

Remarks by

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I am honored to be invited to attend this meeting and to participate in your deliberations.

You have asked me to look ahead to trends in banking during the next decade and, in particular, to discuss the ways in which minority banking is likely to be affected by the oncoming changes in American banking as a whole. This, of course, is a big order which cannot be adequately addressed in the time you and I can give it today. But it is interesting and important to think about the future, if only in a general way.

Much of what happens in the decade ahead will be the result of actions taken by the government, primarily the Congress. Changes in the laws -- laws already enacted, laws under consideration, and laws yet to be thought of -- will have a significant impact upon the range of banking services available to the public and upon the cost and efficiency of banking as an industry.

If one were to believe that the next decade would be as full of banking legislation as the last, "significant impact" would be a very inadequate way indeed of describing it. I believe -- and I hope -- that most new banking legislation will be technical and additive to the new laws we already have.

As you may be all too well aware, the acts of the Congress in the field of banking are likely to result in a stream of new banking regulations from Federal bank supervisors, including the Federal Reserve Board. Even relatively old laws, such as the Truth in Lending Act that became effective in 1969, can still continue to generate new regulatory waves

Of course, in focusing on the great changes that legislation, and regulation under legislation, has been bringing to banking, I am leaving

aside another wellspring of change. This is technical and administrative innovation. If anyone doubts the scope and force of this type of change, they need only recall that certificates of deposit were an innovation only a decade or so ago, an innovation that ushered in the broad turn to liability management in banking. Or they could recall that computerized accounting, calculation and communication are only a few years old, in terms of general usage. Yet, in only a brief time, computerization has brought us so near to general use of electronic transfer of funds that this technology has called forth a new law aimed at protecting the ordinary banking consumer in the use of electronic transfer. Such technological and administrative innovation is sure to continue, and small as well as larger banks should take advantage of the opportunity to use it, where feasible, to give the public better service while maintaining profits.

But let us glance back, very briefly, at some of the legislative changes that have altered banking so much in the past decade. I have mentioned the basic consumer credit protection law, the Truth in Lending Act. As with so much of the ensuing legislation in this field, the Congress directed the Federal Reserve to write implementing rules and carry much of the enforcement burden. What was thought of as a simple law requiring that consumers be told the real cost of using credit, by now has burgeoned into a regulation of some 100 printed pages, more than 1,000 staff opinion letters and some 150 staff interpretations, to say nothing of whole new laws, such as Fair Credit Billing and the Consumer Leasing Act.

In 1970, the Congress amended the Bank Holding Company Act to include one-bank as well as multi-bank holding companies. Under this legislation, the structure of banking in the United States has been altered

generally and profoundly. Here, the Federal Reserve was given sole rule-writing and administrative authority.

The Equal Credit Opportunity Act of 1974 and later amendments have further altered banking's legal responsibilities by the Act's prohibition of discrimination in lending -- implemented by the Federal Reserve's Regulation B -- on the basis of sex, marital status, age, race, color, creed, national origin and other matters.

More recently -- and skipping over a great deal -- the Congress enacted a sweeping alteration of the nation's banking laws known as the Financial Institutions Regulatory and Interest Rate Control Act of 1978. This law places limits on loans to insiders, namely executive officers, major stockholders and in some instances directors. It also requires reports on loans made to such individuals and restricts management officials from serving with more than one depository institution. It is of interest to note that, by regulation, agencies have allowed minority banks to "borrow" management officials for a limited period of time for training purposes or to fill a temporary management gap.

Also, the requirements relating to the acquisition of insured banks and bank holding companies were tightened, particularly as regards the necessity of submitting comprehensive information about the acquiring party and details of the proposal. And, of course, I am sure you are aware of the new prohibitions against preferential treatment in dealings with executive officers, directors and major shareholders of banks which have correspondent relations. Again, this gives only a glimpse of the many and complex provisions (21 titles) of this omnibus piece of legislation. The Federal Reserve Board was directed to write regulations implementing a number of the Act's new requirements. Let me just mention, in addition,

that the International Banking Act of 1978 brought foreign banking in the United States under Federal supervision and authorized the expansion of Edge Corporation activities.

