NOTE: This transcript of the Secretary's notes is not to be regarded as complete or necessarily entirely accurate. The transcript is for the sole use of the members of the Federal Advisory Council.

H.V.P.
W.J.K.

The Secretary's notes of the meeting of the Federal Advisory Council on September 16, 1968, at 9:30 A.M. in the Board Room of The Madison, Washington, D.C. All members of the Federal Advisory Council were present except Mr. George S. Moore. Mr. William H. Moore, Chairman, Bankers Trust Company, New York City, attended as an Alternate.

The Council approved the Secretary's notes for the meeting of June 3-4, 1968.

The President of the Council stated that Mr. Holland, the Secretary of the Board of Governors, had mentioned that the Board would like the Council to consider alternative meeting days. The proposed changes would fit more conveniently into the schedule of the Board of Governors. Mr. Mayer said that the Council would be happy to consider the proposed changes and that the Secretary would poll the members of the Council to determine whether or not they would be available on certain selected days of each month.

ITEM I A

ECONOMIC CONDITIONS AND PROSPECTS.

A. HOW DOES THE COUNCIL APPRAISE THE GENERAL ECONOMIC OUTLOOK FOR THE FALL AND WINTER, NOW THAT THE TAX INCREASE HAS TAKEN EFFECT? COMMENTS WOULD BE ESPECIALLY HELPFUL ON THE PROBABLE EXTENT AND DURATION OF THE STEEL INVENTORY ADJUSTMENT, ON INDICATIONS FROM CUSTOMER CONTACTS OF CAPITAL INVESTMENT PLANS, AND ON INDICATIONS OF ANY CUTBACKS RESULTING FROM REDUCTIONS IN FEDERAL GOVERNMENT PURCHASES OR NEW ORDERS.

President Mayer read Item I A and invited the members of the Council to comment. A brief discussion followed. It disclosed general agreement that the rise in business activity in the fall and winter months will moderate now that the tax increase is in effect. Several members mentioned that the slowing of economic activity also will reflect the liquidation of steel inventories accumulated during the summer months in anticipation of a steel strike. Estimates of the build-up of steel inventories suggest that the adjustment will last at least through this calendar year.

Contacts with customers indicate that capital investment plans are proceeding on schedule with some step-up in outlays as corporate managements strive to offset increasing labor costs. The larger investment outlays also reflect the rise in the cost of plant and equipment. The members of the Council reported only minor cutbacks in output resulting from reductions in the federal government's new orders or purchases.

ITEM I B

B. WHAT IS THE OUTLOOK FOR THE COST AND AVAILABILITY OF MORTGAGE FUNDS AND FOR RESIDENTIAL CONSTRUCTION ACTIVITY IN THE COUNCIL MEMBERS' RESPECTIVE REGIONS?

President Mayer then read Item I B. In the brief discussion which followed the members of the Council reported that the supply of funds for residential construction activity and mortgages has improved and that this trend is likely to continue. This development, together with the generally lower structure of interest rates which has characterized the money market, has resulted in slightly lower mortgage rates. The increase in the availability of funds suggests some further decline in rates. Several members cited the relaxation of usury laws which has tended to increase the supply of mortgage funds.

ITEM II A

BANKING DEVELOPMENTS.

A. WHAT IS THE COUNCIL'S ASSESSMENT OF THE PROBABLE STRENGTH OF BUSINESS LOAN DEMAND IN THE FALL? HAVE THERE BEEN ANY INDICATIONS OF A FURTHER SHIFTING OF SHORT-TERM FINANCING INTO THE COMMERCIAL PAPER MARKET, OR OF CORPORATE INTENT TO REPAY DEBT THROUGH THE ISSUANCE OF LONG-TERM SECURITIES?

The President of the Council read Item II A and invited comment from the members. The Council expects business loan demand in the fall to rise only seasonally. A number of members reported some shifting of short-term financing into the commercial paper market. There has been little evidence to date, however, of debt repayment through the issuance of long-term securities. Several members anticipate such a development if and when long-term interest rates decline somewhat further.

ITEM II B

B. WHAT ARE THE COUNCIL'S VIEWS REGARDING THE LIQUIDITY POSITION OF BANKS? DOES IT BELIEVE THAT BANKS WOULD WISH TO INCREASE HOLDINGS OF SHORT-TERM SECURITIES SUBSTANTIALLY IF THEY COULD OBTAIN FUNDS FROM C/D'S OR OTHER DEPOSIT SOURCES?

The President of the Council then read Item II B. The members of the Council were in agreement that most bankers in the money centers would like to improve their liquidity positions. Specifically, they would like to increase their holdings of short-term securities if they could profitably obtain funds of the proper maturities from C/D's or other deposit sources.

ITEM II C

C. DOES THE COUNCIL BELIEVE THAT BANKS WILL SIGNIFICANTLY INCREASE THEIR INTEREST IN MORTGAGES AND MUNICIPAL BONDS, NOW THAT INTEREST RATES HAVE DECLINED SOMEWHAT AND THERE IS LESS PRESSURE ON CURRENT POSITIONS?

President Mayer read Item II C. The Council concluded that if the pressure on the current positions of banks eases further, bankers will increase their holdings of mortgages and municipal bonds.

ITEM II D

D. WHAT IS THE COUNCIL'S VIEW REGARDING CURRENT AND PROSPECTIVE INFLOWS OF CONSUMER-TYPE TIME DEPOSITS? HAS THE RECENT TAX INCREASE HAD ANY NOTICEABLE EFFECT ON SUCH FLOWS?

The President of the Council then read Item II D. A brief discussion followed. It was acknowledged that it is difficult to determine at this early date whether the recent tax increase has had an effect on the flow of consumer savings. Savings are increasing but at a slower rate than a year ago. Most members anticipate that inflows of consumer-type deposits may moderate further in the months ahead. This will reflect not only the impact of the recent tax increase but, in addition, the rise in Social Security tax payments that will take effect early in the year.

ITEM II E

E. WHAT ARE THE VIEWS OF COUNCIL MEMBERS ON THE RECENT BOARD ACTION ALLOWING STATE MEMBER BANKS, UNDER SPECIFIED CONDITIONS, TO OWN AND OPERATE CERTAIN KINDS OF SUBSIDIARY CORPORATIONS AND LOAN PRODUCTION OFFICES?

President Mayer read Item II E. After a brief discussion, the Council concluded that in general it looks with favor on the recent Board action allowing state member banks under certain specified conditions to own and operate certain kinds of subsidiary corporations and loan production offices. This reflects not only a more flexible approach to bank operations, permitting an expansion of bank services, but, more importantly, the action also tends to equate the competitive position of state member banks with national banks.

ITEM II F

F. WHAT ARE THE COUNCIL'S VIEWS REGARDING THE APPROPRIATE ROLE OF ONE-BANK HOLDING COMPANIES IN THE U. S. BANKING STRUCTURE? DOES THE COUNCIL HAVE COMMENTS ON A PROPER LEGISLATIVE FRAMEWORK FOR THE OPERATIONS OF SUCH COMPANIES?

The President of the Council read Item II F. An extended discussion followed which disclosed wide divergence of views. The members unanimously favored expanding the financial fields in which commercial banks are allowed to operate. If such new areas are in the public interest, banks should be permitted to engage in them directly or through subsidiaries or through a holding company. The majority of the members of the Council do not believe that one-bank holding companies should be allowed to become conglomerates. After further discussion it was concluded that the Council would limit its formal written reply and instead permit various members to comment orally on the question.

ITEM III

BALANCE OF PAYMENTS.

