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Study #15 Effect of Govt Lending Agencies
&Postal Savings Sys Upon Banks
Bank Suspensions Study of 1936

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MISCELLANEOUS

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#15 CLIPPINGS (NEWSPAPER)

CLIPPINGS

R. S. Hecht, Pres., Hibernia Bk. & Tr. Co., New Orleans
Hearings - S. 4115
March 1932

413.1a
Pod 8

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Senator FLETCHER. Have postal savings banks interfered with your deposits?

Mr. HECHT. I should not think they have interfered with deposits in cities so much, but they have taken a great many deposits in the smaller banks in the country, in neighborhoods where bank failures have occurred. Whenever uneasiness develops over the failure of one bank in a given country district there is the natural tendency of persons to put their money into the Postal Savings System.

J. E. Woods, President the Teague National Bank, Teague, Tex.

Hearings - S. 1715 and H. R. 7617

June, 1935.

p. 960

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Concerning the operation of the Postal Savings System, I wish that I might impress upon the members of your committee the serious inroad that postal savings competition is making upon the operation of the smaller city banks. The effect of this competition has been most damaging to banks in towns ranging in population from 2,000 to 5,000. It is not because these banks have compacently accepted this condition that relief from this menace has not been persistently urged upon the Congress, but it is because of the fact that during the past 2 years each session of Congress had had under consideration major banking bills, which the legislative committees of our associations have felt were of such vital importance to the banking industry or profession as a whole that they should concentrate their efforts on these major bills; and as the small-town banks are the ones that are

bearing the brunt of this competition the matter of urging relief has been deferred pending settlement of the major measures.

It is my opinion, arrived at after careful study of the postal savings question, that the operation of the Postal Savings System has served to dry up credit in our erstwhile prosperous communities more than any other cause that possibly could be reached by legislation. The ideal functions of a bank are to provide facilities for impounding the earnings, savings, and the liquid wealth of the community and use it as the basis for legitimate credit which is used in the channels of trade and the building up of worthy enterprises in the community. Any enterprise or operation that drains this liquid wealth from the community that produced it will retard the development of and, if continued long enough, will wreck the community economically.

Senator BYRNES. It is your information that the postal savings deposits have increased during the last few years?

Mr. WOODS. Is it; yes, since the deposit insurance it has increased.

Senator BYRNES. The figures I saw within the last few weeks show no increase, or a very slight increase.

Mr. WOODS. Possibly the current figures; but over 1934 I understand they increased $10,000,000. I believe that is shown in the Postmaster General's report.

Senator COUZENS. What interest do they pay?

Mr. WOODS. Two percent.

Senator COUZENS. What are you paying?

Mr. WOODS. We pay 2 percent on savings accounts. The average country banker, before the postal savings competition became so great, had very few interest-bearing accounts.

Senator TOWNSEND. The competition of the postal savings bank forced the country bank to pay that interest?

Mr. WOODS. Yes. The country banks cannot benefit by this deposit insurance like the city banks can because we have to compete with the postal savings. The city banks can take our money that we used to get as interest on daily balances, and they do not have to pay it. They kind of break even and, in a way, offset their expenses.

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This is just what is happening in the operation of the Postal Savings system. In many towns having good banks, deposits in postal savings almost equal the deposits in the banks and where this condition exists contraction of local credits and the resulting stagnation in business are apparent.

It was confidently hoped that when the insurance of deposits became a reality that the Congress would, at least, eliminate from the Postal Savings System all competitive features, if not repeal the act in its entirety. This hope was strengthened by statements made by our efficient Comptroller of the Currency, Hon. J. E. T. O'Connor, in an address delivered at the annual convention of the American Banker Association in Chicago in 1933 and on several occasions. In his Chicago address, Mr. O'Connor, in commenting upon the growth of the postal savings, said:

> When the insurance fund becomes operative most of this money will be returned to the banks and Congress will be justified in repealing the Postal Savings Act.

Contrary to Mr. O'Connor's prediction, postal savings deposits have increased rather than decreased; the total deposits at the close of 1934 being $1,207,200,000. While all but a negligible percentage of

this total is in postal savings offices in towns where one or more insured banks are located, it might be argued that the existence of the System is necessary to provide a safe depository for funds where no insured banks are located. Granting that in a few cases that is true, can it be argued that it is necessary to penalize the whole banking industry of the Nation to accommodate the convenience of just a few? To the argument that might be advanced by some that we have not gone far enough with our experiment with insurance of deposits to insure its permanency and warrant the repeal of the Postal Savings Act, we of the smaller banking cities who are suffering from what we honestly feel is an unjust and unwarranted Government competition, suggest that for the present instead of repealing the Postal Savings Act the law be so amended that the payment of interest on deposits be discontinued. In the alternative, if it is deemed the best policy to check and gradually eliminate the operation of the System, reduce the interest paid on postal savings deposits one-half and that to be paid on strictly time deposits. It is suggested that provision be made for reduction of interest from 2 percent to not over 1 percent on time deposits and prohibit the payment of certificates of deposit before maturity as the law now applies to time deposits in banks. The present rate of 2 percent was fixed when the act was passed in 1910 at a time when banks paid 4 percent and more on open deposits and although changed conditions have reduced interest rates until member banks of the Federal Reserve System are now prohibited by law from paying any interest on demand deposits, the interest on postal savings deposits has not been changed.

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As an excuse for continuing the Postal Savings System, the argument has been advanced that the System is used largely by our citizens of foreign extraction who could not be trained to use our banking system. A close observation and study of the operation of the System in Texas reveals that the postal savings is patronized less in centers thickly populated by citizens of foreign extraction than in places where the foreign population is negligible. The argument also is sometimes advanced that the total is made up of very small savings accounts, too small for the banks to handle and which remain on deposit from year to year. While the average deposit in postal savings per depositor is about $500, an investigation will reveal that a big percentage of the total amount is composed of deposits of from $1,000 to $2,500 per person; and as evidence of the activity of the accounts, it is noted that deposits during the fiscal year ending June 30, 1934, amounted to $966,000,000 and withdrawals amounted to $955,000,000. It has also been suggested by some who seem to favor the continuance of postal savings that postal savings depositors are only small depositors that commercial banks do not want and on which accounts the banks make a service charge. That argument is not correct as banks generally accept savings accounts no matter how small and charge only on the small active accounts that are expensive to handle.

In appealing to you gentlemen, who have given the matter of banking and its relation to the welfare of our people so much of your time and consideration, to give us relief from this unwarranted competition, I am sure that I express the sentiment of every banker in the country who has felt the damaging effects of its operation.

Mr. Klattner
Mr. Hersey

#15

THE COMMERCIAL & FINANCIAL CHRONICLE--ABA Convention--Nov. 1935

4B.1a

Address of the Pres., James C. Bolton, VP Rapides Bank & Trust Co., Alexandria, La.--(State Bank Div.)

Pocket

Report of Committee on Federal Legislation

Recommendation that Congress be urged to pass legislation at its next session for discontinuance of the Postal Savings System is contained in the report of the Committee on Federal Legislation. The report was signed by C. J. Kirschner, Vice-President Markle Banking & Trust Co., Hazelton, Pa., as Chairman. "I feel," says Mr. Kirschner in the report, "it should be suggested that something be done by Congress on account of the unfair competition occasioned by Postal Savings. Since we now have Deposit Insurance there seems to be absolutely no necessity for Postal Savings offices, except possibly in a few remote villages who are without banking facilities. If Congress does not agree to discontinue the Postal Savings System it should at least reduce the rate of interest to banks from 2½ to 1%."

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Mr. Blattner
Mr. Heisley

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SOURCE: THE COMMERCIAL & FINANCIAL CHRONICLE--ABA Convention
Nov. 17, 1934

"A Better Year for Savings" --by Henry S. Kingman, Pres., Svgs. Div.
Treas. Farmers & Mechanics Svgs. Bk., Minneapolis

P. 66

Postal Savings

Postal savings reached their high point in December 1933, with deposits of almost $1,209,000,000. Since that date a decline has occurred. As of June 30 1934 the figure stood at $1,197,900,000; and since then there has been a further reduction of approximately $4,000,000.

Although the bank crisis is definitely in the background, postal savings have showed little diminution. Their rapid rise began in the winter of 1931.

In October of that year they passed the $500,000,000 mark, and by February 1933, aggregated $1,000,000,000.

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Recently banks have found the handling of postal savings funds so unprofitable that they have turned them back to the Post Office Department. By the end of June 1934 almost $232,000,000 had been returned. A part of this huge sum has been placed in Government securities at an average rate of 2½%. On June 30 1934 the Treasury provided a special issue of $35,000,000 5-year 2% notes, and at the same time the Post Office Department invested postal savings amounting to $35,000,000 in Federal Farm Mortgage 3s to bring up the average.

Under the law the interest rate to depositary banks can not be reduced below 2¼%, with a rate of 2% paid by the Government to the depositor. The trustees of postal savings have the right to reduce to 2¼% the rate to depositary banks. However, they have never changed it from the higher figure, claiming that to do so would bring a loss to the system. Of the total of $1,197,900,000 on June 30 1934, there was redeposited in banks $694,575,000. This represented 58% of the total deposits of postal savings.

Originally postal savings was developed as an agency which would reach into territory untouched by banks and also supply a service to foreign nationals who in their own country were accustomed to postal savings banks. During the time of the severe bank crisis the proponents of postal savings urged the enlargement of the system so as to insure, as they said, adequate protection to the savings of the people.

Now under the Federal Deposit Insurance Corporation and several State insurance systems bank deposits up to $5,000 are insured. Immigration has been definitely checked. The avowed purpose of postal savings, to afford banking opportunities to people in districts without banks, has not been fulfilled. There exists then no real reason for the further continuance of postal savings. At present the rate charged depositary banks is too high. The interest charge against the Government for these funds is excessive in comparison with the rate paid by the Government on its other obligations.

More than a year ago the Savings Division proposed a resolution that the law be changed so as to establish a deposit limit in one account in postal savings of $1,000, and to fix the rate to be paid by postal savings depositary banks at a rate not exceeding 1½%, with the rate to the depositor to be fixed by the Board of Trustees of the Postal Savings System. Thus, a flexible rate would be established, with power in the hands of the Board of Trustees to fix a rate to the depositor, which would assure adequate profit to the System.

Mr. Blattner
Mr. Gersley

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COMMITTEE AND OFFICERS' REPORTS—SAVINGS DIVISION

(15)

A Year of Change—By Gilbert L. Daane, President Savings Division, and President Grand Rapids Savings Bank, Grand Rapids, Mich.

The savings business during the past year has been one of discouragement. Vicious political attacks, popular hysteria, widespread unemployment and depreciation of security prices have tended not only to cause new deposits to lag, but also to make deep inroads in previous deposits. People could scarcely be expected to think clearly or to act with moderation in a period of such widespread stress and uncertainty.

Savings money in the United States has been invested largely in securities based on real estate, public utilities, railroads and industries, and only a relatively small part in the securities of the Federal Government or its sub-divisions. In this respect our banking practice differs from that in Canada and Great Britain. There the chief dependence is placed upon the obligations of the National Government.

Industry in the United States is normally at such high tide that the investments held by savings banks afford a maximum of safety, liquidity and marketability. The last four years have been abnormal. Values have floated away over night. Banks have found themselves confronted with declining security prices on one hand and frantic demands from their depositors for cash on the other. Despite this, savings banks have notably withstood the pressure which so frequently brought ruin to many financial institutions. The crisis through which banks are passing, of course, reveals mistakes of the past. There is a real danger that in a precipitate revamping of banking practices elements of strength as well as of weakness may be discarded.

Too diverse demands have been made on savings banks: One, that they maintain excessive liquidity; the other that they extend credit to a greater degree than ever before. Banks cannot do both. When a savings bank proclaims a liquidity of 50% or 60% or 70% it emphasizes the lack of service to its community and becomes simply a warehouse for money. All over the country, events show, banks with time deposits were attempting to do a commercial business. Disastrous results can only follow a policy such as this. It would seem that contract time deposits with proper segregation of savings assets would help solve the problem.

The Savings Division, during these troubled days, has sought to give aid and comfort and to supply counsel to many banks. More than ever before it has been a department of personal service. In a time of such popular confusion it was no easy problem for bankers to follow a course alike satisfactory to banks and their depositors.

Because bankers could leave their posts only with difficulty during the past year, the Savings Divisio held but one Regional Savings Conference, that in New York on Jan. 26-27 1933. Since problems affecting banks were basic and arose out of the very fundamentals of American business, the addresses and discussions at the conference dealt with municipal and State finance, real estate mortgages; how cities once in financial distress were rehabilitated financially, and how States threatened with financial difficulty might recover without loss to the State's credit or undue burden on the citizens. The wisdom of this policy in formulating a program was confirmed by the attendance which was second only to the largest during the nine years the conferences have been held.

The Savings Division has received numerous complaints from individual bankers, clearing house associations and State bankers associations relative to the competition of postal savings with savings in banks. The condition is a most difficult one and the Division has handled it with vigor. Under the law a depositor in postal savings receives simple interest at the rate of 2%. The trustees of the Postal Savings System have the right to demand an interest rate from depositary banks of not more than 2½% and not less than 2¼%. Reduction of the rate from 2½% to 2¼% would cause a loss to the Post Office Department. The 2½% rate returns a considerable net profit to the Post Office Department. As you know, the Post Office Department has for years operated at a loss. The postal savings feature is nurtured very carefully because it is one of the few activities of the Post Office Department which returns a profit.

This situation, therefore, caused the Government to pay 2% on a sum of one billion dollars when it could have borrowed money in the open market at less than 1%. At the same time pressure was made on banks to have them take the money at 2½%. Many of them, on a patriotic impulse, paid 2½% for money which they did not need and could not use profitably.

