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Chairman— A. J. WEGMANN, President Bagille's Seafood Co., Inc. New Orleans, La.

Financing of Fishing Vessels by Commercial Banks

CHARLES T. TAYLOR, *Assistant Vice President, Federal Reserve Bank of Atlanta, Atlanta, Ga.*

The Federal Reserve Bank of Atlanta, since it is a central bank, does not make loans to business or agriculture except under extraordinary circumstances. It is primarily a bankers' bank. As such it performs what might be called "facilitating services," including the provision of currency and coin, clearing checks, and acting as a fiscal agent for the federal government. Perhaps of even greater importance, however, is its share in the responsibility the Federal Reserve System has for managing the nation's money supply, or in the words of the Federal Reserve Act, "accommodating the needs of commerce, agriculture, and industry."

Those who manage the money supply must obviously be informed of the nature of the economy of the region served by the bank. Consequently, our interest in the fishing industry grows up out of a research program, one purpose of which is to learn more about the economic structure of the Sixth Federal Reserve District, which includes the states of Alabama, Georgia, and Florida, the southern halves of Louisiana and Mississippi, and the eastern two-thirds of Tennessee.

The writer, therefore, is only an outside observer and not in direct day-to-day contact with the actual financing of fishing vessels. Consequently, this paper will be limited to the consideration of two points: general observations about commercial bank lending policies, and observations on how commercial banks have been able to finance fishing vessels within the framework of these policies.

Although many of you have a clear conception of the structure and policies of commercial banking and how these matters affect bank lending, others often do not have this basic knowledge. The following quotation taken from a letter from a fishing-boat captain some time ago illustrates the point.

> "I have been connected with the fish industry of the United States and Canada for the last 63 years in all its branches . . . . It has always been a wonder to me why the banks have not gone after this fishing industry business. I have always claimed that the security is far sounder than the farm loan is . . . Right now there is a body of men who have the best security in the world so if you know of any banks that would be interested in loans to the fish industry I would be very much interested in going into details."

Although this particular letter applies to the fishing industry, we could well insert farming industry or practically any other than you might name. The chief complaint made about commercial bank financing is that the bankers will not make loans for long enough periods, that they will not make them in large enough amounts, and that they require that repayment start too soon. For example, some agricultural experts want banks to make loans extending from five to ten years with no repayments to be made within two or three years. "Why," these and other persons ask, "are bankers blind to the opportunities of making such profitable loans?"

To answer this question a word about the structure of the commercial banking system is in order. Under our American system all commercial banks are privately owned and operated. Some are chartered by the national government and are called national banks. These banks must be members of the Federal Reserve System. Others chartered by the state governments may be members of the Federal Reserve System if they so desire, and if they meet certain requirements. All member banks, both national and state, must be members of the Federal Deposit Insurance Corporation, but non-member state banks also may be insured banks. Before securing charters banks must meet certain specifications set up by law and are subject to periodic investigation by the supervisory authorities. Despite the various types of charters issued, laws, and supervision, however, there is much more uniformity in commercial banking operations than might appear. Although bank examinations are made to insure that banks are being soundly operated, except in certain limited cases bankers themselves are the ones that determine how large a loan they will make and to whom they will lend and on what terms they make their loans. Lending policies are probably determined more by what are regarded as sound banking principles by all types of bankers than by the particular laws that might stop them from making certain types of loans.

Bank lending policies are greatly influenced by the nature of the bank's liabilities, the overwhelming part of which are demand deposits subject to immediate withdrawal at any time. To some extent bankers can predict that during certain periods of the year withdrawals will greatly exceed new deposits. In Miami, for example, deposits in October are likely to be about 15 per cent lower than in April. But the bankers must also be prepared for a withdrawal of deposits resulting from other factors that they cannot predict so easily. Perhaps they may lose some of them to their competitors. Perhaps a year or two from now economic conditions will cause deposits to flow out of their communities.

Unfortunately, bankers, like anyone else, are not infallible prophets, and since they do not know exactly what will happen in the future the bankers must set up certain safeguards in their operations against unfavorable contingencies. On the basis of past experience, therefore, bankers have found it necessary to keep a large proportion of their assets in the form of secondary reserves that can be converted immediately into cash. Generally this accounts for their government security holdings, which earn considerably less than loans, but which can be liquidated, if necessary, with little or no loss. Investment in government securities, however, would not earn the reasonable profits that are essential to a soundly operated bank. Moreover, bankers know that their success depends to a considerable extent upon the prosperity of the communities they serve, and that this prosperity requires bank credit. They are, therefore, interested in making loans, but they must consider many factors other than the credit-worthiness of a particular loan application in making their decisions about how much credit they will grant to private industry, and on what terms they will grant it.

