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# Federal Reserve Notes

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## FED ISSUES PAPER ON CREDIT SCORING

The Federal Reserve Board of Governors last month issued a staff paper discussing methods by which the anti-discrimination rules of Regulation B can be applied to credit-scoring systems. The Board's original proposals, issued in April, had been criticized by consumer groups for treating credit scoring systems differently than judgmental systems under Equal Credit Opportunity (ECO) rules. When issuing the staff paper, the Board said that the purpose of its original request for comment "was to make Regulation B a more effective tool for eliminating discrimination in credit granting."

The Fed's staff paper noted that all credit analysis, whether performed judgmentally by loan officers or by credit-scoring systems, is based on the principle that past credit experience predicts future credit performance. "Judgmental systems rely upon the experience of credit officers to identify the characteristics of past creditworthy customers that are reliable indicators of creditworthiness. A credit-scoring system uses statistical methods to evaluate and compare past creditworthy and noncreditworthy applicants.

"In a scoring system, the numbers are used to construct a combined score for individual applications to determine whether credit should be extended. As distinct from most judgmental systems, which involve a subjective

*(Continued on page 4)*

## CHINESE DELEGATION VISITS S.F. FED

The Federal Reserve Bank of San Francisco welcomed Finance Minister Zhang Jingfu and 14 other officials from the People's Republic of China, at a late July meeting at the Reserve Bank. San Francisco was the last stop on a U.S. tour for this group, which was composed mostly of Finance Ministry officials, but also included representatives of the People's Bank of China, the Ministry of Foreign Affairs, and the State Planning Commission.

In his welcoming remarks, Reserve Bank President John J. Balles said, "Trade and financial relations between the United States and the People's Republic of China have increased rapidly in recent years. Many of us forget, however, that these relations date back to the very beginning of our country." He noted that the first act of the first U.S. Congress supported the China trade by placing a heavy duty on tea from Europe and reducing duties on tea imported directly from China.

Balles added, "Times have changed considerably since the sailing-ship era. Yet in this world of jet aircraft and container-cargo ships, new ties are being forged between your country and ours. In the 1970's, both countries are participating more and more in the rapidly growing trade and finance of the diverse Pacific Basin region. I trust that your visit to this country will lead to even greater progress along these lines."



**Zhang Jingfu, Finance Minister of the People's Republic of China (left), meeting with John J. Balles, President of the Federal Reserve Bank of San Francisco.**

Senior Vice President Michael W. Keran described for the visitors the Federal Reserve's basic responsibilities in the areas of bank supervision, banking operations and monetary policymaking. Assistant Vice President Hang-Sheng Cheng added a description of the Reserve Bank's Pacific Basin program, which encompasses conferences, publications, technical assistance, and two-way visits between top-level Fed officials and heads of the central banks of Pacific Basin countries.

Several directors from the Reserve Bank's five offices attended the dinner held after the meeting. They included Mrs. Howard Ahmanson (Chairman of the Board, Caroline Leonetti, Ltd.), C.M. Berry (President, Seattle-First National Bank), Ole R. Mettler (President and Chairman of the Board, Farmers and Merchants Bank of Central California), and Robert A. Young (Chairman of the Board and President, Northwest National Bank).

*(Continued on page 4)*



**J. Paul Morley, Bank Relations and Public Services Manager at the Reserve Bank's Salt Lake City Branch, opens a new bag of Anthony dollar coins. Deseret News photo.**

## **ANTHONY DOLLAR CAMPAIGN CONTINUES**

The commercial-banking system placed 280 million Susan B. Anthony dollars in circulation during July, the first month the new coin was available. The U.S. Bureau of the Mint plans to produce a total of 950 million Anthony coins by the end of 1979, to meet the demand for the new dollar.

Treasury and Federal Reserve officials made a number of appearances promoting the new coin during the summer period. Treasury Under Secretary Bette Anderson visited San Francisco and Los Angeles this month, calling attention at each stop to the cost advantages of the new coin. She noted that the dollar coin lasts ten times as long as a dollar bill, so that the coin could save taxpayers as much as \$50 million a year in production and handling costs. Also, if the coin becomes widely accepted, the Bureau of Engraving and Printing could postpone plans to build a new \$100-million facility to produce dollar bills.

