

# FEDERAL RESERVE BANK OF SAN FRANCISCO



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1989

## 1989 ANNUAL REPORT

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The cover painting, created by William Rosenthal, Graphics Specialist, suggests the balancing and creative tension that Bank management will experience as the Bank faces the challenges of the 1990s.

The interviews inside question key Bank management on anticipated developments in their particular areas and the steps the Bank is taking to address these challenges. The 1988 *Annual Report* looked back at the Federal Reserve's first 75 years. The 1989 *Report* looks forward to preparations for the next 75 years.

The Federal Reserve Bank of San Francisco is one of twelve regional Reserve Banks which, together with the Board of Governors in Washington, D.C., comprise the nation's central bank.

As the nation's central bank, the Federal Reserve is responsible for making and carrying out our nation's monetary policy. It also is a bank regulatory agency, a provider of wholesale priced banking services, and the fiscal agent for the United States Treasury.

Federal Reserve Bank  
of San Francisco

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The Federal Reserve Bank of San Francisco serves the Twelfth Federal Reserve District, which includes the nine western states—Alaska, Arizona, California, Hawaii, Idaho, Nevada, Oregon, Utah and Washington—Guam, American Samoa, and the Northern Mariana Islands.

This District is the largest in terms of geographic size and population, and the busiest in terms of economic activity considering employment, income and the diversity of industries—all of which affect the structure of banking in the West.

To serve this expansive region, the San Francisco Reserve Bank has five offices: the headquarters in San Francisco, and offices in Los Angeles, Portland, Salt Lake City, and Seattle. Each office provides financial services to the public and banking institutions in its locale.

# From the Chairman

It has been an honor to preside as Chairman of the Board of Directors on the seventy-fifth anniversary of the Federal Reserve Bank of San Francisco. A diamond jubilee is always cause for celebration because it is a measure of past achievements and implies that one has been well prepared for the future.

Directors have assisted in that preparation throughout the Bank's history. We offer independent assessments of business conditions for consideration in setting monetary policy. We also contribute business expertise in overseeing management and financial issues.

From a businessperson's perspective, the Twelfth Federal Reserve District is blessed with an unusually dynamic economy that draws on an enormously diverse, talented, and growing labor force.

Fundamental strengths that should stand the region in good stead over the long term include its proximity to Asia and the Pacific Basin, its leadership in high-technology research and development, a rich supply of natural resources, and its overall large size and diversity.

Trade with many rapidly growing Asian countries will continue to stimulate both export sales and the financial activities that keep our port cities bustling. Indeed, trade and service industries accounted for more than 60 percent of the West's job growth in the past five years.

Our technological leadership should help us in such manufacturing sectors demanding innovation as semiconductors, biotechnology, and computers. The strength of the commercial aircraft industry plus the District's overall health should mitigate the effects of declines in defense contract activity.

Natural resources and recreational attractions would seem to ensure a basis for further growth. During the past two years, most western farmers have enjoyed healthy income, lumber and paper producers have benefited from record output, and there has been a resurgence in copper, gold, and silver mining. Entertainment centers and the West's scenic wonders will continue to draw more and more visitors from throughout the world.

Historically, our economic, social, and natural resources have resulted in population growth far exceeding the national average. We can expect future growth to stimulate further the demand for goods and services.

Future growth will also present some of our major challenges. Residents of established metropolitan areas, for example, are already familiar with environmental concerns, overburdened transportation systems, and high housing costs, to say nothing of the problems of crime, drugs, and the education crisis.

In addition, while the West as a whole tends to do well, economic growth continues to be uneven across its various parts. Economic conditions in Alaska depend strongly on the performance of the oil industry; mining activities are more important to the Salt Lake City area. Arizona continues to adjust to a downturn in its real estate prices at the same time that real estate and construction activities are picking up in the Puget Sound area and other parts of the Pacific Northwest. California also is experiencing a slowing of real estate activities from their heated pace of the last few years.

The Federal Reserve will continue to play an important part in establishing an environment that fosters continued economic health.

The participation of the public, through Reserve Bank directors, in the Federal Reserve's decision-making is unique among government institutions. It is a tradition we are proud to uphold.

In closing, I want to express the thanks of the Board to all the employees of the Bank who performed so well and with such dedication at the time of the Bay Area earthquake. As Bob Parry reports in his comments, the Bank's performance in the face of this challenge was extraordinary. We are very proud of the courage and skill of our people.

*Robert F. Erburu*

**Robert F. Erburu**  
**Chairman**



From left, Carolyn S. Chambers, Deputy Chairman, Robert T. Parry, President, Robert F. Erburu, Chairman, and Carl E. Powell, First Vice President.

# From the President

As Bob Erburu has pointed out, a seventy-fifth anniversary can be an auspicious event. We at the Federal Reserve Bank of San Francisco have tried to make sure our seventy-fifth is an especially favorable indication of what is to come.

The Federal Reserve operates in an environment affected by advances in electronic technology and continual, major regulatory and economic changes.

We must respond to the challenges presented and exploit opportunities in every facet of our operations. In the pages that follow key staff members talk about some responses that involve the whole Federal Reserve System and others that are initiatives particular to the San Francisco Reserve Bank and regional conditions.

In the area of wholesale banking services, our goals are as broad as they are simple. We strive to improve our services to financial institutions in all market segments so their customers, and ultimately the public at large, will benefit from an improved payments system.

The watchwords in this area are consolidation, standardization, and automation. The approaches represented by those words have helped us enhance the quality, efficiency, and integrity of our services.

Our preparedness was proven after the October 17 earthquake in the San Francisco Bay Area. We recovered our computer system and communications network within two-and-a-half hours with no loss of data. According to our contingency plan, the Los Angeles Branch was prepared for a relocation of San Francisco functions, but relocation proved unnecessary. All critical customer services were provided to financial institutions the next day, as scheduled.

Another of the Federal Reserve's vital policy responsibilities is the supervision and regulation of bank holding companies and state-chartered member banks. We have the charge of encouraging and maintaining a safe and sound banking system and of ensuring compliance with community development legislation.

The tremendous challenges in this area include the need to reform the deposit insurance system, to plan for expanded bank powers, and to cope with extended interstate banking activity in our District in 1990. To meet these challenges, we require a skillful and knowledgeable work force. We are committed to the ongoing education of examiners and continue to do research in current banking issues.

I also would like to mention the establishment at our Bank of the Center for Pacific Basin Monetary and Economic Studies. The countries of the Pacific Basin are of growing importance to the United States. For some time, our trade with them has exceeded our trade with the European community. Here at the edge of the Pacific Ocean, we are particularly well-situated to make a unique contribution through the Center to policy-oriented research on monetary and financial issues.

In preparing for a constantly changing environment, we are guided by well-established goals and a sense of responsibility to the public and financial institutions. We are here to serve, in a responsive and efficient manner.

Our success in doing so, for so many decades, is a tribute to the contributions of our staff and directors. Indeed, they are the ones who keep us continually revising and innovating, always adapting to change and preparing for the future.