On the surface, the provisions of this Act may seem irrelevant to many small banks which do not operate in the international domain. However, it highlights the fact that foreign banks may be a very real competitive force in local markets. The extent to which foreign banks take advantage of the opportunities available to them will affect the share of the market open to smaller banks.

Another major piece of legislation that has recently been enacted is the Community Reinvestment Act. This law requires each depository institution to make a good faith effort to meet the credit needs of its community and gives rather broad powers to the financial regulatory agencies to encourage compliance. Thus, the examinations of financial institutions will now include an assessment of efforts to meet community credit needs and this appraisal will be taken into account when applications are considered for new branches, mergers or acquisitions. For banks such as many of yours, rarely is there a question of involvement in the community. However, it is possible that some large banks may derive substantial deposits from local areas and concentrate their lending in national and international markets. In order to meet CRA standards, some large banks may become more interested in lending funds in low and moderate income areas or previously neglected local markets. In this case, many minority banks may be in an excellent position to draw new loanable funds into their market areas. Local community banks with knowledge of their markets may become valued participants in loans with larger banks. They may through such participations reduce their own positions in loans,

allowing them resources to participate in other loans and thus further diversify their risk.

But there are probably more changes to come. The Congress now has before it proposed legislation of a fundamental character, including a re-examination of the legislative ban to inter-state branching by banks. It is considering legislative action affecting banking in a number of other areas, most notably with respect to two issues -- automatic transfers and the burden of membership in the Federal Reserve System. At this time one can only speculate but there is a possibility that the Congress could enact new legislation relating to the range of financial institutions having to hold required reserves as well as the level of these reserves. At the same time, also under such legislation the Federal Reserve System might be required to charge for the services it provides to banks. Such charges would be designed to reduce the burden on banks of membership in the Federal Reserve System.

If this move toward explicit pricing does eventuate, the banking industry in general must be aware of what it costs to offer specific services to the public. This would be especially true in the case of automatic transfers and Negotiable Order of Withdrawal (NOW) accounts. Thus, small and minority banks will have a number of new options as to the services they may wish to offer the public. At this point, it is not clear whether it will be feasible or cost effective for all small and minority banks to offer all of the services of which banks will be capable in the new financial environment. Studies within the Federal Reserve System indicate, for example, that break-even size for individual NOW accounts may be as high as \$500. If that finding is about right,

smaller banks located in communities where per capita incomes are depressed may hesitate to offer such accounts to their depositors.

My aim in discussing banking legislation is to emphasize one key point: much of what happens in the banking industry in the years ahead will be the result of Acts of Congress recently passed and presently contemplated. These laws will significantly alter the environment in which financial institutions must operate. Out of it all one may reasonably expect higher professional and management standards, more vigorously enforced consumer protection measures, greater involvement of institutions in community development activity, more equitably shared burdens of required reserves among depository institutions, and higher costs of loanable funds as Regulation Q ceilings are gradually removed and ATS and NOW accounts become more widely used. But above all, there will be more intense competition not only among banks but also between banks and other depository institutions.

How can minority banks fit into this new more competitive environment? Not easily. Surviving in such an environment will be difficult for all banks. It will be especially so for minority banks. This is so because too many are far less than "optimum" size. Moreover, there are not competitive shelters of the kind that benefited the minority life insurance companies in their early years of development. Minority banks must face the chill wind of competition without the cushion of adequate resources, must enter the big game without adequate tablestakes.