HOW DOES THE COUNCIL APPRAISE THE OUTLOOK FOR THE REMAINDER OF THE YEAR FOR (1) DEMANDS FOR EURO-DOLLAR LOANS AT FOREIGN BRANCHES OF U. S. BANKS, (2) EURO-DOLLARS ADVANCED BY BRANCHES TO HOME OFFICES, AND (3) DIRECT BORROWINGS FROM FOREIGN BANKS BY U. S. BANKS (I.E., NOT THROUGH FOREIGN BRANCHES)?

The President of the Council read Item III. During the discussion of this item, the members indicated that they anticipate a continued strong demand for Euro-dollar loans at foreign branches of U. S. banks. Several cited, however, that this demand is not as intensive as it was earlier in the year. A somewhat lessened pressure on the reserve position of U. S. banks suggests that the volume of Euro-dollars advanced by branches to home offices may decline. This same pattern is likely to characterize direct borrowing from foreign banks by U. S. banks.

ITEM IV

ARE THERE ANY PARTICULAR SUGGESTIONS THAT THE MEMBERS OF THE COUNCIL WOULD WISH TO CONVEY TO THE BOARD REGARDING ITS IMPLEMENTATION OF THE TRUTH IN LENDING LEGISLATION?

President Mayer read Item IV and reported briefly on a memorandum that had been prepared by the Mellon Bank after consultation with the ABA staff on the implementation of the Truth-in-Lending legislation. It was subsequently agreed that the memorandum, with some minor editing, should be made a part of the Council's reply to the Board of Governors on the Agenda.

ITEM V

WHAT ARE THE COUNCIL'S VIEWS ON MONETARY AND CREDIT POLICY UNDER CURRENT CIRCUMSTANCES?

The President of the Council read Item V and invited comment from the members. After some discussion the Council decided to acknowledge in its Memorandum the difficulty of determining credit policy because of the delayed impact of the recently enacted fiscal legislation and the lags involved in monetary policy. Because of the apparent continued strength in the economy, a number of members thought the recent reduction in the discount rate may have been premature. It was decided to emphasize that it was important that the beneficial effects of fiscal restraint not be lost so that the strength of inflationary pressures would be lessened. The Council also suggested that if and when additional reserves need to be supplied to the system, that consideration be given to a reduction in reserve requirements rather than using open market operations.

The meeting adjourned at 12:25 P.M.

THE COUNCIL CONVENED IN THE BOARD ROOM OF THE FEDERAL RESERVE BUILDING, WASHINGTON, D.C., AT 2:30 P.M., ON SEPTEMBER 16, 1968. ALL MEMBERS OF THE COUNCIL WERE PRESENT EXCEPT MR. GEORGE S. MOORE. MR. WILLIAM H. MOORE, CHAIRMAN, BANKERS TRUST COMPANY, NEW YORK CITY, ATTENDED AS AN ALTERNATE.

The members of the Board's staff, including Mr. Daniel H. Brill, Senior Adviser to the Board, participated in an audio-visual presentation of economic and financial developments, as well as a review of the use of statistics on money supply as an indicator of monetary policy.

* * * *

THE COUNCIL RECONVENED AT 5:30 P.M., ON SEPTEMBER 16, 1968 IN THE BOARD ROOM OF THE MADISON. ALL MEMBERS OF THE COUNCIL WERE PRESENT EXCEPT MR. GEORGE S. MOORE. MR. WILLIAM H. MOORE, CHAIRMAN, BANKERS TRUST COMPANY, NEW YORK CITY, ATTENDED AS AN ALTERNATE.

The Council prepared and approved a Confidential Memorandum to be sent to the Board of Governors relative to the Agenda for the joint meeting of the Council and the Board on September 17, 1968. The Memorandum was delivered to the Federal Reserve Building at 9:45 P.M.

The meeting adjourned at 6:55 P.M.

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THE COUNCIL RECONVENED AT 10:15 A.M. ON SEPTEMBER 17, 1968, IN THE BOARD ROOM OF THE FEDERAL RESERVE BUILDING, WASHINGTON, D.C. ALL MEMBERS OF THE COUNCIL WERE PRESENT EXCEPT MR. GEORGE S. MOORE. MR. WILLIAM H. MOORE, CHAIRMAN, BANKERS TRUST COMPANY, NEW YORK CITY, ATTENDED AS AN ALTERNATE.

The Council again reviewed the Confidential Memorandum to be sent to the Board of Governors and amended its reply to Item II F. The amended version of the Memorandum is attached and made a part of these minutes.

The meeting adjourned at 10:30 A.M.

CONFIDENTIAL

MEMORANDUM TO THE BOARD OF GOVERNORS
FROM THE
FEDERAL ADVISORY COUNCIL
RELATIVE TO THE AGENDA FOR THE JOINT MEETING
ON SEPTEMBER 17, 1968

1. Economic conditions and prospects.

A. How does the Council appraise the general economic outlook for the fall and winter, now that the tax increase has taken effect? Comments would be especially helpful on the probable extent and duration of the steel inventory adjustment, on indications from customer contacts of capital investment plans, and on indications of any cutbacks resulting from reductions in Federal Government purchases or new orders.

The Council anticipates that the rise in business activity in the fall and winter months will moderate now that the tax increase is in effect. The slowing of economic activity also will reflect the liquidation of steel inventories accumulated during the summer months in anticipation of a steel strike. The estimates of the build-up of steel inventories suggests that the adjustment will last at least through this calendar year.

Contacts with customers indicate that capital investment plans are proceeding on schedule with some step-up in outlays as corporate managements strive to offset increasing labor costs. The larger investment outlays also cover a rise in the cost of plant and equipment. The members of the Council reported that they had little indication from their customer contacts of cutbacks in output resulting from reductions in Federal Government new orders or purchases.

B. What is the outlook for the cost and availability of mortgage funds and for residential construction activity in the Council members' respective regions?

The supply of funds for residential construction activity and mortgages has improved, and the members of the Council expect that this trend will continue. This development, together with the generally lower structure of interest rates which has characterized the money market, has resulted in slightly lower mortgage rates. With an increase in the availability of mortgage funds, some further decline in rates may occur. In some states, the relaxation of usury laws has increased the supply of mortgage funds.

2. A. What is the Council's assessment of the probable strength of business loan demand in the fall? Have there been any indications of a further shifting

of short-term financing into the commercial paper market, or of corporate intent to repay debt through the issuance of long-term securities?

The Council expects business loan demand in the fall to rise only seasonally. A number of members of the Council reported some shifting of short-term financing into the commercial paper market. There has been little evidence of debt repayment through the issuance of long-term securities. However, several members of the Council anticipate such a development if and when the long-term interest rates decline somewhat further.

B. What are the Council's views regarding the liquidity position of banks? Does it believe that banks would wish to increase holdings of short-term securities substantially if they could obtain funds from CD's or other deposit sources?

The members of the Council believe that most bankers in the money centers would like to improve their liquidity positions. They would like to increase their holdings of short-term securities if they could profitably obtain funds of the proper maturities from CD's or other deposit sources.

C. Does the Council believe that banks will significantly increase their interest in mortgages and municipal bonds, now that interest rates have declined somewhat and there is less pressure on current positions?

If the pressure on the current positions of banks eases further, the Council believes that banks will increase their holdings of mortgages and municipal bonds.

D. What is the Council's view regarding current and prospective inflows of consumer-type time deposits? Has the recent tax increase had any noticeable effect on such flows?

It is difficult to determine at this early date whether the recent tax increase has had an effect on the consumer savings flow. Savings are increasing, but at a slower rate than a year ago. Most members of the Council anticipate that the inflows of consumer-type deposits may moderate further in the months ahead. This will reflect the impact of the recent tax increase and the rise in Social Security tax payments that will take effect early in the year.