I thank them, including those directors who completed terms of service in 1989: on the San Francisco Board, Rayburn S. Dezember (Chairman of the Board and Chief Executive Officer, Central Pacific Corporation, Bakersfield, CA) and John C. Hampton (President and Chief Executive Officer, Willamina Lumber Company, Portland, OR); on the Los Angeles Branch Board, Howard C. McCrady (Vice Chairman, Valley National Corporation, Phoenix, AZ); on the Portland Branch Board, Paul E. Bragdon (Assistant to the Governor for Education, State of Oregon, Salem); on the Salt Lake City Branch Board, Robert N. Pratt (President and Chief Operating Officer, Bonneville Pacific Corp., Salt Lake City, UT); and on the Seattle Branch Board, Carol Nygren (Partner, Laventhol & Horwath, Seattle, WA), Irma Goertzen (Goertzen & Associates, Health Care Consultants, Seattle, WA), and William S. Randall (Chairman, President and Chief Executive Officer, First Interstate Bank of Washington, N.A., Seattle, WA).



**Robert T. Parry**  
**President**

## Hang-Sheng Cheng, Vice President, International Studies

*The San Francisco Reserve Bank will open the Center for Pacific Basin Monetary and Economic Studies starting in 1990. How did the Center come about?*



The Center is a culmination of 15 years' effort. This Bank was a pioneer in economic research in the Pacific Basin area back when very few people in the United States or anywhere else recognized the Pacific Basin's growing importance to the world economy.

Over the years, the Bank has conducted research on Pacific Basin economics, sponsored international conferences, promoted central bank cooperation by serving as the center institution for the Clearinghouse for Pacific Basin Central Bank Economic Research, and hosted visiting staff members from Pacific Basin central banks.

All these activities will continue under the Center but they will benefit from a more formal structure and an expanded scope. The Center will have four resident staff economists. In addition, it can accommodate up to three visiting scholars to interact with the staff economists and one another.

The Center will conduct research seminars and international conferences, and will have its own publications for worldwide dissemination.

*What issues will the scholars in the Center be focusing on?*



Being a central bank, we want this Center to focus on monetary and financial subject matters as they relate to macroeconomic developments and policies in Pacific Basin countries. Looking into the 1990s, we see two broad issues confronting all Pacific Basin countries.

The first one, of course, is trade. The Center will focus on the macro-economic aspects, that is, emphasize trade in relation to national output, domestic inflation, and economic growth, rather than trade's impact on specific industrial sectors.

The second issue is growing international financial market integration among Pacific Basin countries and its impact on national economic growth and the conduct of monetary policy. The U.S. financial market is the most sophisticated, but markets in the other countries are rapidly evolving. Given our superior technology in financial businesses, our experience, and our expertise, we have a lot to contribute to enhancement of knowledge in this area.

*What is the significance of this Center?*

We're at the beginning stage. But it's exciting to build something of enduring value to the Federal Reserve and the nation.

We live in an interdependent world. As such, the importance of the Pacific Basin to the U.S. economy will certainly continue to grow into the next century.

The United States is very lacking in its understanding of the economies of the region. The Center can do its part to enhance awareness and understanding.

You might call the Center the Federal Reserve's contribution to international understanding. It will serve as the Federal Reserve's listening post on the Pacific Region.

**Marilyn Garland**  
**Manager of Employment and Employee Relations**

*What changes does the Bank expect in the workforce of the 1990s?*



*What kind of work environment will these changes result in?*

*These policy changes seem to entail a change of attitudes on the part of employers.*



We expect major changes, some stemming from demographic patterns and some from societal changes.

For example, we'll be looking at the maturing of the baby boom generation and the emergence of what we might call the "baby bust" generation. We also anticipate more minorities and females in the workplace.

With the on-going advances in technology, we see increased demand for skilled workers, especially those proficient in the use of personal computers and other high-technology applications.

At the same time, there is growing concern about the adequacy of education and the qualifications of entry-level workers.

For one, the competition for qualified workers will become more intense as a result of the baby bust generation.

We, as an employer, will need to offer more adaptable programs for salary and benefits administration, as well as policies that can accommodate part-time work, job sharing, flexible schedules, etc.

We will also have to focus efforts on training and development to ensure that the skills of employees are up-to-date and that entry-level workers have the necessary basic skills.

The 1990s will be a decade of change for both managers and workers. The Bank will have to exhibit flexibility and sensitivity in order to adapt to the changing work force.

This will enable us to effectively utilize *all* of our human resources since each person, regardless of race, sex, and age, and perhaps because of those differences, has a positive contribution to make to the future of the Bank.

We're fortunate in that we have already benefited from the diversity of the Twelfth District. We are confident that our staff will be able to respond to the challenges of the future as well.

**Sara Garrison, Senior Vice President, Finance and Product Management, and Manager, System Electronic Access Functions Office**

*From all accounts, banking has embraced the era of electronics. Electronics can speed the flow of payments, ensure timely delivery and accuracy, provide additional auxiliary information such as tracking and control procedures, and offer greater security. How does the Federal Reserve intend to fit into this electronic environment?*



*Can you be more specific?*



Don't forget electronics offers tremendous cost-containment and productivity advantages over a manual, labor-intensive environment.

The Fed is responsible for the efficiency of the payments mechanism. Since the basic payments mechanism is already very efficient and smooth-running, the way we can improve upon it is by encouraging broader use of electronic access vehicles to take advantage of the efficiency and quality gains that can be made through further automation.

During the past few years, we've taken a forward-looking approach by standardizing and improving the electronic payments system. Our strategic issues include what types of services or service enhancements we need to connect electronically, how we can respond to the increasing demand for more timely information services, and, probably equally importantly, what types of security we need in support of various services.

We're also looking at how we can encourage electronic access in those areas where it has not been used extensively, such as check payments and securities services.

In other words, we are promoting a variety of electronic mechanisms to improve the payments mechanism.

For example, we are standardizing and simplifying computer-interface protocol specifications so that more institutions can link up with us.

We're trying to get smaller depository institutions to use a standard intelligent terminal software package for access to Federal Reserve services. We are now in the process of converting from software products that are unique to each Reserve District to one standard software package developed by the New York Fed, called FEDLINE II. FEDLINE II is an integrated, fully secure software package that gives access to all our services.

We're also putting out several different versions of our bulk data software, for batch-based systems (as opposed to transaction-based systems), so we can accommodate more of our medium- to large-volume user base.

And shortly, we'll be promoting a low-volume, delivery-only PC device geared toward ACH delivery for our small volume depository institutions. These users, who may only receive a data file from the Federal Reserve two to three times a month, are looking for a very simple, very inexpensive solution for receiving electronic ACH data from us.

**John Gleason, Senior Vice President, District Operations,  
and Chairman of the System Subcommittee on Securities and  
Fiscal Services**

*In what new directions do you see  
Treasury Securities Services moving?*

The Federal Reserve Banks and the Treasury are moving in the direction of making Treasury securities much more accessible to individual investors. At the same time, we're streamlining and automating the process. We're trying to replace paper handling with all-electronic processing.

We're moving in these directions very rapidly. I'm talking about a horizon of the next 5 years, not 10 or 15 years out.

