

Remarks

Roger Guffey, President

Federal Reserve Bank of Kansas City

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I am delighted to be in beautiful Wyoming again and to take part in the annual convention of the Wyoming Bankers Association. When I was invited to speak at this gathering, I was pleased, for a number of reasons. One, of course, is the unsurpassed natural beauty of this area, which has considerable drawing power for flat-landers such as myself. Another reason is that I enjoy the hospitality of Wyoming bankers. I would like to recognize and express our appreciation for the bankers and others from Wyoming who have served the Federal Reserve Bank of Kansas City and the System so ably.

In my 10 years at the Kansas City Bank, I've known and respected people like Homer Scott of Sheridan--who played a major leadership role as a member of our Board of Directors and board chairman at Kansas City for 5 years. Similarly, John Hay of Rock Springs, who served on both our Omaha and Denver Branch boards; and Felix Buchenroth, from Jackson, now a director of our Denver Branch, have shared generously of their counsel in recent years. It is a pleasure to say publicly here how much we at the Fed value their contributions.

As many of you may know, I've been president of the Federal Reserve Bank of Kansas City for almost a year and a half now, and I can say without reservation that these months have not been dull! You will recall that just over a year ago, an important topic in banking was financial reform, including some proposals in Congress which would have seriously eroded the ability of the Federal Reserve to pursue an independent, nonpolitical course on monetary policy. If that issue alone wasn't enough to keep us busy last year, then there was the matter of formulating a monetary policy to help keep the economic recovery going while at the same time guarding against renewed double-digit inflation.

If 1976 was a lively break-in period for me at the Bank, 1977 has been just as interesting. This year, our efforts have included improving our understanding of the impacts

of the new competitive environment for financial institutions which appears to be just over the horizon. At the same time, the issue of Federal Reserve membership--a matter of critical importance in many ways--has been drawn into sharper focus, involving all of us in the Federal Reserve System in seeking a workable and equitable solution. And, as usual, there are the continuing concerns about monetary policy: that is, just what level of money and credit will enable the nation's economic growth to continue while at the same time working towards reducing further the rate of inflation?

As I have traveled across the Tenth District for the last year or so, talking with bankers at association gatherings and at meetings held by our Board of Directors with about 400 bankers--and as I have received many letters from bankers and seen the comments of industry leaders in the press--I hope we've gained valuable insights into the matters which concern you. This kind of dialogue is healthy, and you may be assured that so long as I remain at the Federal Reserve Bank of Kansas City, we will have many opportunities to exchange views with you.

Before leaving these more personal comments, I want to add another observation gathered from a year or so of traveling throughout the District. I'm more convinced than ever that in nearly every community in the District--and probably in the nation--bankers are assuming their proper role as community leaders. Of course, bankers make business judgments every day which affect the economic life of their communities. But more than that, bankers are frequently on the leading edge of improvements in the quality of life in their cities and towns, by guiding the civic, charitable, and cultural efforts which lead to community progress. In a broader sense, it's the bankers in each community who support efforts to improve and preserve our free enterprise system and the opportunities it offers. I have seen the traditional inclinations of bankers to accept the responsibilities of leadership and how it has paid big dividends in the form of better communities. We commend you for that and encourage you to maintain and strengthen your commitment to this type of leadership.

Because bankers are often in the forefront of positive changes occurring in their communities, and because the banking industry seems to be in a constant condition of change or at least impending change from technological, competitive, legislative, or regulatory forces, it seems to me appropriate to consider with you for a few minutes the idea of managing change.

All of you are agents for change in your own communities--making business and financial decisions leading to economic growth, and in civic leadership activities leading to improvements benefiting your neighbors. Perhaps the concept of change is even clearer for you here in Wyoming than in some other areas because of the explosive growth as a result of expanding demand for and development of the oil, gas, and coal resources so abundant in your state. The energy boom certainly represents massive changes in many Wyoming cities and towns and in the financial institutions serving those communities.

In the 1970's, we have come to recognize that change is a powerful force in all facets of our personal and professional lives. The phenomenon of change affects every decision we make. Intelligent acceptance of change often is the key to successful integration of worthwhile new elements into our everyday life. Banking certainly has not been exempt from change, nor are bankers necessarily devoted to the status quo. For many bankers, change is the incentive to explore new opportunities.

