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Address of J. L. Robertson, Member of

Board of Governors of the Federal Reserve System

before the

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Telling fairy tales is not a specialty of mine, but having had the privilege of being on your program in prior years, I must tell you of the little boy who was taken by his mother to see the picture "Snow White and the Seven Dwarfs". They arrived about half-way through the movie, just before Snow White took a bite of the witch's poisoned apple. Then they left at the same point in the next showing. As they walked up the aisle, the little boy kept glancing over his shoulder trying to get that last glimpse of the screen. Finally, he said to his mother: "If she takes a bite of that apple again, she's crazy!"

Now, far be it from me to question the judgment of your officers in inviting me to be with you again this year. For my part, any excuse I can use to get back to Nebraska is a good one. The only thing that troubled me about coming back this time was the question: What will I talk about?

I could talk about the dollar - and about how the dollar doesn't do as much for people as it used to. But I knew if I did that, I should have to point out in some detail that people are not doing as much for the dollar as they used to. Finally, I decided to talk about an institution intimately affecting both people and the dollar, namely, the Federal Reserve System. I shall pursue this subject despite the facts that, first, only one out of three banks in Nebraska - and none of the three banks in my home town of Broken Bow - is a Federal Reserve member; and second, that talking about the Federal Reserve will expose me to charges of boasting, or of the even worse crime of trying to entice new members into the System.

There are, however, considerations on the other side. After all, 74 per cent of the bank deposits in Nebraska are in member banks. Also, many of Nebraska's 277 nonmembers are banks that could not qualify for membership until the capital requirements law was amended just four months ago.

Still other reasons make the Federal Reserve System the most fitting topic for me to talk about today. One is that in recent months we have heard so many derogatory things about certain parts of government that, in fairness to other parts of it, something ought to be said on the other side. A second is that most people know little about the Federal Reserve System in spite of the bearing it has upon their lives and fortunes as one of the world's great reservoirs of economic strength. And a third is that, being a native of Nebraska, and having served on the Federal Reserve Board for nine months, I think it appropriate to report to you on what I have learned about it firsthand.

Of course, everybody knows some things about the Federal Reserve System. To almost everybody, it means a nationwide organization of some

7,000 member banks holding 85 per cent of the bank resources of the country, twelve regionally-located Federal Reserve Banks with twenty-four branches (one located in Omaha), and a Board of Governors in Washington composed of men appointed by the President with the advice and consent of the Senate.

The thought of the regional Federal Reserve Banks, for most people, is a reminder of the many services the System provides for American business and finance. They picture these banks in terms of the amount of currency they handle each year - enough bills to make a stack 350 miles high, which in falling would litter the highways from Omaha to Minneapolis with one, five, ten, and twenty dollar bills. Or they see the banks clearing checks, your checks and mine - 20,000 checks each minute we sit here, enough in a year to reach to the moon and half-way back.

But there is another less spectacular and less well known side of the Federal Reserve System. First of all, it is an efficient organization of 20,000 people, all working toward a single goal: serving the public interest by helping to keep the economy moving along on an even keel, adequately supplied - but not overloaded - with the money needed for producing goods and services on the American scale. It is not a government organization in the usual sense. The people who work for it are not hired as government employees, and they are not paid from government funds. The Federal Reserve does not operate on tax money. Quite to the contrary, it turns over to the government each year the bulk of its earnings, a turnover amounting last year to more than a quarter of a billion dollars.

Yet this organization, which works exclusively for the people, must be classed as "government" in the highest sense. It is an organization that operates in a nonpolitical way to join the hands of banking and government to further the prosperity of American agriculture, industry, and commerce.

In fact, as I see it, the System constitutes one of the best illustrations of democracy at work. The team of 20,000 Federal Reserve workers is directed by more than 250 private citizens. These are the men who serve as directors of the Reserve Banks and their branches - men who contribute their time and efforts to make the organization's performance efficient and effective. To read the roster of their names is to know that they rank among the leading citizens of the nation. They might well be called the keymen in the Federal Reserve System. They serve as listening posts through which the System can keep an ear on the heartbeat of the economy across the nation. They provide advice and counsel that help the System in formulating policy to keep that heartbeat strong.

Nobody would think of labeling these directors as government employees, yet I am sure everyone would agree that they are public servants, for they have dedicated themselves to carry out a public function in the public interest - their reward being the satisfaction they get from doing their country a service.

Now in these past nine months, I have not been able to meet all the directors or all of the 20,000 men and women of the Federal Reserve. But I have been able to observe the work of many of them, including all the Chairmen of the Boards of Directors of the Federal Reserve Banks, the Presidents of those banks, the members of the staff of some of them, the members of the Federal Advisory Council, and, of course, the members of the Board of Governors and all of its key personnel. And I want to report to you that among all of those people there runs a single chord, tying them to the characteristic of the Federal Reserve that I like best - integrity. In any organization, public or private, brilliance is desirable, but integrity is essential.