*What are some examples of this  
orientation?*



The individual investor is already using Treasury Direct, which is a book-entry system in which investors have their own Treasury accounts, and payments for principal and interest are made directly into the investor's checking or savings account at their financial institution.

Treasury Direct has made the Federal Reserve the place to go to buy Treasury securities. As a result, our services have become much more oriented toward the retail customer.

In 1990 and 1991, most Reserve Banks will be converting to the Treasury's Regional Delivery System for issuing Savings Bonds. Under this program, Savings Bond issuing agents will transmit applications and payments from their customers to our regional processing centers, which will print the bonds and mail them directly to the purchasers.

In 1990, we'll also be installing a new Treasury Tax and Loan (TT&L) system at all twelve Reserve Banks. That will enable us to adapt quickly to changes in Treasury rules, and to implement those changes concurrently for all TT&L depositories.

*What other changes in the securities  
services environment can you identify  
and what goals will guide the  
Federal Reserve's response to this  
environment?*



There is constant innovation in the types of securities being issued, and, as in the case of stripped securities, new uses are being found for existing instruments.

Securities markets are also becoming more international in scope. But even within the United States, more government agencies are entering or reentering the securities market and using the Federal Reserve as their fiscal agent.

We're taking a fundamental look at the whole securities transfer system. What we're aiming for is a system that can adapt more quickly to different types of marketable instruments and that will enable us to make changes simultaneously everywhere.

One option is a more centralized system that would allow us to change our capability nationwide by testing and installing in only one site.

We are also considering building in the capability for extended processing time frames, potentially to the point of supporting round-the-clock securities transfers.

**Charlie Huffstetler, Director, Custody Services  
Los Angeles Branch**

*With all the talk about electronic funds transfer, home banking via computer, and debit cards, is there a future for cash?*



*What are your plans for dealing with this currency deposit growth?*

*And in the long-term?*



Actually, currency deposits throughout the Federal Reserve System are growing faster than we anticipated. We know what contributes to growth—economic development, ATM use, cash policies of depository institutions and how they manage their own vault space, and so on—but it's more difficult to establish the relationships among the different factors and the unique contribution of each.

The rate of growth in the Twelfth District is higher than the national average. In Los Angeles alone, we receive 7-10 million notes and ship out 7-8 million notes a day.

We are actually being crowded out of our vault! To us, it doesn't look like a cashless society will materialize any time soon.

Our challenge is to manage this deposit growth. We have a zero-loss standard, that is, we do not lose a single penny of what institutions send us for safekeeping or processing. At the same time, deposit growth forces us to strive for more efficiency and productivity.

In the short-term, we have been able to squeeze as much of the artificiality out of the volume growth as possible by better articulating and enforcing our cross-shipping policy. This policy says if an institution deposits currency with us, it cannot order currency of the same denomination from us five business days prior to or following the deposit of that denomination.

Long-term, we are concentrating on better storage, processing, and automation. Our first generation storage concept is containerization. We put currency in stackable modules so that we can use the vertical space in our vaults more efficiently. The second generation approach will most likely involve automated means of retrieving and stacking containers. We may use bar codes and mark sense technology to help with inventory control.

In 1990, we will begin replacing our present currency processing equipment. The equipment authenticates, counts and sorts currency, reads bills with lasers, and automatically destroys worn currency for replacement with fit or new. The new equipment will allow us to process more currency at lesser cost with fewer units. They will have about fifteen percent more capacity. We are also exploring ways to configure the equipment to increase productivity.

Finally, we have already begun reviewing facets of cash operations to find further opportunities for automation. We could use computers more thoroughly to monitor differences in cash counts when we debit and credit institutions' accounts; we could also use them for inventory control and management.

In the future, we might even establish remote currency processing units. Right now, these units are located in each of our Branch offices and in San Francisco. But because the Twelfth District encompasses such a large geographic area, units located nearer large and distant financial communities could reduce operations and transportation costs while increasing convenience for everyone concerned.

**Gene Thomas, Senior Vice President  
Supervision, Regulation, and Credit**

*How will more interstate banking affect supervision and regulation?*



We already have some experience with interstate supervision and regulation because many bank holding companies in our District own banks in more than one state.

The process is moving more and more toward an examination of the consolidated entity, where the upper tier company—say, the bank holding company—is the focus of attention as the “umbrella” over the entire organization. We rely on regulators in other districts to examine and supervise the subsidiary banks that reside in their areas. Our inspectors collect and analyze that information, incorporate it into a consolidated report, and present their findings of the overall financial condition to the management and directors of the upper tier.

There’s always a very high level of cooperation between federal and state banking agencies. We expect interactions will continue to intensify, and the linkages will be broader and filled with greater amounts of information.

*To compete in a varied financial marketplace, banks have been asking for expanded powers such as investment banking, insurance, and real estate development. What different skills would this demand of regulators?*



I don’t know that it requires different skills, but it will require us to apply our skills to a broader range of supervisory issues. Examiners are very good at examining credits on a micro basis, and the financial condition of holding companies on a macro basis. The introduction of new products and expanded powers is recognized as one of the major training challenges and we are putting a lot of effort into the ongoing education of examiners.

The most fundamental change that has taken place recently in the financial industry has been deregulation. Congress repealed many regulations that, for decades, governed the behavior of institutions. As a consequence, supervision, which assesses the riskiness of that behavior, had to be bolstered. Supervision has become more important as the means of ensuring that risks are well-managed and contained, or accounted for by higher levels of bank capital.

One of the propositions repeatedly put forth is functional supervision, whereby existing agencies would regulate new powers legislated in their areas of responsibility. For example, if holding companies were authorized stock underwriting powers, the Securities and Exchange Commission, already the regulator of the stock market, would assume supervision of that function. Functional supervision, of course, would make the idea of consolidated supervision more important.

*How has the Federal Reserve planned for the future in supervision?*

In specific terms, we conduct planning sessions in the fourth quarter of each year where we draw up a schedule of bank and bank holding company examinations for the coming year.

In a more general way, since one cannot foresee specific developments that will unfold, we look at systems and organizational matters. These involve budgeting for adequate staffing, staff training, ensuring competitive compensation and the like so that we can be prepared and on call for almost any need.

As the central bank, we know we will be called on to do things considered extraordinary. Our participation in the interagency savings and loan intervention program in 1989 is an example. We provided teams of examiners who, for about a three-month period, participated in the intervention at seven S&Ls; also, the discount window extended credit to a large ailing thrift experiencing a liquidity strain.

## Kelly Walsh, Community Affairs Officer

*In 1989, the federal regulatory agencies issued a joint statement affirming the importance of the Community Reinvestment Act (CRA). The CRA was designed to end redlining and other discriminatory policies. What is the significance of the new policy statement?*



The policy statement was meant to guide regulated institutions and others on the requirements of CRA, and to identify appropriate ways for institutions to meet their obligations under the Act. The policy statement was developed from the experiences of the supervisory agencies over the last eleven years.