E. What are the views of Council members on the recent Board action allowing State member banks, under specified conditions, to own and operate certain kinds of subsidiary corporations and loan production offices:

In general, the members of the Council look with favor on the recent Board action allowing State member banks under specified conditions to own and operate certain kinds of subsidiary corporations and loan production offices. This reflects not only a more flexible approach to bank operations permitting an expansion of bank services, but more importantly, the action also tends to equate the competitive position of State member banks with national banks.

F. What are the Council's views regarding the appropriate role of one-bank holding companies in the U.S. Banking structure? Does the Council have comments on a proper legislative framework for the operations of such companies"

The members of the Council are in favor of expanding the financial fields in which commercial banks are allowed to operate. If such new areas are in the public interest, banks should be permitted to engage in them directly, or through subsidiaries, or through a holding company. The majority of the members of the Council do not believe that one-bank holding companies should be allowed to become conglomerates.

Some members of the Council will comment orally on the question.

3. Balance of payments.

How does the Council appraise the outlook for the remainder of the year for (1) demands for Euro-dollar loans at foreign branches of U.S. banks, (2) Euro-dollars advanced by branches to home offices, and (3) direct borrowings from foreign banks by U.S. banks (i.e., not through foreign branches)?

The Council anticipates a continued strong demand for Euro-dollar loans at foreign branches of U.S. banks. There is some evidence, however, that this demand is not quite as intensive as it was earlier in the year. The somewhat lessened pressure on the reserve positions of U.S. banks suggests that the volume of Euro-dollars advanced by branches to home offices may decline. The same pattern is likely to characterize direct borrowing from foreign banks by U.S. banks.

4. Are there any particular suggestions that the members of the Council would wish to convey to the Board regarding its implementation of the Truth-in-Lending legislation?

The Board will find attached a memorandum outlining in some detail suggestions regarding the implementation of the Truth-in-Lending legislation.

5. What are the Council's views on monetary and credit policy under current circumstances?

The Council is aware of the difficulties of determining credit policy because of the delayed impact of the recently enacted fiscal legislation, and the lags involved in monetary policy. However, because of the apparent continued strength in the economy, as evidenced by the behavior of most indicators, including retail sales, automobile deliveries, and new orders, as well as the persistence of the upward pressure on prices, many members of the Council believe the recent reduction in the discount rate may have been premature. It is highly important that the beneficial effects of fiscal restraint not be lost and that the strength of inflationary pressures be lessened.

If and when additional reserves need to be supplied to the system, the Council believes that consideration should be given to a small reduction in reserve requirements rather than using open market operations.

MEMORANDUM ON IMPLEMENTATION OF THE TRUTH-IN-LENDING LEGISLATION

One key feature of the Truth-in-Lending Act is that consumer financing and consumer instalment sales are to be treated basically alike. This was a feature that the banking industry fought hard to achieve. In the case of term loans, instalment loans, and revolving loans, creditors must disclose the annual charge on the same basis. For a time, it appeared that department stores might be permitted to mention only the monthly interest rate on revolving credits whereas banks would have to specify the simple annual rate.

The Council believes that in carrying out the proposed equal treatment of consumer financing and consumer sales industries, the detailed regulation to be promulgated by the Federal Reserve System should aim at as much uniformity as possible within any industry and between one industry and another. There are several leading examples of this:

1. With regard to instalment sales by stores of one kind or another, the time-price differential is clearly a finance charge, comparable to interest rates on instalment loans. Therefore, retail stores should not be given any competitive edge vis-a-vis banks and other lenders in the terms and conditions of contracts and advertising of time-price sales, as compared to the contract and conditions of advertising pertinent to instalment loans made by banks and other lenders.

2. With regard to the advertising of credit cards, the rules should be made precise to insure competitive equality as between banks and other issuers of credit cards. It is clear that, with the possible exception of credit unions, the interest rates and other terms offered to borrowers by commercial banks will be more favorable than those offered by others--e.g., department stores, oil companies, etc. The fact that bank terms are more advantageous to the public should not be allowed to be diluted by permitting retail stores to advertise in a way that conceals this matter.

There are several other matters pertaining to bank credit cards that are worth noting:

1. Since the merchant discount feature does not tend to change prices to consumers, there should be no requirement that the merchant discount be included in the required computation of finance charges made to holders of bank credit cards.

2. Since late charges, where applicable, are intended to compensate banks for the special handling costs and other costs associated with late payments, there should be no requirement that late charges be included in the required computation of finance charges to holders of bank credit cards.

Finally, it should be noted that the Truth-in-Lending Act authorized the Federal Reserve Board to waive the Federal statute in the case of any state which enacts substantially similar legislation and enforces it effectively. During the long period in which the Truth-in-Lending Act was being considered in the Congress, the general position of the banking industry was that it would be preferable to have legislation in the field of the disclosure of finance charges enacted by the states, partly because the whole area of interest rates, usury laws and creditors' remedies were already under state regulation and could be adequately handled by the states, and partly because it was felt that if the Federal Government got into the field of disclosure of finance charges, it would soon go beyond that into the field of creditors' remedies--which in fact proved to be the case in the Truth-in-Lending Act. Given the foregoing background, therefore, we would favor action by the Federal Reserve that would facilitate the transfer of administration of truth-in-lending programs to the states under state legislation as quickly as possible, provided only that such state administration would not interfere with the need for uniform administrative interpretation and hence competitive equality as between banks, other lenders, and retail establishments in terms of required contracts, statements of finance charges, and advertising of credit terms.

ON SEPTEMBER 17, 1968, AT 10:30 A.M., THE FEDERAL ADVISORY COUNCIL HELD A JOINT MEETING WITH THE BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM IN THE FEDERAL RESERVE BUILDING, WASHINGTON, D.C. ALL MEMBERS OF THE COUNCIL WERE PRESENT EXCEPT MR. GEORGE S. MOORE. MR. WILLIAM H. MOORE, CHAIRMAN, BANKERS TRUST COMPANY, NEW YORK CITY, ATTENDED AS AN ALTERNATE.

THE FOLLOWING MEMBERS OF THE BOARD OF GOVERNORS WERE PRESENT: CHAIRMAN WM.Mc MARTIN, JR., VICE CHAIRMAN J. L. ROBERTSON; GOVERNORS MITCHELL, BRIMMER, DAANE, MAISEL AND SHERRILL. MR. ROBERT C. HOLLAND, SECRETARY, MR. KENNETH A. KENYON, DEPUTY SECRETARY, AND MRS. SEMIA, TECHNICAL ASSISTANT, ALSO WERE PRESENT.

The minutes of the joint meeting are being prepared in the office of the Secretary of the Board of Governors of the Federal Reserve System. Their content will be compared with the notes of the Secretary of the Council. Assuming they are in substantial agreement, they will be reproduced and distributed to the members of the Council.

The meeting adjourned at 12:35 P.M.

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The next meeting of the Council will be held on November 18-19, 1968.

A meeting of the Board of Governors of the Federal Reserve System with the Federal Advisory Council was held in the Board Room of the Federal Reserve Building in Washington, D. C., at 10:30 a.m. on Tuesday, September 17, 1968.

PRESENT: Mr. Martin, Chairman
Mr. Robertson, Vice Chairman
Mr. Mitchell
Mr. Daane
Mr. Maisel
Mr. Brimmer
Mr. Sherrill

Mr. Holland, Secretary
Mr. Kenyon, Deputy Secretary
Mrs. Semia, Technical Assistant, Office of the Secretary

Messrs. Simmen, Still, Mayer, Wilkinson, Craft, Kennedy, Fox, Nason, Conn, Stewart, and Larkin, Members of the Federal Advisory Council from the First, Third, Fourth, Fifth, Sixth, Seventh, Eighth, Ninth, Tenth, Eleventh, and Twelfth Federal Reserve Districts, respectively

Mr. William H. Moore, Chairman, Bankers Trust Company, New York, New York

Mr. Prochnow, Secretary of the Council
Mr. Korsvik, Assistant Secretary of the Council

The Council member from the Second District, Mr. George S. Moore, was unable to be present at this meeting, and in his absence the District was represented by Mr. William H. Moore.

