

NEWS RELEASE



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ADAPTING TO THE ONE CONSTANT---CHANGE

Address by

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before the

EXECUTIVE BANKERS CONFERENCE
of the
OHIO BANKERS ASSOCIATION
Neil House

Columbus, Ohio

Wednesday, December 8, 1965
8:00 P. M.

ADAPTING TO THE ONE CONSTANT--CHANGE

You may be assured that the invitation to address you tonight was indeed welcome. It affords an opportunity that I greatly appreciate to meet with each and every one of you. In the bank supervisory agencies we know that our effectiveness is heavily dependent on the formal and informal contacts made with the banking community in conferences such as this one. These occasions give us a deeper and broader appreciation of the aspirations and the problems of the financial institutions under our supervision and thus provide us with the insight and the knowledge so essential to the successful discharge of our responsibilities to foster a vital, dynamic banking system serving the public interest.

Tonight I shall comment briefly on a characteristic of our environment that is always with us--and that is change. Change is an immutable feature of our lives--although this may sound like a paradox. It affects the family unit, the community, the nation, and the world. And it has always been a distinguishing feature of the banking scene. But it seems to me that changes--particularly in banking--have been occurring recently more frequently and faster than in earlier years. This is partly the result of technical advances in transportation and communications, which have permitted greater integration of markets serving the financial community as well as commodity traders--at home as well as abroad. But

changes have also been brought about by political developments--such as closer ties among the free nations of the world and more general recognition of the fundamental interdependence of nations--or by economic developments affecting all nations. These changes in turn have had their impact on the banking industry and on the bank regulatory agencies.

Banks and bank supervisors alike have responded to these changes--at times with a delay and at times promptly. The effectiveness of this response has, as a consequence, varied from time to time and from one situation to the next. But I think I can safely say that banks have proved highly adaptable to the changing circumstances in which they have found themselves--and have also been able on occasion to anticipate change and prepare for it. The members of your association can rightfully lay claim to inclusion in this group.

In the next few moments, I shall review some of the major economic changes since World War II that have had a significant influence on the banking system and at the nature of the response that has been evoked from banks. Then I shall consider the effect of these changes on the bank supervisory agencies and how their responses have been conditioned by new developments.

A brief recital of just a few high points of the period since 1945 will support my conclusion that this nation's banks have chalked up a commendable record in adapting to change. Despite various problems this year, for instance, banks have been able to accommodate sizable demands for

credit and are expected to report record net operating earnings. The record, of course, should not be cause for complacency--for the record is not perfect. But it is a good one--and one that should provide the incentive for improvement.

One of the major economic changes since the end of World War II of current topical importance is the changed--and changing--role of the U.S. dollar. At the end of World War II, the United States was the strongest country in the world, both politically and economically--partly because it had escaped physical damage. The U. S. dollar, as a result, was the most sought-after currency for settlement of international payments and as a universally acceptable store of value. This was the period of the dollar shortage--and of massive U. S. foreign aid programs for reconstruction and rehabilitation. As the wartorn countries recovered from the destruction of war, the U. S. dollar declined in relative importance, and the currencies of other countries--such as Germany, France, and the United Kingdom--gained wider circulation in international payments.

Owing to these developments, the U. S. payments position registered sizable and persistent deficits from 1958 on, and foreign dollar holdings began to increase faster than the need for dollars. In this instance, the response of both the United States and other nations to the emergence of international payments imbalance was slow because the international adjustment mechanism works much less smoothly than the internal adjustment process and because institutional barriers further complicate balance of payments adjustments. Once the nature of the imbalance was understood, however,

remedial measures were taken by the United States and other countries. But progress has been slow since the factors immediately responsible for the deficit have varied over the years and have called for different remedies.

Nevertheless, it can be said that the international payments system is now in a stronger and more balanced condition than before when the dollar was almost the sole international currency. The international payments system, moreover, is currently entering a new phase of its evolution which will test its flexibility and adaptability. The results will affect all of us and necessitate further adaptation.

This nation's response to its over-all payments imbalance consisted of greater reliance on fiscal policy to stimulate domestic economic expansion and on monetary policy to maintain interest rates at levels that would discourage money flows abroad without hampering economic activity at home. The resultant pattern of interest rates, as you all know from experience, has had an important impact on bank operations.