For a bank to be truly effective in its CRA programs, the statement says that it must make CRA a part of its planning and management process. CRA is foremost a lending activity; it should be dealt with as a matter of policy inside the institution; and it should be known and understood throughout the organization.

The policy statement is enlightening in other areas as well. It specifies that the regulators, in their evaluation of a bank's CRA performance, will no longer put much reliance on promises of future performance. It also encourages banks to expand their annual CRA statements to include descriptions of efforts to ascertain community credit needs, of services designed to meet those needs, and of programs to market such services effectively.

The policy statement also has a message for community organizations. The regulators expect those organizations to open up and maintain communications with financial institutions to make their needs and concerns known. Community organizations are encouraged to comment on a bank's CRA performance at the earliest possible time and not to postpone conveying their concerns until an application for business expansion is filed by a bank or its holding company.

*How does the Fed foster the goals of CRA?*

Most of our community affairs function is directed at facilitating communication between banks and their communities and encouraging the establishment of various programs—lender consortia, community development corporations (CDCs) and public/private partnerships—to get funds into areas that are underserved and in need of economic development.

We are proud to have helped in the formation of several programs in recent years to provide affordable housing finance and small business lending in distressed commercial areas. We have also provided guidance and support to organizers of CDCs within the district.

*What are some of the future challenges for CRA?*



Banks are now providing more leadership in addressing their communities' needs than ever before, and we foresee this pattern continuing. Banks have become more sensitive to the needs of their communities; they are more willing to consider creative ways to serve their communities; and they have found that community development lending can be profitable.

But there are still tremendous unmet credit needs in our communities. The need for affordable housing is acute, and there is an increasing need for improved flows of capital to the small business community in virtually every town and city. There also continues to be a need for resources to enhance rural economic development efforts. These are major challenges to people and institutions with an interest in the economic vitality of their communities.

**Larry Washteyn, Senior Vice President  
Computer Services Group**

*What is a "communications network" as you would use the term?*

On voice communications from telephone to telephone, it's everything between the two telephones that carry the voices through. For data transmissions, it could be everything between two computers.

An analogy is the line between two dixie cups. Our concern is how to improve and control the string.

*Communications has become important as its own area of study, almost distinct from what occurs on the communications network. Why?*

Long ago, we recognized the importance of electronic access in funds transfer because of the significant business benefits it confers. Communications networks are key to electronic transmissions, and now we're looking to networks to do more.



We're also recognizing that communications networks offer us real potential for changing how we conduct aspects of our business. For example, they are required to support centralized applications and functions, consolidation, and going to regional processing.

The idea that we could process checks in this District's northern offices but locate the data center in San Francisco is only feasible through an appropriate communications network.

Communications networks also play a vital role in disaster recovery. They not only support but make possible a national disaster recovery site, or various regional and buddy systems to back up the portion of the system that has been struck down.

The communications environment is also increasingly important in defining and providing aspects of security for data transmissions. It allows us to control access to the network and to ensure privacy through encryption.

*What has the Federal Reserve planned in terms of new communications networks?*



The Conference of First Vice Presidents has approved a new network design for implementation between 1991 and 1994. It would completely replace the current interdistrict network and the twelve district networks with one unified, integrated, national, and more cost-effective network.

It's meant to satisfy business requirements for increased reliability and availability, for handling much higher volumes of data, and for integrating all communications—voice, data, and even video.

What we hear on a national level is that we're probably getting into a 24-hour a day, 7-days a week network operation in the 1990s.

We want that network to be transparent to Fed users and customers. That is, we want them to be able to focus on the business they're doing without being distracted by how they're doing it or where the processing center they're communicating with is located.

## **Gordon Werkema, Vice President, San Francisco Operations**

*What kind of environment will the Fed face in check services in the future?*

An environment with interstate banking on a nationwide basis is on our doorstep. Our preliminary research indicates that depository institutions will want expanded information services, which we traditionally call payor bank services, so they can improve cash management services they provide to their customers.

The realization of processing technologies in checks also will greatly transform our environment. We expect to automate more of check processing, for example, in the adjustments process, which has been labor-intensive.

We will witness the gradual evolution of checks toward a combined paper and electronic payment system, whereas to date it has mainly been a paper-based system.

*What are some examples of payor bank services?*



Payor bank services involve the electronic extraction of information from paper checks, and in many instances, transmitting that information to the paying bank electronically. That information can include the magnetic ink line of processed checks or totals organized by the bank's key corporate accounts.

Payor bank services may be especially useful for institutions in remote locations, such as Alaska and Hawaii. As paper checks make their way to those locations, the information contained in them will have been transmitted almost immediately after we processed the checks, allowing the institutions to update accounts more quickly and provide superior service to their customers.

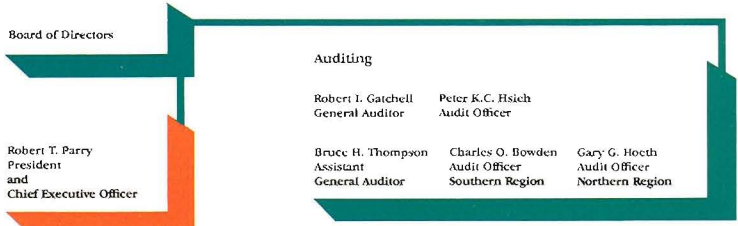
Further down the road, a refined payor bank service could exploit image processing. Image processing captures the entire check front and back in digital form. Electronic images of checks can then be transmitted to paying banks and paper checks can remain at the initial point of entry. In fact, we recently completed a pilot image project in our government check operation that has demonstrated clearly the benefits of this technology.

*These technological advances will offer institutions a competitive edge, but they must involve a cost as well. What about institutions that are not as sophisticated?*



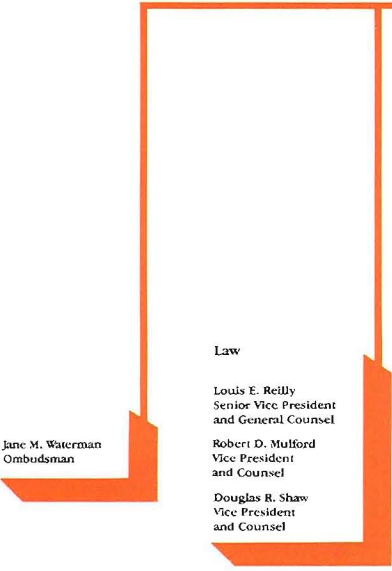
Above all, we must create check products that serve all depository institutions' needs. We are conducting research that will indicate what electronic check services institutions want and how much they are willing to pay for them. In 1990, we will start developing products based on financial institutions' and the Treasury's needs in this area.

Having said that, I hasten to add that the industry looks to the Fed to be a low-cost provider of basic check clearing services. We intend to continue to meet that need while seeking to develop check processing technologies for the future.

