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Address of J. L. Robertson, Member of the
Board of Governors of the Federal Reserve System

before

The Independent Bankers Association
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"Emerging Challenges"

After I accepted your invitation to meet with you today I began to ponder the situations you have faced in the past, are facing now, and must face in the future. In doing so I was struck by the tremendous changes that have taken place in this country during the past half century.

The Industrial Revolution began two hundred years ago, but most of us were born into a world that in some ways was closer to 1757 than to the world we know in 1957. It is true that when the twentieth century began our country had a network of railroads, tremendous factories, universal education, pasteurized milk, typhoid inoculation; but - viewed broadly - at the turn of the century the characteristic way of life of most Americans was restricted and provincial. Over a third of our people lived on farms.

I can remember as a boy - as can those of you who were lucky enough to live in a place like my home town of Broken Bow, Nebraska - the lamplighter riding by on horseback and standing on his saddle to light the gas lamps which lit the unpaved streets. At that time the carriage and wagon industry was still putting up a game though losing battle against the automobile, and more than a few people considered airplanes a defiance of heaven. In 1920 the first radio station began to broadcast. Twenty years ago the medicines that we have already stopped calling "miracle drugs" were still in the experimental stage, and the whole field of nuclear energy had barely passed beyond the threshold of theoretical physics. We can hardly recall our existence before the days of wide straight highways, over sixty million automobiles and trucks, air travel, radio and television, dial telephones, and air conditioning.

This same period has witnessed the emotional and physical strains produced by two world wars, several booms and a disastrous bust, floods, droughts, inflation and deflation, and what have you.

The increasing industrialization of our country and the increased recognition of the obligation and the power of the government to promote economic stability and progress have led to changes both in law and in the philosophy of American banking which have changed the American bank - almost beyond recognition - externally and internally.

If the president of a small bank of fifty years ago were to reappear today and look over the institution, he would have difficulty believing what he saw. Its very size would astonish him; its loan portfolio would be unrecognizable; and there would be something else that he never saw before - an investment portfolio. I suspect he might be somewhat confounded by the existence of such things as Federal insurance of

deposits, government guarantees of one sort or another, and a host of so-called built-in stabilizers designed to moderate business cycles, strengthen the banking structure, and encourage public confidence. If he browsed around a bit among people on the street I believe he would be amazed at the universal assumption that deposits in bank are as safe as currency in pocket - and much of the time a lot more convenient.

Our economy has been one of remarkable long-term growth, marred and scarred from time to time by cyclical ebbs and flows of varying severity and duration. The process of growth has been one of continuing, if irregular, adaptation to changing conditions. Despite important structural changes, the United States still has a highly competitive free-enterprise economy. The banking system, and financial institutions generally, as an integral part of the economy, have made major adaptations, although not without a considerable amount of growing pains and many mistakes. This process is still going on, although somewhat slower than some of us would have it. On occasion, adaptation has been too long delayed or inadequate, with unfortunate consequences. Today, as in the past, our ability to meet emerging challenges promptly and effectively will determine our economic future.

It is for that reason that I would like to delve into the future - the not too distant future - and try to see some of the probable changes which will present challenges for bankers. I do so with some trepidation, for like others I have been spending practically all my time trying to keep abreast of changes as they occur - a task which is more than full time by itself. I suspect that most of us have felt satisfied with just holding our place, and in this we have - with perhaps more luck than we deserve - been fairly successful; but for the future, I prophesy, that will not be enough.

Not being an economist, I am free from the inhibitions that discourage those professionals from making bold prognostications about the future. As a matter of fact, it does not take too much imagination to see what I see in the crystal ball - always absent war. In the time available it is impossible to present the details of the picture, but perhaps a glimpse here and there will suffice for my purposes, and you can fill in the gaps according to your own views.

I see a country in 1965 - only eight years off - of about 193 million people crowded around metropolitan centers, but stretching out further and further along arterial roads, extending the present phenomenon of suburbia. Since 1950 the population growth of 10% has been mainly concentrated in areas surrounding major cities. Within standard metropolitan areas the outlying parts grew about six times as rapidly as the cities themselves, and the increase in metropolitan areas was about four times that for other parts of the country. The picture of the future

comes into focus a little better when we add the fact that while the population of the United States is expected to rise by 17% from 1955 to 1965, a projection of present trends indicates startling redistributions. For example, the anticipated increase in population of the five states expected to grow most rapidly ranges from 36% to 63%, while at the other extreme some states are expected to show declines ranging up to 15%.

And what about the economy as a whole? Here a very few strokes will serve to sketch the picture. Since 1929 the gross national product has risen to \$412 billion - it has more than doubled after allowing for higher prices. By 1965 - assuming a continuation in the increase of the labor force (it should be about 80 million by then as compared with 71 million now) and of productivity per man-hour (the annual increase has averaged $2\frac{1}{2}\%$ over the past quarter century and nearly $3\frac{1}{2}\%$ over the past decade) - even with a moderate decline in average hours, a gross national product of \$550 billion or more (in 1956 prices) is not only possible but probable.

