

# FEDERAL RESERVE BANK OF CHICAGO



# ANNUAL REPORT 1968

The year in review .....	3
Regulatory changes .....	13
The bank's operations .....	15
Financial statements .....	20
Directors .....	22
Officers .....	23
Appointments, elections, and retirements .....	24

**To member-banks of the  
Seventh Federal Reserve District**

Business activity continued to increase. The performance was marred, however, by excessive price inflation. The year saw, for example, both one of the decade's biggest increases in total spending and the fastest rise in prices since the outbreak of the Korean War. The outlook for 1969 is far from certain.

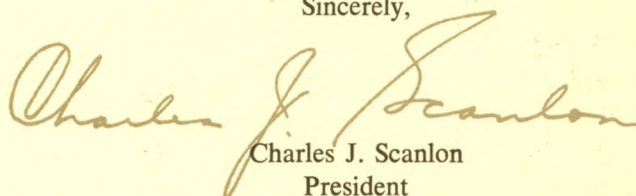
The bank's financial statements reflect both the effects of monetary-policy actions taken to moderate unstabilizing economic changes and the increasing levels of business activity in the district. Assets of the bank increased over \$600 million, reaching a total of nearly \$12.8 billion. Net earnings were \$417 million, compared with \$331 million in 1967. Of that, \$406 million was transferred to the Treasury.

The volume of transactions handled by the bank continued to rise with the increase in business activity. The bank cleared and collected 1 billion checks, received and counted 690 million pieces of currency and over a billion coins, and performed services for the federal government that included issuance of 29 million Savings Bonds and processing of 3.4 million tax receipts. Services of the discount window were used by almost 250 member-banks.

To help maintain an efficient payments mechanism and keep up with the steadily rising workload in a labor market becoming increasingly tight, the bank has continued to adopt new equipment, procedures, and training programs. Several innovations were made in bank operations. Changes were also made in directors and official staff.

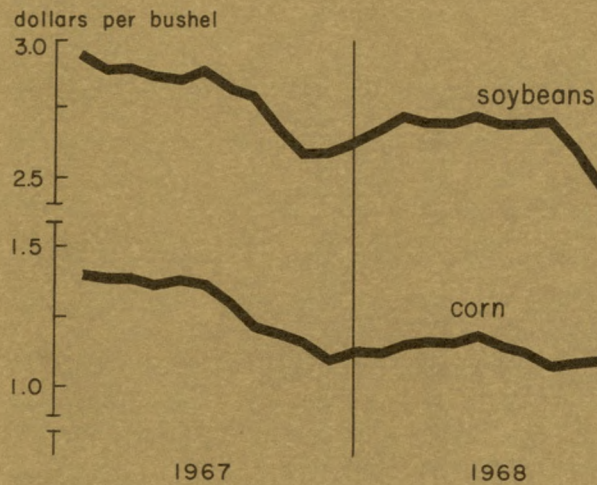
On behalf of the directors, officers, and staff, I thank you for your cooperation and counsel during the year, which have helped us provide continued high-quality service to the public through the member-banks of the Federal Reserve System.

Sincerely,

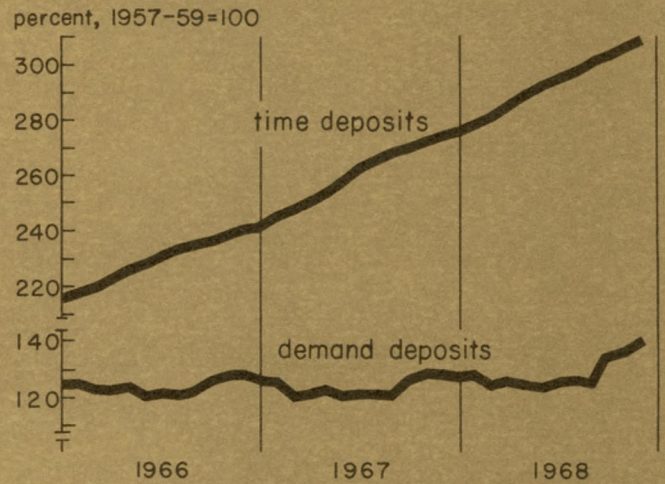
  
Charles J. Scanlon  
President

December 31, 1968

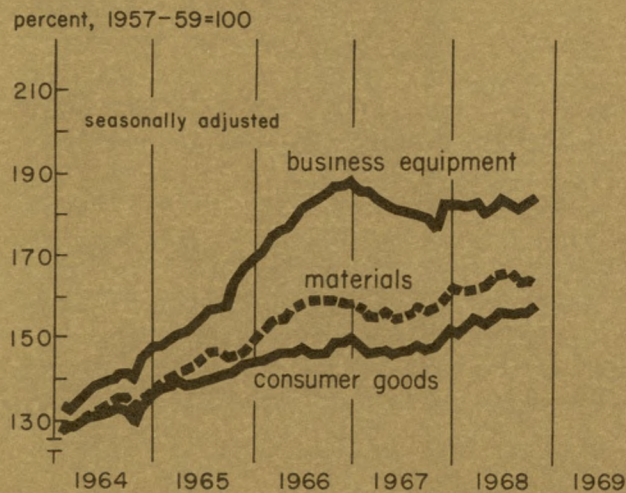
### Prices of major crops lower



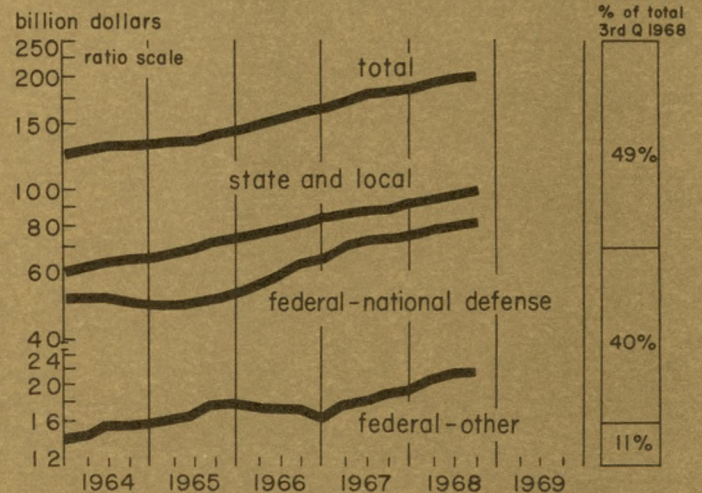
### Deposits rise at agricultural banks



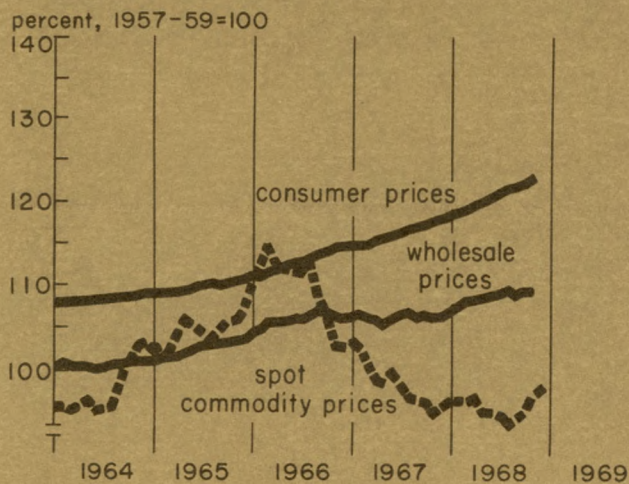
### Industrial production components up



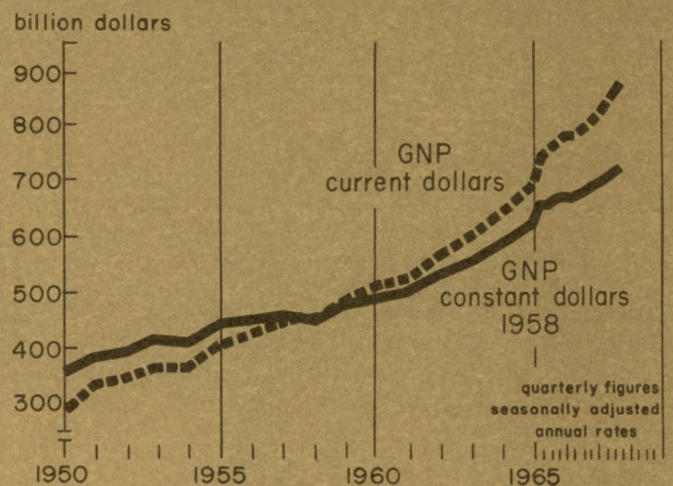
### Government spending higher



### Major price indexes rose



### Higher prices inflated spending



# The year in review

**B**usiness activity increased rapidly in 1968—in the district and the nation—with most indicators toward year-end suggesting continued vigor in the principal private sectors—retail trade, construction, and purchases of business equipment. The performance was marred, however, by excessive price inflation as demands pressed on resources, especially manpower. There were no clear signs that these pressures had abated in the final months of the year, although there were hopes that such signs would appear early in 1969.

Total spending on goods and services increased 9 percent in 1968, about the same as in 1966, which had seen the largest increase of the decade. Prices, however, averaged 4 percent higher than in 1967, far the largest increase since 1951. With adjustments for price changes, real output increased about 5 percent, twice as much as in 1967 but less than any other year since 1963. Given the limitations of manpower and no-better-than-average gains in output per manhour, the year's advance in physical output was near the economy's practical potential. Still more spending would have been reflected almost entirely in still more price increases.

## Why inflation continued

The year began with expectations that upward pressures on prices would ease. Unused plant capacity in basic industries, faster growth in the labor force, a slower rise in military outlays, and the proposed tax surcharge were expected to dampen price increases. Instead, prices rose faster than in 1967, continuing an acceleration that started in 1963 and picked up new momentum when U. S. forces were committed to action in Vietnam in 1965.

Demands for additional workers pressed the unemployment rate down still further from the already very low levels of 1966 and 1967, with rates for the Seventh District going even lower than for the nation. Nationwide, increases in worker compensation negotiated by major unions averaged 6 percent, compared with 5 percent in 1967, both of which were far higher than increases in production per man-hour. Strikes and threats of strikes in major industries, such as motor vehicles, copper, and steel, together with rapid employee turnover and high absenteeism (both of which are associated with tight labor markets) hampered improvements in efficiency.

The fiscal measures adopted at mid-year—raising taxes and reducing planned spending—had less impact on total demand than had been expected. Growth in money and credit was very

rapid in 1968, with both the public and private sectors borrowing heavily to accommodate increases in spending.

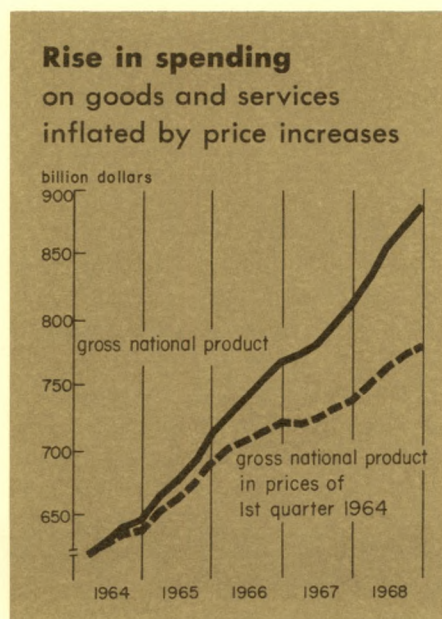
Despite ample plant facilities and adequate supplies of most raw materials, many sellers responded to rising costs and reduced profit margins by raising prices. And most of the increases were sustained in the marketplace by strong demand.

## The federal fiscal package

From mid-1965 to mid-1968, federal expenditures rose faster than private expenditures. Defense accounted for more than half the increase, but outlays for nondefense purposes also rose substantially, mainly in the form of transfer payments to individuals and grants to state and local governments.

The rate of increase in defense outlays slowed starting in the third quarter of 1968, with further increases attributable largely to higher pay for military and civilian personnel. Procurement was reduced, and output of military goods began to decline. Temporarily at least, one of the most expansionary and inflationary forces was dampened.