It is high time that postal savings, which in the case of some States has drained one-tenth to one-half of the total time deposits, be restrained. Is it a wise policy for the Government, through one Department—the Post Office Department—to be draining money, the very life-blood of commerce, industry and trade, from the State; and through another Department, the Reconstruction Finance Corporation, to be syphoning it back again, with the expense of all the machinery involved in both operations?

Naturally the Post Office Department should suffer no loss through postal savings. Should not the law be revamped so that banks would pay a reasonable rate, probably 1%, for the postal savings deposits, and the Board of Trustees of the Postal Savings System have the right to fix the rate to be paid the depositor by the Government? But why should savings banks have to suffer at all from competition of their own Government?

Hope of better days lies ahead for bankers in the savings business. Savings are the great bulwark against the spectre of unemployment, old age and dependency. Pride, a sturdy virtue, sustains the practice of savings through banks. When again prosperity dwells among us savings undoubtedly will resume their high place.

As President of the Savings Division I express my heartiest appreciation to the officers of the American Bankers Association, the members of the Executive Committee of the Division, and to the officers and members of the other Divisions, Sections, Commissions and Committees.

Report of Committee on Nominations—Election of Officers.

The following report of the Committee on Nominations of Officers was presented by Raymond R. Frazier, Chairman, President of the Washington Mutual Savings Bank of Seattle, Wash.

President: Henry S. Kingman, Treasurer Farmers & Mechanics Savings Bank, Minneapolis, Minn.

Vice-President: Howard Moran, Vice-President American Security & Trust Co., Washington, D. C.

Members Executive Committee for Three-year Term: Philip A. Benson, President Dime Savings Bank of Brooklyn, N. Y.; William J. Lum, Secretary-Treasurer Dime Savings Bank, Wallingford, Conn.; Roy R. Marquardt, Assistant Vice-President First National Bank, Chicago, Ill.

Member of Executive Committee for One-year Term: Bradley Curry, Cashier American Trust & Savings Bank, Chattanooga, Tenn.

[The above were duly elected, after which the meeting adjourned.]

Mr. Platten
Mr. Hersey

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THE COMMERCIAL & FINANCIAL CHRONICLE--ABA Convention--Oct. 22, 1932

State Banks and Their Important Field of Service--by L. A. Andrew, VP.
First Bank & Trust. Co., Ottumwa, Iowa

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Those who insist upon a Government controlled unification of our banking systems should be practical and build such a system around the Postal Savings Bank. That is a Government bank for sure, running behind in earnings every year, all of which is made good by taxpayers, including our banks which have in it their meanest competition. Postal Savings Banks have accumulated nearly a billion dollars in deposits, all at the expense of our present banking systems and have been the direct cause of the scores of failures of National and State banks. However, it would make an ideal set up for an extension of the Government controlled unification of banking idea.

Mr. Klettner
Mr. Hersey

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THE COMMERCIAL & FINANCIAL CHRONICLE--ABA Convention--Nov. 1935

The Banker and the Federal Deposit Insurance Corporation--Some of Their Mutual Interests--by Leo T. Crowley, Chmn. FDIC

#4

Substitute Private for Government Credit

In your search for new sources of income I am impressed by the possibility of obtaining loans that are now going to different agencies of the Government. The President has stated that the Administration is desirous of having the Government withdraw from the field of private financing just as soon as private business is able to take its place. I feel that banks should make more courageous efforts to substitute private for Government credit. Just as the FDIC cannot take the place of good management, the Government will not be able to carry on indefinitely the functions of our banking system. The end of Government encroachment upon your business is, therefore, up to you.

P. 24

Restrict Postal Savings to Bankless Communities

I hope the day is not far distant when the system of Postal Savings will be confined to communities without banks. Now that deposit insurance is upon a permanent basis, it seems fitting that the Government should evidence its good faith in it by restricting the business of Postal Savings. If this be done, many banks will be able to increase their deposits, extend more loans, and, consequently, be in a position to make more money.

Mr. Blattner
Mr. Hersey

p. 16

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on, permit me to express my deep appreciation
iastic and wholehearted support which the bank-
tion have accorded my rather inexpert efforts
hat, in my opinion, are proper standards for
e lawyers, the doctors, and members of other
ave boasted of their codes of ethics, and their
justified, for a large part of the progress these
ave made in claiming and holding public esteem
ir adherence to a code of ethics.

s of yesterday has subsided; the picture pre-
to-day is one of hope and good faith. You have
A few, no doubt, will still imitate the ostrich
d in the sand, but the great majority of our financial leaders are looking toward clearing skies, with high resolve, with courage and with faith. Let us go forward together, rendering a service to a mighty people and deeply appreciative of their confidence. And may our actions vindicate their faith.

and never to make a prophecy. These facts, however, and my general knowledge of the banking situation impel me now to predict that the present six months' period will be the best the banks of the nation have enjoyed for more than four years.

Com. & Financial Chronicle - ABA Convention - X-11/35

#15

Defense of Government Intervention

By Marriner S. Eccles, Chairman of the Board of Governors of the Federal Reserve System

Mr. Chairman, Ladies and Gentlemen:

After the remarks of the Chairman, I assure you that it is rather embarrassing for me to appear before you. I feel he has given you reason to expect altogether too much.

I did not prepare a written address for this occasion, feeling that I should like to come before you in more or less of an informal way, as a banker talking to bankers, as a business man talking to business men. I should like to talk to you as I would talk to my closest friends and associates.

Most of my life has been spent in the field of banking and business and until I unexpectedly went to Washington, less than two years ago, I had never occupied a public position. I, therefore, can talk to you and approach the questions which I am sure we are all deeply interested in, only as a practical business man and banker.

I am reminded in meeting with you to-day of the contrast between the conditions under which we are now meeting and the conditions under which this same meeting was held three years ago.

Three years ago, after pursuing what were considered sound fiscal policies, after attempting through every effort to balance the budget, after maintaining the gold standard, after avoiding any increase in taxes, we found ourselves confronted with disaster. We found that the national income had diminished in less than three years from $81,000,000,000 to less than $40,000,000,000 and we found that tax collections also fell.

We found that we were confronted with an army of unemployed of more than 12 millions of people. We found the banking system in a state of collapse. We found deposits had declined by more than one-third as a result of credit contraction, bank failures and hoarding. We found that though every effort was made to balance the budget, some Government bonds had sold as low as 83 and other high-grade securities held by banks were selling at such a price that had they been sold on the existing market, there would have been few banks in the United States in which the capital was not either completely wiped out or seriously impaired; that under the auspices, gentlemen, of what is considered orthodox economics, under the conditions that were expected to produce confidence and induce private industry to undertake to put people to work and to result in increased borrowing from the banks and thus in restoration of the necessary volume of deposits, we found that the economic life of the country was in a complete collapse.

To-day, in a recent compilation I had made with reference to the value of stocks, I find that as compared with the low prices of 1932, there is an appreciation of more than $20,000,000,000 in the quoted value of stocks listed on the Exchange. That has not been brought about by an increase in credit extended by banks because neither brokers' loans nor bank loans on collateral have increased. It has been caused by the fact that those who had money were investing in securities because they were aware of the increase in the earnings and the prospective earnings of the corporations whose securities are listed.

Contrast that picture with the condition of the corporations in 1932, when the income tax reports made by all corporations to the Treasury of the United States showed a net loss before dividends and before income taxes of more than $3,750,000,000. The quoted value of bonds listed on the Exchange, of which there were some in your portfolios that meant bankruptcy and insolvency to you, has increased by more than $7,000,000,000 since early 1933. The bankruptcies, which had reached the astounding proportions at that time of more than 25,000 for the first nine months of 1932, with total liabilities aggregating more than $750,000,000, to-day are less than 9,000 for the first nine months of this year, with liabilities around $170,000,000.

Bank failures for the first nine months in 1932 exceeded 1,000 and the deposit liabilities for banks failing were nearly $600,000,000. For the first nine months of this year, bank failures numbered 80, with deposit liabilities of approximately $36,000,000. These figures include the banks which were not licensed after the bank holiday and which were forced to liquidate later because it was not possible to reorganize and open them; they comprise most of the amount.

Bank deposits, due to credit contraction made on the part of the bankers (and I do not blame any banker; I was as busy in the field of private banking as any one could be in an effort to remain liquid, to be able to meet the demands of the depositors due to lack of confidence in the banking structure) have increased from a low point of $12,000,000,000 to $17,500,000,000, or above the level of 1929. When I say bank deposits I mean the adjusted demand deposits of member banks, which exclude inter-bank deposits and Government deposits.

The National income which had fallen to a little less than $40,000,000,000 for the year 1932 rose to nearly $50,000,000,000 for 1934. The figures are not available for the current year, but I believe that at the present rate of business activity the National income in the next 12 months will come close to $60,000,000,000, or about half-way back to the National income of 1929.

The Government receipts, which had fallen from better than $4,000,000,000 in 1929 to around $2,000,000,000 in 1932—as estimated in the last announced estimates of Federal revenue, will reach for the fiscal year ending June 30 1936, a figure of $4,470,000,000, or an increase of approximately $2,400,000,000.

GENERAL

Greater latitude has been provided as to time of repayment and the character of assets on which loans may be obtained from Federal Reserve banks. This should prove to be a bulwark in times of stress.

Much has been accomplished in the light of past experiences, and, with intelligent leadership in the banking world and among our public, the causes which brought about the total collapse of the banking structure should never recur. It is a sad commentary on American leadership that 12,677 banks with $7,510,640,000 in deposits have closed during the past 12 years. Some of these failures have been due to poor management and bad investments, but in addition, this nation has been overbanked. A mad scramble to establish a bank opposite every gasoline station across this continent is not a situation which can be contemplated with any degree of satisfaction. For the first time in the history of banking in this country, Congress has provided a means to correct this condition by giving to the FDIC the power to refuse to insure a State bank until certain conditions have been complied with, and particularly until a necessity for the State institution has been shown.

From Oct. 31 1932 to Oct. 31 1935 only 66 primary National banks have been chartered by the Comptroller's office; 29 for the year ending Oct. 31 1933; 26 for the year ending Oct. 31 1934, and 11 for the year ending Oct. 31 1935. This is the smallest number of National banks chartered in any three-year period during the past 30 years. Prior to that time the office records were not segregated as to primary organizations as distinct from conversions or reorganizations.

We shall now consider the present condition of our National banks. Let us compare the call report for National banks for June 30 1934 with that for June 30 1935. Loans and investments in 1935 were $18,085,103,000, an increase of $1,038,807,000 over 1934; total assets were $26,061,065,000, an increase of $2,159,473,000; total deposits were $22,518,-246,000, an increase of $2,585,586,000. If we include all banks, National, State and private, comparing the same two periods, we find an equally favorable picture. Loans and investments on June 30 1935 were $44,632,288,000, an increase of $1,911,641,000 over 1934; total assets were $60,393,057,000, an increase of $4,233,132,000; total deposits were $51,586,-123,000, an increase of $4,961,082,000.

On Dec. 31 1928 National banks reported the largest amount of deposits and assets ever reported in the National Banking System. Let me give you these figures as of Dec. 31 for 1928 and the succeeding years: On Dec. 31 1928, total assets amounted to $30,589,156,000; for the same day in 1929 they were $28,882,483,000; in 1930, $28,799,684,000; in 1931, $24,662,286,000; in 1932, $23,310,974,000; in 1933, $21,747,483,000; in 1934, $25,629,580,000, and on June 30 1935 they were $26,061,065,000. Total deposits on Dec. 31 1928 amounted to $24,347,380,000; for the same day in 1929 they were $22,773,493,000; in 1930, $22,871,646,000; in 1931, $19,244,347,000; in 1932, $18,518,107,000; in 1933, $17,589,-882,000; in 1934, $21,676,303,000, and on June 30 1935 they were $22,518,246,000.

It will be noted that total assets and total deposits continued to decrease from Dec. 31 1928 to Dec. 31 1933. They showed a marked increase on Dec. 31 1934, and again on June 30 1935. On the latter date the total assets were 85.20% of the total assets on Dec. 31 1928, and the total deposits on June 30 1935 were 92.49% of the Dec. 31 1928 figure, which was the largest in the history of the System. It should not be overlooked that on June 30 1935 there were 2,204 less National banks than on Dec. 31 1928.

Probably a more significant figure is that for bills payable and rediscounts. On Dec. 31 1928, National banks had borrowed and were indebted in the sum of $785,309,000, and on June 30 1935 the National banks owed $4,643,000, or less than 1% of the figure for Dec. 31 1928.

During the past year there probably has been more discussion of the earnings of banks than of any other subject connected with banking. For the year ending June 30 1932 the National banks had a deficit of $139,780,000, or 8.91% based on capital; for the year ending June 30 1933, a deficit

places the whole future of those dependent upon him, and, in many cases, of children unborn. Proper emphasis has not been placed upon this most important function of our banking system. When one contemplates the number of trusts, the amounts involved, and the increase in this particular branch of business, one cannot but feel that a high compliment is implied to the integrity of those entrusted with what might be called merely sacred powers.

There are 1,578 National banks with active trust departments. They are administering 129,711 individual trusts, with assets aggregating $9,251,291,947, and in addition are administering 16,801 corporate trusts and are acting as trustees for outstanding note and bond issues amounting to $11,-605,145,026. Compared with the year 1934, these figures represent a net increase of 8,577, or 6.2% in the number of trusts being administered; an increase of $734,740,203, or 8.6%, in the volume of individual trust assets under administration, and an increase of $120,683,289, or 1.05%, in the volume of note and bond issues outstanding for which National banks have been named as trustees.