It was agreed, since Chairman Martin had to leave shortly to begin an out-of-town trip, to turn first to topic 2-F on the agenda, as follows:

> What are the Council's views regarding the appropriate role of one-bank holding companies in the U.S. banking structure? Does the Council have comments on a proper legislative framework for the operations of such companies?

> The members of the Council are in favor of expanding the financial fields in which commercial banks are allowed to operate. If such new areas are in the public interest, banks should be permitted to engage in them directly, or through subsidiaries, or through a holding company. The majority of the members of the Council do not believe that one-bank holding companies should be allowed to become conglomerates.

President Mayer remarked that an earlier draft of the Council's statement had indicated that the majority of the members did not believe that one-bank holding companies should be allowed to engage in nonfinancial activities. However, those words had been deleted because they were not easily susceptible of definition. The Council had also deleted a paragraph that attempted to identify elements that would be important in the framing of legislation. The Council had concluded that in order to reply adequately to that part of the question it would be necessary to review the law thoroughly. In the absence of such a review, for which there had not been sufficient opportunity, any suggestions offered might have been wide of the mark.

There was agreement by a majority of the Council, President Mayer continued, that one-bank holding companies should not be allowed to become conglomerates. However, at least one member present dissented from that view, as did the member from the Second District, who was not present. A number of the members had rather strong views on the matter, which the Board might be interested to hear.

Chairman Martin stated that the Board would like to hear both the strong and the more moderate views.

President Mayer then turned to Mr. Simmen, who remarked that he had a personal interest in the question because his bank, through a plan of reorganization and merger, was about to become wholly owned by a one-bank holding company. The bank had taken this step because, although the 64th or 65th largest bank in the U.S., it was confined to the limits of the small State of Rhode Island. Also, for the past year or so the bank had been in the courts because of litigation brought by a service bureau contending that the City of Providence and the bank had no right to enter into a contract whereby the bank would operate the city's computer. The bank had felt for some time that there was a need to compartmentalize in order to provide specialized services for which it was qualified, rather than just to compete with nearby smaller banks for deposits. To accomplish that purpose through a registered bank holding company had seemed out of the question not only because of the competitive situation in the small State but also because the bank would then be restricted from going beyond State lines.

Mr. Simmen believed it would be well to proceed cautiously with respect to legislation, in the absence of apparent problems regarding the several hundred holding companies that already owned only one bank. If legislation were approached without careful study, restrictions might be imposed that would inhibit expansion of services through one-bank holding companies in much the same way banks were now hampered. In the case of his own bank, the published proxy statement to stockholders had specified that the purpose of the new arrangement was to engage in financially-related activities. The plan had been approved by 85 per cent of the stockholders, with objections from less than 1 per cent. Moreover, he understood that the Comptroller of the Currency would have examining power with respect to any activity of the holding company, and thus examiners could determine whether or not unsound paper was being thrust upon the bank or whether the holding company was engaging in any activity that would impinge on the record of the bank.

Chairman Martin inquired whether Mr. Simmen visualized that consideration might be given to engaging in a completely nonfinancial activity and whether he would regard that as proper.

Mr. Simmen replied that management had no such plans in mind. The organization would be capable in the leasing field and in rendering computer services to customers. As indicated in the proxy statement, however, the organization would plan to stay within the areas it knew best.

In response to a question by Governor Robertson, Mr. Simmen indicated that at the moment he would not be inclined to oppose a limitation that would confine one-bank holding companies to activities related to banking and financing.

President Mayer suggested that it would seem preferable if any such limitations could be specified by the banking agencies. If the Congress had to deal with the question, it would be subjected to many pressures, with unpredictable results.

Governor Robertson then read from a list of activities being conducted by the several hundred existing one-bank holding companies. In response to a question whether the businesses mentioned were conducted by holding companies the organization of which had been initiated by a bank, Governor Robertson indicated that the list encompassed all holding companies that owned one bank, regardless of the manner in which the holding company had come into being.

Mr. Still commented that his bank--of moderate size--was considering the formation of a one-bank holding company, one reason being that management viewed the bank as otherwise vulnerable to takeover by interests with which it might not care to be associated.

Governor Robertson recognized the point but observed that any limitations, statutory or administrative, presumably would have to apply across the board.

Mr. Kennedy noted that the majority of the Council had taken a position in favor of one-bank holding companies, operating in banking and related fields. The majority would not favor conglomerates, engaging in the diversity of operations Governor Robertson had cited. Mr. Kennedy felt strongly that banks--and their holding companies--should stay within the area of financing; troubles had occurred in the past when banks stepped out of that area. However, he would be loath to see the problem of definition submitted to the Congress because its ramifications were so great that inequities might result. That was why the Council had been probing into whether the Board had authority to issue regulations on the subject and whether specific legislation could be avoided. The situation was critical at this stage because many banks, observing the accelerating trend toward formation of one-bank holding companies, were apprehensive of being frozen out if they did not take such action now.

Mr. Conn remarked that although the intent of Congress had been well expressed in the 1956 Act with respect to registered bank holding companies, there appeared to be a complete hiatus in the law with respect to one-bank holding companies. This permitted a development that the Congress apparently had never intended. It was unfortunate that, while the activities of multi-bank holding companies were limited by statute and by the Board, holding companies that owned only one bank could engage in the range of operations suggested by the list Governor Robertson had read. He had no objection to an extension of powers within the field of banking, but if banking institutions went beyond that field they ran the risk that some of their powers would be given also to other types of institutions, such as savings and loan associations. If banks were to engage in the steel business, for example, they would have little basis for urging that no one else should be permitted to engage in the banking business.

If banks spread their operations too far, Mr. Conn continued, sooner or later there were bound to be abuses. For example, if a steel company owned a bank through a holding company, it could select the management. If the steel company then wanted to place some of its paper in the bank, the management would scarcely be in a position to refuse. He did not believe the examination process would be an adequate safeguard; a bank could hardly be stronger than its owners, and a bank examiner did not have sufficient knowledge to appraise the operations of a steel company or a dairy. Yet if the steel company or dairy went broke, the bank was bound to be affected. If abuses occurred and legislation was passed, all banks were likely to be hurt. Although bankers might have the respect of Congress as bankers, they would not have the same support upon moving out to nonbanking fields. Many Congressmen would certainly view any extension of banking powers as contrary to the public interest, and he feared that inroads might in fact be made on the latitude now available to the banks. If the Board had regulatory authority in this area, and he supposed such authority must exist somewhere, he believed it would be in the public interest, and in the interest of banking, to specify by regulation that the powers of one-bank holding companies could not exceed those exercised by registered bank holding companies.

Governor Brimmer said it was his understanding that the Board did not have such power; because of the loophole in the law, the organizers of a one-bank holding company need not apply to the Board for approval. For a number of years the Board had recommended to the Congress repeatedly that the definition of a bank holding company be extended to encompass companies that owned only one bank, and thus put them on the same footing as companies that were now required to register. He inquired whether the Council was suggesting that the Board drop that campaign.

President Mayer replied that the Council was merely expressing concern that if the subject was opened up in the Congress many interests would press to restrict banks unduly, perhaps to an even smaller area than their present scope of operations.

Governor Sherrill pointed out that if one-bank holding companies initiated by banks were limited to financially-related activities, nonbank corporations presumably would be precluded from owning banks. He inquired whether the Council's thinking implied acceptance of that principle.