Notwithstanding your familiarity with it, let me discuss for a moment the job the Federal Reserve has to do, and how it carries out its responsibilities, with the cooperation and support of the System membership. And then I hope you will give me, as some of you have in the past, the benefit of your experience, and counsel, so that together we can work for improvement.

Besides providing an elastic currency and serving as lender of last resort, the System bears primary responsibility for influencing the supply, availability, and cost of money and credit. Here the objective is, on the one hand, to prevent excessive expansion in the money supply and thus to curb inflationary pressures; on the other hand, to prevent excessive contraction in the money supply that could accentuate deflationary forces.

The method of contracting or expanding the supply of money and credit varies considerably under different economic conditions, but the Board's principal means include selling or purchasing government securities in the open market and extending credit to member banks through discount operations. Changes in member bank reserve requirements must also be listed as a tool which can be used to affect the availability of credit, even though it is a rather inflexible instrument of monetary policy.

Powerful though System actions can be in mitigating economic swings and preserving the integrity of the dollar, I hope no one is laboring under the misapprehension that monetary measures alone can achieve the goal of stability at high levels of production and employment. Many other factors, both public and private, play important roles. Fiscal operations of the federal government are a primary influence, especially with the government's income, expenditures, and debt at present high levels. The activities of consumers and businessmen are important, particularly as they increase or decrease their use of credit and their rate of spending. All of which underscores the need for coordinated public and private action if the stability of our economy is to be assured.

To help provide a basis for coordinated action, the Federal Reserve System undertakes another activity: developing information adding to the knowledge and understanding of economic forces and factors, both here and abroad. One important purpose in providing this information is to facilitate the job of the men who manage the member banks of the System.

I noticed that the October issue of "Banking" magazine asked five prominent economists to pick out, for the benefit of busy bankers, the most important economic indicators available from all sources - a sort of "All American" team for the man who doesn't have time to keep up with all the players. Three Federal Reserve reports were placed among the ten top indicators by four of the five members of this economic panel. Several other Federal Reserve statistical reports were nominated by one or more of the economists.

Without the aid of banks and business concerns throughout the country, some parts of our contribution to economic thought would be impossible, and I want to express our appreciation for the cooperation of those who help by informing us about their operations. I have great confidence in the information you furnish us and you can have full confidence, too, in the information we give you in return. I have heard competent outsiders describe the research staffs of the Board and the Reserve Banks - which sift, compile, and evaluate the economic information assembled by the System - as "the best in the business". I shall not gild the lily by adding my own appraisal, but I will say that the Federal Reserve places the same emphasis on the integrity of its economic data, as it does on its other operations.

Now, lest anyone be misled into believing that - despite my protestations - I am bent on enticing nonmember banks to join the System, I would like to devote a minute or two to the subject of bank supervision.

When the Federal Reserve Act was adopted nearly forty years ago, one of the three objectives set out in its preamble was to establish "a more effective supervision of banking in the United States". This was in spite of the fact that the Comptroller of the Currency already had and still has primary responsibility for the supervision of national banks and state supervisory authorities occupy a similar role for state-chartered banks.

Why did Congress connect supervision with authority to regulate money and credit? Not with the idea that supervision through the examining process should be used as a tool to carry out economic policies. The Federal Reserve System can and does make a very great contribution toward moderating business fluctuations and maintaining high levels of employment and production, but it does so as a reserve banking institution, working through open market operations, discount policies, and reserve requirements - <u>not</u> bank supervision. The Board of Governors made this clear in its replies to the Patman Committee's Questionnaire early this year.

The real reason for connecting the task of bank supervision with the authority to regulate money and credit was that Congress realized that an effective reserve banking system had to be predicated upon a sound commercial banking system.

We on the Federal Reserve Board believe the purpose of bank supervision is to aid in the maintenance of a system of strong individual banks, with sound assets, sound management, and sound operating policies. If we can fortify the banking system by developing strong banks in times like these, banks which are responsive to changing conditions as well as to the needs of their communities, those same banks will be a mighty bulwark against the forces of instability.

Today, things are pretty good in Nebraska. People are making money. There have been no bank failures for a long time. In fact, banks here have taken very few losses during recent years. But let me ask: Will these conditions obtain always? How long has it been since the last really bad crop year in Nebraska? How long since you had two or more successive bad years?

Let us think a minute about agriculture, remembering that farming provides more than one-fourth of the individual income of Nebraskans and that the economy of Nebraska is much more directly dependent on prosperous agricultural conditions than is the country at large.

For the last five years cash receipts from farm marketings in Nebraska have averaged more than a billion dollars. That is an increase of more than 400 per cent since 1940, far outstripping the increase for the nation as a whole. According to the Department of Agriculture, the average income of Nebraska farmers is almost twice the average of other American farmers. This shows how much the enterprise and hard work of Nebraskans can accomplish, with an assist from the weather.