The Revenue and Expenditure Control Act, passed in late June, imposed a 10-percent surcharge on corporate profits taxes (effective January 1) and individual income taxes (effective April 1), accelerated the payment of corporate taxes, and extended certain excises scheduled to expire. These tax measures are expected to increase federal receipts about \$15 billion in the fiscal year ending June 30, 1969. Congress also directed that federal expenditures be held to a total of \$180 billion for fiscal 1969. Certain categories of expenditures were excluded, however. Increases in outlays for Vietnam, inter-



est on the public debt, veterans' benefits, and payments from Social Security trust funds (specifically exempted from cuts under the act) will cause total expenditures to rise several billion dollars beyond the legislated "ceiling."

Many were convinced for more than two years before the act was passed that fiscal as well as monetary restraints were needed to dampen inflationary pressures. The act provided some of this restraint. Without this legislation, the huge \$25-billion deficit in the federal budget for fiscal 1968 would have been approached in fiscal 1969. As things are now, the budget is expected to be about in balance.

Opinions regarding the extent of the impact of these fiscal measures on the private economy have varied. Certainly, the "overkill" of inflation many feared did not occur in the second half of 1968. Consumers and many businesses increased their expenditures substantially.

Efforts to reduce the federal deficit are clearly contributions to economic stabilization. Moreover, the full impact of the more restrictive tax and expenditure policies will not register until well into 1969. Social Security tax rates were increased in January 1969, and many people will have additional payments to make on their 1968 income-tax liabilities because the higher withholdings from payrolls did not begin until July, even though the tax surcharge was passed retroactively to April. Also, if the rise in government expenditures were to be effectively restrained, the tendency of tax receipts to rise with

income would have a continually tightening effect on private spending. After midyear, expenditure programs will be influenced increasingly by policies of the new Administration and Congress.

### Capital expenditures rise

Total output of machinery and equipment was rising in late 1968, after more than a year of near-stability. But new orders were increasing even faster, partly because of higher prices. Government and private surveys indicated a rise of 8 percent or more in total spending on new plant and equipment in 1969. An even larger rise in outlays of manufacturers was indicated. In years of rising outlays, such surveys have tended to undershoot actual results. About half of the expected increase could be traced to expectations of higher prices.

About a third of the nation's producer durable equipment and even higher proportions of its motor vehicles, farm, construction, and railroad equipment, and electrical apparatus are manufactured in the Seventh District. Especially heavy concentrations of equipment producers are found in the Chicago, Milwaukee, Detroit, Indianapolis, Peoria, and Quad-Cities areas.

Both the rising trends in orders for producer equipment and the results of the surveys have surprised those emphasizing the apparent large amount of unused plant capacity. But much of the existing capacity is not capable of producing goods of required qualities at competitive costs. Some buyers of equipment want not only to reduce costs, especially labor costs, but also to reduce labor requirements because of the problems in recruiting and keeping adequate staffs.

Expenditures on plant and equipment were about 5 percent higher in 1968 than in 1967. But because prices rose about the same proportion, there was little, if any, increase in physical volume. There were large increases in the outlays of airlines, truckers, and public utilities. Railroads and farmers spent substantially less than the year before. Construction companies, mining concerns, merchants, and most manufacturing industries spent about the same amounts both years. Outlays for most categories of equipment, including the depressed categories of farm and

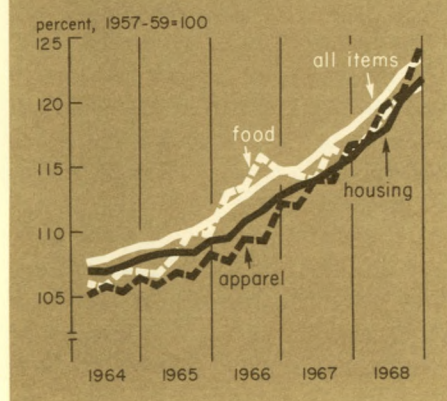
railroad equipment, are likely to increase in 1969.

From 1964 to 1966, expenditures on plant and equipment increased about 15 percent a year—about twice as fast as spending on all goods and services. But in 1967 and 1968, plant and equipment expenditures rose only about half as much as total spending.

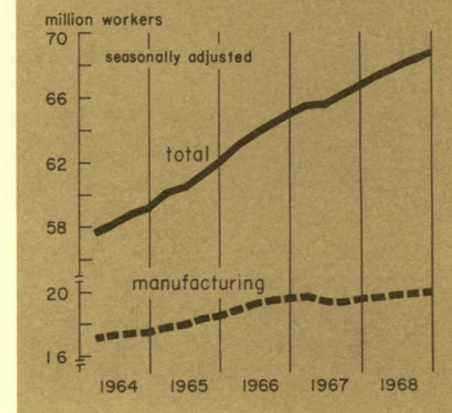
The boom in capital expenditures in the mid-1960s was unprecedented in the postwar period. Coming after a time when business fixed investment appeared to lag badly, investment tax credits and special rules allowing rapid depreciation encouraged outlays on new projects. By mid-1966, backlogs of orders for new business equipment had reached the point where lead times on new orders were stretched out far beyond normal waiting periods. The results were rising prices, discouragement of exports, and stimulation of imports. Excessive demands were made on the resources of Midwest centers specializing in the output of producer equipment.

The reduced tempo of spending on new equipment in 1967 and most of 1968 resulted in steady declines in the backlogs of orders. Most producers vigorously sought additional orders. Trends in the second half of 1968 suggest their efforts were successful. One of the favorable prospects for 1969 appears to be an advance in spending on plant and equipment about in line with the advance in spending on all goods and services. A return to the very rapid growth rates of 1964-66 would suggest

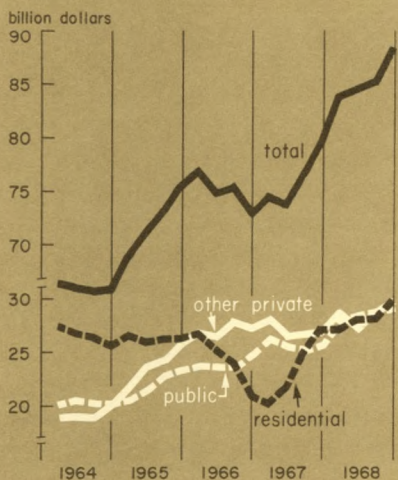
### Prices of all major consumer purchases rose sharply



### Employment of wage and salary workers rose steadily



## Construction activity increased though limited by labor shortage



additional pressures on an economy already over extended.

## Construction costs soar

Outlays on new construction rose more than 10 percent, but allowance for higher costs brings the increase in physical terms down to only 4 or 5 percent. Building materials were in ample supply, although some prices rose sharply. Credit was generally available, although at high rates of interest. Activity was limited, however, by manpower shortages in most building trades.

Electricians, plumbers, carpenters, masons, and structural-steel workers were all in strong demand, especially in the larger centers of the district. Labor contracts negotiated by the building trades called for average increases in compensation of 7 percent or more a year. Most of these agreements were reached without work stoppages, but a strike in Michigan delayed many projects in May, June, and July.

Construction contracts reported by F. W. Dodge were at high levels throughout the year, and they were especially strong in the second half. Contracts for commercial structures and apartment buildings led other types of construction. Many federal projects were delayed or postponed in line with economy programs restricting all but the most essential projects.

At the beginning of the year, 1.4 million housing starts were expected.

Because of prospective credit stringencies, there were fears for several months that the nation could not reach this total, but starts finally proved even higher than projected, exceeding 1.5 million. Savings inflows to thrift institutions, although below the high 1967 rates, held up better than expected. The main strength in housing, however, reflected increases in starts of multifamily structures financed by insurance companies, pension funds, and other investors that do not make single-family home loans in substantial volumes.

In addition to permanently situated housing, purchases of mobile homes—a large proportion of which are manufactured in Indiana and Michigan—increased from a record 240,000 units in 1967 to 300,000 in 1968.

Vacancy rates were low in most of the nation, and especially in the Seventh District, where the Chicago area is reported to have the strongest housing market of any large center. Higher family incomes and a rising trend in marriages suggest a continued increase in home building—assuming the availability of labor and an adequate volume of mortgage credit. Projections for 1969 commonly foresee 1.6 to 1.7 million permanent units and maybe 350,000 mobile homes. The 1968 Housing and Urban Development Act, which provides for federal rent and mortgage subsidies and a variety of other measures to increase the flow of funds into home mortgages, may play an important role in boosting residential construction.

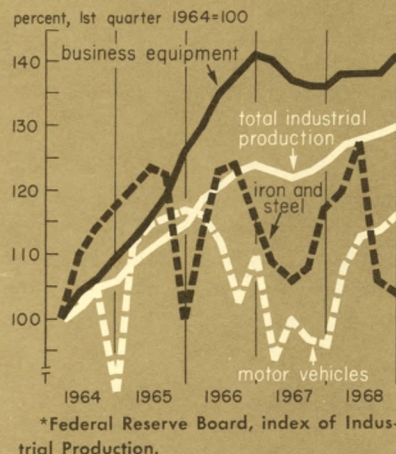
Total construction is almost certain to increase in 1969, with manpower again probably the limiting factor. Private residential and nonresidential building will doubtless increase. Any slack that might develop in the construction industry would signal the activation of delayed federal, municipal, and private projects.

## Record year for autos

Most projections at the start of 1968 indicated sales of about 9 million passenger cars and about 1.6 million trucks. But passenger-car sales reached 9.6 million, well above the expected level and even higher than the record of 9.3 million set in 1965. Truck sales exceeded 1.8 million, reaching a new high by a wide margin.

Developments in the motor-vehicle

## Output of motor vehicles and business equipment rose with total production\*



\*Federal Reserve Board, index of Industrial Production.

industry are of special interest to the Midwest. About 43 percent of the nation's workers engaged in the production of motor vehicles and parts are in Michigan, and 13 percent are in Indiana, Wisconsin, and Illinois.

Auto sales were inflated somewhat in 1968 by a carryover of demand resulting from strikes that cut production in the fourth quarter of 1967. Another factor was the increase in sales of imported cars, which reached 950,000 and accounted for about 10 percent of total sales—the largest proportion since 1959. To compete more effectively with small European and Japanese cars, all major U. S. producers have reported that they are developing "subcompact" models, but they have not announced introduction dates. Part of the rise in truck sales was accounted for by consumers buying vehicles for such personal uses as to carry campers.

Sales of domestically produced autos were at all-time highs for six successive months, May through October. Obviously, strike-deferred demand and higher imports were not the major causes of the record auto sales. The vigor of demand reflected rising incomes, the ability and willingness of consumers to use instalment credit, and the high priority attached to private transportation.

In early summer, large inventories of 1968 models suggested to many observers a slow start on sales of new

models, but stocks were worked off without difficulty. Prices of new cars were raised about 3 percent in the fall, partly because of additional safety equipment required on new models.

Producers were watching sales closely late in the year to keep production schedules in line with expected demand and maintain inventories at desired levels. Buyer response to 1969 models appears to have been excellent, but trends in sales have changed rapidly in the past. Industry leaders were looking forward to a good year in 1969, but sales are not commonly expected to reach the extremely high level of 1968.

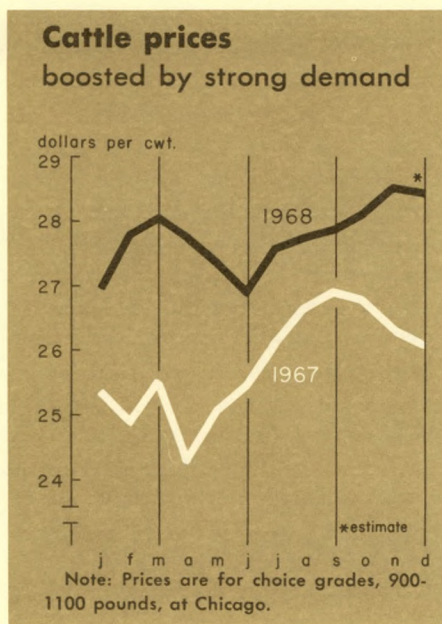
### Steel strike averted

The year's most important labor negotiations in the Midwest were in the steel industry. Almost 30 percent of the nation's steel is produced in Indiana, Illinois, and Michigan. As in 1962 and 1965, a strike was averted by a labor-management agreement reached shortly before the contract termination date—August 1. The new three-year contract provides increases in wages and benefits worth about 6 percent a year. In broad outline, the pact is similar to those previously negotiated in the auto, farm equipment, and construction-machinery industries.

Steel users began accumulating additional inventories in January as a hedge against a possible work stoppage, and purchases of steel accelerated further in April. By August, users had increased their holdings to 15 million tons, from 9 million tons at the start of the year. Part of the 1968 increase in imports of steel was related to strike-hedge buying. Some deliveries from abroad were delayed because a strike closed the St. Lawrence Seaway in July.