President Mayer said the Council's thinking had been mainly in terms of what the banks were doing. The other angle had not been given full consideration. The Council members did not have sufficient knowledge on that score to have formed a judgment, although it was known that there were some hundreds of companies that owned a bank and that fact was intuitively a matter of some concern.

His personal view, President Mayer continued, was that the current trend for so many organizations of all types to buy up other unrelated enterprises was unwholesome. The main purpose of many such transactions seemed to be the aggrandizement of individuals or corporate interests, rather than promotion of the public welfare. He could not foresee the ultimate social effect of this trend, but he suspected it might not be good. It seemed evident that no one would want to take over an insurance company, for example, unless he hoped to gain access to the company's reserves, and banks might also become targets. If such a motive became apparent, one could appreciate the difficulty of the problem that would confront the bank supervisors.

Mr. Wilkinson associated himself with President Mayer's views.

Mr. Conn, referring to Governor Sherrill's earlier inquiry, expressed the view that a distinct difference was involved. If an insurance company, for example, owned 50 per cent of a bank, the bank must continue to operate within the normal purview of banking. If the insurance company's financial condition deteriorated, only its stock ownership in the bank would be jeopardized. This was to be distinguished from a situation where a bank organized a holding company and through it entered into other businesses concerning which it had no real knowledge.

Mr. Kennedy said he regarded the whole question of bank ownership as a serious matter. Despite supervisory efforts, a bank could easily get loaded with poor paper. This was a problem that went beyond the question of banks being owned by holding companies. There was danger that any corporation owning a bank could load the bank with unsound paper.

Mr. Fox commented that it seemed to him the dangers would be just as real in the case of ownership of a bank by a wealthy individual or group of individuals. The law at least had some safeguards written into it that restricted the ability of a bank to finance an affiliated corporation. His reasons for dissenting from the majority position were similar to those Mr. Simmen had mentioned. Everyone's views were conditioned upon his own experience and particular problems. Banks in his area suffered under growth restrictions about as severe as those in any part of the country. Branching was narrowly limited, and the registered bank holding company route seemed to be precluded for practical purposes. Although his bank had no specific plans at the moment, the one-bank holding company route appeared to offer the only feasible way to participate in a general growth pattern. Fears had been expressed regarding the solvency of banks if the trend toward one-bank holding companies persisted, but in several existing situations of which he had knowledge the banks had made excellent progress. The problems of which he had heard stemmed in large measure not from irresponsible corporate ownership but from irresponsible individual or group ownership. If there were loopholes in the law, he believed it would be preferable to amend the law in terms of the type of credit a bank could extend to sister companies than to attack the whole holding company concept.

In answer to a question about banks going into unrelated businesses, Mr. Fox said he would not want to be restricted. The bulk of his bank's deposits came from large corporate customers whose confidence in the bank was vital, and the bank was not likely to jeopardize that confidence by involving itself in ventures that might endanger its solvency. He saw no reason in principle why a one-bank holding company should not be permitted to buy a hotel, for example.

In response to further questions, Mr. Fox said he did not see why a bank charter should be refused to a corporation and granted to a group of individuals who could not provide anywhere near the same degree of strength. If a community need existed, he would not refuse a charter simply because it was applied for by a corporation. As to the responsibility of a bank to allocate resources in the public interest, he believed the profit motive of a bank under corporate ownership would lead it to be just as responsive in that respect as one that was owned by individuals.

In summary, he saw no reason to change the rules relative to granting bank charters simply because the bank was to be owned by a corporation. This did not mean, of course, that anyone who could afford it should be granted a charter, but the rules followed to date need not be changed simply to exclude corporate ownership.

Governor Brimmer expressed an interest in hearing the Council's view, since the majority believed one-bank holding companies should be restricted to financial activities, on the appropriate range of such activities.

President Mayer replied that the Council's thinking had been basically in broad terms--that banks should stay in lines of business that had some relation to banking. No attempt had been made to name such lines of business, and in his own mind he could not at the moment develop a serviceable definition.

There followed an exchange of comments regarding the question of the authority to determine what activities were appropriate within the structure of registered bank holding companies, and Governor Maisel recalled that a number of years ago, in the Transamerica case, the Board had adopted a very narrow view of incidental activities. He wondered whether the majority of the Council was still thinking in terms of such a limited concept. Mr. Nason observed that all of the Council held the general view that there should be some liberalization of the activities in which banks were permitted to engage, either individually or through holding company arrangements. Governor Maisel inquired whether the thinking of the majority would be broad enough to encompass, for example, insurance and instalment finance activities, and several responses were in the affirmative.

Governor Daane inquired whether the Council believed that conglomerate holding companies were unsound per se. The trend of the times was in that direction. The question, then, was whether the situation would be better or worse if banks were left out.

President Mayer said he would not be prepared to classify all conglomerates as bad. Some had experienced sound growth. He had an intuitive feeling that some that had grown very rapidly might not be sound, but only time would tell.

Mr. Moore noted that many people were forming conglomerates because they were hemmed in from further growth of earning power within their own industries, for a variety of reasons. Some of this pressure was now being felt by the banks, which were not growing as rapidly as the rest of the economy and were trying to find some way to stay in the parade. This was the crux of the problem. Although individual members of the Council might view the issue in the light of the particular problems of their own institutions, all were agreed that some liberalization was needed and that it was vital for some way to be found in which the banking industry could grow in its own or related areas to keep pace with the rest of the economy. Otherwise the banks would fall behind. Like railroading, banking would at some point no longer be considered a good business for capital or personnel.

Mr. Kennedy observed that the Council's statement should not be read as condemning conglomerates per se. The focus of that statement had been on banks going into unrelated lines of business through the formation of one-bank holding companies. He did not recall any consideration having been given to the other side of the question. President Mayer agreed, noting that the Council was not fully prepared to respond to the question involved in ownership of banks by corporations engaged in other businesses.

At this point President Mayer remarked that the Council member from the Second District, Mr. George Moore, had submitted certain comments in writing. At the Board's request, President Mayer read Mr. Moore's comments, as follows:

> One-bank holding companies have been a part of the corporate financial industry for many years. They have served the public interest by usefully providing capital and management for commercial banks. We regard this as an appropriate role for the one-bank holding company, which should continue to contribute to the growth and diversification of financial services to the public. Banks owned by a one-bank holding company are now covered by the same supervisory laws as all other banks. Such supervisory regulation in our opinion is ample. The fact that a bank has a single corporate stockholder rather than a group of individual or institutional stockholders should not require the introduction of a new layer of supervision. Our opinion is that:
>
> 1. There are no visible abuses.
>
> 2. Regulatory agencies have already sufficient powers to prevent any abuses from developing and to nip them in the bud. The Comptroller of the Currency is outspoken in saying this.
>
> 3. The public wants and deserves and will support aggressive constructive competition in financial services on a broad front and the congeneric financial holding company is the best vehicle to do this. There are many reasons such as capital-debt ratios, which vary from business to business in the financial world, which support the theory that it is better to do some of these things, such as factoring and leasing,

via the separate corporate route in a financial family affiliated with the bank instead of having it all in the bank itself, wholly apart from the questions which might be raised as to whether a bank may legally perform these functions.

Mr. Nason remarked that he and the president of his bank's parent holding company both felt strongly about two points. First, banks should not be owned by conglomerate interests, because the banks might then be less motivated to serve the public. Banks enjoyed certain unique privileges, but they also had certain obligations to the community, such as allocating funds, which might not be handled responsibly if ownership chose to use the bank's resources selfishly. Second, it would be grossly unfair to accord one-bank holding companies extensive privileges not accorded registered bank holding companies. He would be well satisfied, Mr. Nason added, if the definition of what was related to banking was not spelled out in the law but was left as a regulatory decision for the Board.