These considerations have led bankers to specialize in short-term rather than long-term credit. It is generally only when the demand for short-term credit is so small that normal funds cannot be properly utilized that most bankers make considerable amounts of long-term loans. Immediately after World War II, for example, bankers granted more long-term loans, probably because with ample funds available for lending and the low returns that could be secured on government securities, the slightly higher rates on long-term loans helped to bolster bank earnings. Even then, in the Sixth Federal Reserve District, long-term loans constituted only 14 per cent of commercial and industrial loans. Since then the practice of making long-term loans has apparently become less common.

Bankers also try to maintain liquidity by diversifying their loans. This means, for the smaller bank, that a bank may often have to turn down an application for a loan that apparently meets all other credit standards, merely because the banker already has made several loans to persons in the same industry. Banks in single-industry cities, such as one where fishing predominates, may often not be able to satisfy all credit demands of that industry. On the same basis, however, a bank that has no such loans might want to consider them for the diversification they would bring.

Bankers are doubtful about making loans to persons in industries that are subject to violent swings from prosperity to depression, and where success more often depends upon the vagaries of prices than upon wise and skillful management. They will, therefore, sometimes be reluctant to grant loans to persons who want to get in on "a good thing" that has enjoyed phenomenal success because of major price or demand changes, while at the same time they will grant the loan to a person in the same industry who has had experience and is in for the "long pull."

Bankers dislike making loans to persons or industries about which they do not know enough to be able to make intelligent decisions. This tendency often accounts for the concentration of loans of certain types in one bank rather than another located in the same city. Bankers must be experts to some degree on all the kinds of businesses to which they make loans. Limitations of time and personnel make it impossible for some banks to be informed on all types of industries.

Occasionally legal prohibitions may prevent the granting of specific loans. For example, a national bank cannot make a loan to a single borrower amounting to more than 10 per cent of its unimpaired capital and surplus. On the basis of this provision, smaller national banks may find it impossible to finance the larger and more expensive vessels that have become common in recent years.

Bankers that are members of the Federal Reserve System have the protection that in case of an emergency they may borrow from the Federal Reserve Banks. In recent years practically all borrowing has been secured by government obligations. However, some bankers do not like to have too large a proportion of their loans of a type that is ineligible for rediscount with a Federal Reserve Bank, and such ineligible loans include non-agricultural loans having maturities of over 90 days, whether to purchase vessels or for any other use. These loans, however, may be used as collateral for advances secured from a Federal Reserve Bank at a higher, or penalty discount rate.

More often, however, it is the adherence to what are considered sound banking practices that would determine the acceptability or non-acceptability of any application for credit. In this respect there may be little difference between the actions of national chartered banks, state chartered banks that are members of the Federal Reserve System, and non-member banks.

Working within this framework several commercial banks in this area have been able to make loans to the fishing industry that have been advantageous to both the borrowers and to the banks. They have been profitable to the banks, and at the same time the banks have gained indirectly by fostering the development of an important industry in their areas.

There is no record of the total amount of money that banks have outstanding to finance the fishing industry, a condition that applies to almost all types of industries as well. There is some idea, however, of the types of loans they make, based upon data collected in a survey made a few years ago of commercial and industrial loans. Data obtained from interviews and by correspondence indicate that conditions at the present time are very similar to those at the time the survey was made.

Reports from banks in Florida, Georgia, Louisiana and Mississippi show that most of the credit outstanding to the fishing industry was for a period of less than one year. Only 10 per cent of the total amount of credit outstanding was extended for a period of more than one year. Apparently most of the credit granted by the banks to the fishing industry was used for short-term working capital. A similar survey made in later years would probably show an increase in the proportion of long-term credit granted, since the survey was made soon after the close of World War II and comparatively few boats were being purchased at that time. Over three-fifths of the loans that were outstanding were to borrowers with assets of less than $2,000.

The most common security required by the banks was a chattel mortgage on boats or other equipment, and this applied equally to long- and short-term loans. Endorsement was required as security for about one-fifth of the loans outstanding; almost one-fifth of the loans, probably short-term loans, were unsecured. About three-fifths of the loans outstanding provided for repayment in instalments.

In recent years bankers who have made loans for the purchase of fishing vessels have been pleased with their experience when, in the words of one banker, "the proper practices are followed." One of the most interesting things coming out of the rather limited survey is that, in attempting to arrive at methods by which financing of fishing vessels could be incorporated into what they considered sound loan programs, bankers have arrived at pretty much the same conclusions whether they are located in Georgia or Mississippi.