Under these conditions, disposable personal income in 1965 might be up as much as a third - over a hundred billion dollars more for the American people to spend annually.

To provide for the expanding volume of transactions that will accompany growth in total output and employment, the nation's money supply will have to grow. On the basis of a gross national product of \$550 billion in 1965, the money supply may expand by roughly \$40 billion to around \$175 billion, of which, as at present, demand deposits will likely continue to account for about 80% of the total, and currency 20%.

With respect to the role of government in the general economic picture, I decline to prognosticate, but it cannot be ignored. In 1929, government as a whole, Federal, State, and local, took approximately 8% of the gross national product; today it takes close to 20%. National security expenditures alone now take 10% of product, a larger share than was taken by all of government in 1929. Again in 1929, the federal debt was in the neighborhood of \$16 billion; today it is \$277 billion.

During this period, government agencies have become more important generally in relation to financial institutions. Of particular relevance to the banking community has been the expanded role of the Federal Reserve and the establishment of Federal deposit insurance. And with these changes there has come about a changing attitude toward the role of government in the economy. Perhaps the most significant is the widespread belief that the government can and should take vigorous action to combat serious recession. The passage of the Employment Act of 1946

signalized a widespread acceptance of this attitude, and confidence in the government's willingness and ability to act in this way continues to flourish.

Another factor which must be mentioned, regrettably, is that average consumer prices are 60% higher than in 1929, notwithstanding the fact that there have been some periods of fairly stable average prices - for example, the last five years, excluding perhaps the past year, when upward pressures have gained the ascendancy. At the moment many observers seem to believe that the scales of the future are now tipped in the direction of more or less persistent increases in prices - a mild creeping inflation. I cannot share this view, and indeed I deplore the complacency with which it is accepted in some quarters. Clearly the major challenge to monetary and fiscal policy is to contribute to the maintenance of relatively stable growth, without inflation. Consequently, in the background of my picture of the future is a general environment of steady economic growth (subject to inevitable fluctuations), reasonably full utilization of manpower and industrial resources, and stable average prices, consistent with the aims of the Employment Act of 1946.

I realize this is a rather hazy outline of America in 1965, but it is enough to indicate some of the challenges which are going to face you bankers increasingly in the years ahead. No doubt some of you will see them more clearly than I do, but permit me to mention just a few that are apparent from where I sit.

One thing this prognostication certainly means is that while some small banks may remain small banks, if they are located in the less populated areas, many will become what we now think of as large banks. Unquestionably the growth in incomes and product in the next ten years will bring with it further expansion of banks as they meet demands for a widening range of services.

It means that banks must utilize to the fullest extent technological developments to expedite the work of handling more efficiently and more economically larger and larger volumes of checks and banking transactions. With total and average incomes rising, as they most surely will, there will be substantial growth in number and amount of deposit accounts - both demand and time. Mechanization of banking procedures is now widespread but still inadequate. Many new devices capable of adaptation to banking are becoming available or are in process of development. Already several banks are using electronic devices with vast memories in which to store and process information about their customers' accounts.

It means that loan demands - both individual and aggregate - will be larger and banks must be in a position to handle them. Borrowing

needs will be greater, and perhaps significantly different from today, depending on the way in which technological developments alter existing industries and bring about the creation of new ones.

It means that banks will have to increase their earnings in order to attract more capital and to pay both officers and employees more adequately. Already, population and industrial relocations, with their accompanying shifts of deposits, have strained the capital and even the managerial resources of many banks.

It means that banks must devise ways of attracting a higher percentage of the most intelligent young people into the banking business by adequate salaries and pension plans, by appropriate incentives and training. Of course, every bank today thinks it has the best possible management, but I can tell you, from long experience, that most of the ills to which banking is susceptible can be traced to management deficiencies. Banks will have to redouble their efforts if they are to obtain a fair share of the most capable college graduates and prepare adequately for management succession in the years ahead.

And finally, it means that there will be a definite need for more banking offices and facilities. The manner in which this need will be met will give rise to serious questions. We may be compelled to revise our views as to the type of banking that is best for America. We may have to admit that there is no single type that will ideally meet all requirements. Perhaps there is a proper place for various types of operations.

There has been great debate as to the relative efficiency of large-, medium-, and small-scale enterprises in different areas of production and distribution, but most of us noneconomists have a general sense that in many fields of endeavor big organizations can produce and distribute at lower cost per unit than smaller organizations. We also feel, however, that if these drives toward efficiency and economy, toward maximum utilization of technology on a large scale, are not subjected to some curbs, they can lead to a state of affairs in which scope for initiative, individual independence, and incentive to further advance could be smothered by the inertia and repression that sometimes go with monopoly and undesirable concentrations of power - not only economic, but also social and political.