Production of raw steel reached a record annual rate of 152 million tons in late April, when it began a gradual decline. Shipments of finished steel products from the mills continued to rise, reaching a record high in July, normally a month of reduced activity.

Reductions in inventories of steel began in August and continued in the months following. To the surprise of some industry analysts, new orders began to rise in September and production turned upward again in October. In November and December, orders from most classes of steel users were



strengthening and workers laid off earlier were being recalled. The rise in production was especially marked in the Chicago and Detroit areas, partly because of orders from the auto industry.

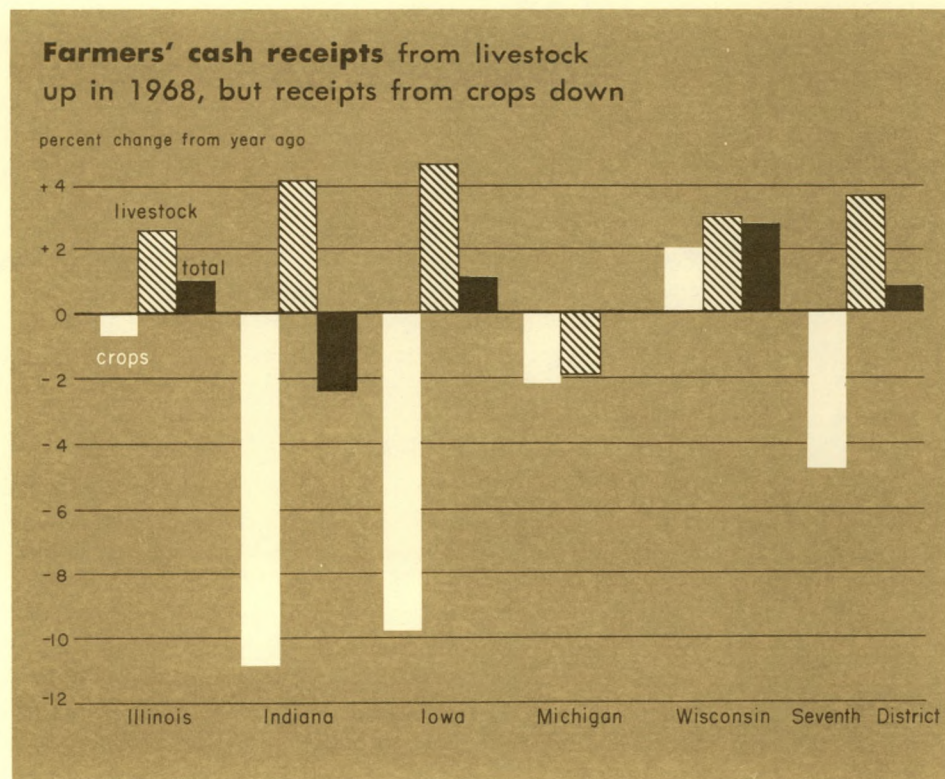
The inevitable decline in steel production after August 1 slowed general business activity in the district, but less than in the months following the wage settlement of 1965. Smaller inventories

had been accumulated, and the rate of use was higher.

More than 130 million tons of raw steel was produced in 1968, close to the 1966 record of 134 million. Shipments of finished steel from the mills totaled about 91 million tons, just under the 1965 record of 93 million tons. Imports of steel from Japan and Western Europe exceeded 17 million tons, half again as much as the previous high in 1967, and accounted for about 15 percent of domestic supplies. Users fabricated more steel than in any previous year.

Steel companies tried to raise prices after the labor agreement, but increases were hard to maintain in a highly competitive market. Prices of some types of steel in excess supply were under downward pressure. Prices of hot rolled sheets were reduced in November, but some of the reduction was restored in December. Numerous adjustments were made for other products, up and down. The price structure for most types of steel had clearly become unstable.

Foreign steel has been delivered to U. S. customers in recent years at \$20 to \$30 a ton less than domestic steel. Unlike imported autos, most imported steel is equivalent to its U. S. counterpart. American companies have protested that foreign producers are aided



by lower labor costs and subsidies and that foreign steel is sold at lower prices in the United States than in home markets. As a result, producers in this country have pressed strongly for quotas, tariffs, or other barriers to limit foreign competition. There were indications late in the year that, faced with such threats, foreign producers were considering voluntary reductions in their exports to the United States. If so, domestic steel production in 1969 is expected to approximate the 1968 total.

### Small rise for farm income

Farmers did not share fully in the rapid rise of the economy in 1968. Producers' gross incomes were bolstered by higher receipts from sales and substantially larger government payments. But production costs were also up, limiting gains in net income to only a small rise over the year before.

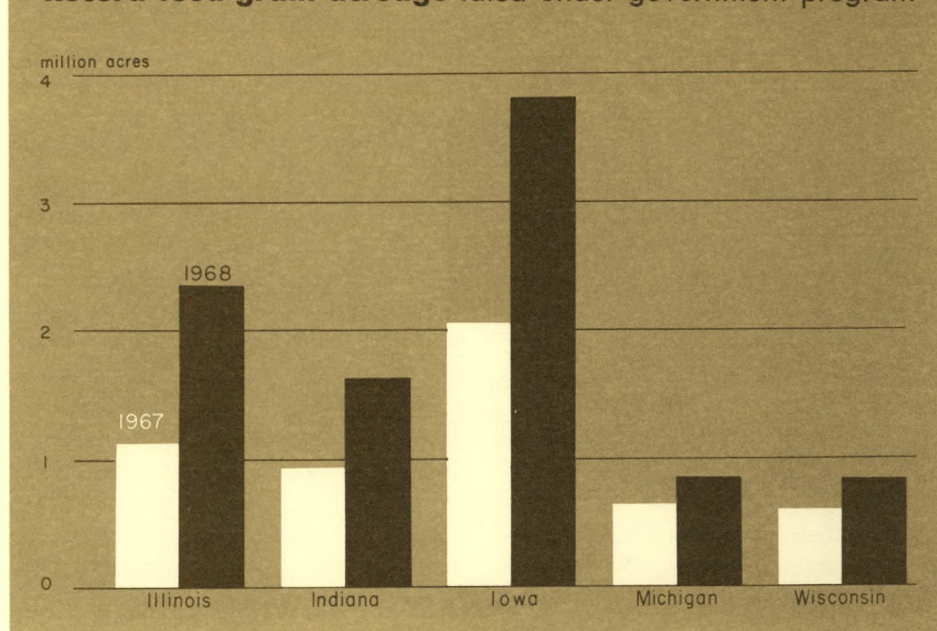
Livestock feeders generally fared better in the district than farmers growing crops. Although more feeding boosted meat production about 4 percent, prices continued high as a result of strong consumer demand. Cattle prices averaged \$2 a hundredweight higher than in 1967. While prices of hogs averaged slightly less than in 1967, they held up better than might have been expected in the face of the increase in supplies. Favorable prices combined with reduced feed costs to raise returns of most feeders above the level for 1967 and most other years.

Dairy farmers also received higher incomes and for much the same reasons—higher prices (government price supports were raised early in the year) and lower feed costs. Dairy herds continued to decline, but at a slower rate than in 1967.

Grain producers were in much the same situation as the year before. Rapid expansion in grain inventories, resulting mainly from the bumper 1967 harvest, brought a revision in the government's feed-grain program that made participation more attractive. District farmers responded by diverting a record 9.4 million acres from feed-grain production—nearly 4 million more than the year before.

Despite a substantial reduction in the acreage planted to corn—the district's important feed grain—another year of favorable weather and continued im-

**Record feed-grain acreage idled under government program**



provement in farming practices pushed yields to record highs in four states of the district. Only in Illinois, where a record of 100 bushels per acre was set in 1967, did yields decline. The result was that production for the district as a whole was only 5 percent less than the record in 1967.

Prices of corn averaged well below 1967 levels throughout the year. For producers participating in the government program, however, larger payments about offset the lower prices.

Soybean production increased, reflecting both larger acreage and higher yields. Output broke the record set in 1967 by about 20 percent. Prices were depressed much of the year, not only by the 1968 crop but also by the huge carryover from 1967.

### Farm investments declined

Many farmers reduced purchases of new capital goods. Purchases of tractors, the largest expenditure item, were off about 23 percent. Purchases of combines and balers, also important equipment items in the Midwest, declined 13 and 12 percent, respectively.

Average land values were higher in all states of the district. But the increases over 1967 were small, apparently reflecting tight credit conditions and low crop prices. In Illinois, the nation's leading producer of corn and

soybeans, land prices declined in the third quarter. In Iowa and Indiana, the district's other major grain producing states, statewide gains in land prices averaged less than 1 percent. The gains were larger in Michigan and Wisconsin, where cash grain crops are less important. Fewer transactions in farm real estate were reported, the slack off being attributed to reductions in both offerings and demand.

### Farm credit use larger

Farmers of the Midwest continued to make greater use of credit. At midyear, real-estate loans at district banks were about 12 percent higher than a year before. The rise was near the increases of other recent years and surprisingly strong in view of the further increase in mortgage interest rates and the apparent softening in the farmland market. Because credit granted by major non-bank lenders remained low, bankers probably extended a greater proportion of the district's total farm-mortgage credit than in 1967.

Nonreal-estate loans to farmers also increased—reaching a level about 7 percent higher at midyear than in mid-1967—but only about half as much as in the two previous 12-month periods. The smaller increase was associated with the decline in crop acreage and the reduction in purchases of

farm machinery. Many farmers also tried to hold down borrowings because of their lower incomes and the higher costs of credit. Demand for short-term farm loans was reported to have picked up later in the year. This probably reflected the sharp increase in cattle feeding, a major factor affecting loan demand.

More than two-thirds of the agricultural bankers surveyed in late fall reported funds more available than in the previous year. Near year-end, demand deposits at rural banks were up 5 percent from a year before and time deposits were up about 13 percent.

### Balance of payments

The balance-of-payments deficit improved markedly during 1968, both on a liquidity basis and on the basis of official transactions, with the result that exchange pressures on the dollar were lessened late in the year. Improvements in the payments balance, however, may have largely reflected the economic problems in England, France, and West Germany and the political developments in Czechoslovakia that precipitated large flows of funds within and out of Europe. If so, the improvement, based on capital flows, was probably

temporary. The U. S. trade balance deteriorated substantially last year, and at year-end there was only limited basis for expecting significant improvement in this important component of the overall payments balance in 1969.

In defending the dollar against the pressures of continued payments deficits and speculation in exchange markets, heavy reliance was placed on the network of currency swap agreements that make specific amounts of one country's currency available for another to draw on as needed. The swap network was nearly doubled last year—the total authorized lines rising to more than \$10 billion. Federal Reserve drawings totaled \$... million at year-end, compared with \$1.8 billion a year before. Holdings of foreign currencies rose more than \$1 billion.

Important in stopping the outflow of gold early in the year was an agreement reached in March with other major central banks to maintain the existing currency parities and abstain from buying or selling gold in private markets. The central banks also agreed not to sell gold to other monetary authorities for use in replacing gold sold to the private market. This stabilized the price of gold used in official transactions be-

tween countries at \$35 an ounce while allowing the price in private markets to respond to shifts in supply and demand.

Recurrent speculative movements of funds, reflecting doubts about the viability of existing exchange relationships between currencies, have their roots in both the imbalances in international flows of goods, services, and capital and in political developments in various countries. While it was necessary on several occasions in 1968 to undertake special measures to moderate exchange pressures on the dollar, the basic strength of the dollar depends not on such short-run efforts but on the long-run ability of American business to compete effectively in world markets. This ability, in turn, depends largely on the trend of costs in the United States relative to trends in other major industrial countries.