An analysis of the $8,341,958,034 of invested trust funds belonging to the private and court trusts under administration revealed that 48.74% was in bonds, 29.28% in stocks; 7.96% in real estate mortgages; 7.16% in real estate, and 6.86% consisted of miscellaneous assets. The investment of

The foreign trade figures are approximately 40% in excess of the foreign trade figures in 1932.

Industrial production reflected in the Federal Reserve's seasonally adjusted index is now at 89% of the 1923-1925 average, raising it from a low point of 58 in 1932, a gain of more than 50%.

The wholesale price index of commodities, using 1926 as a basis of 100, had fallen to a low of 60 in February of 1933. It had risen to 81 in September of this year.

In the field of farm products wholesale prices had dropped as low as 41% in February 1933. The were up to 80% last September. The farm income, which dropped from $10,-500,000,000 in 1929 to something over $4,000,000,000 in 1932 is estimated for this year to be back to nearly $7,000,-000,000, a gain in that field of $2,500,000,000.

I could go on and cite many other factors, such as increased building activity, revival in the capital market, increase in employment and payrolls, but enough has been given to mark the impressive improvement between the condition of three years ago and the present time in every field, financial, commercial, industrial, agricultural, and fiscal.

What is the reason for this change? It is not a result of accident; it is not a result of letting nature take its course. For three years nature was permitted to take its course in an effort to revive confidence. Little legislation that was disturbing to business was passed. No Banking Act of 1935 was pending to make bankers hesitate to make loans.

But a condition was reached, even as early as the spring of 1932, when Government intervention became unavoidable; because the Government wanted to intervene, but because the entire financial and credit structure was in a state of disastrous contraction. The Reconstruction Finance Corporation was organized to support the crumbling structure.

The Government had financed the grain and cotton stabilization corporations in order to help agriculture.

The Home Loan bank system was organized in order to help the urban mortgage situation. But the scale of intervention was entirely inadequate and the forces of deflation had been so much underestimated that a complete collapse resulted in the following spring.

No one objected to an unbalanced budget in order to bolster up the banking, the insurance, the railroads, and the credit structure generally. Is it consistent or possible to think that Government could intervene in the field of private credit through the banking, insurance, and other private structures and at the same time refuse to intervene in order to stop the foreclosure of farm mortgages, which reached an appalling figure, to stop the foreclosure of home mortgages, which reached a figure as high as 35,000 in one month?

Is it possible to justify the use of Federal credit resulting in an unbalanced budget in the fields referred to, and at the same time permit 12,000,000 men who wanted work to go unemployed?

Business claims the liberty of employing and discharging men when their services cannot be used profitably, and that is its right. But what about the liberty of the men under the conditions that we were confronted with in 1932 and 1933? If a Government is justified in incurring an indebtedness of $25,000,000,000 to protect its citizens against the encroachment of a foreign enemy in times of war, is not a Government justified in using its credit for the purpose of taking care of those people who found themselves in a position of destitution because of the failure of private industry to give them employment?

The RFC put a foundation under the banking structure. The Emergency Banking Act passed at the time of the bank holiday permitted the Reserve System to loan not only to National and member banks but to State non-member banks against any sound asset. When that was announced by the President of the United States over the radio, the people of the country who had withdrawn their deposits in the form of currency and who had attempted to transfer it out of the country stopped that practice, which was totally destructive to the entire credit and banking fabric.

When the people were told that the Reserve System could issue Federal Reserve bank notes against mortgages, against collateral loans and against other good assets held by the banks, without regard to gold backing, without regard to eligible paper backing, without regard to Government bond backing, they brought back into the banks during the next year $2,000,000,000 of currency which they had taken out.

The RFC has rehabilitated the capital structure of banks to the extent of approximately $1,000,000,000 and it has loaned over $800,000,000 to the receivers of closed banks so as to prevent the forced liquidation of assets and to give to depositors immediately available funds, so as to relieve them and to enable them to put that money into circulation.

The Home Owners' Loan Corporation was established for the purpose of relieving home owners in distress and up to the present time has loaned approximately $3,000,000,000. The work of that institution is nearly completed. The distressed mortgage is a thing of the past. Real estate values have been stabilized and are advancing. Rents have been on an increase for two years and doubling up is lessening. New home construction is increasing and the HOLC will be through with the work it has done, with more than a billion dollars of unused authorization to its credit.

It not only served as a debtor relief but also served equally as a creditor relief. The mortgages held by the savings banks, the insurance companies and the commercial banks, which they were unable and unwilling to carry, were taken over and funded over a longer period at reduced rates by the HOLC.

The Federal Farm Mortgage Corporation was organized and $2,000,000,000 of bonds were provided fully guaranteed by the Government, these funds to be loaned to Federal Land banks in exchange for the bonds of these banks, backed in turn by mortgages and to be issued as proceeds of mortgage loans by the Land Bank Commissioner.

The Federal Land banks are institutions going back about 20 years. In 1932 they were unable to sell their bonds on the market. These same bonds are now selling at a premium and a substantial amount of them have been refunded into issues bearing lower interest rates. When it was impossible to sell them, the Government agency set up for the purpose took those bonds and issued bonds guaranteed by the Government. That has stopped the collapse of the farm mortgage market, until to-day I hear that there are more farms being sold than are being foreclosed upon.

These three great creditor agencies have largely done their work. No one is more anxious than the Federal Government to have the private credit agencies take over the load.

The Federal Housing Administration Act was passed for the purpose of attempting to induce the private credit agencies of this country to make loans for construction purposes on insured mortgages and for modernization. Not one dollar of Government funds goes into those loans. The Federal Government was attempting to create a mechanism by which to attract private funds into the field of credit, and get the Government out.

The RFC is collecting far more than it is lending. It has loaned about $5,000,000,00 and has collected more than one-half of the total amount of the loans.

In the field of relief, which we so often refer to as "waste," we have the thousands of miles of public roads, we have the excellent work done in our CCC camps, we have repaired and rebuilt schools, water systems and sewer systems. Truly not all self-liquidating projects. It is possible for the Government to spend money for social purposes, and it should not always judge or gauge its expenditure by whether or not it is a self-liquidating project. The problem of private profit and self-liquidation belongs to the field of private business and not to the Federal Government.

Now let us see if the results as enumerated are worth the cost of intervention, which resulted in an unbalanced budget. I would like to remind you that we had an unbalanced budget as early as the fiscal year ending in 1931 and that the deficit for the fiscal year ending June 30 1933, exceeded $3,000,000,000, that the Government s interest-bearing debt increased from $20,584,000,000 in February 1933, to $28,-432,000,000 in September of 1935, an increase of $7,848,-000,000.

Deduct the assets, including cash on hand, the gold profit in the Stabilization Fund, the Government s proprietary interest in organizations such as the RFC, and you have a net increase in the Government debt of about $3,000,000,000. But let us take the larger figure for the purpose of comparison. Let us take the amount of the gross deficit.

Should we be alarmed over that situation? Should some of the increases which I have referred to—such as the $20,000,000,000 increase in the quoted value of listed stocks without taking into account an increase of from $15,000,000,000 to $20,000,000,000 in the National income in one year—give us any cause for concern about even the amount of the gross deficit? Does it mean that we are putting a a great burden upon posterity?

If you will recall, during the 10 years from 1920 to 1930, while the Government debt, which had been $26,000,000,000 incurred almost entirely in a period of two short years, was decreased by about $10,000,000,000, this country at the same time added $100,000,000,000 or more to its new wealth in the form of increased productive facilities and we purchased $10,000,000,000 of foreign security issues and reduced the Federal income taxes during that period four different times. If we could do it then, why think that we cannot do it again?

I should like to commend to your attention Lord Macaulay's "History of England," in which he recounts how the British debt from the period of the contest with Louis XIV rose from £50,000,000 to more than £800,000,000 and how "at every stage in the growth of that debt it has been seriously asserted by wise men that bankruptcy and ruin were at hand. Yet still the debt went on growing; and still bankruptcy and ruin were as remote as ever."

I cannot read all of the statement, but I am going to quote a few high lights from it.

After telling of the repeated outcries against the debt, he told how it kept mounting, yet how England prospered despite the prophets of disaster, and he continues:

"The beggared, the bankrupt society not only proved able to meet all its obligations, but while meeting those obligations, grew richer and richer so fast that the growth could almost be discerned by the eye. . . ."

"While shallow politicians were repeating that the energies of the people were borne down by the weight of the public burdens, the first journey was performed by steam on a railway. Soon the island was intersected by railways. A sum exceeding the whole amount of the National debt at the end of the American wars was, in a few years, voluntarily expended by this ruined people in viaducts, tunnels, embankments, bridges, stations, engines. Meanwhile taxation was almost constantly becoming lighter and lighter; yet still the Exchequer was full. It may now be affirmed without fear of contradiction that we find it as easy to pay the interest of 800 millions as our ancestors found it, a century ago, to pay the interest of 80 millions.

"It can hardly be doubted that there must have been some great fallacy in the notions of those who uttered and of those who believed that long succession of confident predictions, so signally falsified by a long succession of indisputable facts. To point out the fallacy is the office rather of the political economist than of the historian. Here it is sufficient to say that the prophets of evil were under a double delusion. They erroneously imagined that there was an exact analogy between the case of an individual who is in debt to another individual and the case of a society which is in debt to a part of itself (which pays interest to itself); and this analogy led them into endless mistakes about the effect of the system of (Government borrowing and) funding.

"They were under an error not less serious touching on the resources of the country. They made no allowance for the effect produced by the incessant progress of every experimental science, and by the incessant efforts of every man to get on in life. They saw that the debt grew; and they forgot that other things grew as well as the debt (that taxes are high or low in relation to National income)."

At the bottom of the depression we would have been worse off with no taxes at all than we are to-day with the taxes that we have.

"A long experience justifies us in believing that England may, in the 20th century, be better able to bear a debt of16 hundred millions than she is at the present time to bear her present load. Be this as it may, those who so condifently predicted that she must sink, first under a debt of 50 millions, then under a debt of 80 millions, then under a debt of 140 millions, then under a debt of 240 millions and lastly under a debt of 800 millions were beyond all doubt under a two-fold mistake. They greatly overrated the pressure of the burden; they greatly underrated the strength by which the burden was to be borne."

That was a century ago when the debt reached £800,000,000. To-day that debt is nearly 10 times that figure, and the standards of the people of England, not only the working man, but the business man, are higher than they were then. They are far better off as a society after carrying the debt than they were at that time.

Have we not yet learned that what we cannot afford is not the burden of carrying the National debt, but is an army of idle men and unutilized facilities? For the cost of what we lost in the last few years as a result of permitting deflation to run far on its course before checking the devastation—the loss in National wealth and the National income from idleness of millions of men and innumerable productive facilities would run into more than $150,000,000,000. The entire amount of our present National debt is less than four months of the normal National income.

It seems to me that it may be interesting to compare the picture of England with that of the United States so far as debt is concerned. The debt of the United Kingdom (and that does not mean only the central Government, it means all public bodies) was 194% of the National income in 1934. In the United States, the debt of all public bodies was 74% of the National income. The total interest paid by all public bodies on their debt in England amounts to 8% of the National income; in the United States, a little over 3% of the National income.

I do not want to give you men the impression that a budgetary deficit is desirable. I only want to point out to you that it is not the serious thing it has been magnified to be. The serious thing is the loss of $40,000,000,000 in our annual National income, which the capitalistic system, when left to itself without adequate Government intervention, brought about by the year 1932.

We shall not continue to have a budgetary deficit when the conditions that caused the deficit, the reduction in National income, are corrected. As National income increases, Federal income increases, and as Federal income increases the need for Government spending decreases, because of an increase in activity, employment, prices, &c.

And that is the trend to-day. From more than $4,000,000,000 in 1929 the Federal income dropped down at the bottom of the depression to $2,000,000,000, and is now back at more than $4,000,000,000.

The deficit which reached a peak in the fiscal year ending June 1934 was approximately $4,000,000,000, and it is estimated that in 1936 it will be $3,280,000,000.

I should like to sum up what I think all this means to bankers. I feel that you have every reason in the world to have confidence that the system of private industry and the system of private banking has a future if you will but profit by the lessons of the past, if you will but do your part and step out into the field and extend not the type of credit that you may prefer to extend, 90 days or 6 months credit, but the kind of credit that there is a demand for in your communities. You don't hesitate to buy in the market finance company paper and intermediate credit bank paper at as low as 1%. Why don't you short-circuit the funds and lend directly to those in the community that are going outside and paying from 5 to 12% for credit from the very institutions which you are financing at 1%?

Why don't you, when you are the custodians of $10,000,000,000 of the savings funds of the people, invest those funds in the field where such funds should be invested? They are the same type of funds as the funds that the insurance companies, the mutual savings banks, and the savings and loan associations are investing, and if you are going to hold those funds and pay interest on them, you must put those funds in the long-term mortgage market, in the long-term bond market, and you can do it with every security.

You are loaning on a basis of values that is not inflated, and if you want the Government and the Government agencies to get out, then it is up to you to get in. If you prefer to buy Government bonds and bonds guaranteed by the Government, to act as your cushion, then you cannot complain about the Federal Government being a competitor with you in the field.

If the Government had chosen or desired to destroy private banking, it needed to do nothing at all. In 1932, private banking had completely destroyed itself. But the Federal Government believed in private banking, and in private initiative, and in private business, and for that reason it

saved the banking system for the bankers to do a better job in the future than many had done in the past.