Governor Sherrill inquired whether, since the fundamental problem leading to the desire to get outside the confines of banking was growth of profits, the Council members believed that a restriction to financially-related activities, with a definition that was not too stringent, would provide sufficient room for growth for at least several years to come. Replies by several members of the Council were generally affirmative, though Mr. Fox responded in the negative.

Mr. Conn commented that the growth of banks had, generally speaking, been satisfactory. Net operating earnings had been increasing, and the industry was in a sound position. Banks enjoyed special privileges conferred upon them by legislation, and they operated on other people's money. Yet they were not satisfied and wanted to engage in other activities, while at the same time arguing that others should not be permitted to engage in banking.

Mr. Fox remarked that if there were a different kind of banking structure in his area he might feel less strongly about the need for new avenues of expansion. In his area there were many activities that required funds and the banks were limited in achieving deposit growth.

Governor Robertson said he could remember well the events of the 1920's and 1930's that had led to the passage of the Glass-Steagall Act. Because of the abuses that had occurred, the banking fraternity found itself without influence in the framing of corrective legislation. It seemed to him that many of the same mistakes were being repeated in the present period. He hoped that the Council would continue to study the question of the proper scope of bank activities and offer recommendations soon, because he thought that legislation would be forthcoming. If abuses occurred before solutions were found, the banking industry would not get the kind of legislation it preferred, but something much more restrictive.

The other topics were then taken up in the order presented on the agenda. (Chairman Martin had left the meeting during the course of the foregoing discussion.)

1. Economic conditions and prospects.

   A. How does the Council appraise the general economic outlook for the fall and winter, now that the tax increase has taken effect? Comments would be especially helpful on the probable extent and duration of the steel inventory adjustment, on indications from customer contacts of capital investment plans, and on indications of any cutbacks resulting from reductions in Federal Government purchases or new orders.

The Council anticipates that the rise in business activity in the fall and winter months will moderate now that the tax increase is in effect. The slowing of economic activity also will reflect the liquidation of steel inventories accumulated during the summer months in anticipation of a steel strike. The estimates of the build-up of steel inventories suggest that the adjustment will last at least through this calendar year.

Contacts with customers indicate that capital investment plans are proceeding on schedule, with some step-up in outlays as corporate managements strive to offset increasing labor costs. The larger investment outlays also cover a rise in the cost of plant and equipment. The members of the Council reported that they had little indication from their customer contacts of cutbacks in output resulting from reductions in Federal Government new orders or purchases.

Governor Brimmer inquired whether Council members had any feeling about the extent to which consumers might be attempting to maintain their expenditures by increasing their borrowing and by drawing down their savings. He was somewhat puzzled by the lack of response to the surtax in the consumer sector. He would have thought that by now the figures would have begun to reflect some reduction in the rate of expansion of consumer expenditures.

Mr. Kennedy responded that the Council members were also concerned about the level of consumer spending and the delayed impact of the tax package. The most recent available information on retail sales reflected all-time highs. Comments by directors of his bank indicated some expectation that October or November might see a beginning of the dampening of consumer spending that had been anticipated in September.

Governor Daane inquired to what extent Council members believed that the strength of the consumer sector reflected wide-spread inflationary expectations.

Mr. Kennedy commented that it was hard to judge. Consumers felt that prices were going up rather than down, generally speaking, and they were aware that serious unemployment or a real economic downturn were probably not in the picture; the danger of fiscal overkill had been largely dismissed from people's minds. However, he doubted that consumer goods were being purchased to any large extent simply as a hedge against price rises. President Mayer suggested that the successful clean-up of the 1968 model automobiles may have reflected to some degree expectations of substantially higher prices for the 1969 models. Another comment was to the effect that there had been so many wage and salary increases throughout the corporate and public sectors that many people were not feeling the pinch of the tax increase as much as they otherwise would have.

B. What is the outlook for the cost and availability of mortgage funds and for residential construction activity in the Council members' respective regions?

The supply of funds for residential construction activity and mortgages has improved, and the members of the Council expect that this trend will continue. This development, together with the generally lower structure of interest rates which has characterized the money market, has resulted in slightly lower mortgage rates. With an increase in the availability of mortgage funds, some further decline in rates may occur. In some States, the relaxation of usury laws has increased the supply of mortgage funds.

Governor Robertson inquired to what extent, if any, banks had been increasing their percentages of real estate loans in the past year or so, and Governor Maisel remarked on the recent increase of real estate loans in the New York area.

Mr. Moore commented that with the recent relaxation of legally permissible rates in the State, there had been some increase in mortgages on single-family dwellings. However, apartment projects appeared to be drying up somewhat because of the prohibitive cost of land. Governor Maisel asked if the volume of construction might represent in part the working out of a backlog, and Mr. Moore agreed that it might, because earlier a great deal of mortgage money had gone out of the State in search of better rates.

Governor Brimmer, reverting to Governor Robertson's question, observed that figures he had reviewed in the spring of this year indicated that real estate loans as a proportion of total assets of commercial banks had receded somewhat from the position reached in 1967, which reflected an increase over 1964-65. He inquired about the position of banks with which Council members were affiliated.

Mr. Moore said that real estate loans represented only a small percentage of total assets at his bank, as at most of the large New York City banks. He did not think his bank would be increasing that percentage substantially, in view of the bank's location and the nature of its business. For banks outside New York City, real estate loans were a major portfolio item, and he believed those banks would be adding to them.

President Mayer noted that his bank had continued making mortgage loans under all conditions. The bank operated a lot of branches, and the making of mortgages was an important item of business. However, the bank's ratio of real estate loans to other loans was probably less than it had been four or five years ago because of the large increase in total loans.

In response to an inquiry by Governor Robertson regarding the ratio of mortgages held by banks to those held by nonbank institutions, response was made that a decline probably had occurred.

2. A. What is the Council's assessment of the probable strength of business loan demand in the fall? Have there been any indications of a further shifting of short-term financing into the commercial paper market, or of corporate intent to repay debt through the issuance of long-term securities?

The Council expects business loan demand in the fall to rise only seasonally. A number of the Council reported some shifting of short-term financing into the commercial paper market. There has been little evidence of debt repayment through the issuance of long-term securities. However, several members of the Council anticipate such a development if and when the long-term interest rates decline somewhat further.

Governor Brimmer observed that at one time some banks were expressing concern about the competitive aspects of the commercial paper market and were urging the Board to do something. He inquired how the Council members now viewed that market.

President Mayer replied that he looked upon it more kindly than he had some time ago, because he did not know what would have been done during the recent period of expansion if the commercial paper market had not been available to meet some of the financing demands.

Mr. Moore expressed the view that, academically speaking, the commercial paper market did present a serious competitive problem. A great deal of financing was being done through that market that banks otherwise would have done. It was a serious competitor when a bank was looking for loans, even though the market was supported and made possible by the banks. What, if anything, should be done about the problem, he could not say.

Mr. Mayer said he was not so sure that the commercial paper market was as fully dependent on the banks as might be thought. He suspected that buyers could be found for much of the commercial paper even if it was not backed by bank credit lines.

Mr. Kennedy agreed with President Mayer's view. Some commercial paper was being issued without any real backing. He believed there was some cause for concern on that account. But the problem came down essentially to the matter of rates and he had no suggestions as to what might be done.

Mr. Nason observed that the commercial paper market had been a valuable device during the credit crunch of 1966, and that it was a profitable device as far as his bank was concerned. It provided a way to accommodate next-to-prime customers with ease, while the bank could maintain contact by virtue of its supporting lines of credit. He did not foresee a period when his bank would have difficulty in finding profitable investments for its available funds.

Mr. Fox expressed agreement with Mr. Nason's comments.