### Bank credit up sharply

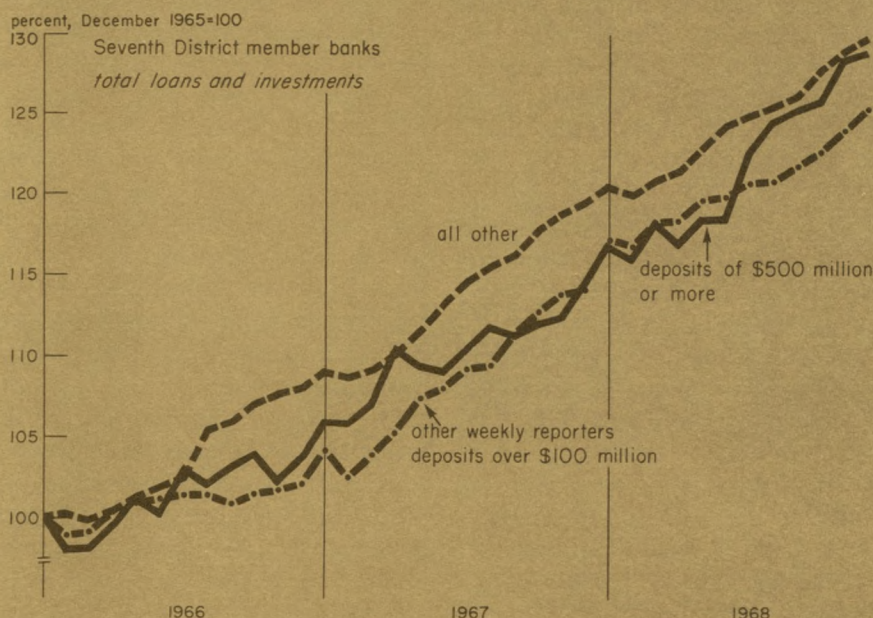
Strong demands for funds came with the rise in public and private expenditures. The amount of credit commercial banks supplied varied with their ability and desire to obtain loanable funds. Although expansion in total bank credit was moderate early in the year, it was very rapid in the second half. Total loans and investments of member-banks in the Seventh District rose about 11 percent—roughly the same as the record set in 1967. Although the patterns of growth shifted with the types of credit and classes of bank, the gain for banks in the district about matched the gain for the nation.

District banks reported substantial gains in all major types of earning assets, but loans rose faster and government securities slower than in 1967. Stronger loan demand persisted throughout the year, especially at the district's largest banks. Total loans of banks with deposits of \$500 million or more rose 11 percent in the 12 months ended November 1—more than twice the rise in 1967. The district's 15 banks in this size, located in six major Midwest cities, account for nearly half the deposits and more than half the earning assets of all its member-banks.

Until late in the year, business demand for loans was a small factor in credit growth. In the year ended October 30, commercial and industrial loans, which make up half the total

### Large and small banks

show similar growth in credit since 1965, despite sharp differences in shorter periods



loans at the largest banks, increased only 6 percent, compared with 10 percent in 1967 and 16 percent in 1966. The more modest growth in business loans reflected reduced demands by such important users of credit as machinery producers and mining companies. Loans to public utilities and producers of primary metals increased substantially. All growth in business loans of large banks was accounted for by term loans with original maturities longer than one year. Such loans rose about 20 percent at banks that report this information and now account for more than half their total business loans. Term loans increased relative to total loans in nearly all industries.

Real-estate loans increased 17 percent at the largest banks and 15 percent at those with deposits of \$100 to \$500 million. These increases were 50 percent larger than in 1967. Both groups of large banks also reported fairly strong increases in loans to consumers and nonbank financial institutions. Both classes of loans reflected the sharp rise in expenditures for consumer durables, especially automobiles.

Total loans of smaller banks—those with deposits under \$100 million—also rose about 11 percent, which was slightly more than in 1967. In all five district states, banks of this size reported large gains in real-estate and consumer loans. Nonreal-estate farm loans increased less, however, than the year before.

Part of the loan increase at smaller banks reflected their growing practice of selling surplus reserves in the federal-funds market. Such transactions are classified as loans in the semimonthly reports of small banks. Starting early in the spring, the federal-funds rate averaged well above yields on most other short-term investments. High returns, plus the liquidity of one-day maturities, make this market a very attractive outlet for excess funds. During a two-week period ending in early October, average sales of federal funds by member-banks with deposits under \$100 million were nearly twice the sales for the same period in 1967. Although less than half these banks participate in the market, federal-funds transactions accounted for nearly 12 percent of the total rise in their loans and represented about 3 percent of their total loans outstanding.

### Governments and municipals

Changes in bank investments largely reflected strong demands for credit by federal, state, and local governments. Treasury issues were larger than in any other year since World War II. District member-banks' holdings of government securities and government-agency issues rose almost as much as loans. New state and local issues set another high, and they too were bought in large volume.

Purchases of U. S. governments were concentrated at the largest Chicago banks dealing in Treasury issues. These banks increased their holdings more than would normally be associated with the distribution function, however. An important factor contributing to the larger holdings was undoubtedly the expectation that interest rates would decline after midyear and prices of securities would rise. As loan demand strengthened and interest rates rose toward year-end, dealer-banks reduced their portfolios of governments. Meanwhile, in contrast to a substantial rise in 1967, most nondealer-banks reported either declines or only small increases in holdings of governments.

Member-bank holdings of other se-

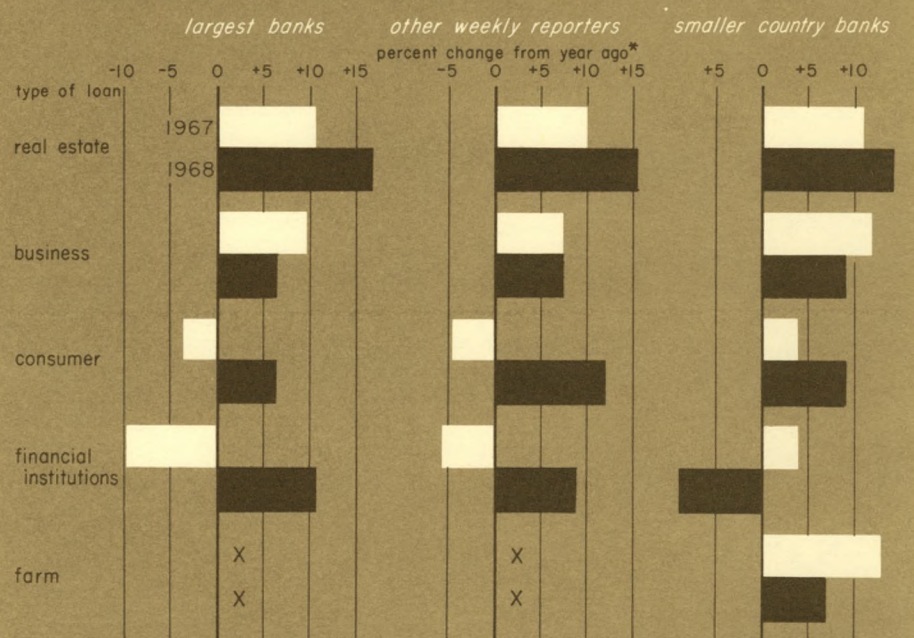
curities, mostly municipals, rose 15 percent. Bank holdings of municipals continued to rise faster than either loans or U. S. governments. Although the total rise was roughly the same as in 1967, the largest banks accounted for a much larger proportion. As in the case of governments, increased holdings of municipals by these banks reflected both the role of the banks as underwriters of new issues and expectations of rising market prices. Smaller banks in Indiana and Iowa, however, also acquired municipals faster than they had the year before.

### Time deposit growth moderated

Changes in total credit outstanding closely paralleled changes in deposits. The exception was the largest banks, which have access to the capital and Eurodollar markets. Of the district states, Indiana, which modified its restrictive regulations over time-deposit interest rates, showed the largest gains in deposits.

In the first half of the year, the rate of deposit growth dropped sharply from the 1967 rate, especially at the largest banks. However, these banks issued large amounts of negotiable CDs in the

### Mortgages were the fastest growing loan component in all three bank size groups



\*Year ended October for weekly reporters and June for smaller banks (deposits under \$100 million).  
X: Negligible.

summer and early fall, when market rates were lower. Their net gain for the year was about the same in dollar amount as the year before.

Many banks also promoted the sale of smaller deposit certificates. A new device to attract personal savings was the 90-day notice "golden passbook" account. Interest up to 5 percent can be paid on these accounts. Most banks require a minimum opening balance of at least \$1,000. That way, they can both attract new savings and retain funds of regular passbook savers looking for higher yields. At weekly reporting banks with total deposits of \$100 million or more, passbook savings declined about \$300 million during the year while "other" time deposits (excluding negotiable CDs) increased more than \$1.2 billion.

Total time deposits of member-banks in the district rose 11 percent, compared with 17 percent in 1967. Although time deposits continued to be the major source of bank funds, demand balances rose almost 6 percent—one of the largest gains on record.

More than three-fourths of the deposit growth of member-banks in the past five years—whether banks were large or small—has been in time deposits. During that time the composition of bank assets has shifted toward longer-term assets, especially real-estate loans and municipal securities. Loan-deposit ratios have also risen, reducing bank liquidity. The trend reflects both the feeling of reduced need for liquidity and shifts into assets with higher yields.

#### Monetary policy—aims, actions

The year opened with monetary authorities facing an inflationary situation in which rising prices threatened not only domestic economic stability but also the position of the dollar as a world currency.

Given the already high level of interest rates and apprehension over a possible repetition of the credit squeeze of 1966, it was hoped that the surtax proposed by the President in mid-1967 would be adopted early in 1968 and relieve monetary policy of some of the burden of providing needed restraint. Pending fiscal action, the Federal Reserve took a number of restrictive steps.

Effective in January, reserve requirements on demand deposits of more than

\$5 million were increased half a percent—from 16.5 to 17 percent at reserve city banks and from 12 to 12.5 percent at country banks. This action, announced just before the turn of the year, was the first increase in required reserves on demand deposits since early 1951. More than \$500 million of member-bank reserves were absorbed initially, but the impact on the ability of banks to extend credit was moderated through open-market operations.

In March, the Federal Reserve discount rate was raised from 4.5 to 5 percent. And in April, it was raised to 5.5 percent. The earlier increase was prompted in part by large outflows of gold associated with speculation that the gold price might be raised. The further increase in April followed a Federal Open Market Committee decision to move, in view of the continued acceleration in economic activity and upward pressures on prices, toward firmer money-market conditions.

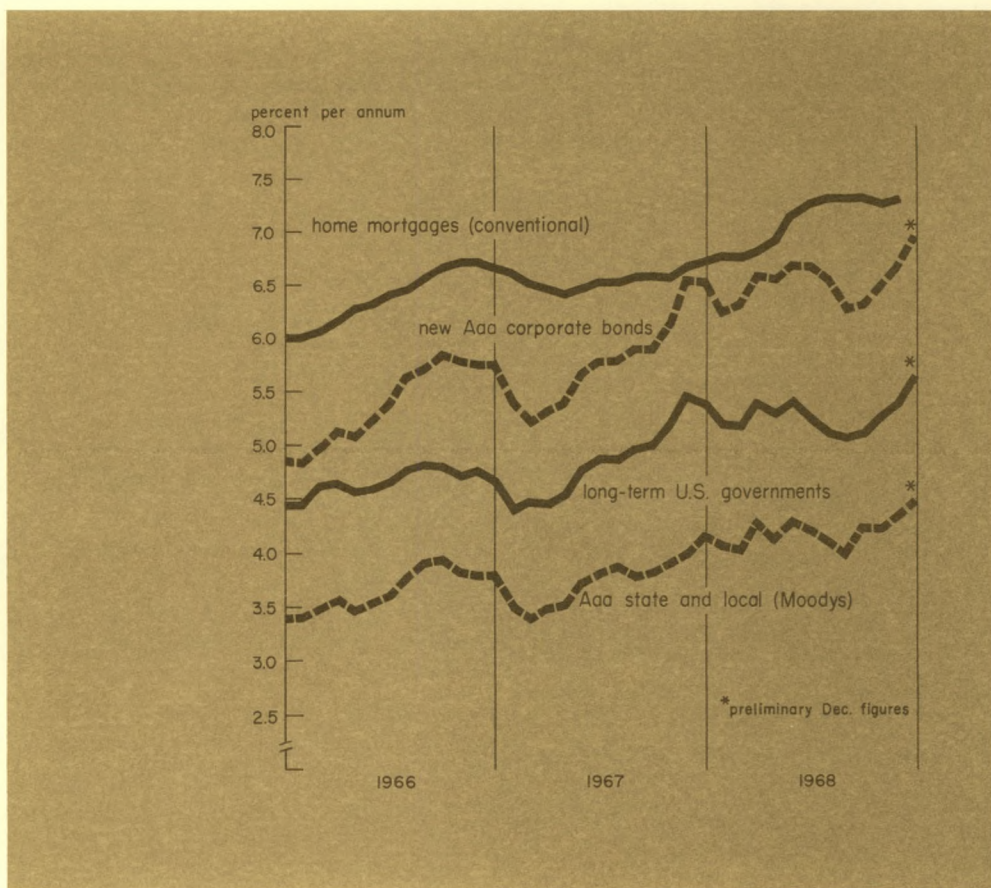
Concurrent with the second boost in discount rates, Regulation Q was amended to raise the maximum interest

rate on large CDs with maturities of 60 days or more from a flat 5.5 percent to a scale ranging up to 6.25 percent on certificates with maturities of 180 days or more. With market rates on competing money-market instruments rising to new highs, ceiling rates on CDs with longer maturities were lifted to avoid large runoffs to other investments.

