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Remarks of

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Member

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Being acutely mindful of the old adage, "A prophet is not without honor save among his own people," it is a privilege for me to be with you this morning. It is also an honor to participate with Mrs. Hills and Mr. Connally.

Many of you have commented that I picked a good time to leave the mortgage business and go to work for the U.S. Government. However, I can assure each of you, having seen both sides, that if you think the mortgage business is exciting, you ought to try serving on the Federal Reserve Board at a time when monetary and economic policy are the subject of such intense public discussion. Such service will not only change your point of view, but also change your working hours severely.

From my new point of view, I would like to talk about two subjects which bear on the future of the mortgage banking business.

Although most of you are familiar with Regulation Z, the Truth in Lending requirements, and the Real Estate Settlement Procedures Act -- already tottering under its burden of paperwork and delay -- I doubt if you truly understand the broad range of borrower-lender relationships which are coming under Federal control with the tide of present and proposed legislation. As a quick indicator of the shape of things to come: two other large and sensitive areas of your life and business are to come under governmental monitoring on October 28 -- just eight days away -- when the Fair Credit Billing Act and the Equal Credit Opportunity Act come into force. The Federal Reserve, as Congress directed it to do, has written the regulations implementing these laws.

Let it be clear that I am not attacking the objectives of these laws -- a fairer free enterprise system. Free enterprise will continue to make this the strongest and best nation on earth only if it works properly. But I have a deep and growing concern that what is developing in this "consumer" legislation is the very antithesis of the ways in which a well functioning society should go about improving itself by seeking to release the beneficial energies of freedom of economic choice. There is a contradiction in terms involved; if you can only seek to improve a free society by legislating and regulating the details of its inter-relationships, you have abandoned faith in freedom and put your foot on the path to the authoritarian state. I, for one, believe there continues to live in this country that consensus that our free society should continuously make itself a fairer society by its openness to competition and change as the prime means of assuring betterment for all of us in the future; as our free society has bettered all of us in the past.

But, contrary to the very run of the fabric of our society, I sense an attitude by some claiming to represent consumers that they are vigilante adversaries of all business, particularly creditors. They appear to view creditors as "doing in" consumers, and to feel that it is time to get even. Some of them feel that creditors intentionally have denied certain groups credit, in a hostile selection process. This is the stuff of paralyzing class warfare, which has been the terminal malignancy of many past and some present societies, where people were free.

Within this context of faith in the process of freedom to improve our lives through the forces of competition, we need a better understanding of how free enterprise functions. We need to realize that business, including creditors, depends entirely upon the good will of its customers -- the public at large. Creditors are eager, we should remember to extend credit to all creditworthy people. It is their business to extend loans, not to turn them down.

But customers will not borrow if the cost of credit becomes unrealistic. This, in turn will drive many creditors -- the small and weak first -- out of business. And the many new strictures being placed on lending cannot fail to raise costs. These costs are working in the long run to increase the cost of credit to consumers and other borrowers. To the extent they stultify lending along bureaucratically defined lines, and drive lenders out of business, sources of credit contract. Also, competition is further limited by less innovation on the part of creditors for new ways to attract a customer's business. The recent Real

Estate Settlement Procedures Act is a good example of this type of problem.

In a broader sense, I am concerned that much of this consumer legislation is dealing with the most fundamental of economic relationships. The vital aspect of any economy is the willingness and the ability of its consumers to buy and the willingness and the ability of its providers of goods and services to sell. If consumer protection legislation or regulation, however well intentioned, results in impeding the ability of either of these groups to serve or buy from the other, our economy would be materially damaged. It has been the willingness of our consumers to continue buying and their ability to secure credit to give full effect to their purchasing power which have, to a large measure, led us out of the recession of 1975.

In the months ahead, all of you in your day-to-day operations will be required to change the way you presently do business as a result of new regulations and laws. For example, as I have noted, on October 28th, you will become subject to the Fair Credit Billing Act, the Equal Credit Opportunity Act, and expanded requirements for disclosure of closing costs on transactions not covered by RESPA. Let me encourage each of you to learn as much as you can about these requirements. I also encourage all of you to make positive suggestions for improvement in the implementing of the regulations. Where we in the Federal Reserve have had the task of rule writing, it has been our aim to reflect fully and fairly, as best we can understand it, the intent of Congress in writing these laws. But, like all humans we are subject to error. So you need to let us know when you find, or feel, that we are wrong.

Another aspect of consumer legislation is also causing me some concern, namely, the anti-redlining proposals. Some states have already passed legislation or regulation in this area. Many feel that the Congress is likely to pass legislation this year or next. If the legislation passes nationally, its immediate impact will be to lessen the marketability of mortgages as institutions become currently concerned about saver reaction. Over the long term, I predict that the pendulum will swing back to a more reasonable position.