> B. What are the Council's views regarding the liquidity position of banks? Does it believe that banks would wish to increase holdings of short-term securities substantially if they could obtain funds from CD's or other deposit sources?

The members of the Council believe that most bankers in the money centers would like to improve their liquidity positions. They would like to increase their holdings of short-term securities if they could profitably obtain funds of the proper maturities from CD's or other deposit sources.

President Mayer expressed the view that most of the banks would be hesitant about increasing their holdings of securities unless matched by CD's in approximately the same maturity range.

Governor Sherrill noted that there had been a slight rise recently in rates outside New York City for 30-59 day CD's and he inquired what factors might have been involved.

Mr. Moore replied that although money had been somewhat easier recently, there had not been any big break in rates. They had drifted down, and some were likely to back up occasionally, but the changes were likely to be temporary. The occurrence to which Governor Sherrill referred may have had some relationship to the approaching tax date.

Governor Mitchell inquired whether the Council was concerned about what might be interpreted as a speculative position in securities at this point. Some banks had taken large positions, apparently expecting interest rate changes that would provide capital gains.

Mr. Kennedy questioned the use of the word "speculative." As a dealer bank, his institution participated in markets. For a while, buyers were not to be found, and the dealers were caught.

A number of nondealer banks that had at one stage withdrawn from the municipals market had recently been buying heavily as a portfolio adjustment move.

Governor Mitchell agreed that perhaps speculation might be too strong a term. However, some institutions were in overextended positions and were heavily dependent on a turn in rates. It was natural for an institution to increase its position moderately in anticipation of a turnaround in rates, but some of the positions appeared immoderate.

C. Does the Council believe that banks will significantly increase their interest in mortgages and municipal bonds, now that interest rates have declined somewhat and there is less pressure on current positions?

If the pressure on the current positions of banks eases further, the Council believes that banks will increase their holdings of mortgages and municipal bonds.

Mr. Nason observed that the Board's question covered two different kinds of investments. Governor Sherrill inquired to which of the types banks were likely to give precedence, and several members named municipals.

D. What is the Council's view regarding current and prospective inflows of consumer-type time deposits? Has the recent tax increase had any noticeable effect on such flows?

It is difficult to determine at this early date whether the recent tax increase has had an effect on the consumer savings flow. Savings are increasing, but at a slower rate than a year ago. Most members of the Council anticipate that the inflows of consumer-type deposits may moderate further in the months ahead. This will reflect the impact of the recent tax increase and the rise in social security tax payments that will take effect early in the year.

President Mayer remarked that this question was posed at a rather difficult time. Among other things, August always tended to be an erratic month, and it was not easy to draw conclusions from the data.

E. What are the views of Council members on the recent Board action allowing State member banks, under specified conditions, to own and operate certain kinds of subsidiary corporations and loan production offices?

In general, the members of the Council look with favor on the recent Board action allowing State member banks under specified conditions to own and operate certain kinds of subsidiary corporations and loan production offices. This reflects not only a more flexible approach to bank operations permitting an expansion of bank services, but more importantly, the action also tends to equate the competitive position of State member banks with national banks.

Governor Sherrill inquired whether any of the Council members had misgivings about the establishment of offices to produce loans across State lines.

After comments by several members reflecting uncertainty about the impact of the ruling on State laws, Mr. Larkin expressed the view that the banking community had not yet really appraised the effect of the ruling and therefore it was too early to say what the response would be. He doubted that there would be any misuse of the decision for the time being. In fact, he was not sure what would be regarded as constituting an abuse. Possibly, to go to an extreme, the conduct of nationwide banking through loan production offices would be so regarded. However, it was impossible now to predict the ultimate effect, or to define "proper use," and developments would have to be awaited.

President Mayer remarked that a bank presumably would have little immediate interest in the ruling if its problem was to obtain deposits to make the loans already available to it within its own community, and Mr. Conn observed that if a large New York City bank, for example, established a loan production office in Oklahoma City it would have to generate a lot of loans to make up for the balances it would lose. Mr. Moore commented that, despite such risk, some banks might choose to establish such offices because they would rather have the loans than the deposits. Mr. Fox noted that many banks already had "walking loan production offices." The opportunity now permitted seemed to involve just a question of degree.

Mr. Conn said that within the framework of the interpretation he could not see that branch banking was involved. The establishment of loan production offices would not appear to be contrary to the laws of Oklahoma, except perhaps in the sense of foreign banks coming into the State and doing business. An arrangement whereby an office simply generated loans did not seem very different from what was already being done.

3. Balance of payments.

> How does the Council appraise the outlook for the remainder of the year for (1) demands for Euro-dollar loans at foreign branches of U.S. banks, (2) Euro-dollars advanced by branches to home offices, and (3) direct borrowings from foreign banks by U.S. banks (i.e., not through foreign branches)?

The Council anticipates a continued strong demand for Euro-dollar loans at foreign branches of U.S. banks. There is some evidence, however, that this demand is not quite as intensive as it was earlier in the year. The somewhat lessened pressure on the reserve positions of U.S. banks suggests that the volume of Euro-dollars advanced by branches to home offices may decline. The same pattern is likely to characterize direct borrowing from foreign banks by U.S. banks.

Mr. Kennedy said that when the foreign credit restraint guidelines were stiffened at the first of the year there had been a great demand by many corporations to insure that their foreign credit needs would be met. Because of this demand most banks that operated in the foreign field built up Euro-dollar credits that had not been entirely used. Now that the credit lines were fairly well established for this year, his guess was that there would be some further use of them as corporations were required to answer to the Department of Commerce toward the end of the year.

Governor Robertson asked whether the Council had given any consideration to the problem involved in the move by a number of banks to establish "shell" facilities in the Bahamas. President Mayer replied that the Council had not discussed the question. It was his personal feeling, however, that there was a degree of risk in such operations that some banks might not envisage, for example, if a period of stringency in the Euro-dollar market should occur.

Governor Maisel referred to the Council's statement and inquired whether there was not the possibility that Euro-dollar rates might decline faster than CD rates, thus maintaining the relative attractiveness of Euro-dollars.

Mr. Moore commented that although Euro-dollar rates had eased slightly they were still relatively high. Even though the demand for such funds might not be quite so intense, there was a great deal of activity in that market, with many people involved in borrowing various amounts.

Mr. Kennedy observed that the question involved not only the use of Euro-dollars but also the supply of them, which depended in part upon actions of foreign central banks and the Bank for International Settlements. Moreover, it must be remembered Euro-dollars were used extensively by parties in a variety of countries, not just the U.S. Some U.S. banks had been worried about the supply of Euro-dollars drying up and what they would do if it did, but so far they had been able to get by. In the case of his bank, the choice between Euro-dollars and CD's was primarily reliant on comparative rates at any given time.

4. Are there any particular suggestions that the members of the Council would wish to convey to the Board regarding its implementation of the Truth-in-Lending legislation?

One key feature of the Truth-in-Lending Act is that consumer financing and consumer instalment sales are to be treated basically alike. This was a feature that the banking industry fought hard to achieve. In the case of term loans, instalment loans, and revolving loans, creditors must disclose the annual charge on the same basis. For a time, it appeared that department stores might be permitted to mention only the monthly interest rate on revolving credits whereas banks would have to specify the simple annual rate.

The Council believes that in carrying out the proposed equal treatment of consumer financing and consumer sales industries, the detailed regulation to be promulgated by the Federal Reserve System should aim at as much uniformity as possible within any industry and between one industry and another. There are several leading examples of this:

1. With regard to instalment sales by stores of one kind or another, the time-price differential is clearly a finance charge, comparable to interest rates on instalment loans. Therefore, retail stores should not be given any competitive edge vis-a-vis banks and other lenders in the terms and conditions of contracts and advertising of time-price sales, as compared to the contract and conditions of advertising pertinent to instalment loans made by banks and other lenders.

