study along with the Treasury's conclusions and proposals.

Cost of services performed by banks

In evaluating the services performed by banks, the Treasury decided that any service provided primarily as a service to customers, or as a marketing device, or for which the banks levy a charge to the individual recipient of the service, should not be compensable. For example, since the survey showed that most banks do not handle subscriptions to Treasury issues without a fee this "service" did not qualify for compensation. Using the criterion described above only two activities were judged to be compensable: the maintenance of the tax and loan account itself (assuming it were maintained in some form); and the issuance, redemption, and exchange of savings bonds. Employing data from the survey (which reflects calendar year 1972 figures), the Treasury estimated that in the aggregate it cost banks about \$64 million to provide these compensable services.

Earning value of tax and loan accounts

The Treasury also developed estimates of the earning value of tax and loan account balances to commercial banks. Using the three month bill rate as a surrogate for the potential return to be gained from investing tax and loan account balances (and adjusting for reserve requirements and FDIC assessment) the Treasury estimated that banks received an implicit gross return of \$325 million in 1972.

* Prepared by Raymond Lombra, Economist, Government Finance Section, Division of Research and Statistics.

The Treasury emphasized that the excess of this figure over compensable costs, \$260 million, probably overstates both the increment to bank profits derived from tax and loan accounts and the benefit that would accrue to the Federal budget from substantially modifying the present system. It is possible, for example, that banks pass on part or all of this excess to the public in the form of lower costs for banking services or to the Treasury in the form of lower borrowing costs on new issues with tax and loan account crediting. Further, to the extent bank profits rise, the corporate income tax recovers part of the excess. 1/

Treasury conclusions and recommendations

After apparently considering a number of alternatives, the Treasury concluded that tax and loan accounts should be retained in order to minimize the impact of Federal financial transactions on the distribution and level of bank reserves and on the money market. Other schemes examined either raised administrative costs significantly or would have had undesirable effects on the money market. This conclusion coupled with the findings described above--that is, that the implicit bank return on the accounts is well above the costs of services provided--led the Treasury to recommend adoption of alternative procedures that would enable the Treasury to earn a return on its cash balances and provide banks with explicit reimbursement for services found compensable.

On the investment side the debt managers plan to experiment with 30-day commercial bank time deposits. However, since the average "life" of a tax and loan deposit is usually about 10 days, the Treasury does not believe this innovation will be very productive. In addition to the above, the Treasury also plans to intensify its efforts to raise its operating balance at Federal Reserve Banks. This action will, other things remaining the same, also earn a return for the Treasury, because the System will have to purchase securities to offset the reserve effect of the Treasury's action, thus raising Federal Reserve earnings and, therefore, the System's payment to the Treasury. The most promising technique advocated by the Treasury was direct investment in money market instruments, such as repurchase agreements. This latter approach, however, will require enabling legislation, because the Treasury, while it has the authority to hold deposits cannot hold market instruments.

1/ It should be noted on the other hand, however, that using the bill rate rather than, say, the funds rate, may bias downwards the estimated earning value of tax and loan accounts.

Finally, with regard to the services provided by banks which were deemed compensable the Treasury proposed the following: (1) the issuance, redemption, and exchange of savings bonds should be compensated by fees paid from appropriations; and (2) costs related directly to the servicing of tax and loan accounts should be covered by the residual value of the accounts which will remain in banks. 1/

1/ It is not clear from the report what type of "formula" will be used in determining the level of tax and loan balances which will remain in individual banks.

SUPPLEMENTAL APPENDIX D*
TAX-EXEMPT CORPORATE POLLUTION CONTROL BONDS

Tax-exempt pollution control bonds for corporate purposes were authorized by Congress in 1968 as a special type of industrial revenue bond, as part of a package which severely restricted the use of industrial revenue bonds for other purposes. Since the first issue under this authority in April 1971, this method of financing grew to a level of over \$2 billion in 1973. Earlier this year, 1974 volume was projected to be about \$2.5 billion; however, actual volume will likely fall short of that figure due to adverse market conditions. Thirty-nine States have passed necessary enabling legislation, including all the major industrial States except Massachusetts and New Jersey.

Pollution control bonds are, for practical purposes, tax-exempt corporate bonds. The bonds are issued by a State or municipal governmental unit, with the proceeds utilized to finance new, non-productive pollution control equipment or facilities for a specified corporation. The facilities are initially owned by the issuing authority, and leased or sold on an instalment basis to the corporation. Payments by the corporation are scheduled in such a way as to equal the required interest and principal payments on the bonds. Generally, when all the bonds mature, the corporation will either own the facility or have the option to buy it for a nominal amount. The corporation guarantees payments, and provisions are generally made so that bond-holders will be treated as senior creditors of the corporation in the event of bankruptcy. Thus, rating agencies grade these issues on the basis of the corporation's soundness, and debt ratings of the governmental unit are not affected.

The primary benefit to corporations of pollution control bonds is, of course, the ability to borrow in the tax-exempt market, which in the current market translates generally into interest rate savings of 2 to 3 per cent. In addition, corporations are allowed to treat pollution control facilities financed by tax-exempt bonds as if they were owned for Federal income tax purposes. Other benefits include the ability to obtain 100 per cent financing, the lack of SEC registration requirements, access to new sources of financing, and in some cases favorable State and local tax treatment on such facilities.