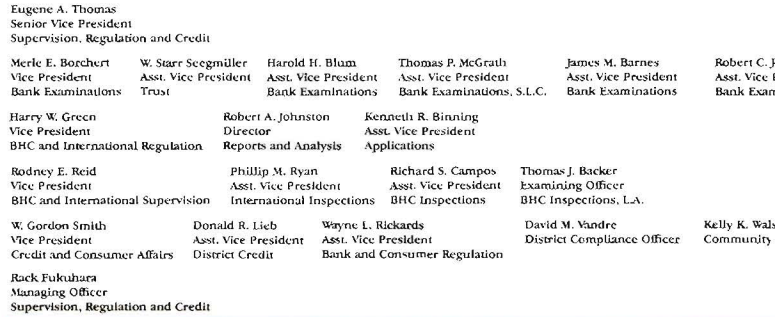


Robert T. Parry  
President  
and  
Chief Executive Officer

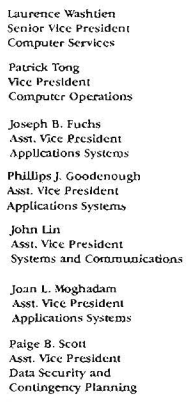
Carl E. Powell  
First Vice President  
and  
Chief Operating Officer



**Supervision, Regulation and Credit**



**Computer Services**



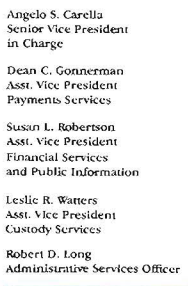
**Secretary's Office**

Elizabeth R. Masten  
Vice President  
and Secretary of the Board

**Personnel and Administrative Services**



**Portland Branch**

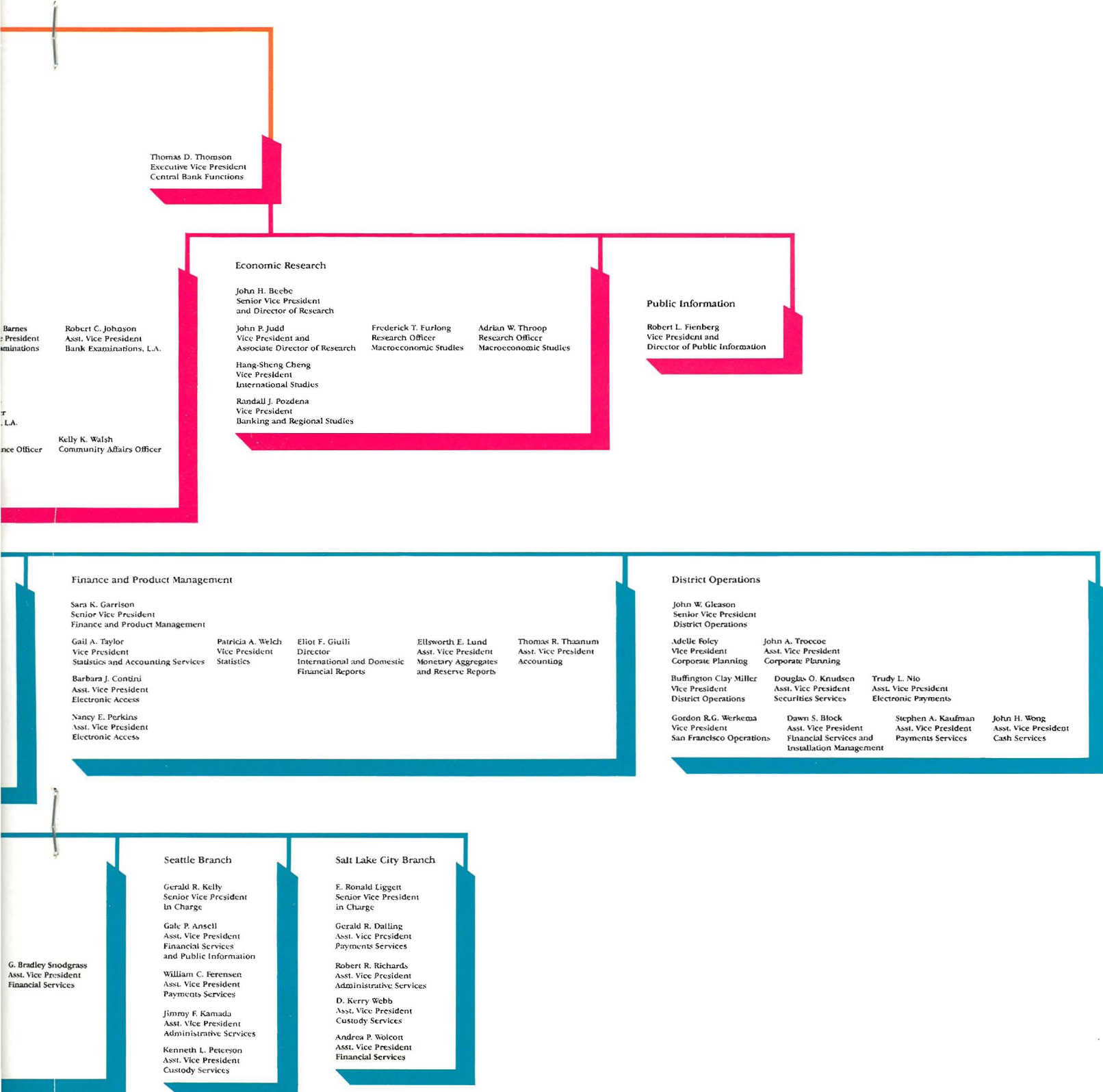


**Los Angeles Branch**



# Organization Chart

February 1, 1990



# Highlights of 1989

## Economic Research

Domestic macroeconomic research focused on the sources of business cycles—including aggregate demand and supply factors, and financial constraints; on forecasting current quarter real GNP; on the inflation-unemployment trade-off; on the effects of monetary policy on federal government revenue; and on potential targets of monetary policy, including commodity prices, nominal income, and the price level.

International research considered the usefulness of exchange rates as targets for monetary policy, the impact of fiscal policy on interest rates in the setting of international financial integration, and the role of exchange rates in determining trade surpluses and economic growth in certain Pacific Basin countries.

Banking and financial markets research focused on the market's perception of bank risk, the causes of Japanese entry into California banking, price behavior in California deposit markets, funds transfer system risk, and deposit insurance reform. The economists directed drafting of a position paper on insurance reform for the Council of Federal Reserve Bank Presidents.

Regional economic research studied regional economic cycles, natural resource pricing, and agriculture and agriculture credit markets. Bank economists provided support to the Bank President's chairmanship of the San Francisco Bay Area Economic Forum and produced a major paper on regional transportation problems.

An academic conference focused on the role of supply-side and financial factors in business cycles, and financial factors and risk in banking.

The program of Asian visiting scholars was expanded in preparation for the opening of the Center for Pacific Basin Economic and Monetary Studies in 1990.

## Public Information

An expanded media relations program involved meetings with editorial staffs and reporters and senior management and the issuing of news releases on bank developments and economic research to enhance public awareness and understanding of the Federal Reserve.

The Salt Lake City Branch installed a new lobby exhibition explaining branch activities and their relation to the Federal Reserve System.

The economics education effort involved offering workshops for high school teachers in Oregon and Utah and increased direct contacts with school districts. In addition, a second computer-animated video about money's relationship to spending was completed for free distribution to high schools nationwide.