In the Mountain States, Utah Governor Scott Matheson received the first Anthony dollar released in that state from Wendell J. Ashton, Chairman of the

*(Continued on page 4)*

## **WALLICH REPORTS ON EURO CURRENCIES**

Federal Reserve Governor Henry Wallich rejected "the extreme view that the Eurocurrency market is an unrestrained source of monetary and exchange-market instability," in testimony before a House Banking Subcommittee last month. But Wallich added that the existence of this market makes the execution of monetary policy more difficult. "There is a danger that, if measures are not taken to moderate the growth of the Eurocurrency market, the problem will grow over time and the prospects for controlling inflation will correspondingly worsen."

The Eurocurrency market is an international banking market in deposits and loans, which are denominated in currencies other than the currency of the country where the bank is located — for example, dollar deposits and loans of banking offices in London. Eurodollars account for about three-fourths of the Eurocurrency market, with about half of the remainder being Euromarks.

Wallich noted that the scale of the Eurocurrency market can be overestimated, with the gross total of foreign-currency liabilities of banks in industrial countries amounting to \$800 billion (end-1978 data). But this figure is inflated by a large volume of interbank activity, that neither contributes to the liquidity of the nonbank public, nor is associated with any extension of credit to nonbanks.

When various interbank transactions are eliminated, the new monetary liabilities in the Eurocurrency market amount to roughly \$150-175 billion, of which about one-third is counted in the monetary statistics of some country. Thus, the so-called "stateless" money in the Eurocurrency market — that which is not counted in national monetary statistics — is on the order of \$100-120 billion.



**Henry C. Wallich**

Wallich argued, however, that the importance of the market should not be underestimated. The absolute numbers involved are large, and are growing much faster than the domestic monetary and credit aggregates of most major nations. For example, from the end of 1974 to the end of 1978, Eurocurrency liabilities to nonbank institutions grew about 18½ percent annually, on the average — several times as fast as the standard U.S. monetary aggregates.

Consequently, Wallich called for careful monitoring of this rapidly growing market. In addition, he said, "Careful consideration should be given to making monetary restraints operating on the Eurocurrency market move more parallel with restraints on domestic markets."

He added that any approach adopted should seek to preserve the benefits that flow from the existence of the Eurocurrency market. "The market is extremely competitive and efficient. It facilitates movements of large volumes of funds from savers to investors across national borders at low cost. In doing so, it helps to finance temporary current-account imbalances and improves the efficiency of investment worldwide."

*(Continued on page 3)*

## WALLICH REPORTS

(Continued from page 2)

As another guideline, Wallich said that any approach adopted should help contribute to keeping the volume of international liquid assets within bounds. "Little would be achieved, and a great burden would be placed on some institutions, if part of the market were restricted and another part were left unrestrained to take up the slack, or if Eurocurrency banking activity could easily be shifted into new unrestricted forms." In this regard, he welcomed the growing tendency for foreign central banks to adopt the American approach toward bank supervision — which involves considering the safety and soundness of U.S. banks abroad when reviewing proposals of banks to expand their international operations.

The Fed governor said that, with due regard to these and other considerations, the Federal Reserve has examined several ways that the Eurocurrency market might be brought under greater control. One possible technique would entail placing reserve requirements on the Eurocurrency liabilities of banks' head offices, branches and affiliates, no matter where located. "Those countries whose banks and banking affiliates have a significant presence in international markets would be expected to act in concert with respect to their banks." This approach, if adopted, would minimize the likelihood that large reserve-free markets would emerge through the efforts of banks whose head offices are located in non-participating countries.

Representatives of the Federal Reserve and other central banks are now studying the reserve-requirement and other possible approaches. Wallich noted that the technical difficulties are considerable. Thus, he concluded, no action is likely on Eurocurrency-market controls until after the current study is completed. 🐾

## HIGH-SPEED CURRENCY MACHINES INSTALLED



As it did previously with high-speed check-sorting equipment, the Federal Reserve System is now leading an effort to develop a more efficient and cost-effective method of verifying, counting and sorting currency. The Federal Reserve Bank of San Francisco and nine other Reserve Banks have installed or will be installing in the near future a "Currency Verification Counting and Sorting System" with an optimum feed rate of 1,200 notes a minute, which will not only detect counterfeits but also determine the fitness of the currency processed. The equipment will supplement but not replace this District's polybag/shrink-wrap program.