Also in March, margin requirements on listed stocks were extended to cover lenders other than banks, brokers, and dealers. And in June, margins for all lenders were raised from 70 to 80 percent. Requirements for convertible bonds, which had been imposed only shortly before, were boosted from 50 to 60 percent.

The system's open-market operations, provided only a moderate increase in reserves to support deposit and credit expansion in the first half of the year. From late November 1967 until mid-1968, total reserves of all member-banks, adjusted for effects of the changes in reserve requirements, grew at an annual rate of less than 4 percent. That was faster than during the period

Interest rates reach new highs in all sectors



of restraint in 1966 but well below the very rapid increases made during most of 1967. Between November and June, the annual rate of growth in bank credit slowed to less than 7 percent, compared with 11 percent during that period a year before.

As in 1966, the overall availability of bank credit was closely related to the rate at which major banks acquired funds through the issuance of CDs. When yields on securities available in the market move up to the Regulation Q ceilings, CDs tend to run off. Despite the April increase in rate ceilings, the growth of time deposits slowed in the first half to an annual rate of 5 percent, compared with 16 percent in 1967.

The money supply—demand deposits and currency held by the public—continued to rise rapidly, partly because the Treasury reduced its deposits at commercial banks. Currency increased 40 percent faster than the year before.

With the adoption of restrictive fiscal measures in June, a slower rise in both economic activity and credit demands

was widely expected. Partly as a result of these expectations, interest rates declined. To bring Federal Reserve discount rates more into line with the market, they were reduced in late August from 5.5 to 5.25 percent. Open-market operations were also aimed at “accommodating the tendency toward somewhat less firm conditions in the money market.”

Credit demands remained strong, however, and bank loans and investments rose sharply. Commercial bank credit rose in the third quarter at an annual rate of almost 20 percent—faster than in any other quarter since early 1958. Some of the increase probably represented “reintermediation”—an increase in the banks’ share of total credit extended—as the large banks were able to bid successfully for CD money.

Meantime, the decline in interest rates was reversed. In recognition of both the higher market rates and the need for increased restraint, Federal Reserve discount rates were restored to the 5½-percent level after mid-December. Be-

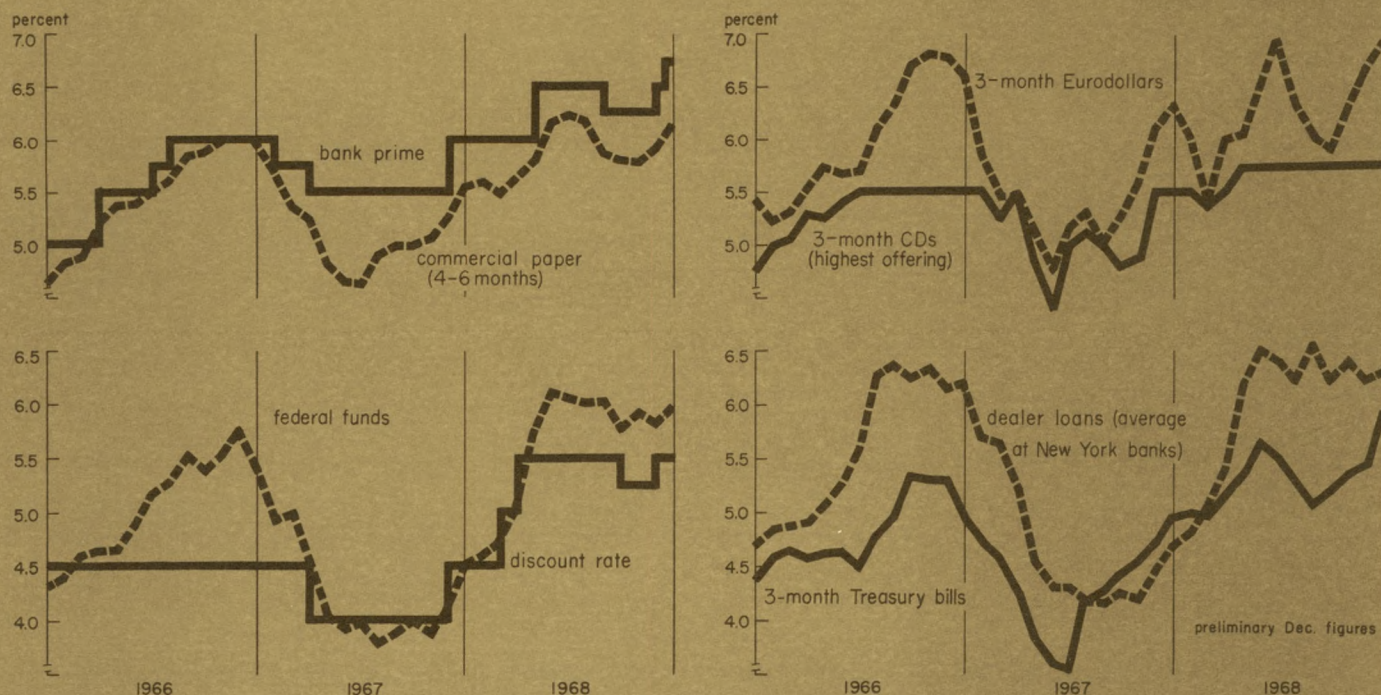
fore year-end, rates offered on all CD maturities were again at Regulation Q ceilings and outstandings were declining.

### Interest rate patterns

At year-end, most interest rates were at new highs in the experience of today’s generation. Temporary downswings in rates during the year were attributed mainly to expectations of slowing credit demands and to the accommodation of monetary policy to fiscal action and Treasury financing needs. Upswings were associated with underlying strength in the demand for funds.

Yields on short-term securities rose relative to those on long-terms, exceeding them in some markets. Early in the year, the cost to banks of borrowing in the federal-funds or Eurodollar markets moved well above yields on short-term securities and remained so during the May-to-August period of declining rates. The persistence of this pattern reflected expected capital gains on sales of securities associated with the expectation of further declines in yields.

The basic interest rate major banks



charge prime business customers was changed four times—from 6 to 6.5 percent in April, to 6.25 percent at most banks in September, back to 6.5 percent in early December, and to an all-time high of 6.75 percent later in the month.

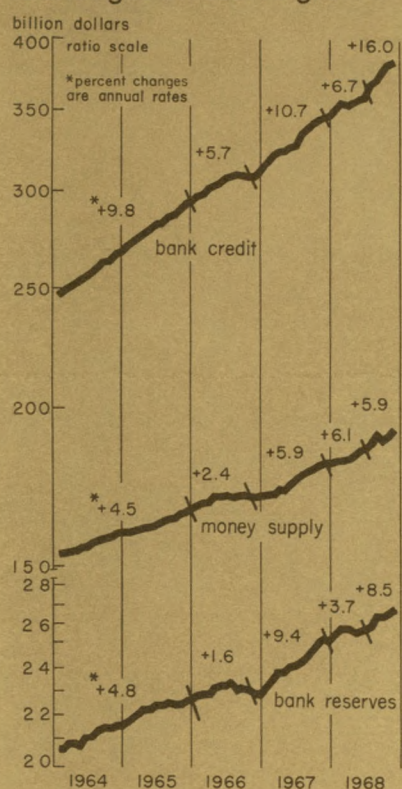
In long-term markets, changing spreads were related to special factors affecting the supply and demand for funds and securities. The municipal market had to cope with the largest volume of new issues on record. The volume of municipals was further swollen by sales of industrial revenue bonds before year-end, when issues larger than \$1 million would lose their tax-exempt status. Fewer new securities were issued in the corporate market than in 1967, partly because of increased use of industrial revenue bonds and the commercial-paper market. As in other years, new issues of long-term governments were again barred by the 4.25-percent statutory coupon ceiling.

Residential mortgage rates rose sharply in the first half of the year and more slowly in the second. Despite high interest rates, the flow of funds into mortgages was well maintained, partly

### Assets and deposits of the district member banks rose at a pace similar to 1967, but differed markedly for some groups of banks

	Gross loans		U. S. government securities		Other securities		Total deposits	
	1967	1968	1967	1968	1967	1968	1967	1968
(percent change in twelve months ended October)								
<b>All member banks</b>	+ 9	+11	+13	+ 9	+15	+15	+11	+ 8
<b>By size</b>								
Over 500	+ 5	+11	+19	+22	+10	+19	+13	+ 5
100-500	+14	+10	+24	+ 4	+30	+ 7	+11	+ 7
All other	+10	+12	+ 5	+ 0	+18	+14	+10	+10
<b>By area</b>								
Major cities								
Chicago	+ 9	+ 7	+11	+30	+ 5	+19	+10	+ 4
Detroit	+ 8	+17	+38	+ 9	+18	+18	+12	+12
Milwaukee	+ 2	+ 8	+51	+ 1	+ 4	+ 6	+ 9	+ 3
Indianapolis	+ 2	+20	+15	+18	+ 6	+19	+ 6	+17
Des Moines	+11	+10	+ 6	0	+68	-13	+16	+ 7
Other areas								
Illinois	+10	+10	+ 6	- 1	+23	+16	+10	+ 9
Michigan	+12	+14	+10	- 3	+19	+11	+12	+11
Wisconsin	+10	+14	+ 5	- 1	+30	+ 8	+12	+10
Indiana	+ 5	+12	+ 5	+ 1	+19	+21	+ 7	+16
Iowa	+12	+ 7	+ 6	+ 9	+16	+23	+11	+11

### Money and credit move diversely in response to changes in reserve growth



as a result of liberalization of usury laws in several states. Heavy commitments by major mortgage lenders at year-end and sluggish savings flows into intermediaries suggested no near-term decline in home financing charges.

Interest rates will be influenced—in 1969 as in 1968—by credit needs of private and public borrowers as well as by monetary policy. Despite expected reduction in federal demands for credit, the many factors influencing other credit needs make the future course of interest rates uncertain.

### Unsolved problems for 1969

In the fourth quarter, a resurgence in retail trade, a sharp increase in orders to manufacturers of durable goods, further tightening of the labor market, and continued price increases all showed the economy retained strong momentum. As the year drew to a close, many observers were projecting these trends into 1969, expecting continuation of the tight labor market and little, if any, moderation of price inflation.

The seeming failures of fiscal restraint in 1968 cannot be taken as evidence that higher taxes do not tend to reduce private spending or that curtailment of public spending does not release resources to meet other needs. The restraints imposed in June were intended to dampen excessive exuberance, not cause a decline in total business activity. The restraining influence of the fiscal package simply was not adequate in the face of the increases in nonfederal spending and borrowing.

Price inflation to the extent experienced in 1968 has not been accepted by the public or its leaders in business, labor, and government as either desirable or necessary for economic growth and high employment, and it clearly is an important source of the weakness in the U. S. balance of international payments. A matter of high priority in the new year, therefore, must be a search for better tools and methods of economic management. The answer may be partly found in a more effective combination of monetary and fiscal policy.

# Regulatory changes

The board of governors made a number of important changes in Federal Reserve regulations in 1968 and proposed others for further consideration in 1969.

To help reduce pressure on the dollar built up from the accumulation of dollar-balances abroad, the board revised the guidelines for restraint of foreign credit. Issued January 1, these revisions lowered the ceiling on the amount of foreign credit extended by banks. The board also directed banks to reduce outstanding loans to West Europe and directed other financial institutions to repatriate liquid funds, reduce their holdings of certain foreign assets, and stop all new loans and investments in West Europe not essential for financing U. S. exports. The initial goal—an inflow of more than \$500 million in 1968—was exceeded by a comfortable margin. The program is to be continued essentially unchanged in 1969.

In March, the board broadened Federal Reserve regulation of stock-market credit. Two regulations—Regulation T, which limits the credit brokers and dealers can extend on registered securities, and Regulation U, which limits the credit banks can extend for the purchase or carrying of such securities—were amended to include debt securities convertible into registered stock. The initial margin requirement was set at 50 percent. At the same time, the board issued Regulation G, which extends margin regulation to include lenders other than banks, brokers, and dealers with significant amounts of loans on covered securities.