Despite the advantages, many companies, especially smaller firms, have determined that the time and expense of issuing tax-exempt

* Prepared by Daniel Krabill, Economist, Capital Market Section, Division of Research and Statistics.

bonds exceed the potential benefits. One reason is that these tax-exempt issues tend to be smaller than normal corporate issues, as pollution control expenditures at various plant locations must generally be financed by separate bond offerings. Also, tax-exempt status must be assured for each issue, on the basis of either a special IRS ruling or counsel's opinion based on established precedent. In addition to these financial reasons, some large companies have not used tax-exempt financing in order to avoid possible public criticism.

Volume

The volume of tax-exempt pollution control bonds grew rapidly from 1971 through the end of 1973, but has decreased somewhat during the first half of 1974, as shown in the following table.

	Tax Exempt Pollution Control Financing (billions) ^{1/}	Percentage of State and local Market ^{1/}
1971	.1	.4
1972	.5	2.4
1973	1.8	7.7
1974 (first half)	.8	6.2

^{1/} Bond Buyer (excludes most private placements, and short-term bond anticipation notes).

Private placements are generally excluded from the above figures. The Bond Buyer estimates that roughly \$250-350 million in direct placements is excluded from their 1973 figures, but that this portion of the market has dried up considerably in recent months.

The decline in volume during the first half of 1974 can be attributed primarily to market factors, despite a 14 per cent increase in long-term State and local financing over 1973 levels, and to a slow-down in new rulings on eligibility from IRS. The decline seems to be temporary, since the volume of planned issues has increased and now totals \$2.1 billion, and the level of pollution control investment is expected to grow.

Publicly sold pollution control issues are generally term bonds with fixed maturities of 25 or 30 years, a very unusual type of instrument for the tax-exempt market. Placements with banks usually are structured more like loans, with maturities in the 3- to 10-year range and generally with floating interest rates tied to the prime rate. Some corporations make it a practice to limit maturities to the expected life of the pollution control facilities, while others maximize the maturity regardless of the expected life in order to maximize the benefits of tax-exempt financing.

Sales of both public and privately placed issues have previously been concentrated in a relatively narrow range of investors, primarily banks and casualty companies, who have recently cut back purchases of pollution control issues. In aggregate, banks and casualty companies have increased their holdings of tax-exempt issues; however, they seem to be purchasing the more standard shorter-maturity, fixed-rate serial bonds.

Brokers have thus turned increasingly to individuals. It would seem that sales to individuals should increase significantly in coming months as brokers re-orient their sales strategies, especially in the light of the willingness of corporations to pay higher interest rates than are paid on municipal bonds with similar ratings and maturities.

The use of pollution control bonds is concentrated to a large extent in a few industries. Electric utilities raised \$712 million via this route in 1973. Other major industries in this market include metal processing and refining, paper, chemicals, and oil.

Growth Potential

The volume of pollution control financing in future years depends primarily on the level of capital investment which is eligible for such financing, which in turn is closely related to the requirements of the Environmental Protection Agency and the various States. The following table provides figures for actual and projected corporate investment in pollution control facilities, some portion of which is eligible for tax-exempt financing.

	Pollution Control Investment (billions) ^{1/}
1970	2.5
1971	3.2
1972	4.5
1973	5.7
1974 (projected)	7.4
1977 (projected)	9.3

^{1/} Annual McGraw Hill Surveys.

Pollution control investment can be expected to turn down after 1977, when most existing standards will have been met, but will likely continue at a lower level due to new and changing Federal standards, State requirements, new technology, and additions to productive capacity.

Assuming no major changes in EPA standards or in IRS policy, and no Congressional action similar to that taken in 1968 to limit industrial revenue bonds, the above figures indicate that the volume of pollution control bonds should recover from its current decline, increase over the next several years, perhaps to a level of \$2.5-\$3.5 billion, and then turn down in 1977 or 1978.

One major unresolved issue, which could result in a significant increase in pollution control bonds, concerns the eligibility of investments to control radiological pollution from nuclear power plants. The industry is asking IRS for rulings that would make an additional \$1-2 billion per year eligible for tax-exempt financing, a very large percentage of which would likely be financed in this market.

Tax-Exempt "Commercial Paper"

One recent innovation in tax-exempt financing that seems likely to grow is short-term tax-exempt financing for construction of pollution control facilities. The Virginia Electric and Power Company (VEPCO) innovated in this area in December 1973, and now has \$44.5 million in tax-exempt "commercial paper" outstanding, with rates paid holding at a constant ratio of 60 per cent of the prime rate. Two other utilities are known to be utilizing this method of short-term financing but, instead of selling this paper publicly through a commercial paper dealer, are placing it directly with banks.

Effect on Market for Tax-exempt Securities

The effect of pollution control bonds on the cost and availability of funds for other tax-exempt borrowers is very difficult to determine, but would seem to be greater for those issues with longer maturities. The substitutability of various types of debt securities for one another in the market, and thus the spreading of interest cost effects of an increase in volume of one type of security, is much less complete in the tax-exempt market than in other markets. Many corporate investors in such securities are limited in their purchases by the amount of their taxable income, and many large money market investors such as pension funds are tax-exempt and thus have no need for tax-exempt bonds. Thus, increased volume must be absorbed by a relatively small class of investors.

As a result of the rapid growth of pollution control bonds, some pressure is being exerted, primarily by issuers of State and local government bonds, to eliminate tax-exempt status on these bonds. This activity parallels the events of 1968, when industrial revenue bonds were severely limited by Congress after they had grown to the point where they were affecting State and local borrowing.