

From: Federal Reserve Bank of Cleveland
For immediate release

"NEW HORIZONS FOR BANKERS"

A talk made by President RAY M. GIDNEY of the Federal Reserve Bank of Cleveland on Thursday January 23, 1947, at Hotel Statler, Cleveland, at a Forum sponsored by Cleveland Chapter, American Institute of Banking.

I am glad to come before the Cleveland Chapter at this fine series of Forum meetings. I was greatly impressed by the Forum meetings held last year and felt that they represented a really fine achievement. The talks by Loring Gelbach on "Bank Management", by Sidney Congdon on "Public Relations in Banking", by John Thompson on "What Industry Expects of Banking", by George Gund on "Inflation", and the excellent panel discussions which followed, set a standard which will be very difficult to approach in this and subsequent meetings. They covered the important phases of our business so well that for tonight I shall have to attempt a new approach. I am most pleased that you are to have the benefit of such a strong panel group as that represented by Rodney Lien, Frank Beam, Randy Harris and George Herzog.

One of the great things about the American Institute of Banking is the unique opportunity which it offers to get together for discussion and consideration of what is going on in the banking business and what we must do to meet the problems which must be successfully solved if our banks and we, individually, are to prosper. The Institute has been a tremendous force in making banking a profession in which all banks have an interest in the broader aspects of the business in which we are something like public servants and from which we derive our living. I think that in recent years we have in banking a better relationship between the workers of all banks than will be found in any other business and that this is in no small part due to the influence of the A.I.B. I believe also that all of us in the banking business have a responsibility to understand

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what is going on in the business and economic field and that we can exert a considerable influence upon the general public because of the understanding of business and economic subjects which is traditionally a duty of bankers to acquire. George R. James, a former member of the Federal Reserve Board and a very practical and successful Memphis businessman, used to say that what this country really needed was a better knowledge of fifth grade arithmetic. Today I believe there is a great need not only for a knowledge of fifth grade arithmetic, but also for an understanding of broad accounting procedure including particularly a clear idea of the meaning of balance sheets and operating statements. We have learned to split the atom and do many wonderful feats of mental activity but the large part of our people including many who are highly skilled and learned in matters of science and economics do not seem to have even an elementary acquaintance with the meaning of business balance sheets and earnings statements. There is clearly much lack of understanding of what it means to keep the assets of a single business greater than the liabilities and how easy it is to have red ink show up in the profit and loss statement. The single business multiplied many times stands for the nation's business. These are matters which bank people do understand and which they have the duty of explaining to others.

The subject assigned to me tonight is "New Horizons for Bankers". It is very broad and timely and gives opportunity for discussion much more lengthy than is possible at this Forum. On December 31st President Truman declared the hostilities of World War II officially ended. We are now definitely in the post war period and can appropriately pause to take account of stock and look ahead to the working out of the great problems of the after war period.

Back in the days when I was taking a course in Public Speaking given by the New York Chapter of the American Institute of Banking, which you see didn't

take very well, my attention was drawn to the opening lines of Daniel Webster's reply to Hayne, delivered to the United States Senate on January 26, 1830, or just about 117 years ago, and which fits well the purposes of tonight's discussion. Daniel opened his address by saying, "When the Mariner has been tossed for many days in thick weather and on an unknown sea, he naturally avails himself of the first pause in the storm, the earliest glance of the sun, to take his latitude and ascertain how far the elements have driven him from his true course. Let us imitate this prudence and before we float farther on the waves of this debate return to the point from which we departed that we may at least be able to conjecture where we now are."

It would take too long to describe in full detail where we now are or how we got here, but we can sum it up by saying that we have come through the world's greatest war with the greatest expenditure of lives and materials that the world has ever seen. Problems both national and international are great. As to the international, in Cleveland we have had brought to us by the Council On World Affairs the recent report from the World---an unusual opportunity to learn from representatives of many nations what they consider world needs and what they think the United States should do on connection with that.