It seems to me, in summing up the review I have made, that an analysis of the nature, the cost and the timing of Government intervention, and of the recovery factors brings out conclusions which are inescapable. First, in order to keep our productive processes going and expanding, we must maintain a reasonable balance between our productive facilities and consumer buying power. Failing this, money becomes idle because it cannot find profitable outlet for investment, unemployment develops because buying power is insufficient to absorb the output of industry.

This results in the commencement of a period of deflation. It causes a contraction of debt, a reduction in spending, and, if the cycle is allowed to continue, this inevitably results, because the cycle is self-accelerating, in general prostration and bankruptcy. It is as necessary to intervene to correct a situation of this sort as it is to prevent a cycle of inflation.

There will be one thousand bankers saying that inflation should be avoided and that public authorities, public officials in the Reserve System and in Government should stop inflation, whereas there is possibly a handful who feel, or at least have felt, that deflation should not be allowed to go its normal and natural course; that the natural law should be interfered with. I cannot reconcile these two positions. I see no greater evils in inflation than in deflation. In fact, I think of the two, deflation is far more destructive to bankers.

It is necessary to intervene to correct a situation of this sort, just as necessary as it is to prevent a cycle of inflation. Only Government, which is all of us, is capable of acting collectively to offset and neutralize the effect of the downswing and by its spending and the use of its credit effect the necessary distribution that private capital, left to the individual, has failed to effect. Action taken promptly by Government to stop the process of deflation in its inception will tend to keep up the National income and correct maldistribution and inequitable distribution, and at an infinitesimal cost compared with the cost to society as a whole if deflation is allowed to run its natural and destructive course. For Government to decrease its spending at the outset of a deflationary period, when every one else is doing likewise, only accelerates the forces of deflation and does not create confidence. In such a situation capital does not flow into productive facilities because they are already excessive in relation to consumer buying power.

How can we say that individuals, corporations and banks, with funds to invest, will be inclined to use those funds to put people to work, when funds already invested are becoming less profitable daily, as buying power decreases and unemployment squads? Confidence in the business world is the outgrowth of an opportunity to invest funds profitably. Funds are invested profitably only when there is sufficient buying power to purchase the output of increasing productive facilities.

I have attempted to portray the effects and the evils of deflation. We hear much about the evils of inflation. How is it possible to have inflation when men are idle and plants are idle? There can be speculative excesses when surplus funds bid up stocks or real estate, but general inflation can only come about by increasing the means of payment in the hands of the people who are willing to spend faster than we can increase production. We are a long way from such a period of inflation. The idle balances of corporations and of individuals, even in 1929 with business going at a maximum, were very largely responsible for the stock market inflation.

It must be evident from what I have said that we are in no immediate danger of inflation as a result of a budgetary deficit or as long as we have the facilities to produce and the men willing to work. We have seen from the experience of the past three years that it is possible, through adequate Government intervention, to turn the tide of deflation to what has been termed "reflation." Is it not reasonable to conclude that had intervention come sooner and on a more adequate scale, it would have taken far less spending and lending by the Federal Government to arrest and reverse the process of deflation?

The bankers above all have been the beneficiaries of the Government's intervention. The Government alone could and did replenish the supply of deposits when individual borrowers were lacking and when banks had no other profitable outlet for their funds than the investment in Government securities. Banks bought Government securities, not because of compulsion, but because they had no other avenue of profitable investment.

The Federal Reserve System has purchased no Government bonds, has given no support to the Government bond market for two years, and the present amount of outstanding credit by the Federal Reserve System is less than it was in the spring of 1933. The excess reserves of the banks, which make money cheap, which induce them to purchase securities and make loans at present low interest levels, are a result very largely of gold imports. Banks bought Government bonds, not because of compulsion, but because they had no other avenue for profitable investment. Government bonds, far from being a burden, have been a Godsend.

Those who talk about boycotting Government bonds suggest to me a drowning man to whom a life line is thrown out but who objects that it is an interference with his individual right and liberty to drown. Speaking as a banker, business man and capitalist, I urge you as bankers to contrast the conditions and the prospects under which you meet to-day with the conditions and the outlook of three years ago and to ask yourselves how the transition has been brought about.

I am not prepared to admit that we must always have with us a vast army of unemployed. I am not ready to confess failure in making our individualistic capitalistic society function so as to utilize to the fullest the Nation's resources of which, by far, the most important is human labor. I do not believe that we are so wanting in intelligence and courage, or that we are so blind to the lessons of experience as to conclude that we are incapable of managing our affairs more prudently and more efficiently in the future than we have in the past.

I do not see how any thoughtful man can challenge the conclusion that in order to preserve our capitalistic system, our institutions and traditions, we must use such governmental means of economic and monetary management as we now possess in achieving a greater stability in the economic order and in creating conditions under which our man power and productive capacity may be utilized to a maximum in the production and the distribution of wealth.

The Federal Reserve System, with its authority over margin requirements and—under the Banking Act of 1935—its clarified responsibility for reserve requirements, discount rates and open-market operations, is in a better position than ever before to exert its influence toward the attainment of a greater degree of stability and the avoidance of inflationary and deflationary extremes.

These powers, if exercised harmoniously, in conjunction with those possessed by the Federal Government through the Treasury—and to attempt to exercise the divided powers separately or conflictingly would be fatal—can, I am confident, contribute much to the achievement of a stable, orderly economic progress, free from violent extremes, and conducive to a maximum productivity and distribution. This involves neither a regimented nor a restricted economic order. It calls for Government intervention only to the extent that the exercise of governmental authority affecting monetary and budgetary factors may be a stabilizing and corrective influence in an individualistic, capitalistic system when it, left entirely to itself, generates distortions, lack of balance and cyclic extremes.

The Government must be the compensatory agency in this economy; it must unbalance its budget during deflation and create surpluses in periods of great business activity. In the light of experience and in the interest of the public in

general and of private banking in particular, it seems to me to be conclusively demonstrated that business and banking leadership should lend its full sympathy and support to the kind and extent of Government intervention that I have outlined. Only then, it seems to me, can private banking be assured of safe and profitable operation in the future and be freed from the uncertainties due to recurrent evils of booms and depressions.

Railroads

By JESSE H. JONES, Chairman of the Reconstruction Finance Corporation.

Mr. President and Members of the American Bankers Association: It is a pleasure to meet with you again. But you are entitled to new faces at your annual meetings, so I promise not to accept an invitation to address you next year should I be so fortunate as to receive one. My subject this year is "Railroads," but I shall make no effort to stay on the track. Time was during the last few decades when it was popular with the public and in legislative halls, to cuss the railroads and charge them with everything vicious. Some of this was justified, and while there will always be abuses and incompetency in the affairs of railroads, just as in every other form of human activities, the attitude of the American people toward the railroads is changing.

This changed attitude is characteristic of our people. They are always sympathetic toward the fellow in difficulty. Furthermore, we are beginning to realize that the railroads belong to the public—the policyholders in insurance companies, depositors in savings banks, &c.

I hold no particular brief for the railroads, but they are entitled to fair deal from the public, as well as at the hands of our legislators; also from their competitors in other forms of transportation. This latter can be had through regulation and supervision of their competitors, similar to that under which they operate.

The Old Man of the Sea—their bankers—should be removed from their backs, or subjected to stricter regulations as to their rates and charges. Entirely too many railroads are dominated by bankers who sit on their boards, or dominate them in other wasy, and who make money out of their financing. Indirectly they charge the roads entirely too much for their services as directors by continually striving to offer the investor an attractive rate of interest, promoting their own business. Under these circumstances it is difficult if not impossible for them to properly represent the borrowing roads. In other words, their take-off is sometimes too heavy—if you get my meaning.

I see no particular objection to a banker sitting on the board of a railroad, provided he has no interest, direct or indirect, in the road's financing—no friends to favor—no "scratch my back and I'll scratch yours." All of this is within the law, and railroad banking as carried on, is perhaps legal, but public sentiment is against a continuation of it in the old way, just as it is against special privileges and rebates in any form.

I am as anxious as any of you can possibly be, that the Government get out of the money lending business as soon as possible. But it should not get out too soon. I am inclined to the opinion that the Government can very properly assist in railroad financing, getting their capital requirements at fair but comparatively low interest rates, and at much less financing costs.

I would not favor lending unlimited Government credit to the roads, nor losing in the lending, but they are so much a part of us as a country, so essential to the national welfare, that the Government can afford to help in this respect. Their operating costs are continually on the increase, and sometimes by legislative action. The Government regulates their rates, and should suprevise and scrutinize their management and expenditires more and more. It is but fair, therefore, that we help them with their financing.

While abuses are much less now than in years past, they should be eliminated as far as is possible to eliminate them.

Though privately owned, railroads are a public utility. They should be operated first to provide good, safe and adequate service. Next, they should be operated in the interest of the investors in their securities, and without manipulation or fancy bookkeeping, to serve a particular purpose or favor a particular interest. The perpetuation of poor management through small cliques who may be in control of a property should be made mpossible. Railroads were built largely by promoters through Government subsidies in one form or another, Federal, State and local. Millions of acres of land were given them and much money in bonuses and loans. And while promoters are essential in new developments, some of them have been none to scrupulous nor too wise, and investors that follow in many instances have paid the price.

It is recognized that railroads are the most essential factor in transportation, but it is nevertheless a fact that on the whole railroads must be overhauled to meet present day conditions, and the demands of an ever-exacting public. In the overhauling the investor will take a loss, just as investors in other methods of transportation have taken losses, as railroads, highways and air service have supplanted older methods. The time has come when transportation should be treated as a unit, including in that unit railroads, waterways, highways and airways. As the newer and more modern are developed, the older must give way.

One of our troubles is we have not made proper provision for amortizing the investment in our railroads. When they were earning well, we were entirely too willing to believe that these earnings would go on forever, and proceeded to so value them and to deal in their securities accordingly. Good accounting prompts liberal depreciation charges against all plant investments. Railroads should be no exception. As a matter of fact, many of our better roads have already paid for themselves in earnings that have been distributed to the securityholders, and if the ownership had been a continuing one, there would be no loss to the investor. Upon the whole, railroad management has done unusually well in reducing operating costs as their gross has fallen off. It is surprising that more of them have not come to grief during these lean years, when, upon the average, their gross has been cut almost in half.

If we admit that in the development of our country most of the railroads that were built were useful, we must now admit that with the advent of highway and air transportation, the constantly increasing use of the Panama Canal and inland waterways, and with injustices in certain water rates, we cannot support all railroad mileage. There should be consolidations and eliminations of unprofitable mileage. Many duplications of service and competing schedules could be eliminated. There is nothing new in consolidations, nor objectionable if not carried too far. Every principal railroad system in the country is the result of consolidating many small lines, independently built and independently owned, into one great system.

We could not have had a highly developed and an efficient railroad service without these consolidations, and the problem now is to effect enough more consolidations to eliminate destructive competition and to raise our whole rail system to higher standards; with the single purpose of having the best possible rail service at the least possible cost. There could be a substantial reduction in railroad mileage without seriously affecting the service or reducing employment. Better tracks, new and better equipment, maintenance, and better service, would require all, if not more, labor than is now being employed by the railroads, both directly and indirectly.

There will always be objection to any proposed reduction in railroad mileage. No community is willing to give up a mile of railroad, a railroad office or a railroad employee. And again, the railroads are heavy taxpayers, and local taxing authorities are loath to give up this source of revenue. But sound reasoning cannot defend the continued operation of railroad mileage that does not directly or indirectly pay its cost.

We are entitled to all forms of transportation—the more modern, the more pleasing, and the more convenient the better—but in getting it, we should be as reasonable as we are in trading in the old car for a new one. Railroads without sufficient patronage, depreciate, become obsolete and dangerous. But farms wear out, too, homes and business buildings deteriorate and become obsolete; banks, business, and industry have their ups and downs (and during recent years they have been mostly downs). So the railroad investor, however innocent, must expect to take his loss just as investors in every other form of property have taken theirs.

I do not want to be too pessimistic about the future of our railroads, for it would not take a very great increase in revenues to put most of them in the black again. But much new capital will be required to put them in condition to handle the increase. How to get this increased capital is a problem, in all probability a Government one. Therefore, the outlook for the investor in railroad securities is none too promising. We have in the course of reorganization several very prominent railroads, and others will follow, so we might as well look the situation squarely in the face and be sensible about it. I have thought, and still think, that generally speaking the first mortgage holder, regardless of the terms of his mortgage, should not be permitted to all all of the earnings, leaving nothing for junior security holders. Interest rates are substantially lower and the first mortgage holder should be willing to accept some reduction, while the junior positions suffer much more. I might add that I feel this same way about first mortgage holders of other properties as well as railroads not now in bankruptcy, but that inevitably will be, if the first mortgage holder takes everything and becomes the overlord.

I am aware of the sanctity of contract—and that the first mortgage holder took a smaller yield in order not to speculate. But as a matter of fact mortgage securities, railroad and otherwise, have been sold with representations as to safety by the issuing houses, and most junior bondholders were told that their bonds were good or they would not have bought them. I do not believe in moratoriums by statute, but I do believe in fairness between security holders, and that first mortgage holders should not by an attitude of greed and oppression arouse such resentment as results in legislation, or attempted legislation, to protect equity holders.

I looked after a small herd of cattle on a ranch one long hot summer in Texas, when a boy of 12, and the water in the creek got very low. When it did, the big steers and cows would crowd the little fellows out, and I was continually fighting the big ones, trying to give the little fellow a chance. Some first mortgage holders have reminded me of that experience.