## Supervision, Regulation, and Credit

Overall, the financial health of state member banks was good and improving; earnings at most banks increased and the volume of asset problems was declining.

An intensive program of cross-training for commercial and bank holding company examiners was developed along with a comprehensive on-the-job training program for two staff members from the People's Bank of China.

Examinations at seven troubled savings and loans were conducted as part of the interagency response to national thrift problems. This effort was an addition to ongoing examination responsibilities and was the second largest commitment of examiner resources within the Federal Reserve System.

Also in connection with thrift problems, the Credit Unit participated in a joint lending program to troubled savings and loans and established a warehouse to control collateral security.

At year-end, 21 state member banks were subject to special supervisory attention, down from 26 at year-end 1986.

Applications to acquire additional banks and nonbank companies increased significantly with a large number representing interstate bank acquisitions. As a result of applications approved, the Bank extended its supervisory purview over additional banks and other companies in the Twelfth District.

A financial reporting system was redesigned to provide better access to financial data as well as to enhance data manipulation and report-generating capabilities. A System application for information on the structure of banking organizations was installed and preparations were made for a national database effort, the National Information Center.

A Community Affairs Officer was newly appointed and the Community Affairs Unit sponsored or participated in several community development conferences around the District. The Unit also completed three community profiles in accordance with the community needs assessment program to identify community credit needs and opportunities.

Major focus was directed at contingency planning and implementation of a same-day disaster recovery capability which met the test following the October earthquake.

Computer-interface customers were converted to new communications protocols, FLASH or FRISC, that provide increased security, reliability, and integrity. Institutions were fully converted to the use of the structured format for third party information in Fedwire messages.

Full day availability on Fedwire increased from 99.62 percent in 1987 to 99.89 percent in 1989—the best among Federal Reserve Banks; critical hours availability increased from 99.86 percent in 1987 to 100 percent in 1989.

## Funds Transfer

## Automated Clearinghouse

Efforts to promote electronic access (versus transfer of information by paper or magnetic tape) to automated clearinghouse service continued to meet with success as 85 percent of all automated clearinghouse return items were submitted electronically—the highest level of automation in the Federal Reserve System.

Full back-up capability between San Francisco and Los Angeles offices was established in the event of disaster, which proved unnecessary after the earthquake.

Already strong performance in the Interregional Exchange continued to improve, averaging a 99.7 percent success rate.

## Electronic Access

Efforts focused on standardizing electronic access mechanisms to achieve greater consistency in product offerings.

Implementation of a mainframe-based electronic access database improved the internal system for managing customer information.

FEDLINE II, an integrated software package that allows depository institutions access to all electronic Federal Reserve services, featured two new services: origination of ACH forward items and online access to securities transfer system.

## Check Services

New check processing software was put in place in the San Francisco office, laying the foundation for Seattle, Salt Lake City, and Portland offices to process checks locally using the consolidated San Francisco data center.

Tests of digital image technology demonstrated its successful use in a production check processing environment; potential future benefits include expedited flows of information, improved records and audit trails, and lower transportation costs.

## Securities and Fiscal Services

Ninety-seven percent of Savings Bond volume was converted to E-Z Clear, which processes paid bonds in the check clearing system.

Securities transfer operations and definitive collateral handling in the branch offices were consolidated into the San Francisco office.

Full back-up capability for securities transfer service in the event of disaster was established in Los Angeles for the San Francisco office.

A new Treasury Information Center in the lobby of the Salt Lake City Branch gives securities customers access to information on marketable Treasury securities and Savings Bonds via touch-screen computer units.

Service availability for securities transfers averaged 99.98 percent for full days and was 100 percent during critical hours in 1989—the best performance among Federal Reserve Banks.

A newly formed Cash Automation Steering Committee will develop a five-year plan to maximize automation in currency handling.

Seven remote coin terminals operated by private coin facilities verified and warehoused coins, thereby improving access to supplies and reducing the costs of transportation and operations.

Preparations were made to install second-generation currency processing equipment.

## Cash Services

## Summary of Operations

	Volume (in thousands)		
	1987	1988	1989
<b>Custody Services</b>			
Cash Services			
Currency paid into circulation	3,044,958	3,207,649	3,405,037
Coin paid into circulation	5,443,894	5,468,011	5,015,454
Food coupons processed	275,531	295,264	309,852
Securities Services			
Savings Bonds original issues	3,835	3,534	3,437
Savings Bonds redemptions processed	217	283	278
Other Treasury original issues**	128	142	396
Book-Entry Securities processed	303	303	685
<b>Payments Services</b>			
Check Services			
Commercial checks collected	2,853,718	3,022,928	3,082,631
Government checks processed	87,945	83,867	82,827
Return items processed	32,090	35,714	37,676
Electronic Payments Services			
Wire transfers processed	13,285	14,224	15,431
Automated clearinghouse transactions processed	174,933	210,867	245,740
<b>Discounts and Advances</b>			
Total discounts and advances*	1,037	1,013	1,329
Number of financial institutions accommodated*	115	104	129

\*Whole number (not in thousands)

\*\*Includes volume processed in the Treasury Direct System



Management Committee members:  
 (From left)  
 Thomas D. Thomson, Executive Vice President  
 Carl E. Powell, First Vice President  
 Robert T. Parry, President  
 Michael J. Murray, Senior Vice President  
 Thomas C. Warren, Executive Vice President, Los Angeles



Branch Operations:  
 (From left)  
 E. Ronald Liggett, Senior Vice President in Charge, Salt Lake City  
 Carl E. Powell, First Vice President and Chief Operating Officer  
 Angelo S. Carella, Senior Vice President in Charge, Portland  
 Thomas C. Warren, Executive Vice President in Charge, Los Angeles  
 Gerald R. Kelly, Senior Vice President in Charge, Seattle

**Board of Directors  
Federal Reserve Bank of  
San Francisco**

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Federal Reserve Agent**

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Chairman of the Board and CEO  
The Times Mirror Company  
Los Angeles, California



Erburu

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President and CEO  
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Chambers

R. Blair Hawkes  
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Malad City, Idaho



Hawkes

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Hull

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and Vice Chairman of the Board  
Hawaii National Bank  
Honolulu, Hawaii



Luke

John N. Nordstrom  
Co-Chairman of the Board  
Nordstrom, Inc.  
Seattle, Washington



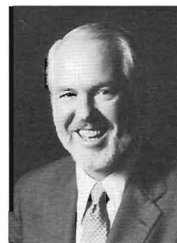
Nordstrom

William E. B. Siart  
Chairman of the Board, President  
and CEO  
First Interstate Bank of California  
Los Angeles, California



Siart

William L. Tooley  
Chairman  
Tooley & Co., Investment Builders  
Los Angeles, California



Tooley

James A. Vohs  
Chairman, President and CEO  
Kaiser Foundation Health Plan, Inc.  
and Kaiser Foundation Hospitals  
Oakland, California



Vohs

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Member**

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President and Chief Operating  
Officer  
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Fargo & Co.  
San Francisco, California



Hazen

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Andrew & Williamson Sales Co.  
Bakersfield, California

**Vice Chairman**

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and Former Small Business  
Advocate, State of Oregon  
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Baszile Metals Service  
Los Angeles, California

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President  
Shasta Foods International, Inc.  
Gonzales, California

Anne Chadwick  
Manager, Trade Policy-Agriculture  
California State World Trade  
Commission  
Sacramento, California

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James T. Heard Management  
Corporation  
Cerritos, California

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Corporate President-Retired  
Dairyman's Co-op Creamery  
Association  
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Avtech Corporation  
Seattle, Washington

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Price, Poulton & Company  
Burley, Idaho

Park Price, III  
President  
Park Price Motor Company  
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Leslie Tang Schilling  
President  
L.T.D.D., Inc.  
San Francisco, California

Henry J. Voss  
Director  
California Department of Food and  
Agriculture  
Sacramento, California

# Los Angeles Branch Board

The greatest strength of this region is its economic diversity and the absence of dependency on a single industry. The other great strength is its geographic location as part of the Pacific Rim.