As an integral part of the processing system, the equipment can immediately destroy, on line, those notes which have been determined as unfit. Consequently, these sophisticated new machines eliminate the need for complex manual procedures now required for currency verification and destruction.

Sometime in 1980, this Federal Reserve District will have six of the new machines in operation — three in Los Angeles, two in San Francisco, and one in Seattle. Reserve Bank staff will be able to handle food coupons as well as

currency with these machines.

The need for new equipment became evident with a sharp expansion in the Federal Reserve's currency-handling workload, which increased 25 percent over the past half-decade, to 8.5 billion pieces in 1978. The Federal Reserve's task was also complicated by the sharp variation in quality of the notes returned as unfit by commercial banks to the Fed.

For many years, Fed employees have performed these tasks manually, with the aid only of certain types of mechanical counters. In particular, destruction of unfit notes has required considerable effort, and demanded special protection procedures. But the cost of this manual operation increased sharply in recent years, as wage rates climbed and productivity stabilized. The rising cost of processing, along with the escalating workload, thus encouraged the Federal Reserve and the Treasury Department to automate the processing function. But now, the whole area of currency verification and destruction — a labor-intensive, security-conscious area — will be replaced by the switch to on-line verification and destruction. 🐾

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### CREDIT SCORING

*(Continued from page 1)*

appraisal of all the material in an applicant's file before credit is extended, credit-scoring systems only value those characteristics that previous statistical analysis indicates are predictive of credit-worthiness."

The Board's April proposal presented alternative ways of applying the anti-discrimination rules of its ECO regulation (Regulation B) to four credit-scoring practices:

- Assigning a score to the number of jobs or sources of income an applicant has, and to his or her sources of income;
- Keeping out of the scoring system the amount of the applicant's income from secondary sources, such as part-time employment, pension or alimony;
- Giving only judgmental reasons for adverse action on a credit decision;
- Selecting reasons for adverse action from an agency model statement, where the credit-scoring system used differs from the model statement.

The deadline for comments on the proposal was August 20, but the Board said that any comments

### CHINESE VISIT

*(Continued from page 1)*

Other guests included Suez Chen (Senior Vice President, Bank of America), Norman C. Eckersley (Chairman of the Board and Chief Executive Officer, Chartered Bank of London), Richard J. Glover (Co-Director, National Council for U.S.-China Trade), Carl E. Hartnack (Chairman of the Board, Security Pacific National Bank), Herbert E. Horowitz (Director of the U.S. Treasury Department's Office of East-West Economic Policy), John W. Kenney (Vice Chairman of the Board, United California Bank), Carl E. Reichardt (President, Wells Fargo Bank), and Thomas R. Wilcox (Chairman of the Board and Chief Executive Officer, Crocker National Bank).

received while the staff was analyzing responses would be fully considered. The Board has sent the staff study to all parties who had commented on the credit-scoring proposals. Other interested parties may receive copies of the staff paper by calling the Law Department, Federal Reserve Bank of San Francisco, (415) 544-2256.

### ANTHONY DOLLAR

*(Continued from page 2)*

Board of Directors of the Salt Lake City Branch of the Federal Reserve Bank of San Francisco. In addition, Idaho Governor John Evans received Idaho's first Anthony dollar from several of the Reserve Bank's Salt Lake City directors — Robert A. Erkins, Mary S. Knox, and J.L. Terteling.

In the Northwest, the Portland division of Safeway stores made an intensive effort to distribute the Anthony dollar. Safeway cashiers distributed an estimated 600,000 dollar coins to their customers during the first two weeks of July, frequently making change with both the dollar coin and the two-dollar bill. And throughout the West, a number of rapid-transit districts asked their customers to use dollar coins rather than bills in fare boxes, as a means of promoting speed and efficiency of service.

To help publicize the coin, the Federal Reserve is offering free copies of a pamphlet called "The Dollar of the Future." For copies, write or call the Public Information Section, Federal Reserve Bank of San Francisco, P. O. Box 7702, San Francisco 94120. Phone (415) 544-2184.