Of one thing I am convinced, railroads are a common problem to us all and will require the attention of our leaders both in and out of Congress if we are to avoid Government ownership. And let me warn you now that we may find many railroad security holders that ordinarily would oppose Government ownership in principle, favoring Government ownership of the roads in the hope of unloading their investment on the Government. In leaving the subject of railroads I should like to say, with emphasis, that re newed ability on the part of railroads to earn and spend for supplies, maintenance, betterments, equipment, &c., would have a far-reaching effect in improving business in all lines.

Banking Act of 1935

Before giving you a short report on RFC activities, I shall refer briefly to the Bank Act of 1935. Others will probably discuss it in detail, but it seems to me that we got an excellent bill. Much of the new bill has been before Congress for several years. The Senate passed a large part of Title II in 1932, but it did not pass in the House. The new Act was considered with great deliberation in committee—longer in the Senate because Senator Glass, as Chairman of the Senate Banking and Currency Subcommittee, is our best authority on Federal Reserve and bank legislation. He feels very keenly his responsibility regarding bank and Federal Reserve legislation, having served for many years on the Banking and Currency committees in both houses of Congress, and as Chairman of each, as well as having been Secretary of the Treasury, and is ever ready to resist proposals that in his opinion will weaken our financial structure or banking laws.

Certain features of the bill as introduced, in the Senator's opinion, had that effect, particularly the provision that the Federal Reserve Board be given absolute authority in the open market operations (the purchase and sale of Government securities). The Senator and his committee resisted this, insisting that the Federal Reserve banks be given representations on the Open Market Committee. When this was agreed to, most other differences were soon ironed out. Though the bill was so changed as to require practically re-writing it, all of which took a great deal of time.

We all owe a debt of gratitude to Senator Glass and the members of his subcommittee, and for that matter, to the entire Senate Banking and Currency Committee; also to Henry Steagall and his committee in the House, for the bill we got. Everyone except those banks that wanted the under-

Mr. Blattner
Mr. Dersey

NATIONAL BANK DIVISION

AMERICAN BANKERS ASSOCIATION

Thirteeth Annual Meeting, Held at New Orleans, La., Nov. 12 1935

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Government Lending Agencies and Their Relationship to Commercial Banks

By WOOD NETHERLAND, Vice-President Mercantile-Commerce Bank & Trust Co., St. Louis, Mo.

Now that the Banking Act of 1935 is a part of our legal code, and as the banking business settles down on a somewhat more even keel, there has developed a growing concern over the activities of Government lending agencies and the extent of their competition with commercial banks. In a recent address at Babson Park, President Rudolph Hecht said:

> . . . I confess that I am deeply concerned over the prospect that the supposedly temporary activities of the Federal Government in practically every phase of the banking business threaten to become permanent.
>
> There are now more than a dozen different Government lending agencies which have accumulated assets of about $10,000,000,000. While no one will deny that many of these organizations were necessary at the time they were created, to bring about a prompt and safe adjustment of the nation's financial and banking structure, which had been shattered by the forces of the depression, still we seriously question whether it is desirable from any standpoint that so large a part of our credit activities should remain permanently under the control of these Government agencies instead of being gradually taken over by the private instrumentalities which, under the changed conditions, should now be able to carry on their proper part in the nation's economic life.

It was, no doubt, this same concern that prompted your Committee to give place on the program to a brief presentation of this subject.

To consider the problem fairly and logically, we must bear in mind throughout our thinking the causes which impelled the Government to enter the lending field; we must examine the nature and scope of its operations, determine whether or not it is advisable for the Government to remain in the field, and if not, how its retirement can be justified.

The economic storm which precipitated the crisis into which the Government projected itself was not new. The history of finance tells of errors similar in nature, though not in scope, to the one which was at the heart of our trouble. Year after year we had gone along assuming that values would continue steadily upward, and the undue expansion of credit on that premise proved to be a colossal mistake. A corollary to that error was the belief that constantly-rising prices would in time liquidate mounting obligations; but the inevitable result followed, and when the mountain toppled over and the decline had spent its force, debtors and creditors alike found themselves prostrate. There were, on the one hand, debtors whose assets and whose earning power had been subjected to serious depreciation; and, on the other hand, creditors holding obligations which, if collected by force, undoubtedly would have invoked serious social consequences. Numbers of our people, those charged with a management of banks in particular, found themselves in the dual role of debtor and creditor, and the interests of the two groups lay so far apart that intervention by some neutral agency was essential to recovery. It seems perfectly reasonable to assume, when any two groups of citizens such as those represented by capital and labor, or by debtor and creditor, find themselves in a desperate situation of this kind, that it is the function of Government to intervene and to help find a way out of the difficulty. This was the Government's principal reason for entering the lending field, and the action met with universal approval. Moreover, it gradually dawned upon society that if the gap between debtor and creditor was to be bridged and chaos prevented, much of the loss incident thereto must be distributed upon the whole citizenry through the medium of the public treasury. I hold no brief for the abuses that seem to be an unfortunate adjunct of most Government operations, nor for the political exploitation that accompanied much of the activity, but when the final cost has been assessed, the Government's lending program will stand out as the most effective part of its major reconstruction efforts.

For the purpose of our discussion to-day I shall eliminate extensive comment on such lending operations as are exemplified in advances to the Secretary of Agriculture for the purchase of commodities in the attempts to peg prices; to emergency relief and construction projects; to the Secretary of Agriculture and to the Farm Credit Administration for so-called "feed, seed, drought loans," in the belief that no one attempts to classify these advances under the category of credit, but rather understands that they represent, for the most part, outright gifts to a stricken citizenship by a paternalistic Government which seeks to help its people through the economic storm and to afford them a kind of shelter until the skies are clear again. There may be some difference of opinion as to when and how these operations are to be discontinued, but surely there exists no thought that they shall occupy any permanent place in our credit structure. It would seem, therefore, that in the brief time at our disposal we can consider only the activities of those lending agencies which affect directly the operations of commercial banks, and that we should determine what, if anything, we are going to do about them. They are:

> The Reconstruction Finance Corporation.
> The Home Owners' Loan Corporation.
> The Federal Land Banks.
> The Short-term Credit Agencies for Agriculture.

It was unquestionably intended that the lending operations of the Reconstruction Finance Corporation should be distinctly of a type calculated to bridge the gap between the debtor and creditor; that it should be a financial power house, so to speak, from which should flow the current of assistance necessary for our private institutions to assume a lenient attitude toward all debtors who had done their honest best, and to insure a normal rather than a forced program of liquidation. Approximately 50%, or $1,884,164,964 of its loans, made under Section 5 of the Reconstruction Finance Corporation Act, were made to 7,439 banks and trust companies, including receivers, of which 75%, or

$1,428,236,858, has been repaid. During the recovery program, however, the Corporation has invested approximately $1,000,000,000 in preferred stock, capital notes and debentures of banks and trust companies from the proceeds of which we assume at least a part of the original loans were retired and the collateral returned. It is difficult, therefore, to estimate to what extent the underlying collateral has been liquidated, but we are, I am sure, in general agreement that liquidation has exceeded our expectations. Moreover, there is no reason to conceal the feeling of satisfaction that has come to the business community as a result of the increase in the values of equities both in the portfolios of our own banks and that of the RFC; and whether we view this as a temporary situation created by Government spending or as definite progress on the road to normalcy, our ability to adjust many otherwise impossible problems has been due to the far-reaching activity of the fountain-head of all Government lending agencies. It might not be amiss to say that the problem confronting the RFC would have been materially simplified and the necessity for loans to banks and trust companies considerably decreased, had not the Corporation been forced to publish its commitments to commercial banks. Notwithstanding the ever-present danger of malfeasance, the reputation of a bank is not unlike the fair name of our women folk—a thing the mere discussion of which invokes unintended but infinite harm. Whether we would have escaped the same baptism of fire in the end is debatable, but the publication of these commitments was unquestionably the greatest single factor contributing to the progressive failures which culminated in the bank holiday. The principle of the necessity for secrecy, for the common good, in certain financial operations is well exemplified by the secrecy which surrounds the operation of the $2,000,000,000 stabilization fund now in the hands of the Secretary of the Treasury for administration. It also serves to exemplify the disposition to proscribe for private industry certain practices and principles of conduct which, when indulged in by the Government itself, through some hocus-pocus, become surrounded with a halo of righteousness. However that may be, the RFC has by no means completed its work. The railroad program, the real estate mortgage problem in all of its ramifications, many drainage, levee and irrigation district situations are yet unsolved, and while progress is being made in all these fields, the liquidating services of the Corporation will likely be needed for some years to come. But as the ability of the Federal Reserve banks, under the provisions of the Banking Act of 1935, to assist in certain emergency situations increases (under proper regulatory provisions which will prevent abuse), it would seem that we should look forward to the eventual retirement of the RFC from the lending field. Recent public information to the effect that the Corporation has been making loans for the construction of new factories to manufacture goods in lines in which there is already serious overproduction seems almost incredible. If this is true, there must have been some extraordinary circumstances which allowed no alternative, for surely such action does not represent a general policy of the Corporation. Certainly with the increased latitude now accorded private instrumentalities both by law and by our present economic situation, it is not too much to insist that the RFC underwrite no new projects which will compete with those already struggling for existence.

The Home Owners' Loan Corporation, which rendered an excellent emergency service on urban mortgages, now holds nearly three billions of home mortgage paper, secured by approximately one million urban homes. With the rehabilitation of our building and loan associations, the re-entry of insurance companies into the home mortgage field, and with the keen competition now in progress between private lending agencies, including banks, under the provisions of Title II of the National Housing Act, there would appear to be no compelling reason for further expansion of this agency; but, on the other hand, there should be a steady continuance of the liquidating program in which it is now or soon will be engaged. Gradually, by change of ownership, settlement of estates, &c., these mortgages will filter back into the private market on sounder terms, and the HOLC will pass into disuse with a feeling of satisfaction over having made a major contribution to the recovery program.

No such machinery as Title II of the National Housing Act has been devised for farm mortgages, and although in a recent short comparative period, private agencies have made more of this type of paper than have the Federal Land banks, the supply of funds for farm mortgages is yet far too limited for us to dispense with the services of these institutions. The greatest adverse feature of farm mortgages for commercial banks, now, as in the past, is the element of non-liquidity. There is no well-developed market where such securities may be disposed of in the event of necessity, as is the case with urban mortgages, and those interested have, for nearly half a century, endeavored to devise some system whereby this liquidity might be supplied for farm mortgage loans. The farm loan system, originally represented by the Joint Stock Land banks and the Federal Land banks, was an effort to supply this liquid requirement. It is unfortunate that because of the depression and, in a few instances, because of mismanagement, the Joint Stocks were obliged to enter into liquidation. But as mortgages made to a Land bank are pledged as security for its outstanding bonds, and as these bonds enjoy a ready market, the net effect of the system is to provide commercial banks and investors generally with an avenue for financing farm mortgages without sacrificing the all-important element of liquidity. It is to be hoped that the Federal Land Bank System may soon bring to an end its emergency program, and that the direction of its operations be returned to a nonpartisan board, as originally provided for under the administration of Woodrow Wilson. It is contrary to our sense of democracy that the management and power incident to the operation of so vast a financial structure should, in the last analysis, be lodged in a single individual, as the Governor of the Farm Credit Administration. This is merely the statement of a principle and is in no way intended to reflect on the man who presently occupies the position, one whom I regard as the most efficient Administrator in Washington to-day.

In reviewing the activities of the two great agencies handling real estate mortgages, namely, the HOLC and the Federal Land Bank, we should not be unmindful of the valuable aid they provided for our commercial banking system during the rehabilitation period. Initiating their emergency activities for the avowed purpose of relieving banks of slow and uncollectible paper, they have made a definite contribution to a more liquid banking condition, and the reopening of many of our banks is directly traceable to the activities of these two Government agencies. This is aside from the service rendered to hundreds of thousands of borrowers who were saved from foreclosure by having their loans refunded on more liberal terms than it was possible for other creditors to grant.

Notwithstanding the fact that many of our members do not feel that real estate mortgages are desirable investments for commercial banks, further and continuous study should be given to the real estate mortgage problem by both our State and National Associations. Real estate loans predicated upon sound appraisals are still prime investments, and we should not content ourselves with the conclusion merely that they do not at present fit our investment program. The field is too large and too lucrative to abandon simply because, for the time being, we do not have the proper machinery within our banking structure. We should further explore the possibility of such a deposit contract, on time deposits, as will permit investment in sound real estate securities without subjecting our institutions to the danger of non-liquidity.

Perhaps the most potential source of competition for the country bank in the future, and the one which is now a matter of deep concern, is in the short-term credit field, which has been invaded by the Government-sponsored short-term credit agencies, authorized to make loans for general farming purposes and chattel mortgages on crops and live

stock. Here, again, our criticism should be temperate, for both immediately preceding and directly following the bank holiday, when deposits were shrinking, country banks were unable to make loans of this kind, and thus the Production Credit Associations and the Agricultural Credit Corporation filled a very definite need. As a matter of fact, had not this system been in operation during the years 1933 and 1934, it is difficult to see how farmers in many sections would have obtained their legitimate credit needs. But with the banking situation stabilized, bankers, for the most part, feel that the country banks are now in a position to take care of all the sound short-term credit needs. In many sections of the country, notably in territories containing large terminal markets for commodities and live stock, commercial banks and private loan companies are experiencing substantial competition from these Government agencies. They handle a sizeable volume of a most desirable type of paper, such as commodity loans, feeder cattle loans, and others, much of which, if made by a commercial bank, would be eligible for rediscount at the Federal Reserve Bank. With the initial capital structure of these institutions, as well as organization and promotional expense, underwritten by the public treasury, and their debentures enjoying a close relationship to Government obligations both as to tax-exempt privileges and intimate association in the public mind, obviously they are able to quote more favorable terms to borrowers than can be justified by actuarial experience. Although we are nonplussed by this situation for the time being, it would not be the part of wisdom for commercial banks to engage in credit transactions below the cost of doing business, and while interest rates may be for a time abnormally low due to Government fiat, there will eventually be such a reaction to Government expenditures that rates inevitably will be adjusted to a level in keeping with lending experience.

