Anti-Inflation Program

REMARKS OF HONORABLE H. EARL COOK, DIRECTOR, FEDERAL DEPOSIT INSURANCE CORPORATION, BEFORE THE REGIONAL MEETING OF THE AMERICAN BANKERS ASSOCIATION ON THE ANTI-INFLATION PROGRAM

NEIL HOUSE, COLUMBUS, OHIO JANUARY 23, 1948

Mr. Chairman and gentlemen:

The ABA and FDIC have a common interest in the stability of the economy of our United States

We are met today to discuss and to lay plans control to combat one of the most vicious phenomena of our complex economic world. It is an aspect of that world that in itself has caused and is today causing untold maladjustment and misery, but that is most to be feared because of the utter chaos that follows inevitably when it has run its course.

I refer, of course, to that fifth horseman of the Apocalypse, inflation, and its even more hideous twin, deflation.

Of itself, inflation is not an ominous word; in fact it has a rather pleasant sound. But its connotations are extremely unpleasant. If it occur in a person's ego, then that person is due for an abrupt and unpleasant awakening to reality. If it occur in a toy balloon, then that toy is due for deflation, either through its regular opening or through the more sudden and ignominious death of a loud bang. If it occur to excess in our economy, then the pains that we have felt in the past will seem as nothing to the agony that the future will hold.

The banks, of course, can not win the fight against inflation single-handedly. It is a battle that requires the understanding and the effort and the cumulative force of every individual in this country. But the banks, as credit reservoirs for their communities, and the bankers, as outstanding citizens of those communities can do much by precept, by example, and by patient education to convince our people that inflation cannot, must not and will not be allowed to go its heady way unchecked.

And it is a heady sort of way, comparable in many respects to the exuberant, carefeee, spendthrift glow of a celebrant on New Year's Eve. But just as surely as there is a New Year's Eve with its gaiety and abandon, so there is New Year's Day with its headaches and its remorse and its resolutions. We have tasted the spurious joys of inflation many times before. We also have spent years nursing ourselves back to health after the hangovers set in and vowing that it would never happen again. I hope and pray with all my heart that this time you and I mean what we say, and that we all shall spread the anti-inflation gospel as diligently as the most sincere evangelist preaches his beliefs.

At the risk of oversimplifying a really complex problem, I should like to state as my fundamental belief that the banker can do two things that will retard inflation materially and that will contribute to earlier stability of our economy. These are: First, Bankers must lend only when the credit will increase available supplies of basic raw materials, increase plant capacity, or otherwise help production of needed goods. Second, Bankers must intensify their efforts to encourage savings on the part of their customers to absorb as much as possible of the increased purchasing power that is bidding for the goods and services in short supply. These may seem small plugs thumbs in the dike, but they are steps that will serve effectively as brakes until the full might and resources of the nation can be thrown behind a truly effective anti-inflation program.

The President and the Congress have indicated their awareness of the problem and have taken some steps to unwind the inflationary spiral in an orderly way. There is every indication that the new session of Congress will move further in this direction.

The Federal and State bank supervisory agencies, together with Federal Deposit Insurance Corporation, have made plain their views on what banks should do to help win the fight. In a joint statement issued on November 24, the supervisory agencies and the Corporation said, in part, "Our country is experiencing a boom of dangerous proportions. The volume of bank credit has been greatly inflated in response to the needs for financing the war effort. Domestic and foreign demands for goods and services are exerting a strong upward pressure on prices in spite of the high volume of our physical production. These demands would be inflationary without any further increase in the use of bank credit, but the demand is being steadily increased through continued rapid expansion in bank loans, in addition to other factors outside the control of the banking system.

"A substantial increase in production, agricultural as well as industrial, would be highly beneficial. However, increases can only take place slowly and to a limited degree. In industry, they are dependent upon corresponding increases in the available supply of basic raw materials, plant capacity, and the number and productivity of the labor force. Therefore a further growth of outstanding bank credit tends to add to the already excessive demand and to make for still higher prices.

"The Board of Governors of the Federal Reserve System, the Comptroller of the Currency, the Federal Deposit Insurance Corporation, and the Executive Committee of the National Association of Supervisors of State Banks are unanimously of the view that present conditions require the bankers of the country to exercise extreme caution in their lending policies. It is at times such as these that bad loans are made and future losses become inevitable.