There are two fundamental issues in this legislation. First, we all need to be reminded that our public policy has been to restrict the number of financial institutions we allow to serve a specific market, as an anti-competitive regulatory means of increasing their safety and soundness. But in thus restricting this ease of entry, the public in turn requires that the financial institution serve the convenience and needs of the community which it is chartered to serve. It seems to me entirely proper that supervisory and regulatory authorities incorporate, in their periodic examination procedure, a determination whether the institution is continuing to properly serve the convenience and needs of its own community. This determination should include the needs of savers as well as borrowers. To me this criterion is as worthy of consideration as the financial soundness of the institution.

Second, against this local need we need to weigh the fundamental concept that our available money and savings, like any other commodity, should serve a national market on a competitive basis. The success of the mortgage banking industry has been our best example that the mobility of capital throughout the country has served the interests of borrowers and savers very well. This mobility means that areas that generate relatively small savings can nevertheless get investment funds. Any attempt to create an isolationist condition ultimately causes retaliatory legislation in some form which will lead, in my view, to less, not more, investment in low income areas.

I like the story a well known Texas mortgage banker told me on this subject. During a discussion with some bankers of an eastern state, he reminded them how over the years they had exported their surplus savings capital to Texas where they were able to get a better price for it than they could in their own local markets. Now it looked like they were about to stop doing so. He felt that the people of Texas should review their current policy of exporting their surplus petroleum products. Maybe they had best keep all their oil at home and use it exclusively for Texans. To me, this story points out that one action may make about as much sense as the other.

All of you have heard of the electronic funds transfer system, the National Commission which has been authorized, and the public discussions which are taking place concerning them. It is important to you to recognize that these discussions are not whether this country will have such a system, but how it will be operated. As the electronics funds transfer system matures, it will have a dramatic impact on the methods, procedures, and even the contracts for mortgage servicing, as it increases the mobility of funds.

Let me give you a future possibility to illustrate my point. Before long, it will be possible for a large mortgage investor - let's use FNMA as an example - to offer each mortgagor an 1/8th percent discount on his interest rate, if the mortgagor will authorize FNMA to draw directly on the borrower's bank account for the amounts necessary to make his monthly mortgage payments. It might even be possible that the borrower's bank would guarantee that funds would be available through its willingness to charge the borrower's credit card account for any overdrafts. FNMA could then deposit a magnetic tape, drawing for every loan in its portfolio by designating each mortgagor's bank account number and the correct amount. Through this means, FNMA would get credit for all of these monthly payments in only two days and begin to earn the interest thereon.

The mortgage service would then be able to concentrate on giving more personalized service, deliquencies and attention to problem loans. Such a procedure would change the role of the servicing agent and obviously require changes in their compensation for this service.

While some of you may be thinking that this example may be far fetched, I will predict that similar techniques will be developed much sooner than you realize. The ability of mortgage banking to respond to these changes and to provide better service to borrowers and investors, at lower cost to each, will be the key to the industry's survival and future growth.

During the course of several personal discussions concerning my prospective service on the Federal Reserve Board, I was asked why mortgage bankers, in contrast to other sectors of the housing related industries, usually advocated a more conservative monetary and fiscal position. I feel that this has been true for several reasons.

First, mortgage banking is fundamentally a long range business. When a firm services loans for a thirty year period for declining compensation, it is in a very tangible way, dependent on ultimate control of inflation and on long term economic stability. If these conditions do not exist, the servicing contract becomes a liability rather than an asset.

Mortgage bankers have also seen how inflation has destroyed some real estate value. Unlike bonds, investment real estate has no maturity for repayment of principal. It is dependent on the capitalization of its current cash flow for current values. Inflation has driven up operating costs faster than gross rents. Inflation has driven up the rates of return on capital, resulting in substantially lower real estate market values, even where cash flows have been stable.

Mortgage bankers have seen past public policies result in higher and higher interest rates. These have increased the cost of housing and, thus, decreased the number of potential borrowers in the market for their services. Mortgage companies fared much better when borrowers were paying 4 percent than when they were paying 10 percent.

Mortgage bankers have always had to market mortgages and other real estate credit in broad competition with alternative forms of investment of every type. They have not been circumscribed by limitations and protections designed to assure them a preferential place in the market.

In doing so they know that a stable growing economy, without inflation, has, in the long run, produced the most funds for the most people at the most reasonable cost.

Finally, and most importantly, I am convinced by my twenty-five years of personal association with so many of you, that you are the type of people who place the welfare of the nation first, and your own selfish interests second. You are the type of people with ability to weigh the quick benefits of a current policy against the long term viability of our society and its institutions. Our country needs more people like you who will speak out, not only through trade associations, but who also stand up personally for the things they believe.

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