Our approach to this problem should not be merely one of protest, but likewise one of self-examination, for I am firmly convinced that by proper and sympathetic attention on the part of country bankers to the sound credit needs of farmer borrowers, whatever advantage the Production Credit Associations may have from the treasury subsidy will be overcome. Farmers entitled to credit, for the most part, will much prefer to obtain it from their local banker, where the transaction may be closed without delay, and where the personal contact is an important consideration. If we are to succeed, however, in handling this credit, I should like to say courteously, but nevertheless emphatically, that we must have the proper conception of our duty toward farmer borrowers. It is no affront to remind you that in many sections of the country, particularly as respects tennant-operated farms, unconscionable interest rates formerly prevailed under the burden of which no form of agriculture could survive. Bankers themselves were not altogether responsible for this situation, one of the major causes being the fact that although the bank had two classes of customers, depositors and borrowers, one of these, the borrowing class, was carrying the entire cost of bank operating expense and the payment of dividends to stockholders. Heretofore, to those who had money, banks rendered service without charge, and all of the cost of operation was laid on those who had use for the funds. This has now changed. With the installation of service charges, which are presumed to reimburse the bank for service rendered to those who want their money taken care of, and a lower interest rate on deposits, it is not now necessary to ask such high rates from borrowers in order to produce the same income as was formerly obtained. In short, having found a new source of revenue, we cannot appropriate it all to ourselves; a part of it, at least, should be shared with those who in previous years have carried the entire burden of our operating expenses.

Finally, I would recommend to our captains of finance and to those charged with the operation of our Federal Reserve System a more tolerant and sympathetic attitude toward the credit needs of small independent operators, farmers in particular, than has been heretofore displayed. According all due credit to our great corporate enterprises for their magnificent contribution to our commercial supremacy, it is in the combined efforts of our independent individual citizens that, after all, lie our greatest hope for national security.

This reference to the subject of Government lending would not be complete without some discussion of the moral effect of such activities on our composite national character. More than 4,500,000 of our citizens are now indebted to these agencies—a sizeable voting block, the potential political strength of which is too obvious for comment. Within this group are hundreds of thousands of men and women who have done their honest best and are entitled to the utmost of consideration from their more fortunate fellow men. Again, there are other thousands who are hopelessly involved and for whom liquidation was, is and will be the only solution. Between these two classes there are speculators, minors, estates, old people with no income, and a host of others who make a ready audience for those who have no regard for the sanctity of obligations and who preach the gospel of repudiation. No political administration, however well intentioned, can supply those restraints and restrictions so necessary to sound credit practices without incurring the ill-will of the voters who borrow from it, and thus it is persuaded to follow the line of least resistance. This is particularly true, in a democracy such as ours, where succession is thought of from the short-range viewpoint, and where prosperity now seems to be the real forgotten man. Few people question the necessity for many of the lenient policies adopted to help those who have honestly tried, but the high delinquency record on loans made by the Government lending agencies discloses altogether too much disregard for promises made and is but a practical illustration of what invariably happens when the sovereign enters the lending business. This has the double effect of imposing unnecessary losses on loans already disbursed and serves to retard the flow of credit from private sources, and is altogether an unhealthy situation. No system of credit can function long, or in the end survive, when those who are able to pay find refuge in measures designed to assist only those who are in actual and unavoidable distress. It is essential, therefore, that the granting of credit be restored to private instrumentalities with the greatest possible dispatch in order that our traditional respect for obligations may not suffer wholesale collapse.

Whether we like it or not, we are operating banks in an era when there is a great wave of socialistic thinking which has been interpreted into laws that will be in force for many years to come. Under these conditions our banks have been more and more converted into a public utility with less and less freedom of operation. Perhaps this is well. Time only can prove the value of these changes. It is our obligation to apply ourselves diligently to the task of adjustment to the new order, to the end that our private banking system may be preserved. If I read the temper of the American people aright, they have no desire to see our financial resources directed toward political ends. A sense of the value of individual initiative and of private control is too deeply rooted in our national character to be destroyed even by the most terrific of economic storms. For in this is represented the fundamental tenets of the American faith, the principle upon which our country was founded, by which it has grown great, and to which it must adhere if the republic is to endure. My conception of a well-ordered credit system, and one which older governments have long since found most desirable, is one operated for private profit, alive to its obligation to serve, with such supervision by the Government as will minimize the abuses which all intelligent men condemn. I believe that our private banking system is the one best adapted to the peculiar needs of our wide and diversified national life. It is due to this system, in no small measure, that we have produced 50% of the world's wealth with 6% of the world's population, and notwithstanding statements of reformers to the contrary, this wealth is so evenly divided that immigration barriers must still surround this land of

opportunity lest the peoples of a troubled world make a beaten path to our door.

C. W. Allendoerfer, Vice-President of the Division, who temporarily occupied the chair, had the following to say following the presentation of Mr. Netherland's address:

I am very happy that we have had Mr. Netherland with us. Mr. Netherland knows that subject, as a successful banker in Arkansas, with a knowledge of the needs of country banks and of larger banks. He became President of the Federal Land Bank of St. Louis, which position he left only about 18 months ago to become an officer of the Mercantile-Commerce Bank & Trust Co. of St. Louis. So, when Mr. Netherland brings us that message, it is not based entirely on outside observations; it is the result of his own experience, his own knowledge, his own philosophy gained from that intimate acquaintance with the whole subject.

Mortgages Insured Under Title II of the National Housing Act as Investments for Banking Institutons

By Richard R. Quay, of Counsel, Federal Housing Administration

[The following address of Mr. Quay was delivered before both the State Bank and National Bank Divisions of the Association.]

Mr. Chairman, Gentlemen:

In behalf of the Federal Housing Administration, I wish to express my appreciation of the courtesy and co-operation shown by the officers of your Association in according us an opportunity to appear before you here to-day. I propose to cover briefly those features of a mortgage insured under Title II of the National Housing Act, which make that mortgage an eminently desirable investment for banking institutions. Let me at once allay your fears by saying that I have just now used the term "briefly" advisedly and not rhetorically, for I know that convention seats are hard and that your schedule is a full one. I am also not unaware of the fact that conventions—even of bankers—do not find their sole justification in deliberation upon matters of routine business, nor yet in a preoccupation with the problems of a liquidity which is purely financial in nature. This is all to the good and, as a grateful beneficiary of your hospitality, I should be the last to wish it otherwise.

Being one of those slightly anachronistic individuals who sometimes suspects that bankers, as well as lawyers, have souls, I shall, accordingly, take to heart the truim of the pulpit that "no souls are saved after the first 20 minutes," and, improving upon the clergy, rest content if I can influence the salvation of one or two in 10 minutes. My task is greatly facilitated by the fact that the National Housing Act has now been in existence for almost a year and a half, and that many of you represent institutions which have been actively engaged in the insured mortgage program as approved mortgagees since the first of November a year ago. I am more than willing, therefore, to take judicial notice of the fact that most of you are thoroughly familiar with the broad outlines and general details of that program as a realistic attempt to re-establish our $21,000,000,000 home mortgage debt on a common sense basis, and, at the same time, provide a private capital solution for the already serious and constantly increasing housing problem which confronts this country.

The National Housing Act is simply the statutory expression of the lessons of a very bitter experience in the field of real estate and mortgage finance. I assume that, by the accident of circumstance, all bankers and business men tasted more deeply of that bitterness than did I, and that the lesson which it has for all of us, if we are wise, is, thus, correspondingly easier for you to appreciate than it was for me. I can, therefore, address my remarks to-day, from a mutually understood and brutally factual basis, directly to your intelligence, for ours is a common ground upon which the controversial aspects of social, economic or political vagaries have no place.

I wish first to tell you exactly what kind of a thing a mortgage eligible for insurance under Title II is. I then wish to describe precisely the nature and extent of the additional protection provided for that mortgage by the insurance. After that the issue can safely be left in your hands, since it would be sheer presumption for any mere lawyer to pretend to lecture a group of bankers upon those more refined questions of investment policy and banking practice which fall purely within your own expert province. Once it is accepted that an insured mortgage is, from every point of view, one of the very best investments available to-day—and if that proposition is not now accepted by all of you, I am certain that it eventually will be—I have no doubt whatever that, as bankers, you will understand better than any outsider, who might assume to point them out to you, the possibilities which the insured mortgage offers for that proportion of your portfolios which your applicable law allows you to carry in real estate.

This is equally true whether one is dealing with a National bank of a State bank, for I know of no differences in the situation as it affects either the one or the other, except such arbitrary and technical differences as arise because of the fact that State banking laws vary both among themselves and from the National Banking Act as to particular capital percentage limitations for the several classes of permissible investments. There may also be a further difference between the National bank and the State bank in connection with rediscount privileges. In this respect, however, every State bank which is a member of the Federal Reserve System stands, of course, on a parity with National banks. As I have already indicated, therefore, my only purpose in this address is to emphasize the inherent soundness of the insured mortgage, as such, and not to discuss such legal or other ditinctions as exist between State and National banks. Those distinctions for the most part are simply mechanical, and hence, largely immaterial, as regards their implications for general participation by banks in the insured mortgage program.

1. *The long-term amortized mortgage.* Apart from any question of the contribution to security made by the insurance, any mortgage eligible for insurance under Title II is necessarily, in and of itself, a double A real estate investment. The double A rating is appropriate, not only as a statement of fact, but also as a figure of speech, for the letter A is the first letter of two words which represent the very foundation of the whole insured mortgage program, namely, Appraisal and Amortization.

Sound appraisal bears the same relation to a mortgage transaction as a fulcrum does to a lever. For a mortgage loan, it is the one virtue without which the preservation of any other is practically impossible. After the event it is now easy for anyone to see that the appraisal methods commonly used in the past were shortsighted and utterly haphazard. Their deficiencies were not attributable to stupidity or negligence on the part of mortgage lenders. They were partly the result of the accepted system of home mortgage finance, based upon the short-term, unamortized mortgage partly the result of the absence of statistics capable of supporting reasonable estimates of actual and continuing value. Little attention was paid to, and less was known of, such things as neighborhood trends, population trends, design and construction trends, the relationship between house and lot, and between property and neighborhood or community, to mention several of the intangible but very real factors bearing directly, not upon the present value of a piece of property, but upon its value at the end of five, or 10, or even 20 years—the only value justifying a borrower in contracting a mortgage obligation and a lender in advancing money upon mortgage security.

The system of appraisal developed by the Federal Housing Administration gives careful study and specific ratings to all these elements in accordance with a prescribed routine. The appraisals are made by specially trained appraisers in possession of all available information—information which is continually growing and being classified and assimilated

CROSS-REFERENCE SHEETS

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Pocket

CROSS REFERENCE

"INFLATION DANGER IS STILL WITH US"

American Banker, Dec. 15, 1937

See File # 12

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Bchl

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"STATE BANKERS REAFFIRM THEIR FAITH IN DUAL BANKING SYSTEM"

American Banker, Oct. 15, 1937

See File # 12

4131a
Bsl

CROSS REFERENCE

FILE NO. 15 B

SUBJECT: Address by Leo T. Crowley, Chairman of the FDIC, May 12, 1937, before the Missouri Bankers Association, St. Louis, Missouri.

"American Banking Faces the Future"

SEE FILE NO. 1 D

CROSS REFERENCE

#13.10
Pocket

FILE NO. 15 B

SUBJECT: "Banking Research Survey" by Joseph M. Whalley, Bureau of Business and Government Research, University of Colorado, for the Colorado Bankers' Association

SEE FILE NO. 2 D

CROSS REFERENCE

413.1(a)
Postal

FILE NO. 15B

SUBJECT: "Patman Hits Branch Banks, Would Drop Postal Savings"
AMERICAN BANKER, June 14, 1937

SEE FILE NO. 12A

CROSS REFERENCE

4/3.1a
Pocket

FILE NO. 15B

SUBJECT: "Brodie Warns Government to Mend Its Ways, at Oregon Meet"
AMERICAN BANKER, June 15, 1937

SEE FILE NO. 12A

CROSS REFERENCE

413,1a

FILE NO. 15B Pocket

SUBJECT:

Clipping from American Banker, May 21, 1937 entitled:

"Smith Sees Sound Assets as Stabilizer of Banking"

SEE FILE NO. 3A

FEDERAL RESERVE BOARD
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File No. 15

Subject "Harr Denies Co-operation Might End State Systems"
American Banker, December 12, 1936

SEE

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U. S. GOVERNMENT PRINTING OFFICE: 1929

FEDERAL RESERVE BOARD
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CROSS REFERENCE SHEET

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Subject "Keep Yourself, Public and Washington Officials Informed"
By U. V. Wilcox

American Banker,
Nov, 21, 1936

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File No. 15

Subject "Changing Conditions Call For Bank Study To Adapt Basic Practice"

American Banker Oct. 24, 1936

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Subject Clipping from AMERICAN BANKER, July 29, 1936, entitled "Wisconsin Clamps Down on Federal Loan Associations"

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File No. #15B

Subject Clipping from AMERICAN BANKER, October 24, 1936, "Changing Conditions Call for Bank Study to Adapt Basic Practice" Tom K. Smith's speech before the Robert Morris Associates at Hot Springs, Va.