It was a great and helpful exchange of views---a real World Forum---and we of Cleveland have every reason to take pride in the fact that this city could attract it. High praise is due to Brooks Emeny who led in interesting Henry J. Luce of Time Magazine in the joint project and in carrying it through. I shall not attempt to review the specific matters in which American action was suggested. All speakers, however, were quite frank in saying that America must take a leading part in working out world affairs. The Brazilian representative, Oswaldo Aranha, has coined a timely epigram by saying, "The United States has

disintegrated the Atom---it will now be its mission to integrate mankind." That is a large order. Mrs. Mildred McAfee Horton suggested that we should not be given tasks beyond our capacity and perhaps we can agree that the Aranha suggestion should be considered with this in mind. Throughout the discussion there was appreciation of the fact that to do its part, the United States itself must continue strong, prosperous and active. Henry Luce Brought this out particularly well at the opening luncheon. He expressed the belief that we should make ourselves strong and prosperous, but balanced this statement by recognition that to make this possible as a long time matter, it is necessary for the rest of the world also to work into satisfactory position. He and others were very clear in expressing the view that a prerequisite to satisfactory world progress at this time is a healthy economic condition in the United States because we, more than any other country, have the means to achieve stability and help others to do so. We, as bankers, are keenly interested in the welfare of the world and we can exert much influence in the direction of sound world policies. At the same time, we have a great obligation to maintain sound conditions in our own country and for those of us in the banking line it means maintaining sound conditions in our own banking institutions and among our bank customers. Let us take a look at where we are in our banking and business situation in the United States.

We have made surprisingly good progress in transition to peacetime activities. The year 1946 witnessed the highest levels of peacetime activity in our history, notwithstanding many difficulties too well known to need description. This was true for the nation as a whole and for the Fourth Federal Reserve District. Farm output and net farm income were at record levels, industrial employment and aggregate salaries and wages have been higher than in any other year except at the peak of wartime activity. Net incomes from business operations before income taxes, while disappointing in some lines and generally below the

high level of 1945, have, in aggregate, also been large. Lower taxes and refunds of some wartime excess profits have provided sufficient financial benefits to bring aggregate corporate profits after taxes to above previously existing records reached during the war. The total volume of money payments of all kinds in the nation has probably been higher than in any other year in our history.

At the close of the war our banks had worked into a position which has been spoken of as the soundest on record. A comment I heard yesterday leads me to take a moment here to refer to the study on country banks' U. S. Bonds which appeared in the January issue of Banking. It covered 4,545 banks with deposits less than \$7,500,000. For the average of these banks the maturities within 18 months were 43.6% of total holdings. The lowest state average was 24.3% and the highest 59.3%. Ohio showed 33%. Holdings beyond 14½ years were only 6.6%. Ohio was 10.2%. You have seen figures for large banks and know that generally their average maturities are short. This data regarding the position of the smaller banks is very reassuring. The banks have been quite thoroughly cleaned out of criticized assets which plagued them in the depression period and have become like ivory soap---99 44/100 per cent pure. Perhaps they have been too pure, for a banking system, characterized by the holdings of cash and government securities nearly equal to deposit liabilities, is not in a normal or entirely healthy state. The banking system should have a substantial part of its assets represented by loans if it is doing its part in serving the community and the nation's commerce, industry, and agriculture under peacetime conditions. Therefore, there was, on the part of our banks, a hunger for loans and a desire to move toward a more normal relationship of loans to other assets. There has been a mighty swing in this direction, greater perhaps than is generally realized. During the past year the volume of business loans of banks throughout the nation and in the Fourth District expanded more rapidly than ever before and the amount of outstanding bank loans to business has probably reached the highest figure on record.

So we may sum up the survey of where we are by saying that our banking assets are more diversified than a year ago. There is great activity and widespread prosperity, with exceptions, in commerce, agriculture and industry and with prospects as to continued activity and prosperity dependent in large part on how we conduct ourselves and whether we are able wisely to utilize the many advantages we have and to avoid destructive tendencies of which there are also many.