The region's main economic challenge is to continue steady environmentally sound growth. The great size of this dynamic marketplace will also make uneven demands on the resources of this region.

## Board of Directors Los Angeles Branch

### Chairman of the Board

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Partner  
Jones, Day, Reavis & Pogue  
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Committee of the Board  
Coast Savings and Loan  
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Ignacio E. Lozano, Jr.  
Editor-in-Chief  
La Opinion  
Los Angeles, California

Richard C. Seaver  
Chairman  
Hydril Company  
Los Angeles, California

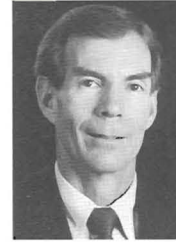
Harry W. Todd  
Managing Partner  
Carlisle Enterprises, L.P.  
La Jolla, California



Burke



Blakely



Jensen



Lovejoy



Lozano



Seaver



Todd

# Portland Branch Board



Hilliard



Compton

This region's sources of economic strength include a stable, well-trained work force, good available open spaces close to population centers, an abundant supply of water, low energy rates, and environmental protection policies that lead most of the states in the nation.

Our challenge is to diversify our economy away from a natural resource base, solve our reliance on property taxes as the principal source of education funding, and address the cost of doing business in Oregon, which may keep some companies from locating in our state.



Kimball



Phillips

## Board of Directors Portland Branch

### Chairman of the Board

William A. Hilliard  
Editor  
The Oregonian  
Portland, Oregon

Stuart H. Compton  
Chairman and CEO  
Pioneer Trust Bank, N.S.  
Salem, Oregon

Stephen G. Kimball  
President and CEO  
Baker Boyer Bancorp  
Walla Walla, Washington

Wayne E. Phillips, Jr.  
Vice President  
Phillips Ranch, Inc.  
Baker, Oregon



Stepp



Suran

E. Kay Stepp  
President  
Portland General Electric  
Portland, Oregon

Sandra A. Suran  
Business Consultant  
Lake Oswego, Oregon



Weight

G. Dale Weight  
Chairman of the Board, President  
and CEO  
The Benjamin Franklin Savings and  
Loan Association  
Portland, Oregon

# Salt Lake City Branch Board

This region has a world-class business environment poised for healthy expansion. Key strengths include a large well-educated and highly motivated work force, excellent transportation for moving raw materials and finished products, and an outstanding quality of life.

The region's primary challenges involve ongoing development of quality education programs and basic infrastructure elements to support further growth in the dynamic decade of the 1990s.

## Board of Directors Salt Lake City Branch

### Chairman of the Board

Don M. Wheeler  
President  
Wheeler Machinery Company  
Salt Lake City, Utah

Gerald R. Christensen  
President and Chairman  
First Federal Savings Bank  
Salt Lake City, Utah

Curtis H. Eaton  
Vice President; Manager,  
Community Banking Area and  
Member of Board of Directors  
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Zions First National Bank  
Salt Lake City, Utah

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Ralston & Associates Management  
and Training Consultants  
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Corporate Development Officer  
Albertson's, Inc.  
Boise, Idaho

D. N. Rose  
President and CEO  
Mountain Fuel Supply Company  
Salt Lake City, Utah



Wheeler



Eaton



Kelson



Rose



Christensen



Hanson



Michael

# Seattle Branch Board

Washington state is in a very favorable competitive position. Business costs are low while property values, rental rates, and labor costs favor economic growth. Alaska's major strengths will continue to include tourism, fishing, mining, and paradoxically, growth in the U.S. military presence. Military budget cuts bode well for Alaska where it is far cheaper to maintain active forces within reasonable great circle distance of potential world hot spots.

Major challenges to the region are financing and regulating growth. In banking, attracting sufficient capital will continue to be a major challenge. A significant concern is the decline of the Prudhoe Bay oil field. Explorations in new areas are showing promise, but the quantity and quality of crude left to be found is still unknown.

## Board of Directors Seattle Branch

### Chairman of the Board

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Chairman and CEO  
Alaska Air Group, Inc.  
Seattle, Washington

B. R. Beeksma  
Chairman of the Board  
InterWest Savings Bank  
Oak Harbor, Washington

Gerry B. Cameron  
President and Chief  
Operating Officer  
U.S. Bank of Washington, N.A.  
Seattle, Washington

Robert P. Gray  
President  
National Bank of Alaska  
Anchorage, Alaska

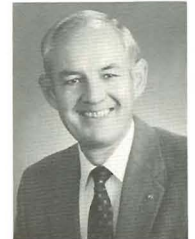
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Spokane, Washington

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Partner  
Foster, Pepper & Shefelman  
Seattle, Washington