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File No. 15B

Subject Clipping from AMERICAN BANKER, September25, 1936, "F. D. Brady for Voluntary Membership in Reserve"

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Subject Clipping from AMERICAN BANKER, September 14, 1936, "Independent Bankers' Resolutions Call for Delegation to A. B. A. Convention, Cut in Postal Savings Rate, FDIC Change

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Subject Clipping from Bkg. Jan. 1936 "Bank Instalment Finance" by John Farnham

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Subject "Proposals for Commercial Bank Reform - Jan., 1930 to Oct. 1934" from file of Com. on Legislative Program

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Subject Clipping from Am. Bker., May 25, 1936, "Whipple Heads Coast Bankers"

SEE

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File No. 15

Subject Excerpt from address of Wilber M. Brucker, Governor of Michigan, at the 46th Annual Convention, Michigan Bankers Asso., July 1932 (Michigan Investor, July 23, 1932)

SEE

File No. Study #11

Letter of

Dated

Remarks

U. S. GOVERNMENT PRINTING OFFICE: 1933 178151

5-29-36

413.1a

THE FEDERAL RESERVE BOARD

CROSS-REFERENCE SHEET

File No. 15

Subject Excerpts from an address by President McLaughlin of the N. Y. State Bankers Association taken from the Proceedings of N. Y. State Bankers Association - 1934

SEE

File No. Study #11

Letter of

Dated

Remarks

U. S. GOVERNMENT PRINTING OFFICE: 1933 178151

5-21-36

4/3.1a

THE FEDERAL RESERVE BOARD

CROSS-REFERENCE SHEET

File No. 15

Subject "Demands Government Competition be Curtailed" - Fred Brady Tells A. B. A. Council Time to Return Credit Streams to Banks - clipping from American Banker for April 30, 1936

SEE

File No. Study #6

Letter of

Dated

Remarks

U. S. GOVERNMENT PRINTING OFFICE: 1933 178151

File 6/10

THE FEDERAL RESERVE BOARD

CROSS-REFERENCE SHEET

File No. 15

Subject Annual Address of the President Leslie G. McDouall Delivered at the convention of the New Jersey Bankers Assoc. at the Ambassador Hotel, Atlantic City May 23, 1936.

SEE

File No. Study 6

Letter of

Dated

Remarks

U. S. GOVERNMENT PRINTING OFFICE: 1933 178151

EXCERPTS

File #15D

Mr Blattner
Mr. Hersey
Miss Hammill

FARM CREDIT ADMINISTRATION
1300 - E Street, N.W.,
Washington, D. C.
Telephone - Di. 1050 - Br. 75

413.1

For release Monday morning
December 28, 1936.
12-24-36

Press Service
No. 8-70

COOPERATIVE FARM CREDIT MORE IMPORTANT IN 1936-7

Continued increase in new agricultural financing and greater importance of cooperative credit institutions may be expected in 1937, according to a statement today by Governor W. I. Myers, in reviewing this year's work of the Farm Credit Administration.

Upturns in cooperative cash financing of crop production, more financing of farm purchases and a larger credit business with farmers' cooperative marketing and purchasing associations featured the 1936 business of the Farm Credit Administration, Myers said.

The 550 production credit associations, making short-term secured loans for crop and livestock production, did a larger business with farmers than any of the other Farm Credit Administration institutions. Their loans during the year aggregated $225,000,000 compared to $196,000,000 in 1935. Farm mortgage loans by the Federal land banks and the Land Bank Commissioner amounted to $184,000,000; loans for farmer-cooperatives $104,000,000; Federal intermediate credit bank loans and discounts for private financing institutions $106,000,000; regional agricultural credit corporations, now in liquidation $34,000,000 and emergency crop loans $17,000,000.

"Substantial increases in financing through the cooperative organizations and continued decrease in emergency lending during 1936 reflects the shift from the emergency demand created by farmers who had no other source of credit after the depression to the increasing group of operators applying for loans because of favorable interest rates, suitable maturities, and other good-business features of the permanent cooperative credit institutions -- Federal land banks, production credit associations, and banks for cooperatives.

Governor Myers predicted that the production credit associations would continue to increase their business in 1937. The loan volume during the past year was higher in 40 of the 48 states in spite of drought conditions which curtailed financing in some sections, he said.

"In the country as a whole, farmers apparently spent more money for equipment, machinery, farm buildings and repairs in 1936 than in any year since the beginning of the depression," the Governor stated. " Their increased purchasing power and the opportunity to get short-term cash loans at the present reasonable rates will furnish an additional motive in 1937 to make up for depression-depreciation in farm plants and equipment."

That farm mortgage loans for the Federal land banks and Commissioner were less than half the 1935 volume was interpreted by Governor Myers as reflecting the continued decrease in emergency refinancing and less pressure by other creditors for liquidation.

"Borrowing for purchase of farm real estate reached a higher level during the year," he pointed out. "More adequate financing for farm purchasing as provided by the Farm Credit Act of 1935, is gradually becoming effective. Since October 1 last year when we began to make tabulations of financing for this purpose, the land banks and the Commissioner have extended approximately $60,000,000 of credit to finance the purchase of nearly 25,000 farms, including farms acquired by the Federal land banks over a period of years and resold on mortgage or contract terms."

The 13 banks for cooperatives put more business on their books during the last half of 1936 than at any time since their organization, according to Myers' statement. Loans outstanding increased from $39,000,000 on June 30 to $72,000,000 on December 1. About $24,000,000 of loans outstanding at that date consisted of commodity loans. Business with cotton marketing cooperatives accounted for a large part of the increase. Operating capital loans outstanding amounted to $29,000,000 and physical facility loans $17,000,000. In addition to the more usual type of marketing and purchasing loans made by the banks for cooperatives, they have extended their services during the past year to several other types of farm business activities such as soil improvement and terracing cooperatives, mutual irrigation companies, cooperative oil and gasoline associations, and mutual fire insurance companies. Interest rates on the various types of loans remained unchanged during the year at 2, 3, and 4 per cent respectively for commodity, operating and physical facility loans.

Preliminary figures on 1936 loans by the various institutions under the Farm Credit Administration's supervision compared to 1935 loans are as follows:

	1936	1935
	(In millions of dollars)	
Farm mortgage credit-		
Federal Land Banks	108	248
Land Bank Commissioner	76	196
Short-term credit-		
Production credit associations	225	196
Emergency crop loans	17	57
Drought relief loans	--	39
Regional Agricultural Credit Corps.	34	90
Federal Intermediate Credit Banks (loans to and discounts for private financing institutions)	106	117
Loans to Cooperatives-		
Banks for Cooperatives	80	66
Agricultural Marketing Act Revolving Fund	20	7
Federal Intermediate Credit Banks	4	44
	670	1,060

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DEPOSIT INSURANCE - Lauchlin Currie assisted by Martin Krost

1. Deposits eligible for insurance

All deposits subject to check, except interbank deposits, are to be eligible for insurance. But only those individual savings and time deposits which do not exceed $5,000 should be included. This recommendation is based on the theory that one purpose of deposit insurance is to make deposit money as safe as notes and that the other is to protect the savings of the poor.

2. Basis of assessment

The deposits eligible for insurance should serve as the basis of assessment. Ideally, the rate of assessment should vary with the probable risk involved, but such discrimination would be politically impossible except in the case of savings banks. A rate of one-tenth of 1 per cent for insurable demand deposits and of one-twentieth of 1 per cent for insurable savings deposits would cover all "normal" losses to the fund. Extraordinary losses should be borne by the Government. Assessments should be suspended when the fund exceeds 2 per cent of insurable deposits.

3. Contribution of the Government

Both the assets and the liabilities of an insolvent bank should be taken over by the fund. If the fund is insufficient to meet these liabilities, the F. D. I. C. should issue Government-guaranteed bonds for the deficiency. All losses to the fund in excess of one-tenth of 1 per cent of the aggregate deposits should be replaced by the Government at ten year intervals. The $150,000,000 contribution of the Government to the F.D.I.C. should be repaid but not that of the Reserve banks.

4. Membership in the Federal Reserve System and the fund

All insured commercial banks should be members of the Federal Reserve System, but membership of savings banks should be optional. The F. D. I. C. should have authority to expel or suspend members from the Federal Reserve System and from the fund.

5. Examinations and receiverships

Office of the Comptroller should be abolished and examining functions of that office transferred to the Division of Examinations of the Board. The Division of Examinations should also admit new members to the Federal Reserve System, pass upon mergers, and have the power to vary the stringency of examinations.

6. Postal savings

The Postal Savings System should be abolished except in communities where no banking facilities exist.

Mr Henry
Mr Hamlin

FEDERAL RESERVE BANK

OF CLEVELAND

November 7, 1936

4/3/15
Pockel

Board of Governors of the
Federal Reserve System,
Washington, D. C.

Gentlemen:

Enclosed herewith you will find our report of activities of the Bank and Public Relations Department of this bank for the month of October.

As matters of information or interest to the Board the following observations are made.

At the meeting of Group Six of the Ohio Bankers Association (west central section of the state) a resolution was adopted opposing compulsory membership in the Federal Reserve System for insured state nonmember banks as provided in the Banking Act of 1935. The same resolution also endorsed the dual banking system and opposed any action which has been taken or may be taken looking to unification of the banking system under federal supervision It is of interest to note that Superintendent of Banks, S. H. Squire, during the course of his remarks to the Group, endorsed the terms of the resolution. We do not have, at this time, a copy of the resolution referred to but one will be secured and transmitted to the Board.

All of our Field Representatives report that, in conversation with member bankers, there has been expressed a doubt as to the good faith of the Board's statement released in connection with the recent increase in reserve requirements of member banks. The idea was expressed that the action was taken solely for the purpose of making more funds available to Federal reserve banks for the support of the government bond market. As indicated above these comments were quite general and come from all sections of the district.

Member bankers, particularly in the southwestern section of Ohio, are complaining of undue activity on the part of the Production Credit Corporation which is active

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FEDERAL RESERVE BANK

OF CLEVELAND

in making loans to farmers particularly in connection with live stock financing. These bankers point out that while the Corporation's rate of 5% looks attractive to the borrower the fact is that the ultimate cost to him is greater than if he were to borrow from the bank at 6%. The truth of the matter appears to be that banks in that section are still maintaining the level of interest rates prevailing in recent years despite the easy money condition. In some of the smaller manufacturing centers complaint is made that city banks are taking over desirable industrial and commercial accounts at substantially lower rates.

At the Forty-fourth Annual Convention of the Kentucky Bankers Association held at Louisville on October 21 and 22, Mr. John Yost, President of the Association, in his opening address told bankers they must "Quit viewing with alarm" recent government activity in the banking field. "All of us should know by now," he said, "that corrective legislation was necessary."

At the general election on November 3 a constitutional provision for double liability on State bank stocks, in the State of Ohio, was repealed.

Very truly yours,

(Sgd.) H. F. Strater
Vice President

S. A. G.
Encl

Form F. R. 131

File #15

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM

Office Correspondence

413.10 Pocket

Date December 17, 1936

To Mr. Morrill

From J. M. Daiger

Subject: Liquidation of emergency-credit agencies.

In view of our recent conversation about the liquidating of governmental emergency-credit agencies, you may be interested in reading the attached copies of letters recently sent to the President and the Secretary of the Treasury by the United States Building and Loan League, and also the attached copy of a memorandum from Dr. Currie and my draft of a letter to which Dr. Currie's memorandum refers.

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COPY

December 10, 1936

My dear Mr. President:

Desiring to facilitate your expressed objective that the Government retire from its extensive credit activities as rapidly as business recovery and the facilities of private institutions would permit, the Board of Directors of the United States Building and Loan League have unanimously approved a proposal for relieving the Home Owners' Loan Corporation of a portion of the individual mortgages which it now holds.

Measured in assets, the great majority of our savings, building and loan associations and cooperative banks are in good condition and actively seeking home-mortgage loans. We find that other trustee institutions, such as banks, trust companies, life insurance companies and mutual savings banks, are active in the mortgage market and a vigorous competition is developing for acceptable home loans to owner-occupants. In view of this condition, our Directors felt that our local, cooperative institutions might render a public service by taking over some of the HOLC advances, giving the borrower of course, the same 5% interest rate, amortization and other terms in the existing HOLC contract.

There have also been some discussions which would indicate that the other private trustee institutions would be inclined to cooperate in a program of transferring a billion or a billion and a half of the HOLC mortgages to private institutions, in case you indicated that this program might be feasible and merit further study and planning.

In general, our institutions have to have a return similar to that charged the borrowers under the Federal Housing Administration's insured mortgage plan, in order to pay a 3 to 4% return on the savings entrusted to them. As their funds come almost entirely from the savings of the working group, they would also have to confine the assumption of HOLC mortgages to acceptable risks, both as regards real estate values and the individual mortgagor. We estimate that probably one-half or more of the existing HOLC mortgages would be acceptable to local institutions at this time.

Such a program would reduce the contingent liability of the Government in the case of mortgages so transferred. There is the further consideration that, in the long run, there would be a real saving

in the HOLC operation, as they will certainly have a mounting operation cost, growing out of the collection problems of a nation-wide agency dealing with over a million small mortgages scattered all over the country. Furthermore, if legislation were enacted to restrain the necessary and wise foreclosure policy now being followed by the HOLC, it would greatly complicate their collection problem and possible create ultimate losses, which might be avoided if a rapid liquidation program were carried out. There is also the possibility to consider of an adjustment of the interest rate on the million HOLC loans to a rate comparable to that prevailing on the Government's farm loans, a policy which might so decrease the income and spread of the HOLC operations as to create or multiply an ultimate loss.