On the domestic scene, the existence of substantial idle plant capacity and relatively high unemployment at the beginning of the current expansion combined with the payments deficit to present a situation unlike any previously encountered. The mix of fiscal policy and monetary policy that was devised to deal with the payments deficit was therefore most appropriate. Its effectiveness has been demonstrated by the durability, strength, and balanced nature of the current economic expansion, which is now entering its 58th month. Payments balance is also being gradually restored, despite occasional setbacks.

But, as the domestic economic expansion continues and as plant capacity and manpower resources become more fully utilized, it is clear that the margin of maneuverability has narrowed. The increased demands occasioned by our commitments in Vietnam, moreover, must be taken into account. Thus, the situation has changed again. Current policies must be tailored to meet these changes--and the tailoring may have to be finer and the impact of various measures more carefully evaluated than was necessary in the early stages of the present expansion. This is the challenge facing us today.

The banking industry has met similar challenges in the past. It is fully equal to the task today. I might cite a few examples here where banks have shown imagination in adjusting to changes in the environment in which they operate. Banks, for example, expanded their activities in the postwar period into mortgage financing and into consumer instalment credit to meet the needs of their customers for housing and for consumer durable goods. More recently, they have made more efficient use of reserve balances through development of the market in Federal funds. With a competitive interest rate structure, they have been able to vie effectively with other financial institutions for the large volume of savings generated by an expanding economy--through time certificates of deposit, savings bonds and certificates, unsecured notes, and debentures. Against the economic background created by the requirements of our international payments position and our domestic economy, they have invested more heavily in higher yielding municipal securities and other assets. To meet the growing credit demands

of the economy, they have expanded their loan portfolios. Relatively heavy investments in loans in turn have been counterbalanced to some extent by greater use of amortized credits and by improved portfolio management practices. This list illustrating bank management adaptability to change could go on and on.

I should like to mention now some of the responses that the Federal Deposit Insurance Corporation is making to changes in the economy at large and in the banking industry in particular. As you remember, the FDIC was organized during the Depression for the primary purpose of restoring public confidence in the banking system. The early history of the Corporation is replete with accounts of the rescue of failing banks, the pay-off of depositors of failed banks, and the strengthening of faltering banks. By the beginning of World War II, however, this mission was largely completed. The banking system served the nation well in wartime and since.

Maintenance of public confidence in our banks continues to be a major concern of the Federal Deposit Insurance Corporation. But the emphasis has shifted--to helping good banks be better banks. It is in this direction that our challenge lies today. We in the Corporation feel that this emphasis will produce the strongest and most effective banking system operating in the public interest.

To help make good banks better, we are currently engaged in developing the capabilities of the Corporation. We are looking ahead and trying to anticipate our needs and our problems in the months and years

ahead. We are undertaking various pioneering studies in banking markets and bank structure to assist us in carrying out our responsibilities. The results are as yet preliminary, but the studies show promise.

As an outgrowth of these various programs, we hope to be able to provide your banks with some helpful management tools. Early next year we are expecting delivery of a computer which will permit us to undertake more sophisticated banking studies using current banking data. We hope to be able to provide data in a form that can be used in studies of market concentration and market penetration, for cost analyses, for comparative studies of financial institutions or particular groups of banks--whether by size, type, location, or other classification. The list can be easily expanded to encompass as yet unexplored fields of investigation. Computerization of banking data--as distinguished from automation of operations--will provide a most valuable tool for bank managers as well as bank supervisors.

Finally, I might mention some programs we are initiating in the area of bank audits. This again is a program that will provide benefits for us and for you. And we pledge our full cooperation in your efforts to develop improved audit techniques and a more uniform system of accounting and reporting. At the present time, we are experimenting with the use of auditor teams in the field along with the regular examining teams in 4 of our 12 districts. Before very long, we hope to have resident auditors in each district who will be concerned with the problem of strengthening

systems of internal control in banks. These, then, are but a few of the ways in which the Corporation is adapting to change--ways which will themselves be modified as circumstances change.

Change is thus a fact of life--and I am sure we are all fully aware of this. Adapting to change is a continuing responsibility--a responsibility that can be difficult when changes occur frequently and the tolerances for error small. This appears to be such a time. Our alternatives may be fewer in number and their impact stronger than heretofore. So, it is essential that we examine all aspects of our current situation closely so that we shall fully understand the implications of action--or inaction. We have adapted to change before--and we can do it again.

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