"It is recognized that a continued flow of bank credit is necessary for the production and distribution of goods and services. The banks of the country have adequately met this important need in the reconversion period. Under existing conditions, however, the banks should curtail all loans either to individuals or businesses for speculation in real estate, commodities or securities. They should guard against the over-extension of consumer credit and should not relax the terms of installment financing. As far as possible extension of bank credit under existing conditions should be confined to financing that will help production rather than merely increase consumer demand." End of quote

Let me emphasize on behalf of the supervisory agencies and the Federal Deposit Insurance Corporation that our views on bank credit policies have not altered during the past two months. We are firmly convinced that the pool of consumer purchasing power must be ~~dried up~~ curtailed, rather than augmented, and we believe that judicious use of their lending power by bankers can accomplish at least half that objective.

It is gratifying to see how your own American
The Ohio Bankers & other organizations represented here
Bankers Association has entered into the fight and has organized this splendid program for education and exchange of ideas. In this case, certainly, even the most crass critic could not accuse the bankers of feathering their own nests at the expense of our Nation's welfare.

The program outlined early this month by Mr. Dodge, your ABA president, and currently being elaborated through a series of meetings such as this, has the unqualified approval of the Federal Deposit Insurance Corporation, and I feel safe in saying that the federal and state supervisory agencies share this view.

Mr. Dodge's program parallels that of the supervisory agencies in that he urges rigid restriction of speculative commodity and inventory loans, postponement of mortgage loans for non-essential building, and priority to borrowers who can turn out needed goods and services in order to keep existing plant facilities functioning at maximum levels and in order to encourage the development of new plant capacity.

The program goes ~~a step~~ further than was possible with the supervisors. It urges a greatly intensified drive to sell Treasury savings bonds to the public and to promote other forms of thrift, such as savings accounts in banks, as a means of absorbing some of the surplus money in the spending stream which would otherwise continue to compete for the goods and services in short supply. Obviously, the supervisors cannot, with any hope of success, tell the people to save, rather than to bid against each other for scarce goods. But you bankers, known and respected in your communities, should be able to make it evident to your neighbors that they are doing themselves and the Nation a great disservice in bidding up scarce items. I hope that you will spread wide this gospel, "Make every dollar you lend, produce; make every dollar you spend buy one hundred cents worth of goods or services."

While we are on the subject of saving, I should like to point out that bankers again can teach by example as well as by precept.

The commercial banks emerged from World War II with assets over twice the pre-war total, while capital accounts were only about 25 percent larger. As a consequence, the ratio of capital to total assets declined sharply during the war period and the average now is substantially below the level which in former years was considered to be a safe minimum. The question of adequate capital did not receive much attention during the war, since it was felt that the banks should be free to purchase as many United States government bonds as might be necessary to finance our war effort. However, that condition no longer applies, and both bankers and bank supervisors must reexamine the entire question of the adequacy of bank capital.

Large scale reduction of the Federal debt and a rapid increase in the rate and amount of bank lending during the past two years have altered the composition of banks' total assets in great degree, the net result being that there has been a sizable gain in the ratio of the so-called "risk assets" to total assets in most institutions. It is axiomatic that an increase in risk calls for an increase in the protection against risk--in this case steady and considerable augmentation of bank capital accounts is indicated.

In some instances the sale of new issues of bank capital stock is difficult these days. Sound banking and supervisory policy, therefore, must call for the establishment of adequate reserves against risk assets and for the steady plowing back of bank earnings into capital accounts. The time to save money is when we are making money. The banks are making money, and I urge that they set an example of thrift and husbandry by judicious use of their earnings.

In conclusion, I cannot overemphasize the importance of the role that you bankers must play if we are to win the battle against inflation. The soundness of our whole economy depends upon the soundness of its financial and monetary systems, and you men are the guardians of those systems, charged with responsibility for their health and their proper functioning. Sound bank management is never a simple task. Today it requires more vision, more unselfish service, and more courage than ever before. The financial fate of our Nation rests in the hands of you men and your colleagues. I hope you will meet the challenge of inflation squarely and fight it with every weapon at your command. I am confident we can win the battle.

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