The most obvious areas of change affecting financial institutions today are related to competitive developments--as discussed earlier by Jerry Lowrie. The changing competitive environment has been aided and abetted by the rapidly evolving electronic funds transfer technology, which may not, as yet, be fully understood as a medium of financial exchange. In any case, because of the dramatic improvement in computer-based systems and their capabilities, most financial institutions now recognize the market potential in expanded EFT systems as a way to improve the array of financial services available to the public.

Furthermore, many bankers now use the new alphabet of banking--EFT, ACH, ATM, CBCT, POS, and RSU--as comfortably as they discuss lending policy or investment strategy. Electronic banking is here and bankers throughout the nation--and, more important, your competitors--already are working to manage the changing technology for expanded customer services and penetration into new markets.

Although the potential economies of electronic payments are just now being documented, the availability to and development of the new technology by savings and loans, credit unions, and other institutions has, in fact, begun to blur the distinctive transaction account or checking account franchise once solely held by banks. As more and more thrift institution customers gain grocery store or telephone access to their interest bearing accounts for everyday transactional purposes--as is true in most of your neighboring states--and as banks themselves enable customers to shift funds at will between savings and demand accounts, your traditional and formerly exclusive checking account service gains new competition. Then, add to these technological factors the pressures and rationale for nationwide interest-bearing transaction accounts--as outlined by Jerry Lowrie--and it's not difficult to begin to visualize the shape of a new financial environment.

Given recent developments, it's apparent that the consumer movement is alive and well and living happily in Washington, as evidenced by gathering support for the concept of the NOW-type accounts. In fact, I believe that consumerism undoubtedly will have a considerable impact on the ultimate makeup of financial institutions and the services you and your competitors offer. As an example of this trend, you might consider the changes occurring in the credit union concept: more liberal interpretations of the commonality of interest principle, expanding credit union powers, and an increasingly mobile work force which has weaker long-term ties to banks. It seems to me that credit unions could become a major competitor for commercial banks in the near future.

In the shorter term, of course, the dimensions of an altered competitive environment for financial institutions will most likely be established as the result of Congressional action--and after lengthy consideration of alternatives. While we at the Federal Reserve Bank cannot predict the features ultimately to be included in any new legislation, we do hold strong beliefs about what should be the essential characteristics of any new competitive financial situation.

For reasons of fairness and equity, and for considerations of monetary policy, we believe that competing financial institutions which have similar powers should be treated similarly in matters of reserves, taxation, capital requirements, and liquidity. We would oppose any change which would give one group of financial institutions a competitive advantage over any other group. In short, we strongly favor competitive equality among depository institutions with similar powers. At the same time, we feel that the direct access of nonmember institutions to Federal Reserve services should not be expanded further until the membership issue has been resolved.

While competitive equality among financial institutions with similar powers is as important a concept to us as it is to you, the questions of Federal Reserve membership and related matters are also key issues which demand resolution, again for reasons of basic equality. We know that member banks--and there are 61 in Wyoming--operate at a competitive disadvantage with nonmembers because of the cost of maintaining sterile, nonearning required reserves.

Recent studies at the Federal Reserve Bank of Kansas City clearly show that there is a significant burden associated with Federal Reserve membership. Furthermore, the burden is relatively greater for small member banks. For example, one study indicated that member banks with deposits under \$100 million experienced a net earnings burden equal to foregone interest on about 2 to 3 per cent of total deposits. This

burden--as a major competitive concern--may not be so onerous among Wyoming members because of the structure of state reserve requirements, but we know the cost of membership is an important consideration for most member bankers here and elsewhere in the Tenth District.

Because of the net cost of membership, we at the Federal Reserve Bank of Kansas City firmly support the concept of equalizing the reserve burden. This might be accomplished by applying reserve requirements against those deposits in any financial institution which may be used for transactional purposes, and thus are part of the nation's basic money supply. Alternatively, we could support changes which would provide a market rate of return on all or some part of the reserves required to be maintained at the Federal Reserve.