A July amendment to the Securities Exchange Act authorized the board to regulate credit on securities traded over the counter. This power had not yet

been exercised at year-end.

As directed by Congress, the board published in October for public comment a proposed new Regulation Z to implement the Truth in Lending Act. This act, signed into law May 29 and scheduled to become effective July 1, 1969, applies to retailers and financial institutions extending or arranging for the extension of consumer credit. In general, the law specifies disclosures that creditors must make regarding finance charges and annual percentage rates, customer cancellation rights on some types of credit arrangements, and standards for advertising credit terms. The proposed regulation, which incorporates provisions of the law, is intended as a complete handbook on "truth in lending." Although the regulation is issued by the Federal Reserve, its enforcement will be carried out by nine federal agencies, each with its own jurisdiction. The Federal Reserve will enforce the regulation at member-banks chartered by the states.

Further changes in statutes affecting the board's authority to regulate the interest paid on deposits resulted in changes in Regulation Q, which implements that authority. The maximum interest rates member-banks can pay on certain types of time deposits were raised in April, and several technical amendments and statements were issued during the year clarifying Regulation Q. A statement issued in June spelled out the limitations on deposit transactions on which member-banks can pay as much as 5-percent interest. The statement reaffirms the underlying principle that the 5-percent rate can be paid only on funds that cannot be withdrawn in less than 90 days.

In September, Congress extended for

another year the board's authority to prescribe different rate limitations for different classes of deposits. Any reasonable basis can be used in determining the limits to be prescribed. At the same time, the board and other supervisory agencies were given authority to regulate all aspects of interest payments on time deposits, including bank advertising.

The same legislation (Public Law 90-505) made permanent the board's authority to set reserve requirements on time deposits of member-banks between 3 and 10 percent. This authority is implemented by Regulation D. Throughout the year, reserve requirements for savings deposits and other time deposits up to \$5 million were 3 percent. For time deposits over that, reserves of 6 percent were required.

Also published in September were technical amendments to Regulation D. These amendments, making changes in the method of reserve accounting, were intended to accomplish two purposes. One was to make reserve management easier for banks both by reducing uncertainties about the amount of reserves required and by allowing banks more flexibility in meeting their requirements. The other was to improve the functioning of the money market by reducing the sharp day-to-day variations in the availability of funds. The amendment (1) established a one-week reserve computation period for country banks, the same as that already applied to reserve city banks, (2) shifted the base for determination of required reserves to deposit averages two weeks earlier, (3) specified the vault cash used in satisfying requirements was the amount held two weeks earlier, and (4) permitted either excesses or deficiencies up to 2 percent of required reserves to be

carried over into the next period.

A preliminary version of Regulation P, implementing the Bank Protection Act of 1968 with respect to state member-banks and reserve banks and branches, was published in November for public comment. The regulation will set minimum standards for security devices and procedures to discourage crime against financial institutions and assist in apprehension of criminals.

Under a new authorization from Congress (also Public Law 90-505), the board amended Regulation A, governing advances and discounts by Federal Reserve banks. The amendment made all obligations eligible for purchase by Federal Reserve banks acceptable as collateral. These include federal-agency securities and other obligations carrying full guarantees of principal and interest by the United States or a federal agency. Some of the major agency obligations this amendment made eligible as col-

lateral for advances are Federal Intermediate Credit Bank debentures, Federal Home Loan Bank notes and bonds, Federal Land Bank bonds, Federal National Mortgage Association notes and guaranteed participation certificates, Export-Import Bank notes and guaranteed participation certificates, notes fully guaranteed by the Small Business Administration, and Federal Housing Administration debentures. In addition, the Federal Reserve System continued to recommend legislation permitting Federal Reserve banks to make advances to member-banks on any collateral acceptable to the reserve banks.

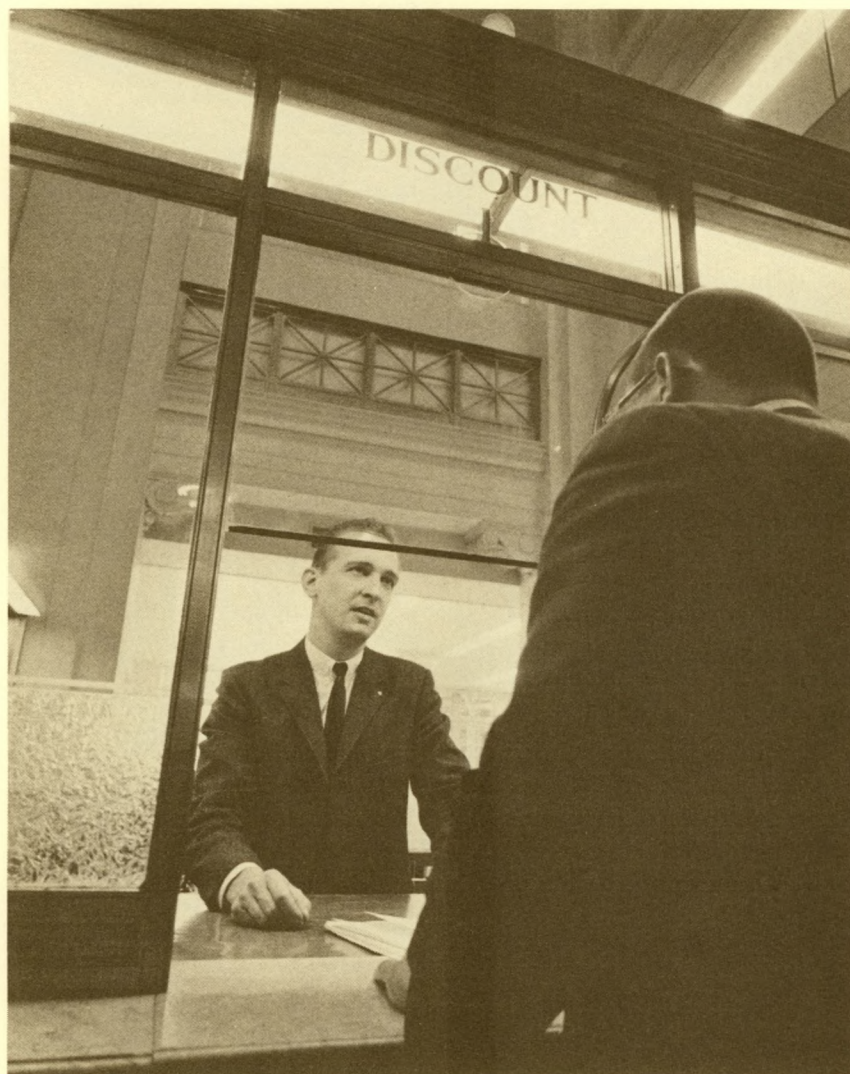
Also published last year was the report of a Federal Reserve System committee, proposing changes in discount policies to encourage more use of Federal Reserve lending facilities. It reaffirmed, however, the general principle that the discount window is intended primarily to serve the needs of member-

banks for short-term reserve adjustments.

Major recommendations were (1) that every soundly operated member-bank be given a "basic borrowing privilege" up to a certain amount and for a certain proportion of its reserve periods, (2) that banks with heavy seasonal bulges in their needs for funds be allowed to use the discount window in meeting such needs, (3) that other short-term credit not covered under the basic or seasonal arrangements continue to be available to member-banks, subject to the same kind of administration procedures as now applied, and (4) that the discount rate be more flexible and more closely aligned with other market rates than had been the case.

The report was published with a view to obtaining comments from member-banks and other interested groups. In the Seventh District, representatives of member-banks were invited to a series of meetings with Federal Reserve staff members to discuss the proposals. Implementation of the proposals would not require legislation.

The board announced several changes in its interpretations of banking laws. Among the most important, from the standpoint of bank management, were changes from earlier views regarding the authority of banks to establish "operations subsidiaries" and "loan production offices." After reexamining the purposes and legislative history of the statutes prohibiting a member-bank from purchasing "for its own account of any shares of stock of any corporations"—except as specifically permitted or as comprised within the concept of incidental powers necessary to carry on the banking business—the board ruled that the incidental-power clause permits a bank to organize its operations any way it chooses. A wholly-owned subsidiary engaged in activities the bank itself is authorized to perform and in the location authorized was judged simply an alternative organizational arrangement to departments. Likewise, the board ruled that, as far as federal law is concerned, an office performing only service functions, such as soliciting loans or assembling credit information, is not a branch and can be established and operated anywhere in the United States.



# The bank's operations

New and improved techniques are constantly sought to help cope with the expanding volume of transactions the bank performs in servicing the payments mechanism. Further progress was made during the year in automating the bank's service functions. Technological innovations with vast implications for the future were adopted, and efforts were intensified to further improve the training and productivity of employees.

An ever-present challenge is the prompt clearing and collection of the steadily expanding volume of checks received from commercial banks and other Federal Reserve banks. These averaged nearly 3.4 million a day last year—nearly 7 percent more than in 1967.

Check processing equipment has been changed as technological advances made faster handling possible. Since the bank first pilot tested high-speed equipment in 1961, the annual volume of checks has increased more than 60 percent. The bank and its Detroit branch processed more than a billion items last year. Magnetic ink encoding, a necessity for high-speed processing, is now nearly universal.

Installation of "third-generation" check-processing equipment was begun in 1968, and full conversion to the new system will be completed in 1969. New techniques made possible by improvements in computers and auxiliary equipment have allowed the bank to maintain fast, accurate service despite increasing

pressures from a heavy workload and a tight labor market. As long as checks continue to flourish as a means of payment, still better systems will be needed for handling them.

Operations of the Cash Department reflected the continued rapid increase in currency in circulation. The shortages of coin that were widespread a few years ago have been largely overcome. The Kennedy half-dollar, however, still does not circulate as an effective medium of exchange. Last year, 27 million of these coins were distributed to banks in the district but they "disappeared" from circulation almost immediately.

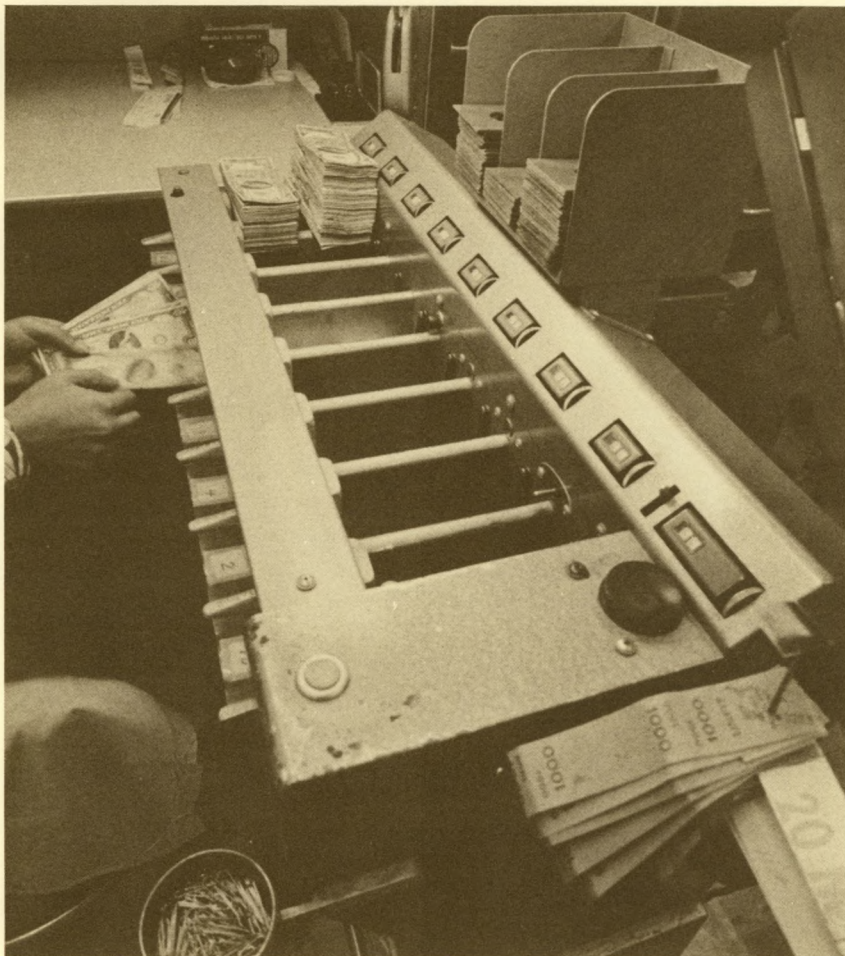
Another step was added to the coin handling function—the separation of dimes and quarters with silver content for return to the Treasury, where the silver is recovered and used to replenish dwindling stocks. The old silver coins are replaced with new clad coins.