Now is a good time to take counsel as to where we are going and what adjustments we should make in our banking equipment, banking practices, banking education and banking operations to bring the best results. Unquestionably the period ahead will call for the highest quality of business and financial statesmanship. We want to maintain the flow of goods and services to our people and the peoples of the world so as to continue to contribute to the future advance of material well-being. At the same time we want to have our individual banks make loans soundly and avoid running into trouble with loans which may go sour or bad. One thing I am very sure of is that the good bank credit man is going to be in great demand and will have plenty of call to exercise his best talents. It is not going to be easy to judge credits with as many variable unknown and uncertain factors as we are likely to find in the credit equations of the next few years. The Cleveland Association of Credit Men recently sent out a letter to its members using the scare headline telling of the engineer of a train or the pilot of an airplane whose failure to observe signals brought disaster. They asked, "Do you see the danger signals? Do you observe the signals when you see them? We know that hundreds of firms in Northern Ohio lose money unnecessarily because their credit men do not see the signals (to a large degree) and (to a lesser degree) do not pay attention to the signals that they do see." There will be need for careful vigilance at the credit desk. Many recent occurrences are so like those which followed the close of World War I that they are danger signals as to credit problems and call for seeing and observing.

In surveying the future we must realize that it will take more than normal skill and effort to even approach the level of business accomplishments which we desire. An editorial in the Wall Street Journal of January 9th has two paragraphs which express a very important fact which is not sufficiently recognized.

"Of course the war did not leave us richer. It left this country and the whole world very much poorer. For a period of years, all efforts were centered on diverting, displacing and destroying the tools of production, that is, the country's capital. That destruction has placed the equivalent of a mortgage on every man, woman and child and the only way that mortgage can be discharged--- unless all of us go through the bankruptcy of a depression---is to increase and cheapen production. That can be done only by the restoration or betterment of tools.

"The thing is analogous to a plumber or carpenter who has gone into debt for a fur coat or some equally non-productive piece of merchandise. The last way he should attempt to meet the instalments on his debt is by not replacing or by selling his tools. Each time he does such a foolish thing, he reduces his power to produce and earn to meet future instalments. Better tools will enable him to earn the extra money to meet his payments."

We are all uneasy because we are finding it hard to keep our living standards at the level to which we are accustomed. It is not surprising that we are having this trouble; it is remarkable that our difficulty is not even greater. To overcome it we must equip our institutions, banking and business, with every facility---organization, mechanical equipment and "know how" that will enable us to produce banking and business services economically while at the same time pay salaries and wages at the higher level to which they have risen. Bank earnings in recent years have been good but the published figures at the close of 1946 indicate that expenses have been growing to an extent which has caused a declining

trend of profit for some banks and is likely to reduce net earnings during the coming year. Therefore, the banks will need the wholehearted cooperation of their employees in working for efficient operations so that the higher costs may be met and the earnings statements continue to reflect healthy earnings. The same need exists in other fields.

Here I should like to take a moment to express approval and satisfaction with the very great improvement which banks have made in the form and scope of the information they give to the public on their condition and earnings. It is only a few years since the only information available to the public on the matter of bank earnings was what could be guessed at or estimated by comparing changes in the statement of condition. Now quite detailed figures are given for various factors affecting earnings and some reports give an expanded description of the banks operations. It is a good and healthy development.

Many writers and speakers have emphasized that efficient production is the one thing that will enable us to keep up the standard of living and to progress and I believe there is general agreement that this is true. When the National Association of Supervisors of State Banks met here last September we were fortunate to have as a speaker at our dinner meeting, President William E. Wickenden of Case School of Applied Sciences. He took as his subject "How to Divide the Fruits of Progress." It was a timely subject, well handled and much appreciated by the Bank Supervisors. The mere statement of this question directs attention to something which is very important. In the first place, there must be fruits of progress if there is to be something additional to divide. The more efficiently produced, the larger the quantity available for distribution and the better the prospect we all have in receiving a comfortable share. If the division is lopsided, progress will be hampered. As Jan Masaryk of Czechoslovakia said at the world affairs meeting in speaking of world production, "There will be enough to go around if we are nice about it." So with our productive efforts, if we work as efficiently as we know how, there will be enough to go around if we are nice about it.

I recently ran across so clear a discussion of the part of capital flow in making for large production and large possible division of product that I would like to read some of it to you. It was written by Thomas Furlong, financial editor of the Chicago Tribune, and struck me as a clear and valuable discussion of an important point.

"The common interest of labor and capital is the outstanding economic fact established by the unrivaled progress made by the United States in the last 100 years. In no other country has the population achieved the standard of living reached here. In no other country has there been the supply of capital for productive use that made possible America's amazing development.

"Future Economic growth in the United States and elsewhere will be limited by the amount of capital available for investment in the machines and equipment that permit bigger production."