First of all, there are bankers who make no loans to the fishing industry at all, even though they are located in coastal cities where fishing is important. Sometimes this results from the attitude expressed by one banker that he feared that if a depression took place there might be so many boats on the market that he would be unable to recover on his collateral. Other bankers simply have had no demands for loans, because few if any of their customers are in the business and, in general, banks prefer to make loans to their own depositors. Other bankers, probably wisely, believe that they do not have sufficient knowledge of the technicalities of the business to enable them to supervise such loans properly. Or, perhaps the demands from customers in other lines of business leave no funds available for financing fishing vessels. Some banks are unable to finance fishing vessels because of the tendency to use larger and larger boats. According to one banker, "the day of the 30 foot shrimp-boat with an automobile engine is past, and a small bank cannot, either because of legal limitations or prudence, make a loan of sufficient size to finance the purchase of a modern large vessel." However, some bankers are active in financing the purchase of vessels.

The bankers' first interest, when making loans to any type of borrower, is in what they call the general credit-worthiness of the borrower, no matter what type of security may be offered for the loan. Decisions about credit-worthiness are based on a number of factors, some of them intangible. First there is the record that the operator has established, evidenced not only by his general reputation, but by financial statements, including a record of his operating results for several years. The banker, of course, will consider his record of integrity and the multitude of other factors that are always considered by loan officers. One banker states that he is reluctant to make loans to persons who do not operate the boats themselves, since success depends so much upon expert supervision. Another states that he does not like to make loans to single-boat operators. Other bankers believe that the prospective borrower should have financial worth outside the boat itself.

After having satisfied himself as to the general credit-worthiness of the borrower, the banker will probably next have to satisfy himself that a chattel mortgage on the boat will meet his requirements. Most bankers then proceed to an appraisal survey. It is here, of course, that the banker needs to have specialized knowledge. One banker relates that the knowledge required includes something about the construction of the boat, the amount and the kind of motive power required, the power generated by the electric plants, the reduction gears, and so on. He is more likely to consider the collateral favorably if the boat has more than one possible use. He will also have to satisfy himself that there are the proper documents and that sufficient marine insurance is carried.

The potential borrower from a bank must generally have a substantial equity in the vessel. Perhaps some banks will lend as much as two-thirds of the value of a new boat or 50 per cent of the depreciated value of an older vessel. Other bankers will lend no more than 50 per cent of the value of the vessel. The loan contract will generally provide for repayment either in monthly or quarterly instalments over a period of no more than three years, and sometimes only two years.

Financing fishing vessels is, of course, not the only type of lending by which banks grant credit to the fishing industry. Many banks help provide working capital by short-term loans, either secured or unsecured, to wholesalers and to packers. Although by no means the only source, commercial banks have been able to help satisfy the credit needs of the industry.

Financing of Fishing Vessels in the Gulf States

JOHN J. FAUBION, JR.
First State Bank, Port Lavaca, Texas

As a banker I want to go on record that I like the commercial fishing industry — every phase of it. Also, I am somewhat apologetic for the reticence with which the banking fraternity has recognized this, America's oldest industry, as the sound bankable business that it really is.

Bankers have a reputation for being somewhat cold and calculating, and possibly that is why banks have been so slow to recognize the importance of the fishing industry and what it means to the nation, the community, and the bank itself.

When I moved to the Texas Coast in early 1947 the commercial fishing industry meant nothing to me. My knowledge of commercial fishing was limited to the lone little fish market in our West Texas town, and the odor of it was a poor introduction to the industry. Port Lavaca, at the time I moved there, was primarily a cotton and cattle town, insofar as banking was concerned. Rice was a new industry for us, and in self defense we had to get out of our bank and learn something about rice. This got us in the learning habit, I suppose, for it was not long before we also made it a point to spend some time out of our bank learning about another new industry — commercial fishing. It was not long before we began to notice that the checks for the seafood industry going through our bank were larger and more regular in their appearance than previously.

Then, in early 1948, a bright-eyed young man came into the bank and wanted to talk about a loan to build a new shrimp trawler. Our first impulse was to turn him down flat, but we had inaugurated a new attitude toward the public in our bank, this new attitude being one of definite friendliness while endeavoring to learn something about the new industries in our community. So we listened to the young man instead of dismissing him with a flat "no".

This man's appearance, alertness, obvious educational background and aggressiveness did not fit into the vague pattern we had in our mind of a commercial fisherman. After listening to him for a few minutes we were sincerely interested in his proposition, and asked him to return the next day. This gave us a chance to evaluate what he had told us about himself and about the operation of modern shrimp trawlers. What we learned, we liked. This not only clinched the loan for this, our first applicant, but sold us on the feasibility of lending money on shrimp trawlers and to the seafood industry in general.

We have been financing fishing boats ever since the first contact with the industry in early 1948. On November 12, 1953, we had outstanding