"Book-entry" procedures have been adopted for Treasury securities held in custody. The technique is expected to save considerable time, space, and manpower. It will gradually be extended to other activities where it is applicable. As fiscal agent for the United States, the bank is authorized to issue book-entry Treasury securities by making entries on its records when Treasury securities are deposited as collateral for advances to member-banks, as collateral for tax and loan accounts or deposits of public money, or for the sole account of a member-bank instead of safekeeping of definitive Treasury securities.

Also in its capacity as fiscal agent for the United States, the bank issued and redeemed a near-record dollar-volume of marketable U. S. securities last year. Reflected in the high level of activity

Over a billion checks were processed in 1968





More than two-thirds of a billion pieces of currency were received and counted, and well over a billion coins



were both the large increase in total U. S. debt during the calendar year and the larger refinancing operations stemming from shorter average maturities. Nevertheless, marketable securities accounted for only a small part of the total number of U. S. securities the bank handled. Nearly 29 million U. S. Savings Bonds were issued through issuing agents and about 19 million were redeemed.

Computer applications have also brought improvements in the efficiency of other bank operations. Maintenance of the reserve accounts of member-banks has been automated in recent years, allowing complete statements to be sent to banks having such accounts at the close of every business day. Entries in tax and loan accounts of all Treasury depositaries in the district are also automated. With the adoption of the new "lagged" method of reserve accounting, required reserves are calculated and the information sent to each member-bank before the opening of the reserve period for which they apply. This is followed at the end of the period with a statement summarizing the member-bank's reserve position and

## OPERATIONS

	Value		Number of items	
	1968	1967	1968	1967
	(millions)		(thousands)	
<b>Clearing and collection</b>				
Commercial bank checks . . . . .	\$ 330,898	\$ 309,890	927,631	863,177
Government checks* . . . . .	22,569	21,888	96,504	96,489
Other items . . . . .	987	729	1,837	1,841
<b>Currency and coin</b>				
Currency received and counted . . .	\$ 4,759	\$ 4,565	689,106	670,337
Coin received and counted . . . . .	114	142	1,040,498	1,243,796
Unfit currency withdrawn from circulation . . . . .	1,308	1,271	277,150	279,131
<b>Safekeeping of securities</b>				
Definitive securities**				
Securities received . . . . .	\$ 4,085	\$ 10,541	304	370
Securities released . . . . .	8,615	9,357	399	300
Coupons detached . . . . .	160	290	3,007	3,090
In safekeeping on December 31.	4,774	9,304	1,500	1,595
Book-entry Treasury securities***				
Securities deposited . . . . .	\$ 17,024	—	17	—
Securities withdrawn . . . . .	11,943	—	13	—
On deposit on December 31 . . .	5,081	—		
<b>Discount and credit</b>				
Total loans made during the year.	\$ 14,515	\$ 6,583		
Daily average outstanding . . . . .	135	51		
Number of banks accommodated . .			(244)†	(198)†
<b>Investment</b>				
Purchases and sales of securities for member banks . . .	\$ 1,324	\$ 1,551	13	14
<b>Transfer of funds</b>				
Funds transferred . . . . .	\$1,311,161	\$1,077,563	910	824
<b>Services to the U. S. Treasury</b>				
Marketable securities				
Issued . . . . .	\$ 13,962	\$ 13,434	439	393
Serviced:				
Securities received . . . . .	18,795	14,945	253	232
Securities delivered . . . . .	23,597	20,677	792	634
Redeemed . . . . .	17,996	18,517	943	866
Savings bonds and savings notes				
Issued . . . . .	1,402	1,313	28,773	26,756
Serviced:				
Bonds received for reissue . . .	140	161	700	730
Bonds delivered on reissue . .	140	161	795	827
Bonds delivered on replacement	8	7	95	75
Redeemed . . . . .	1,224	1,120	18,784	17,689
Federal tax receipts processed . . .	19,875	14,833	3,431	2,580

\*Includes postal money orders.

\*\*Includes collateral custodies.

\*\*\*Transactions previously handled through definitive securities.

†Actual number.



More than 900,000 transfers of funds were made for member-banks



Powerfiles were installed in 1968 to speed handling of securities held in custody for member-banks

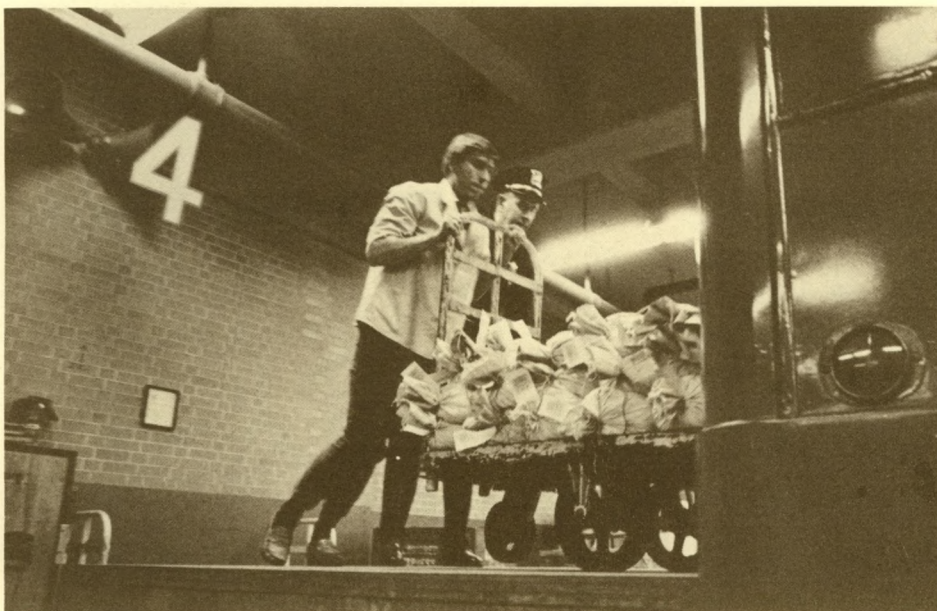


carryover allowances. Both services make reserve accounting easier for member-banks.

Not yet operational but with great potential for the future is an electronic system for transferring bank deposits and financial data. Last year, the Federal Reserve System contracted for the key segment of a computerized network designed to speed up the movement of money, securities, and statistics between Federal Reserve banks. The contract calls for a central communications switch to be installed at Culpeper, Virginia. The new installation, due to be operational in late 1969 or early 1970, will replace the leased-wire network now in use.

The new equipment will be compatible with computer facilities being developed for the use of commercial banks and may eventually be linked to them. With teletype equipment, the Federal Reserve System handled a daily average of 9,000 money transfers last year. With the new equipment, it can transfer funds and other data far faster.

**Mechanization** has eased the burden of moving large volumes of coin



Over 277 million pieces of unfit currency were withdrawn from circulation



The equipment will also operate with much greater capacity, both accommodating expected increases in transactions and allowing for gradual lifting of restrictions on use now imposed by the limitations in capacity of teletype equipment.

Automation requires the development of special skills and knowledge. Additional emphasis has been placed on employee-training programs as part of the bank's effort to keep up with the demand for its financial services. Some 800 employees participated in at least one in-bank training program last year,

and plans call for development of several new training programs in 1969. Videotape capability will be acquired as an aid in broadening the training efforts.

Even with increasing mechanization, the tight labor market incident to the high level of economic activity has limited the bank's ability to acquire needed staff. It is adapting its employment program to aid in upgrading the skills of people previously not qualified for employment. The results are expected both to contribute to a better community and to tap a potential source of needed manpower.



# Financial statements

## STATEMENT OF CONDITION

<b>Assets</b>	<b>December 31, 1967</b>	<b>December 31, 1968</b>
Gold certificate account.....	\$ 1,678,565,203	\$ 1,491,111,512
Redemption fund for Federal Reserve notes.....	328,249,237	—
Total gold certificate reserves.....	\$ 2,006,814,440	\$ 1,491,111,512
Federal Reserve notes of other banks.....	53,537,000	58,011,000
Other cash .....	66,709,213	26,966,975
Discounts and advances:		
Secured by U. S. government securities.....	\$ 8,823,000	\$ 49,330,000
Other .....	—	15,000,000
Total discounts and advances.....	\$ 8,823,000	\$ 64,330,000
U. S. government securities .....	7,817,282,000	8,698,315,000
Total loans and securities .....	\$ 7,826,105,000	\$ 8,762,645,000
Cash items in process of collection.....	1,899,444,661	2,027,721,554
Bank premises .....	18,401,695	17,307,944
Other assets .....	280,932,545	377,147,317
<b>Total assets</b> .....	<b>\$12,151,944,554</b>	<b>\$12,760,911,292</b>
<b>Liabilities</b>		
Federal Reserve notes .....	\$ 7,408,002,403	\$ 8,076,160,982
Deposits:		
Member bank reserves .....	\$ 2,918,929,190	\$ 2,988,690,348
U. S. Treasurer—general account .....	107,514,286	549,316
Foreign .....	20,300,000	32,120,000
Other .....	30,647,697	39,110,034
Total deposits .....	\$ 3,077,391,173	\$ 3,060,469,698
Deferred availability cash items .....	1,445,556,417	1,373,103,115
Other liabilities .....	46,274,961	64,695,497
<b>Total liabilities</b> .....	<b>\$11,977,224,954</b>	<b>\$12,574,429,292</b>
<b>Capital accounts</b>		
Capital paid in .....	87,359,800	93,241,000
Surplus .....	87,359,800	93,241,000
<b>Total liabilities and capital accounts</b> .....	<b>\$12,151,944,554</b>	<b>\$12,760,911,292</b>
Contingent liability on acceptances purchased		
for foreign correspondents .....	\$ 22,692,500	\$ 16,468,800

Central banking is concerned primarily with monetary control, a sound banking system, and an efficient payments mechanism. Growth and profits are strictly incidental. Nevertheless, earnings, derived largely from interest on U. S. government securities held in the Federal Reserve System's open-market account, are sizable. Income not needed to cover expenses of the Federal Reserve banks and the board of governors, payment to member-banks of the 6-percent statutory dividend on paid-in stock, and a small addition to surplus, is turned over to the Treasury.

Financial statements of the Federal Reserve banks reflect both the effects of monetary-policy actions and regional differences in the activity and growth of member-banks and their customers.

Total footings of this bank (its home office and Detroit branch) were almost \$12.8 billion on December 31, 1968—up \$600 million for the year. On the liability side, most of the increase reflects additions to Federal Reserve notes outstanding in response to public demand for currency.

Member-bank deposits (reserves) on December 31 were only moderately higher than a year before. Effects of deposit growth and the increase in reserve requirements last January were partly offset by the shift to lagged reserve accounting. Under the new reserve-accounting system, seasonally high end-of-year deposit volume does not affect required reserves until two weeks later.

The system's gold certificates declined nearly \$2 billion in 1968, mostly before the decision reached jointly with foreign central banks in March to stop supplying gold to the London market. The Federal Reserve purchased govern-

## STATEMENT OF EARNINGS AND EXPENSES

ments to offset the contractive effects of the gold drain on bank reserves and domestic credit conditions. Meanwhile, Congress acted to make the entire gold stock available to support the dollar in exchange markets by removing the gold-certificate reserve requirements against Federal Reserve notes.

Later in the year, increases in holdings of foreign currencies, reflecting use of the swap lines with foreign central banks, increased funds available to the market—funds that were partly absorbed by the Federal Reserve's sales of securities. On balance, government securities in the system's open-market account rose only \$3.5 billion, compared with \$5.0 billion in 1967. Federal Reserve banks share in the open-market account and in the system's holdings of foreign currency in proportion to their total assets.

Loans to member banks were, as usual, small on the final day of the year, but, overall, use of the discount window was greater in 1968 than in 1967, although less than in 1966. Out of a total of 974 member-banks in the district, 244 borrowed from the bank at some time during the year. That was roughly 50 more than last year. On the average day, outstanding discounts and advances were \$135 million, compared with \$51 million in 1967.

Higher earnings of Federal Reserve banks in 1968 than in 1967 reflected both higher levels of earning assets and higher average interest and discount rates. This bank's share of interest earned on Treasury securities in the open-market account was \$431 million, up from \$356 million in 1967. Earnings turned over to the Treasury amounted to \$406 million.