This conflict is nowhere more evident than in banking and finance, and nowhere more significant. This is where you and I may have real difficulty in seeing the whole picture. Accustomed as we are to a highly competitive banking system, we sometimes forget how essential such a system is to an aggressive "opportunity" economy like ours. Without

ready availability of credit and other banking facilities, much of our economic progress would be impossible. For this reason the maintenance of vigorous competitive banking is absolutely indispensable, and I believe that a recognition of this principle underlies the existence of such organizations as the Independent Bankers Association.

There is always a temptation to deny the existence of facts that do not harmonize with what we regard as sound principles. But we cannot be true to our responsibilities to the American people and hide our heads in the sand at the same time.

First then, let us agree that some bank consolidations may be motivated by a desire for size and power alone, rather than efficiency, and secondly, that there are some limits to the increased-efficiency curve of large-scale operations. But at the same time let us not deny, for example, that as a matter of dollars-and-cents costs and results, a multiple-office banking organization with low overhead, small staff, uniform procedures, head-office supervision, and locations throughout a large metropolitan area oftentimes can render good service at lower cost than an equal number of separate institutions - in fact, can exist profitably and render valuable service in circumstances where a unit bank would go out of business. I am convinced that we can deal with the problems of American banking organization more effectively if we concede such basic facts - to the extent they are true - and proceed from there.

Perhaps we must conclude at some point that efficiency and economy can be bought at too high a price, and that we should deliberately arrest progress in that direction in order to preserve values that we consider even more precious. But let us make these decisions with our eyes open and after the most careful consideration. Rarely are such problems matters of black and white, or even of black and red, and this is certainly true of the problems that face American banking today, and will be to an even greater degree in the future as our population clusters become even more concentrated.

In trying to spell out in part what the changing picture means for banking, I must not fail to mention a few things that it does not mean. Certainly it does not mean that all an independent banker has to do from here on is to sit on his hands, and hope that some large bank or holding company will come along with an offer to buy his institution for more than it is worth plus a generous pension for the managing officer who helps to put over the deal. It definitely does not mean that we can continue in good conscience - or as good business - to give only the kind of service which our fathers thought was sufficient.

The American people and American business are entitled to readily-accessible, economical, efficient banking service, and one way or another

they are going to have it. It is our duty to furnish the country with the kind of service it must have in order to continue its economic progress. Therefore, let us meet the challenges constructively, and not throw up roadblocks that might prevent further advance.

Early in the nineteenth century there was an organization in northern England called the Luddites, who opposed the introduction of machinery into the textile industry and set out to destroy machines and factories. Their aim was to preserve the right of individuals to earn their living in their own homes bent over a spinning wheel sixteen hours a day. If, inconceivably, they had succeeded, the industrial revolution would have been retarded and the appalling squalor and abject poverty of the eighteenth century prolonged in England. Of course, the tides of progress and change could not be checked. Nor can they be now.

To meet the needs of the future we must devise progressive programs designed to aid the American people to achieve long-term stable economic growth and a continuously higher standard of living. This can be done, but it means that we must guard against complacency, lethargy, and - particularly - a "Let someone else do it" attitude. We cannot continue to live off the fat of the past. We cannot permit sentiment to cloud our thinking.

Let me repeat: the first obligation of the American banking industry is to furnish adequate service to the American people. In steadily broadening this service, as we must, we will encounter conflicting considerations. On the one hand are arrayed efficiency, economy, and ever-improving technology; on the other - but not necessarily in conflict - are individual opportunity and scope for initiative, and the dangers of excessive centralization of economic power. If we fix our eyes and minds on only one side of the picture we may retard unnecessarily the achievement of the economic and social values that are inherent in a due recognition of the opposite factors. We must accept the fact that we are challenged by problems that have no perfect solution - where is perfection in this world? We must seek with intelligence, courage, and restraint a solution that will give the American people convenient and efficient banking service, while maintaining the principles of opportunity, initiative, and competition that have made the American economic system the envy of the world.

All this may seem to you - as it seemed to me when I first thought about it - to be pretty insignificant when compared with the events and problems which are shaking the world today. It is difficult to devote one's energies and abilities fully to the proper ordering of the affairs of one bank, or even the banking system, while all the time, in the back of our minds, is the realization that civilization itself may be blown up any moment.

This is our psychological difficulty today. We tend to feel our success or failure - in fact, our survival or destruction - depends less on our own efforts than on the impact of decisions and events over which we have no control. We sit beneath a Sword of Damocles.

But feelings like these must be overcome. We must discipline our minds and characters to grapple with and master the complexities of our problems. We must possess insight and courage to a degree that men are seldom called upon to exhibit. We must accept the fact that no man completely controls his destiny today; that the work of each of us is a necessary part of a vast and intricate system; and above all, that if each of us feels that his job is not important enough, and therefore neglects it, our civilization is headed for collapse, with or without atomic warfare.

Whatever else America stands for, it symbolizes a way of life in which each individual strives mightily for his heart's desire, and at the same time recognizes the paramount importance of the general welfare, and is willing as a citizen to subordinate selfish interests to the much greater good of his community or his country. This we know and this we can hold to as each of us strives, despite the hazards of the Atomic Age, to contribute to the general welfare by doing his own job to the very best of his ability.