I'm sure we can bank on continued enterprise and hard work by the people of our state. I wish the same could be said for the weather. It troubled me to read a newspaper report a couple of weeks ago that parts of Nebraska, along with adjacent areas in the nation's bread and meat basket, were feeling the effects of drought - that cattle were being placed on winter feed earlier than usual, and that rain was needed rather badly for the fall planting of wheat and grass crops.

The Federal Reserve System, as I said before, can exercise great influence over some causes of economic fluctuations, but to my knowledge no one has yet found a really effective way of controlling the weather.

Common sense dictates looking realistically at the possibilities - the vagaries of the weather, the increased out-of-pocket costs that have accompanied the increased mechanization of Nebraska farms - when one tries to visualize a need for meeting unusual credit demands and when one considers the problem of constructive banking in all kinds of economic circumstances.

We in the Federal Reserve recognize that, in certain events, the Reserve System would have to do far more than it has ever done before in meeting the credit needs of its member banks and thus keeping the transmission of our economic machine properly oiled. Fortunately, the System today is in a better position than ever before to lend its assistance to member banks in times of need. But in return - we believe member banks must earn the right to that assistance by the exercise of prudence and the adherence to sound banking principles in times like the present.

The Federal Reserve does not stand in the front-line trenches of bank supervision with respect to either national or state member banks. As I mentioned before, that position is held by the Comptroller of the Currency and the state bank supervisors. But when Congress imposed on the Board of Governors the task of making bank supervision more effective, it vested in the Board certain powers. For example, it empowered the Board under certain circumstances to remove officers and directors of member banks, to bar member banks from access to the credit facilities of the Federal Reserve, and to oust state banks from membership. Therefore, it is the duty of the System to insist on sound member banks and, if necessary, to use all its powers to achieve that end.

This is not a "club in the closet" approach to bank supervision. It is merely a statement of one of the principles of Federal Reserve policy that bankers are entitled to know. You should also know the reasons therefor.

First, there can be no possible doubt that Congress intended that the Board should exercise its powers to the end that membership in the Federal Reserve System shall constitute a badge of distinction. Second, the Board recognizes that it has an obligation to exercise its supervisory powers in a manner which will to the fullest possible extent protect soundly-managed, soundly-capitalized member banks from the devastating effects of failures of poor ones. Third, if a bank cannot operate soundly in times like these, it has no business being in the System, for in times of stress its failure might jeopardize the benefits which member banks are justified in expecting from the Federal Reserve System. The integrity of the System is more important than the continued membership of any bank. Widespread membership is certainly desirable, but it is more important to have the System composed of good banks than to have the largest possible membership.

All of us realize that the ideal concept of bank supervision can not be put into practice unless there is profound mutual understanding and confidence between the banks and the supervisors. Real progress has been made in this direction over the past few years. Supervisory authorities are aware that further progress depends to some extent, at least, on constantly improving the competence of the examining forces.

With this in mind, the three federal authorities have established in Washington an Inter-Agency Bank Examination School. The first experimental five-week session has just been completed and we are ready to launch another. Like the first one, this class will be picked from among the newer assistant examiners of the three agencies in every section of the country. The faculty is drawn from the top men of each agency. As bankers, you will be interested to know that as a part of the school, we set up a model $4,000,000 bank - complete in every essential detail - to be used as a training ground.

After finishing the school's intensive course, even a young man who has never before seen the "inside" of a bank should not only know more about how to perform his work, but also understand the why's and wherefore's of basic bank records and how to check them.

It is my hope that next year we can establish a graduate school for men who have served their apprenticeship as assistant examiners and are ready to be commissioned as full-fledged examiners.

This school, which in my opinion has great potentialities, could not have been launched without the wholehearted cooperation of the Comptroller of the Currency, Preston Delano, and Chairman Maple Harl and Director Earl Cook of the Federal Deposit Insurance Corporation. It represents one of the finest examples of cooperation among agencies that I have seen in my quarter-century of government service. From the beginning, there has never been a question about who should do the work, or who would get the credit. Everyone pitched in, and the result was an outstanding example of government at its best, working with only one aim - to improve the public service.

I am very glad to be able to bring this example to your attention, and urge you to interest yourselves in other examples of government in action.

If the public service is to be improved, especially now that it has reached such gargantuan size, the people of this country must stop looking at government as something apart from themselves, something manned by men who are continually trying to get their hands on new levers of control. They must start looking at government in its true character, as the servant of the people, composed of men and women who are a cross-section of the people, and who are subject to the will of the people.

It is imperative that we regain some of what we lost with the passing of the frontier, stop looking to government for paternalistic support and protection, and once more stand on our own feet and look to each other for aid and assistance, because power for good is dependent upon the combined strength of us all.