	1967	1968
<b>Current earnings:</b>		
Discounts and advances .....	\$ 2,260,393	\$ 7,089,127
U. S. government securities .....	356,248,931	431,041,066
Foreign currencies .....	3,659,496	11,172,527
All other .....	89,112	89,408
Total current earnings .....	<u>\$362,257,932</u>	<u>\$449,392,128</u>
<b>Current expenses:</b>		
Operating expenses .....	\$ 31,203,311	\$ 32,946,680
Federal Reserve currency .....	3,267,777	2,898,106
Assessment for expenses of Board of Governors .....	1,562,600	2,078,400
Total .....	<u>\$ 36,033,688</u>	<u>\$ 37,923,186</u>
Less reimbursement for certain		
fiscal agency and other expenses .....	4,003,942	4,163,684
Current net expenses .....	<u>\$ 32,029,746</u>	<u>\$ 33,759,502</u>
Current net earnings .....	<u>\$330,228,186</u>	<u>\$415,632,626</u>
<b>Additions to current net earnings:</b>		
Profit on sales of U. S. government securities (net) . . .	\$ 126,148	\$ 132,340
All other .....	243,498	1,255,831
Total additions .....	<u>\$ 369,646</u>	<u>\$ 1,388,171</u>
<b>Deductions from current net earnings:</b>		
Loss on sales of U. S. government securities (net) . . .	\$ —	\$ —
All other .....	2,896	6,240
Total deductions .....	<u>\$ 2,896</u>	<u>\$ 6,240</u>
Net deductions from (—) or additions		
to current net earnings .....	\$ 366,750	\$ 1,381,931
Net earnings before payments		
to U. S. Treasury .....	<u>\$330,594,936</u>	<u>\$417,014,557</u>
Dividends paid .....	5,104,198	5,462,762
Payments to U. S. Treasury		
(interest on Federal Reserve notes) .....	320,748,038	405,670,595
Transferred to surplus .....	<u>\$ 4,742,700</u>	<u>\$ 5,881,200</u>
<b>Surplus account</b>		
Surplus, January 1 .....	\$ 82,617,100	\$ 87,359,800
Transferred to surplus—as above .....	4,742,700	5,881,200
Surplus, December 31 .....	<u>\$ 87,359,800</u>	<u>\$ 93,241,000</u>

# Directors



**WILLIAM H. DAVIDSON**, President  
Harley-Davidson Motor Co.  
Milwaukee, Wisconsin



**EMERSON G. HIGDON**, President  
The Maytag Company  
Newton, Iowa



**MELVIN C. LOCKARD**, President  
The First National Bank  
Mattoon, Illinois



**HOWARD M. PACKARD**  
Chairman of the Finance Committee  
S. C. Johnson & Son, Inc.  
Racine, Wisconsin



**FRANKLIN J. LUNDING**  
Chairman of the Finance Committee  
Jewel Companies, Inc.  
Melrose Park, Illinois  
*Chairman and Federal Reserve Agent*



**HARRY W. SCHALLER**, President  
The Citizens First National  
Bank of Storm Lake  
Storm Lake, Iowa



**ELVIS J. STAHR**, President  
Indiana University  
Bloomington, Indiana  
*Deputy Chairman*



**JOSEPH O. WAYMIRE**  
Vice President, Finance  
Eli Lilly and Company  
Indianapolis, Indiana



**KENNETH V. ZWIENER**  
Chairman of the Board  
Harris Trust and Savings Bank  
Chicago, Illinois

## DETROIT BRANCH



**JOHN H. FRENCH, JR.**, President  
City National Bank of Detroit  
Detroit, Michigan



**GUY S. PEPPIATT**, Chairman of the Board  
Federal-Mogul Corporation  
Detroit, Michigan



**RAYMOND T. PERRING**, Chairman of the Board  
The Detroit Bank and Trust Company  
Detroit, Michigan



**MAX P. HEAVENRICH, JR.**, President  
Heavenrich Bros. & Company  
Saginaw, Michigan  
*Chairman*



**L. WILLIAM SEIDMAN**  
General Partner  
Seidman & Seidman, C.P.A.  
Grand Rapids, Michigan



**B. P. SHERWOOD, JR.**, President  
Security First Bank & Trust Co.  
Grand Haven, Michigan



**GEORGE L. WHYEL**, President  
Genesee Merchants Bank & Trust Co.  
Flint, Michigan

## MEMBER OF FEDERAL ADVISORY COUNCIL



**DAVID M. KENNEDY**  
Chairman of the Board  
Continental Illinois National Bank and Trust Company  
Chicago, Illinois

# Officers



**CHARLES J. SCANLON**  
President



**HUGH J. HELMER**  
First Vice President

**ERNEST T. BAUGHMAN**, Vice President

**CARL E. BIERBAUER**, Cashier

**DANIEL M. DOYLE**, Vice President

**JOHN J. ENDRES**, General Auditor

**ELBERT O. FULTS**, Vice President

**ARTHUR M. GUSTAVSON**, Vice President

**LAURENCE H. JONES**, Vice President

**WARD J. LARSON**, Vice President,  
General Counsel, and Secretary

**RICHARD A. MOFFATT**, Vice President

**JAMES R. MORRISON**, Vice President

**HARRY S. SCHULTZ**, Vice President

**BRUCE L. SMYTH**, Vice President

**RUSSEL A. SWANEY**, Vice President

**JACK P. THOMPSON**, Vice President

**HARRIS C. BUELL, JR.**, Chief Examiner

**GEORGE W. CLOOS**, Senior Economist

**LE ROY A. DAVIS**, Assistant Vice President

**FRED A. DONS**, Assistant General Auditor

**VICTOR A. HANSEN**, Assistant Vice President

**EDWARD A. HEATH**, Assistant Vice President  
and Assistant Secretary

**GEORGE G. KAUFMAN**, Senior Economist

**MRS. DOROTHY M. NICHOLS**, Senior Economist

**RAYMOND M. SCHEIDER**, Assistant Vice President

**KARL A. SCHELD**, Assistant Vice President

**ROBERT E. SORG**, Assistant Vice President

**JOSEPH J. SRP**, Assistant Vice President

**LYNN A. STILES**, Senior Economist

**EUGENE J. WAGNER**, Assistant Vice President

**ALLEN G. WOLKEY**, Assistant Vice President

**ARNOLD J. ANSCHUTZ**, Assistant Cashier

**MISS BUDDIE J. BELFORD**, Assistant Cashier

**JOHN J. CAPOUCH**, Assistant Cashier

**RUDOLPH W. DYBECK**, Assistant Cashier

**FRANCIS C. EDLER**, Assistant Cashier

**WILLIAM H. GRAM**, Assistant Counsel  
and Assistant Secretary

**WILLIAM J. HOCTER**, Administrative Assistant

**ERICH K. KROLL**, Assistant Cashier

**DAVID R. STARIN**, Assistant Cashier

**ADOLPH J. STOJETZ**, Assistant Cashier

**CARL C. WELKE**, Assistant Cashier

## DETROIT BRANCH

**RUSSEL A. SWANEY**, Vice President

**GORDON W. LAMPHERE**, Assistant Vice President  
and Assistant General Counsel

**WILLIAM C. CONRAD**, Assistant Cashier

**LOUIS J. PUROL**, Assistant Cashier

**RAYMOND A. REAME**, Assistant Cashier

**RONALD L. ZILE**, Assistant Cashier

## Appointments, elections, and retirements

The following appointments and elections were announced in 1968.

### Federal Advisory Council

Donald M. Graham, chairman of the board of Continental Illinois National Bank and Trust Company of Chicago, was appointed member of the Federal Advisory Council from the Seventh Federal Reserve District for 1969. He succeeds David M. Kennedy, designated Secretary of the Treasury.

### Directors

Franklin J. Lunding, chairman of the finance committee of Jewel Companies, Melrose Park, Illinois, was redesignated chairman of the Board and Federal Reserve Agent for 1969.

Emerson G. Higdon, president and treasurer of the Maytag Company, Newton, Iowa, was appointed deputy chairman, succeeding Elvis J. Stahr, former president of Indiana University, Bloomington. Stahr's term as director expired.

Three directors were selected to fill expiring terms on the bank's board: Joseph O. Waymire, vice president, finance, Eli Lilly and Company, Indianapolis; Floyd F. Whitmore, president of Okey-Vernon National Bank of Corning, Iowa, and William H. Franklin, president of Caterpillar Tractor Company, Peoria. Waymire was reelected to his second term. Whitmore was elected to succeed Harry W. Schaller, president of Citizens First National Bank, Storm Lake, Iowa, who retired after serving two terms. Franklin was appointed by the board of governors to succeed Stahr, who retired after one term to become president of the National Audubon Society, New York.

At the Detroit branch, B. P. Sherwood, president of the Security First Bank and Trust Company, Grand Haven, Michigan, was appointed to his second term, and Peter B. Clark, president and publisher of the *Detroit News*, was appointed to succeed Guy B. Pappiatt, chairman of the board of Federal-Mogul Corporation, Detroit. Sherwood was appointed by the Chicago board.

Clark was appointed by the board of governors. Max P. Heavenrich, Jr., president and general manager of Heavenrich Brothers & Company, Saginaw, Michigan, was reelected chairman of the Detroit branch.

### Officers

Ward J. Larson, assistant general counsel and assistant secretary, was promoted to vice president, general counsel, and secretary. James R. Morrison, chief examiner, was promoted to vice president in charge of the Bank Examination Department, and Elbert O. Fults, assistant vice president, was promoted to vice president.

Harris C. Buell, Jr. was promoted to chief examiner, and William H. Gram was appointed assistant counsel and assistant secretary. Buell was formerly assistant chief examiner, and Gram was an attorney in the Legal Department.

Eugene J. Wagner and Allen G. Wolkey, both assistant cashiers, were promoted to assistant vice presidents. David R. Starin, a senior auditor, was appointed assistant cashier.

In addition, four vice presidents were promoted to senior vice president, effective January 1, 1969. Seven other officers were also promoted at the start of the new year, five new officers were appointed, and several titles were changed.

Promoted to senior vice president: Ernest T. Baughman was promoted to senior vice president and director of research. Also promoted to senior vice president were Laurence H. Jones, head of Building and General Services; Harry S. Schultz, head of Collections; and Russel A. Swaney, in charge of the Detroit branch.

Karl A. Scheld was promoted to vice president and assistant director of research; Lynn A. Stiles and George W. Cloos were both promoted to vice president and economist; and Gordon W. Lamphere was promoted to vice president and assistant general counsel at the Detroit branch. Also promoted to vice president were Le Roy A. Davis, Edward A. Heath, and Joseph J. Srp.

In addition, Carl E. Bierbauer, for-

merly cashier, was redesignated vice president and control officer.

Employees promoted to assistant vice president are Robert C. Johnson, who has been manager of the Control Department; Joseph G. Kvasnicka, an economist in the Research Department; William T. Newport and William Rooney, both systems engineers in the Planning Department; and Hilbert G. Swanson, chief of the Credit Department, assigned to the Loan Department.

Others with title changes: William J. Hocter, administrative assistant redesignated assistant vice president and assistant secretary, and George G. Kaufman and Mrs. Dorothy M. Nichols, both appointed assistant vice presidents and economists.

In addition, all assistant cashiers were redesignated assistant vice presidents, the title of assistant cashier being discontinued.

### Retirements

Five officers retired: Carl Weiskopf, assistant chief examiner (March 1); Harold J. Newman, vice president (April 1); William O. Hume, assistant vice president (May 1); and Paul C. Hodge, vice president, general counsel, and secretary, and Leland M. Ross, vice president (both December 1). Weiskopf had been with the bank more than 41 years; Newman, Hume, and Hodge more than 34; and Ross more than 27.

Seven employees retired after more than 45 years of service:

Rose J. Buettner	Treeda B. Toner
John Haenle	Henry Volka
Kermit O. Heika	Vera B. Whitman
Frank Lukasch	

Eighteen other employees retired after more than 25 years' service:

Roy P. Anderson	Elizabeth F. Patrny
Edward Bencivenga	Daniel A. Pedersen
Kornelis Bos	David R. Sangster
Clara D. Byberg	Louis F. Schmeidl
Irene Clancy	Violet I. Suder
Elsie C. Hawksley	Julia Vranek
Clarence J. Larson	Agnes H. Wagstaff
Samuel Martin	Selma B. Walker
Eugenia Miller	Irene B. Wallis