2. With regard to the advertising of credit cards, the rules should be made precise to insure competitive equality as between banks and other issuers of credit cards. It is clear that, with the possible exception of credit unions, the interest rates and other terms offered to borrowers by commercial banks will be more favorable than those offered by others--e.g., department stores, oil companies, etc. The fact that bank

> terms are more advantageous to the public should not be allowed to be diluted by permitting retail stores to advertise in a way that conceals this matter.

There are several other matters pertaining to bank credit cards that are worth noting:

1. Since the merchant discount feature does not tend to change prices to consumers, there should be no requirement that the merchant discount be included in the required computation of finance charges made to holders of bank credit cards.

2. Since late charges, where applicable, are intended to compensate banks for the special handling costs and other costs associated with late payments, there should be no requirement that late charges be included in the required computation of finance charges to holders of bank credit cards.

Finally, it should be noted that the Truth-in-Lending Act authorized the Federal Reserve Board to waive the Federal statute in the case of any State which enacts substantially similar legislation and enforces it effectively. During the long period in which the Truth-in-Lending Act was being considered in the Congress, the general position of the banking industry was that it would be preferable to have legislation in the field of the disclosure of finance charges enacted by the States, partly because the whole area of interest rates, usury laws and creditors' remedies were already under State regulation and could be adequately handled by the States, and partly because it was felt that if the Federal Government got into the field of disclosure of finance charges, it would soon go beyond that into the field of creditors' remedies--which in fact proved to be the case in the Truth-in-Lending Act. Given the foregoing background, therefore, we would favor action by the Federal Reserve that would facilitate the transfer of administration of truth-in-lending programs to the States under State legislation as quickly as possible, provided only that such State administration would not interfere with the need for uniform administrative interpretation and hence competitive equality as between banks, other lenders, and retail establishments in terms of required contracts, statements of finance charges, and advertising of credit terms.

President Mayer remarked that the Council's answer had drawn upon a memorandum prepared by the staff of the bank of one of the members. In general, banks had found that merchants' representatives were able to serve their own interests well, at the level of State legislatures, frequently to the disadvantage of the banks. The Council believed it would be unfortunate if the same thing were permitted to happen in the case of the Federal truth-in-lending regulations. The principle of like treatment in the Federal statute had been hard won, and the banking industry would hate to see it eroded.

Governor Robertson commented that the drafting of the basic truth-in-lending regulation was almost completed, and that it was hoped to publish the draft regulation for comment by the middle of October. He urged that the Council members give careful consideration to the draft regulation and let the Board have their suggestions, even before the next meeting of the Council if possible. The Truth-in-Lending Advisory Committee, on which the banking industry was represented, had met last week, and some revisions were to be made in the draft regulation as a result of that meeting. He did not believe there was any point that the Council had mentioned in its answer that had not been covered. However, on a matter as broad and complex as this, something may have been overlooked. It was expected that public comments would be allowed until the middle of November, after which they would be analyzed by staff and reviewed by the Advisory Committee. Plans called for issuing the regulation about January 15, 1969, so as to provide a period of several months before its effective date, July 1, 1969.

The Council could be especially helpful, Governor Robertson continued, with respect to the educational program. It would be necessary to educate lenders and sellers as to what was expected of them, and the banks could play a real part. There would remain the problem of educating the users of credit, and at this point he could not say exactly how the program would be carried out. Another problem related to the need for uniform enforcement. Several agencies would be involved, with the Board's own enforcement chore applying only to State member banks.

Governor Robertson concluded by mentioning that the ultimate goal was to shift the administration of truth-in-lending from the Federal Government to the States. The Federal law provided that this shift could take place with respect to any State that adopted substantially similar requirements. However, there would also be the question whether the State's enforcement machinery was adequate.

5. What are the Council's view on monetary and credit policy under current circumstances?

> The Council is aware of the difficulties of determining credit policy because of the delayed impact of the recently enacted fiscal legislation and the lags involved in monetary policy. However, because of the apparent continued strength in the economy, as evidenced by the behavior of most indicators, including retail sales, automobile deliveries, and new orders, as well as the persistence of the upward pressure on prices, many members of the Council believe the recent reduction in the discount rate may have been premature. It is highly important that

the beneficial effects of fiscal restraint not be lost and that the strength of inflationary pressures be lessened.

If and when additional reserves need to be supplied to the system, the Council believes that consideration should be given to a small reduction in reserve requirements rather than using open market operations.

In response to Governor Daane's request for elaboration of the last part of the Council's statement, President Mayer said the Council thought basically that reserve requirements should come down. Mr. Kennedy observed that it seemed only reasonable that changes in reserve requirements should not all be in one direction. If the requirements were increased at times when credit contraction was needed--as they had been--they should be lowered if and when the situation warranted.

Governor Robertson said he would assume none of the Council members believed that monetary policy should be easing at the present time, and responses indicated that the appropriate stance would be to mark time.

Governor Brimmer noted that when reserve requirements were changed it was generally expected that the new rates would remain in place for quite some time. He wondered whether the Council was suggesting that smaller and more frequent changes should be made.

Mr. Kennedy responded that no such suggestion was intended. Reserve requirements were a blunt policy instrument, and open market operations should be used to effect day-to-day adjustments. However, if a need appeared for expansion of the economy, the opportunity should be used to reduce the present requirements, which were too high. That could be done when a reasonably large amount of reserves was to be added, and the change in reserve requirements could be partially offset by open market operations if necessary.

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Mr. Wilkinson then reverted to the question of the proper scope of bank activities and observed that strategically the banking system was facing a real problem. The rise in resources and interest rates had permitted the banks to hold their percentage earned on assets fairly well, but there was a grinding pressure on profit margins because labor costs and money costs were continually going up. Just as Dupont had lessened its dependence on rayon by going to nylon, the banking industry had to press outward toward new services to buttress the profits available from its traditional operations. It was this basic issue that the banking industry was trying to meet.

Governor Daane inquired whether Mr. Wilkinson believed that the cost of money to the banks would be structurally much higher, in response to which Mr. Wilkinson said his guess was that the ability of banks to reduce the cost of their raw material would become much less flexible. The cost of the bulk of their time money was not going to be as flexible as one might think, and the pressure on profit margins would increase.

Mr. Kennedy added that banks were trying to serve their customers better. A revolution was going on in the business world, and customers were demanding a broader range of services. If banks could not meet the needs, their customers would go elsewhere. It would be better if solutions could be found for meeting these needs within the existing framework. While it was true that there was a profit motive in providing new services, many of the services banks were now in position to provide were needed for economic growth.

Mr. Wilkinson commented that the greater the degree to which banks could move along such lines, the less would be the pressure to go into other businesses.

Governor Sherrill said he took it that Mr. Wilkinson would like to encourage liberalization in interpreting what might be thought of as the field of financing. He had sympathy with that viewpoint. But if it was assumed that there should be a boundary, and the present one was not proper, the question was where the new boundary should be drawn.

Mr. Wilkinson expressed the view that experimentation would be necessary.

Governor Maisel referred to the restrictions imposed by State laws, and Mr. Wilkinson said his personal feeling was that the Board should exercise its best judgment within the confines of the Federal law. That would put pressure on the States to modify their laws.

Mr. Conn commented that there was a limit on how far the framework of Federal law could be stretched in interpreting the term "incidental powers" in section 5136 of the Revised Statutes. At some point it might be necessary to seek liberalizing legislation.

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It was understood that the next meeting of the Federal Advisory Council would be held November 18-19, 1968.

The meeting then adjourned.

Secretary