SUMMARY OF STATEMENTS

By

Marriner S. Eccles

on

THE BANKING BILL OF 1935

Page 18 - Eligibility for Discount

"It is proposed to give the Federal Reserve Board authority by regulation to determine the character of paper that may be eligible as a basis for borrowing at the Federal Reserve banks. This is particularly important at this time because it would encourage member banks to pay less attention to the form and maturity of paper that is offered by would-be borrowers and to concentrate their attention on the soundness of such paper. . .

"What is proposed is not, as has been sometimes alleged, a policy of opening the doors of the Federal Reserve banks to all kinds of paper, regardless of its soundness. On the contrary, it is proposed to place emphasis on soundness rather than on the technical form of the paper that is presented."

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". . . As soon as the Emergency Banking Act of 1933 permitted the banks, both member and nonmember, to get credit in the form of currency from the Reserve banks upon all of their sound assets, the people of the country no longer wanted their deposits in currency. The currency began to come back into the banks and deposits in banks increased.

"Many of the assets considered eligible and held to be liquid were less sound than other assets held by banks which could not qualify for rediscount or as security for borrowing from the Reserve banks.

"An asset that may be considered sound and liquid when business is active and there is a high rate of employment and national income is large, may become frozen and unsound if the national income diminishes. Liquidity and soundness are not determined merely by the substance of a loan or asset at the time the asset is purchased or the loan is made; they depend upon the state of trade and business which follows."

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"It is up to the banking system in so far as it is possible, to maintain a state of trade and business that will preserve soundness.

"To the extent that forced deflation through forced credit contraction is obviated through making available the discount facilities of the Reserve banks--to that extent liquidity is provided. The only liquidity that really exists in a serious depression is the liquidity that is provided through the money-issuing agency, the Federal Reserve banks."

Page 31 - Real Estate Loans

"The fact that bonds are listed and, therefore, are supposed to be marketable, is considered a justification for the investment of funds in bonds in preference to real estate loans. The depression proved that during a period of deflation a ready market for bonds existed only at prices that bankrupted the banks,if they were forced to sell. More banks became insolvent as a result of the depreciation of their bond accounts than as the result of their real estate loans. The fact that bonds were listed and were greatly depreciated put the banks into a condition of insolvency when they were examined, because of the difference between the quoted market price and the cost; whereas in the case of real estate loans it was not expected that there should be a ready market for them, and so long as they were not in default, they were valued according to the amount loaned.

"If we want to be so restrictive in the matter of real estate loans, because they represent long-term investments of funds which may be withdrawn on demand, we should also be restrictive with reference to other long-term investments. Either the banks holding $10,000,000,000 of time funds must lose those funds to the savings and loan associations, to mutual savings banks, or to similar agencies, or they must be permitted to use the time funds in the long-term investment field."

MONETARY PROBLEMS OF RECOVERY

Address of Marriner S. Eccles, Governor of the Federal Reserve Board, before Annual Midwinter Meeting of the Ohio Bankers Association, at Columbus, Ohio, February 12, 1935.

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"Banks in this country perform two main services. They act as middlemen for the investment of a substantial portion of the community's savings, and, through the provision of checking facilities, they supply the bulk of the community's means of payment. So far as the investment of savings is concerned, a large degree of local autonomy should be left with the individual bankers. The state should lay down minimum standards to be observed in the interests of protecting savings of individuals, but these standards can only be minima, and chief reliance for the safe investment of the community's savings must rest on the judgment and knowledge of the individual banker."

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"The restriction of the rediscounting privilege to a particular and narrowly restricted type of bank loan is in accordance with a theory of reserve banking which I think we have now outgrown. The major task of the Reserve Administration is not to encourage the extension of a particular type of loan. The restriction of the borrowing privilege to commercial loans has no connection with regulation of the volume of bank credit or of the access to the Reserve banks. . .

"Hence, the elimination of technical restrictions on eligibility does not involve any danger of excessive use of Reserve bank facilities. But it does enable the Reserve banks to come to the assistance of banks who may have sound assets but may be devoid of eligible paper. For the emergency such a provision was made by the Glass-Steagall Act, but not until great harm had resulted from the inability of the member banks to receive help from the Reserve banks in the emergency."

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". . . I refer to the provision permitting banks to make loans on improved real estate up to 75 percent of its appraised value and on an amortization basis for a twenty-year period, and in an aggregate amount up to 60 percent of their time deposits.

"It has been asserted that this is an invitation to banks to make loans of a character that does not conform to sound banking principles

Address by Chairman Eccles
before Annual Midwinter Meeting
of Ohio Bankers Association, Feb. 12, 1935

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or standards. The collapse of real estate values is cited as an illustration of the dangers associated with such loans. It is constantly stated that the troubles of our banking system were due entirely to the acquisition of long-term assets by the banks. It is suggested that banks in the future should confine themselves to short-dated commercial loans and investments. But I need not tell you that, if this suggestion were acted upon, the result would be fatal to the banks. In October 1934, the eligible paper of member banks, within the meaning of the Federal Reserve Act, amounted to only slightly more than two billion dollars. . ."