"The Swedish economist, Gustav Cassel, shortly before his death two years ago said: 'The high level of American National income can only be explained by the relatively abundant supply of capital in the United States. If we compare the conditions in different countries immediately before the present war, we shall find that the American worker has been approximately twice as amply provided with the means of production as the British workman and has therefore risen to approximately twice as high standard of life.'

"Cassel went on to explain that the peoples of the world who suffer the direst poverty, such as those of China and India, reside in the countries where capital investment in the modern sense virtually is nonexistent.

"Others have marshalled a wealth of historical evidence to show the interest labor has in encouraging larger investment of capital in the tools of production. Before this step can occur there must be accumulation of capital through saving. Although often scoffed at by politically favored 'experts', saving is the one device by which mankind has been enabled to build the machines that increase per capita production and thereby raised man's standard of living.

"Dr. Willford I. King of New York University has shown clearly that the progress achieved by labor in the United States has been brought about by enlarging the production pie, not grabbing a bigger piece of the pie at the expense of other essential economic groups."

There is a good deal more of the article but that which I have read conveys what I think is the point that we must thoroughly grasp. Again it is first a matter of having adequate tools to do an adequate job; second, a matter of using the tools efficiently; and third, of making a division of the results which is sound and fair. It is fair that each participant should receive according to the value of his contribution and sound that the distribution should be such that it does facilitate and not prevent economic growth.

It is important to us that we have in this country the splendid capital equipment which is far above that of any other country, and we must not permit ourselves to doubt that with such equipment we can handle the problems of production and distribution necessary to a high level of employment and good business conditions.

Professor Sumner H. Slichter of Harvard University recently said (Dec. 12, 1946) that he believed two principal conclusions for the immediate future of business are: (1) that the prospects for profits depend on industrial peace, and (2) that important readjustments are ahead in the price structure. Both of these matters are worthy of the closest possible attention from bankers and both will affect the work of the credit man. The satisfactory solution of the first is needed for the efficiency of production which we have been discussing and which should make possible readjustment of price structure in a way which will tend toward equilibrium and permit us to go forward with confidence. Professor Slichter also expresses the view that the most important contribution which business can make is to keep down the prices of finished goods as much as possible and to reduce any prices which are out of line with the general price level.

I believe that business will do its best to make this contribution and I think we can all help by obtaining for ourselves a clear understanding of the problem and helping others to get it. Reduced prices will make problems for the bank credit man but if well handled they will conduce to economic health and they will certainly be welcomed by each of us as a relief from the sharply increased cost of living we have recently known. Notable price reductions have recently occurred and others are going on. The Wall Street Journal has given them front page treatment in a most interesting way. They seem to me to indicate that inflation is finding an effective antidote through the exercise of certain good American qualities; such as, (1) the habit and traditional practice of making and selling at as low a price as possible, and (2) the habit and tradition of holding off on our purchases for personal requirements when we think prices are unreasonably high. I don't mean a buyer's strike but rather the kind of thing that happens when we say, "I think I will wait a bit before buying that item."

Many changes have occurred in banking in recent years and there has been talk about the usual type of commercial loans being a thing of the past and that new fields of bank lending must be developed. Of course we must adjust our practices to the needs of the day, but to a large extent the form changes rather than the substance. I am inclined to apply to banking a French saying - "The more it changes, the more it is the same thing." In looking at our new horizons, I think we have to be alert to recognize the same fundamental things often with considerable difference in appearance and to be alert and adapt to fit our actions to the current practice. There is certainly no place in the active management of a bank for anyone who is not alert and informed and it takes plenty of study to keep adequately informed these days. The A. I. B. is a great help to banks and individuals in this way. But it is also necessary to recognize the sound underlying principles and rules which are changeless.

You remember that Voltaire's character, Candide, after going all over the world and taking part in many fabulous adventures, finally came back home and said, "After all, we must cultivate our own garden." We make big excursions all over the world and enjoy and profit by them, and are inspired with the desire to do our part to help out in world affairs by keeping informed about them and giving sympathetic understanding to the problems of all peoples. This is good but we must come back to the proposition that we render our service world wide and nation wide by doing a good job in our own institution. There we must cultivate our own garden.