I do not agree with those who say that minority banks are largely ornamental. In my view, they have a special and constructive role to play. The rationale -- not accepted by all -- for promoting the development of minority banking is that bankers who live in a community, know the subtleties

of its social interrelationships, appreciate the nature of its aspirations, are more likely to perceive productive ways of meeting legitimate credit needs than bank managers who do not live in or have cultural ties to that community. If correct, this should make better opportunities for minority banks to earn a reasonable profit on funds employed in their communities. In my judgment, this is a plausible rationale, despite the fact that few minority banks have been able to realize the potential benefits or returns inherent in their strategic positions. You and I know many people who earn relatively low incomes and would fail most creditworthiness tests but are doggedly determined to repay their debts. We also know some other types who exhibit all the trappings of creditworthiness but in the end turn out to have been bad risks. We know, moreover, of new businesses that by all conventional odds should never have made it, yet went on to become successful because of the nuances of community tastes and preferences.

The task of minority bankers in the years ahead, it seems to me, will be to utilize their experience, knowledge and insights into the communities they serve to uncover and attract the deposit funds that have, so far, largely escaped them and to find feasible productive projects in which these resources can be profitably employed. It will be difficult but I strongly believe it can be done and done effectively. However, it will take a kind of dedication that we have not yet seen.

Banking is business; business should be based on entrepreneurship; and entrepreneurship means using creative intelligence, imagination, and innovative techniques to achieve business objectives. A true entrepreneur welcomes the challenge of competition and relishes the opportunity to overcome seemingly insurmountable obstacles. Obviously, what is needed for the future is a heightened sense of entrepreneurship.

I have little if any specific advice to give you. You know or should know your markets and communities better than anyone else. There are a few general observations I might make. Larger banks have for some years been engaged in long-range planning and a number have developed quite refined techniques. Small and minority banks should follow a similar path.

In its simplest terms, long-range planning involves the determination of goals and objectives to be achieved over a suitable period (for example, five years) and setting forth the specific steps necessary to reach them. These decisions are reflected in the major items in the balance sheet and income statement projected for each year through the planning period. I always found it useful to make two sets of projections: one on the assumption of no changes in goals, programs or operating procedures; and one based on the assumption of success in the achievement of new goals, including the programs designed to implement them. As it turned out, there was usually a significant difference between the earnings projections based on passive acceptance of "normal" or "trend" growth and projected earnings resulting from programs designed to achieve specific new goals.

The importance of long-range planning is not that it provides any assurance that goals will be reached but that, in addition to giving some notion of what profits will be over the planning period on various assumptions, it forces one to consider in some detail whether a bank's goals are realistic. It requires one to think about the future in ways perhaps not frequently done: about anticipated market and community changes; about new sources of deposits; about possible new lending programs;

about trends in the local economy; and about the probable future course of interest rates.

I emphasized my view that you may expect to face an increasingly competitive environment. I would like now to point to an area where the advantages of cooperation appear large and rewarding, that is, loan participations among minority banks and among minority banks and larger regional or national market banks. Arranging loan participations may enable a group of minority banks to step up to financing projects of high feasibility but which are beyond the resources of a few banks. And, as noted earlier, minority banks through participations with large banks can act as a catalyst in bringing new funds into community development projects. By expanding loan participation activity, minority banks may not only add to the breadth and variety of their lending experience but also increase their exposure to new ways of doing business, thereby reducing their isolation from "main-stream" banking.

Finally, a word of caution. Minority banks should avoid becoming "aid-dependent" or "aid-addicted." There has been a strong push in recent years for government and other special assistance programs for minority banks. I strongly support such programs if they are properly administered and adequately funded. The danger is that political winds may shift, government departments be reorganized and programs may be abruptly canceled. We all remember the Treasury Department's preferential deposit program that was only to be followed by Congressional action requiring the payment of interest on tax and loan accounts. Some outside aid, both technical and financial can be highly beneficial if skillfully utilized. But a bank should not allow itself to slip into a position where such

assistance becomes a permanent crutch, since obviously, a sudden withdrawal or change of programs could threaten its survival.

Looking ahead to the banking environment of the next decade, I am not overwhelmed with gloom. In my view, it will be a difficult, trying and stressful environment for all banks. At the same time, it will be an environment laden with opportunities for true entrepreneurs. The fact that minority banks have survived -- and some have prospered up to the present -- suggests to me that they will prosper in larger numbers in the 1980's.