PP. 18 and 19

"I am fully aware of the fear with which bankers view the extension of other lending agencies and the uneasiness they feel at having to rely more and more on holdings of Government obligations to keep up their income. I might point out, however, that these developments are a consequence of the failure of the banking system to perform its functions adequately. If the banking system would utilize in real estate loans and other long-term investments the savings and excess funds that it now possesses, business activity would be greatly stimulated, and the Government would then be able to withdraw rapidly from the lending field.

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"I am, you will carefully note, criticizing the banking system and not the bankers as individuals. I do not see how you as individual bankers, having to secure liquidity alone and unaided, could safely have followed a different lending policy than you did.

"This, then, is the dilemma that faces the banks. If they go into the longer term lending business, they run the risk of depreciation and of inability to realize quickly upon their assets in case of need. If they do not go into this business, they cannot find an outlet for their funds. Their earnings will suffer and the justification for their existence diminishes. How can this dilemma be solved? It is proposed in the bill to solve it by removing the problem of liquidity as such from the concern of the banks, by bestowing liquidity on all sound assets through making them eligible as a basis of borrowing at the Reserve banks in case of need. This will enable the banks to concentrate their effort on keeping their assets sound and to pay less attention to their form and maturity.

Address by Chairman Eccles
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"Reliance on the form of paper as a guide to soundness and eligibility has not protected the banking system from disaster. We wish to divert bankers' attention from the semblance of paper to its substance; to emphasize soundness, rather than liquidity. To require that a real estate loan shall be repaid in five years, as the present law requires, does not even improve liquidity but rather, through the excessive strain it places on the borrower, acts to promote foreclosures and insolvency.

"What we are proposing is that the problem of liquidity shall cease to be an individual concern and shall become the collective concern of the banking system. A single bank which adopts a policy calculated to pay off all of its deposits at a moment's notice, even though the national income is cut in two, cannot adequately perform its duty of serving its community. Since good local loans go bad when a depression sets in, the bank's portfolio would have to consist of super-liquid open-market paper. What we want to accomplish is to make it possible for banks, without abandoning prudence or care, to meet local needs both for short and for long time funds. We want to make all sound assets liquid by making them rediscountable at the Reserve banks, and then to use the powers of monetary control in an attempt to prevent the recurrence of national conditions which result in radical declines of national income, in the freezing of all bank assets whether they are technically in liquid form or not, and in general unemployment and destitution. . . "

THE BANKING BILL OF 1935

Address by Marriner S. Eccles, Governor of the Federal Reserve Board before the Annual Convention of Pa. Bankers Association at Scranton, Pa., June 5, 1935

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"Another line of criticism of the banking bill is that it would result in a deterioration of the quality of banking assets. On this ground proposed changes in the eligibility and real estate provisions are attacked. The first point to be mentioned in this connection is one that I, from my experience in banking, have well in mind. It is that no matter how desirable short, self-liquidating commercial loans may be, they are not available in sufficient quantity to afford an adequate outlet for the banks' funds.

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". . . If banks are to make a living and serve the borrowing needs of their communities, they must make longer-term loans. If they are to be permitted to accept savings deposits, they should also be permitted to make real estate loans under proper safeguards. We are simply recognizing hard facts, and are endeavoring to make it as safe as possible for banks to serve adequately their own interests and the interests of their communities. We most emphatically are not proposing that banks should make poor loans. For the first time it is proposed to write the phrase, 'sound assets,' into the Federal Reserve Act, and if experience means anything, assets will have to be sound before the Reserve banks will accept them as collateral for advances.

"As bankers, I should think that you would heartily approve a step which looks toward the substance rather than the form of loans; to their quality, rather than to their maturity. I recently had occasion to have an examination made of the form of the assets of all national banks that were suspended in the years 1930-1932, and discovered that on the call dates immediately prior to suspension, real estate loans comprised only 11 percent of total loans and investments; securities held, 30 percent; loans on securities, 18 percent; and all other loans, 41 percent. The bulk of the latter was nominally short-term. It is obvious that a large proportion of paper that is in form short-time commercial paper does not protect the solvency of a bank."

THE CURRENT BUSINESS AND ECONOMIC OUTLOOK

Address by Marriner S. Eccles, Chairman of the Board of Governors of the Federal Reserve System, before the New Jersey Bankers Association Convention in Atlantic City, May 13, 1938

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"Banks can assist in restoring prosperity by affording every possible constructive aid to the revival of sound private financing, and in adapting the lending functions of the banking system to present-day conditions. Federal and state bank examination policies, as well as the Comptroller's regulation governing investment policy, need to be brought into conformity with changed conditions and modern requirements of business and industry. Bankers cannot justly be held responsible for such restrictive governmental banking policies as confuse soundness with liquidity or true worth with current depressed market values. I favor modernization of these practices and regulations, to encourage the bankers to meet changed credit conditions and needs within their own communities, and thus to discourage the alternative which is multiplication of governmental agencies set up to provide credit accommodation that the banking community could and should in normal times be adapted to extend to the public. That accords with my fundamental view that the responsibility of government banking and monetary agencies is to assist the banks to function in the most efficient way to serve the public interest."