George F. Russell, Jr.  
Chairman  
Frank Russell Company  
Tacoma, Washington



Kennedy



Beeksma



Cameron



Gray



Larison



Runstad



Russell

# Comparative Statement of Account

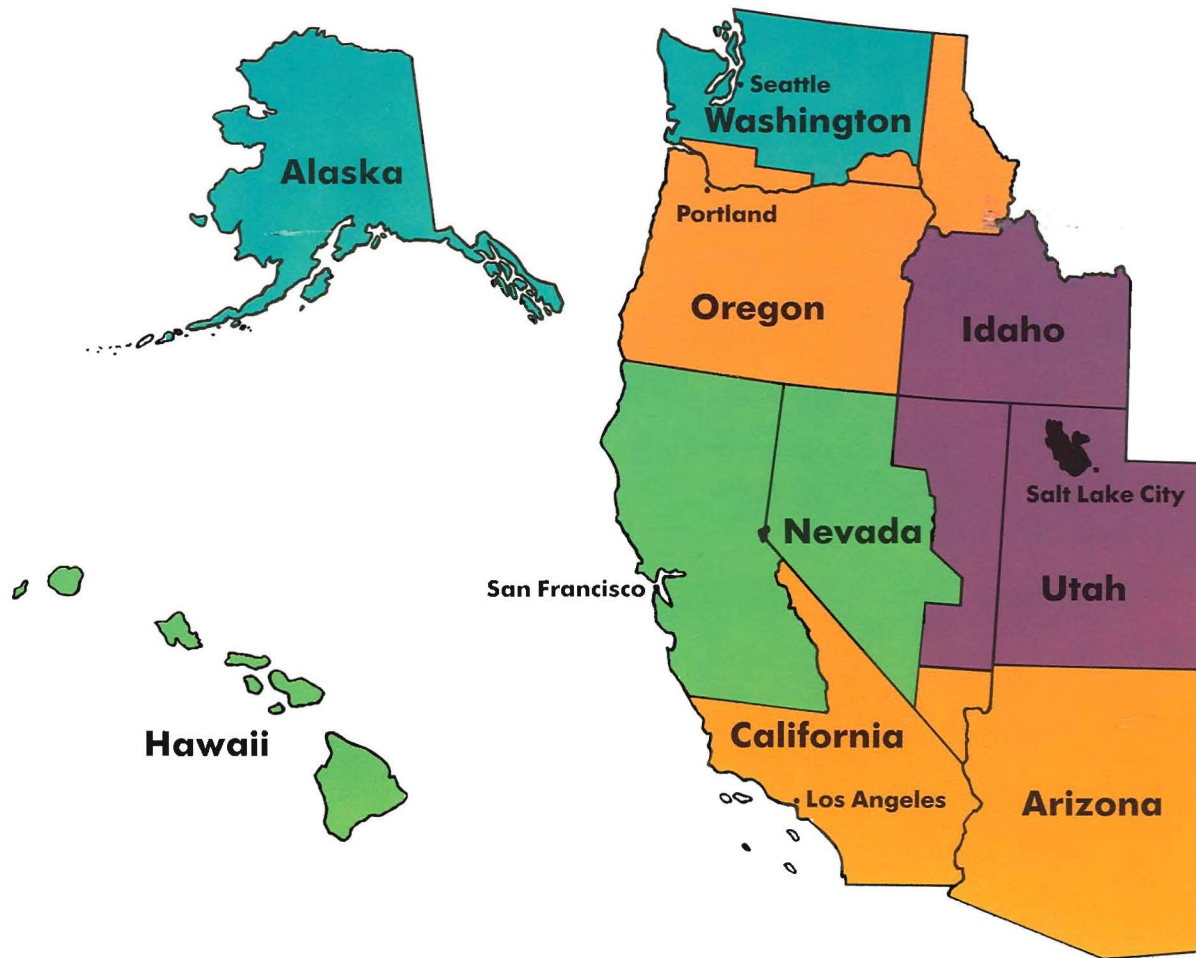
(Thousands of Dollars)

	December 31,	
	1989	1988
<b>Assets</b>		
Gold certificate account.....	1,402,000	1,429,000
Special Drawing Rights certificate account.....	992,000	670,000
Other Cash.....	77,206	66,964
Loans to depository institutions.....	220	10,301
Federal Agency obligations.....	795,571	894,497
United States Government securities:		
Bills.....	12,751,915	14,481,234
Notes.....	11,142,450	11,678,066
Bonds.....	3,757,221	3,842,942
<b>Total United States Government securities.....</b>	<b>27,651,586</b>	<b>30,002,242</b>
<b>Total loans and securities.....</b>	<b>28,447,377</b>	<b>30,907,040</b>
Items in process of collection.....	1,409,038	1,361,760
Bank premises.....	149,708	151,027
Operating equipment.....	32,015	35,103
Other assets:		
Denominated in foreign currencies.....	4,323,816	1,296,176
All other.....	1,000,609	643,112
Interdistrict Settlement Account.....	(2,007,957)	(2,057,633)
<b>Total assets.....</b>	<b>35,755,812</b>	<b>34,502,549</b>
<b>Liabilities</b>		
Federal Reserve Notes.....	25,863,292	24,845,628
Deposits:		
Total depository institutions-reserve accounts.....	7,546,848	7,449,120
Foreign.....	20,700	21,300
Other deposits.....	128,965	26,095
<b>Total deposits.....</b>	<b>7,696,513</b>	<b>7,496,515</b>
Deferred credit items.....	1,234,897	1,170,131
Other liabilities.....	357,290	407,965
<b>Total liabilities.....</b>	<b>35,151,992</b>	<b>33,920,239</b>
<b>Capital Accounts</b>		
Capital paid in.....	301,910	291,155
Surplus.....	301,910	291,155
<b>Total liabilities and capital accounts.....</b>	<b>35,755,812</b>	<b>34,502,549</b>

# Earnings and Expenses

(Thousands of Dollars)

	December 31,	
	1989	1988
<b>Current Earnings</b>		
Discounts and advances.....	5,748	2,243
United States Government securities .....	2,469,140	2,372,524
Foreign currencies.....	143,352	42,680
Income from services .....	78,683	73,807
All other.....	2,197	1,709
<b>Total current earnings</b> .....	2,699,120	2,492,963
<b>Current Expenses</b>		
Total current expenses .....	157,421	144,904
Less: reimbursement for certain fiscal agency and other expenses	0	12,061
<b>Net expenses</b> .....	157,421	132,843
Cost of earnings credits .....	15,585	9,807
<b>Current net earnings</b> .....	2,526,114	2,350,313
<b>Profit and Loss</b>		
Additions to current net earnings		
Profit on prior period adjustments .....	—	—
Profit on sales of United States Government securities (net).....	1,281	3,177
Profit on foreign exchange transactions (net).....	174,406	—
All other.....	1,357	—
Total additions.....	177,044	3,177
Deductions from current net earnings		
Loss on foreign exchange transactions (net).....	—	72,544
All other.....	—	45
Total deductions .....	0	72,589
<b>Net additions (+) or deductions (-)</b> .....	177,044	(69,412)
Cost of Unreimbursed Treasury Services.....	(6,691)	(2,253)
Assessments by Board of Governors		
Board expenditures.....	(12,316)	(11,939)
Federal Reserve currency costs.....	(18,860)	(19,188)
Net earnings before payments to the United States Treasury.....	2,665,291	2,247,521
Dividends paid .....	17,714	17,591
Payments to the United States Treasury (interest on Federal Reserve Notes) .....	2,636,822	2,229,846
Transferred to surplus.....	10,755	84
Surplus, January 1.....	291,155	291,071
Surplus, December 31 .....	301,910	291,155



## Twelfth Federal Reserve District

### San Francisco Office

P.O. Box 7702, San Francisco, California 94120

### Los Angeles Branch

P.O. Box 2077, Terminal Annex, Los Angeles, California 90051

### Portland Branch

P.O. Box 3436, Portland, Oregon 97208

### Salt Lake City Branch

P.O. Box 30780, Salt Lake City, Utah 84125

### Seattle Branch

P.O. Box 3567, Terminal Annex, Seattle, Washington 98124

This Report was designed and produced by Karen Rusk and written by Gregory J. Tong and Karen Rusk. Cover illustration, map and graphics were created by William Rosenthal. Color photography by Paul Schulz.

Federal Reserve Bank of San Francisco  
P.O. Box 7702  
San Francisco, California 94120

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