Commercial bank membership in the Federal Reserve System is a matter of critical importance to us for another reason which, we believe, transcends the question of reserve burdens and the like. While we fully understand the bottom-line reasons why some banks choose to withdraw from the System or that others decide not to join when chartered, nevertheless I am convinced that continued erosion of membership has serious implications for effective monetary policy.

As you know, the initial impact of monetary policy falls directly on member banks and their reserves. But, if because of declining membership, there are fewer and fewer member banks, and a smaller proportion of the nation's banking resources under the direct control of the central bank, there is, in my judgment, strong potential for monetary policy to become less and less precise. As you also know, an imprecise monetary policy can bring unwelcome disruptions to the financial community and, indeed, repercussions throughout the economy. A further complication, growing potentially more troublesome every day, results from the fact that as transaction-type checking account deposits grow in savings and loans or credit unions, for example, those balances, which are in fact,

part of the nation's money supply, are outside the direct influence of the Federal Reserve. As a matter of fact, even if Federal Reserve membership should stabilize at its present level, it's still possible that the growth of these nonbank transaction accounts could disrupt our monetary policy processes to an increasing extent.

Membership is important to us, here in Wyoming and elsewhere. We at the Kansas City Fed hope that we can help manage the change--perhaps by contributing to the thinking of those who will be crafting the ultimate framework of whatever membership or reserve maintenance arrangements may evolve.

In a similar vein, the technological, competitive, legislative, and regulatory changes now affecting banking present unusual challenges to each of you. But as I noted earlier, change can be the onset of opportunity, if change is managed--not manipulated--for the benefit of those affected.

One major opportunity for you to manage the change facing your bank, in my opinion, is to begin now to plan for a new approach to pricing your banking services. For many years, banks have given away demand deposit services, in a sense, or have charged for them in implicit, rather than explicit ways. We all know that NOW-type accounts will cost money--the New England NOW experience suggests, for example, 2 or 3 per cent expense on the NOW deposit. Because you will need to price the interest-bearing demand account to your customers--it can't be "free" anymore--you also will need to understand the cost-price relationships of this service, and all of your services, for that matter. From the customer's point of view, because many financial institutions may be offering similar services, he or she will want to know your explicit price for each financial service, for comparison purposes.

To set your prices, of course, you will need to know your costs. Again, the phenomenon of change will provide the incentive--if not merely the opportunity--for bankers

to improve their understanding of their true costs and the sources of their profits. I might add a little promotional spot here for the functional cost analysis service offered by the Federal Reserve Bank of Kansas City. Several Wyoming member banks already participate in the FCA program, and another 20 or so have inquired this year about it. We encourage you to investigate this free service as at least one means to help you understand the cost structure of your operation.

Along with the overall pricing issue, you also will be considering the impact of possible changes in banking's traditional total customer relationship. For example, how will you be able to retain the warm, personal flavor of your customer relationships if more and more banking transactions occur by means of push-buttons? Similarly, how are you going to shape your marketing efforts to attract the customers who all at once will have a variety of sources for the transaction account services they need. I think you will agree that there are some real opportunities to manage the change occurring in your environment.

As the issues of change in our financial structure--and the inseparable issue of technological impacts--are discussed in national forums in coming months, I know that knowledgeable bankers will continue to draw upon their experience to counsel their lawmakers and regulators. I, for one, am hopeful that our legislators will consider fully the traditional principles of free enterprise in their decisionmaking. Let them establish a financial structure where all like institutions can compete equitably. Let them provide reasonable equity in requirements for capital, for liquidity, for taxation. Let the marketplace decide what institutions should provide what services and at what prices. I am confident that America's bankers would welcome the opportunity to place their wide experience and commitment to public service on the line and take their chances against all comers in the competitive arena.

In closing, I want to say that as inevitable change does occur in banking, we at the Federal Reserve Bank of Kansas City intend to work with you to accommodate this change, to manage it for the preservation of the finest financial system in the world. As we consider these matters, and as we deliberate about monetary policy and other policies affecting banking, business, and the public, I know that I will be able to call upon my Wyoming banking friends for advice, assistance, and support.