The Board of Directors of the United States League, after discussing the matter with leaders and managers of institutions from all parts of the country, pledge the cooperation of the savings, building and loan associations and co-operative banks which have loanable funds, in the event you initiate or approve such a plan. It would, we believe, not only afford the opportunity for the more rapid retirement of the Government from the emergency field than has been thought possible, but would expedite the reduction of Government activity and all risk of loss, without taking from the great group of HOLC borrowers any of the benefits they have received from their Government in time of need.

Respectfully yours,

(Signed)HAROLD T. DONALDSON

President
United States Building and Loan League

To the President,
The White House,
Washington, D. C.

United States Building and Loan League, 333 North Michigan Avenue,
Chicago, Illinois

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December 11, 1936.

My dear Mr. Secretary:

Our group have been giving considerable thought to the problems of our local, cooperative thrift and home-financing institutions in relation to the government, or emergency, operations in the home mortgage field. The attached copy of a letter to the President of the United States from the President of the United States League, Mr. Harold T. Donaldson, deals with one phase of the problem, including a cooperative suggestion which, it occurs to me, might be of interest to the Treasury on account of their responsibility for the financial program of the Government and the securities of the Home Owners' Loan Corporation.

We are anxious to cooperate and I believe that the leaders in the American Bankers Association, the National Association of Mutual Savings Banks, the American Life Convention and the Mortgage Bankers Association of America would also cooperate heartily if such a program could be initiated.

Respectfully yours,

(Signed) MORTON BODFISH

Executive Vice-President

Hon. Henry Morgenthau, Jr.,
Secretary of the Treasury,
Washington, D. C.

Form F. R. 131

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM

4/3.1a

Office Correspondence

Date December 17, 1936

To Mr. Thurston

Subject: Suggested answer to Mr. Draper's letter of November 25 to Mr. Eccles

From Lauchlin Currie

G P O 16—852

COPY

I carried out my suggestion to you and passed this correspondence along to Mr. Daiger, who has been devoting considerable attention to the question of the future of the emergency lending agencies. While he does not care for Mr. Heimann's proposal he is in favor of a policy of active liquidation of the assets of government emergency lending agencies. He feels that the question involves broad political and social considerations and should not be decided in terms of the dollars and cents loss or gain to the government. I, on the other hand, while I do not feel strongly on the matter, am inclined to favor the continuation of the emergency organizations as collection agencies because losses may be thereby minimized and the stigma of "government inefficiency" avoided. I have, in other words, some misgivings over any procedure that would leave the government holding the poorer stuff.

We decided, therefore, that instead of committing the Chairman to either one of these views it would be better to straddle in the reply to Mr. Draper. The enclosed draft was submitted by Mr. Daiger and meets my approval. If the Chairman desires, both Mr. Daiger and I will be glad to present our views on this matter.

413.1

Dear Mr. Draper:

The suggestion made by Mr. Henry H. Heimann, executive manager of the National Association of Credit Men, is an interesting one and merits consideration along with others that have been made with the same essential purpose in view--namely, the sale to private investors of a substantial part of the mortgages, bonds, notes, etc., acquired by various emergency credit agencies of the Government, and the use of the proceeds to retire a corresponding amount of Government obligations.

Offhand, the liquidating mechanism suggested by Mr. Heimann strikes me as being unnecessarily complicated. A great deal of liquidation has already been accomplished by the RFC, for example, not through collections only, but also through the sale of assets to institutional buyers.

In the case of the FHA, no Government loans are involved, since all the lending is done directly by private institutions. In the case of the HOLC, I understand that within the past week a proposal has been sent to the President by the United States Building and Loan League looking toward the purchase of half or more of the existing HOLC mortgages by institutional investors.

As to the amendment to the Federal Reserve Act which Mr. Heimann suggests, that would be unnecessary. A provision of the Banking Act of 1935 already authorizes such advances by the Federal Reserve banks to member banks as Mr. Heimann evidently has in mind.

It is true that the sale of assets held by various credit agencies of the Government would provide a means of reducing the public debt and would increase somewhat the earnings of the private institutions that acquired these assets. At the same time, it would diminish the operating income of the governmental agencies concerned, and thus deprive them of an offset which they would otherwise have against losses.

Of course, the advantages to be gained by turning as many loans as possible over to private institutions may in the long run amply justify, even in operating ecomonies alone, this loss of income to the emergency agencies. The whole question is one that I think deserves careful study, but from the point of view of what is the best governmental policy rather than with an eye to the complaint of Government competition with private business.

I am myself in full sympathy with the idea of removing any just ground for complaint that may exist with respect to the present activities of governmental credit agencies. On the other hand, I think that the emergency activities, in which the Government took over loans that private institutions were eager to liquidate, or were unable or unwilling to handle, cannot be said in any sense to have constituted then, or to constitute now, competition with private enterprise.

One of my assistants, Mr. J. M. Daiger, who has for the past three years given special attention to housing and mortgage matters in connection with Administration measures, has recently been looking into the question of liquidating procedure, and if you would like to talk with him about it I shall be glad to have him get in touch with you.

With kind regards, I am

Sincerely yours,

M. S. Eccles
Chairman

Hon. Ernest G. Draper
Assistant Secretary of Commerce
Washington, D. C.

File # 15

75th Congress
1st Session } SENATE COMMITTEE PRINT

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INVESTIGATION OF EXECUTIVE AGENCIES OF THE GOVERNMENT

REPORT

TO THE

SELECT COMMITTEE TO INVESTIGATE THE EXECUTIVE AGENCIES OF THE GOVERNMENT

PURSUANT TO

SENATE RESOLUTION No. 217 (74TH CONGRESS)
A RESOLUTION CREATING A SELECT COMMITTEE TO INVESTIGATE EXECUTIVE AGENCIES OF THE GOVERNMENT WITH A VIEW TO COORDINATION

No. 1

REPORT ON GOVERNMENT FINANCIAL AGENCIES
PREPARED BY THE BROOKINGS INSTITUTION

Printed for the use of the Select Committee on Investigation of Executive Agencies of the Government

UNITED STATES
GOVERNMENT PRINTING OFFICE
WASHINGTON : 1937

SELECT COMMITTEE ON INVESTIGATION OF EXECUTIVE AGENCIES OF THE GOVERNMENT

HARRY FLOOD BYRD, Virginia, *Chairman*

JOSEPH T. ROBINSON, Arkansas
JOSEPH C. O'MAHONEY, Wyoming

CHARLES L. McNARY, Oregon
JOHN G. TOWNSEND, Jr., Delaware

CONTENTS

INTRODUCTION

The number and diverse character of Federal agencies which are concerned with regulating, supplementing, and assisting private financial operations present a challenging problem of governmental organization. Some of them are of long standing and have permanent functions; others are of recent origin and were conceived to meet temporary needs. With the passing of the emergency which called so many of these agencies into existence, the time is propitious for a careful appraisal of the administrative and liquidation problems which now present themselves and of the possibilities of effecting operating economies through a regrouping or reorganization of existing agencies.

The principal agencies whose work falls within the field of this report are listed below:

- Lending agencies:
  - Farm Credit Administration.
    - Federal land banks.
    - Federal Farm Mortgage Corporation.
    - Intermediate credit banks.
    - Production Credit Corporation.
    - Production credit associations.
    - Banks for cooperatives.
    - Regional agricultural credit corporations (in liquidation).
    - Emergency Crop and Feed Loan Section.
    - Joint-stock land banks (in liquidation).
    - Credit unions.
  - Commodity Credit Corporation.
  - Federal Housing Administration.
  - Federal Home Loan Bank Board.
    - Home-loan banks.
    - Home Owners' Loan Corporation.
    - Federal savings and loan associations.
    - Federal Savings and Loan Insurance Corporation.
  - The Reconstruction Finance Corporation.
  - Federal Emergency Administration of Public Works.
  - Export-Import Bank of Washington.
  - Rural Electrification Administration.
  - Electric Home and Farm Authority.
  - United States Railroad Administration (in liquidation).
  - War Finance Corporation (in liquidation).
- Supervisory agencies:
  - Comptroller of the Currency.
  - Board of Governors of the Federal Reserve System.
    - Federal Reserve banks.
  - Federal Deposit Insurance Corporation.

A number of other agencies exercise some incidental lending authority in connection with other more important functions; among these are:

- Resettlement Administration.
- Federal Prisons, Inc.
- Tennessee Valley Authority.
- Inland Waterways Corporation.
- United States Maritime Commission.

The analysis which follows is divided into three major divisions. Part I gives a brief description of the functions and activities of the various agencies, indicating also their interrelations. Part II is devoted first to an analysis of the problem of liquidation of the governmental loans and investments of the temporary institutions, and second to the possible reorganization of the permanent agencies. Part III deals with the bank supervisory agencies.

The agencies included in this report are of five types: (1) Those which extend credit to farmers; (2) those which extend credit to urban home owners; (3) the Reconstruction Finance Corporation, which has made loans to a wide variety of agencies and institutions; (4) miscellaneous lending agencies whose work has been or shortly is to be discontinued; and (5) those which supervise banking and credit. The Tennessee Valley Authority, the Rural Electrification Administration, the Electric Farm and Home Authority, the Inland Waterways Corporation, and the United States Maritime Commission are discussed in other sections of this report. The Resettlement Administration is considered in this section only with reference to its lending activities; other sections of the report dealing with the larger aspects of its work.

GOVERNMENT FINANCIAL AGENCIES

PART I. DESCRIPTION OF CREDIT-GRANTING AND CREDIT-SUPERVISORY AGENCIES

A. Farm Credit Agencies

The principal agencies which extend credit to farmers are the Farm Credit Administration, the Resettlement Administration, and the Commodity Credit Corporation.

I. SUMMARY OF ACTIVITIES

1. *Farm Credit Administration.*—The Farm Credit Administration is a supervisory agency which exercises supervision over the operations of the agencies discussed below. Its authority is centered in the Governor of the Farm Credit Administration.

(*a*) *Federal land banks.*—These are 12 corporations, the stock of which is held in part by the United States Government, in part by the national farm loan associations, and in small part by individual farmers. The banks make 20- to 30-year first-mortgage loans to farmers in amounts not to exceed 50 percent of the value of the land mortgaged, plus 20 percent of the value of improvements. In general the loans are made through national farm loan associations, composed of farmer borrowers, each of whom is required to purchase stock in the farm loan associations to the extent of 5 percent of the amount which he borrows. The associations in turn purchase stock in the land banks. Each bank is controlled by a board of directors and a general agent of the Farm Credit Administration. General supervision over the 12 banks is exercised by the Land Bank Commissioner. The banks formerly issued their individual bonds, but the present practice is to issue consolidated bonds which are the joint obligation of the 12 banks.

(*b*) *Federal Farm Mortgage Corporation.*—In order to provide for emergency mortgage loans on a more liberal basis than that of the regular land-bank loans, including second-mortgage loans, a supplemental fund of $200,000,000 was made available to the Land Bank Commissioner in the Farm Mortgage Act of 1933. Later the Federal Farm Mortgage Corporation was organized with authority to float bonds guaranteed by the Federal Government to secure funds to make such loans. The land banks exchange their consolidated bonds for Federal Farm Mortgage bonds or sell their consolidated bonds to the Federal Farm Mortgage Corporation for cash. The outstanding Land Bank Commissioner loans were all taken over by the Farm Mortgage Corporation, but the term "Land Bank Commissioner loans" is still used to designate the Farm Mortgage Corporation loans. The directors of the corporation are: The Governor of the Farm Credit Administration, the Secretary of the Treasury, and the Land Bank Commissioner. Its lending operations are carried on by the 1 and banks and the Land Bank Commissioner.

(*c*) *Intermediate credit banks.*—There are 12 intermediate credit banks under the supervision of the Intermediate Credit Commissioner. The stock in these banks is all owned by the United States Government, and the board of directors consists of the same persons as the board of directors of the land bank operating in the same district. The banks rediscount short-term agricultural paper held by banks, production credit associations, banks for cooperatives, and in a few cases make direct loans to cooperative associations. Paper is not eligible for rediscount if its length of term is over 3 years; most of the loans rediscounted run for from 3 to 6 months.

(*d*) *Production credit corporations.*—There are 12 of these corporations. Their stock is owned by the United States Government. The membership of the board of directors is identical with that of the land bank of the district. General supervision is exercised by a production credit corporation commissioner. The Production Credit Corporation makes no loans, but supervises the operations of the production credit associations described below.

(*e*) *Production credit associations.*—These are about 600 in number. They are similar in character to the national farm-loan associations, but operate in the field of short-term credit. Their stock is of two classes: Class A, subscribed by the Production Credit Corporation of the district; and class B, subscribed by borrowers in an amount equal to 5 percent of the loans. About four-fifths of the stock is of class A. The directors are elected by the class B stockholders, subject to the approval of the president of the Production Credit Corporation of the district. The loans, which generally run for from 3 months to 1 year, are practically all rediscounted at the Federal intermediate credit banks. An attempt is being made to consolidate the administrative staffs of these associations with those of the national farm-loan associations. In some cases there is a joint secretary-treasurer, and in others there is joint or adjacent housing.

(*f*) *Banks for cooperatives.*—These consist of 12 district banks and the Central Bank for Cooperatives. They are supervised by the Cooperative Bank Commissioner. Each district bank for cooperatives has the same general agent and board of directors as does the land bank of the district. The capital is nearly all owned by the Federal Government, a small proportion being held by borrowers. The loans are of two classes—facility loans, which run for from 5 to 10 years and are intended to furnish permanent working capital and equipment; and commodity loans, which run for from 3 to 9 months and are intended to finance marketing operations. At the close of 1935 the cooperative banks had outstanding $50,000,000 in loans, of which nearly $20,000,000 were held by the Central Bank. Only two of the district banks—those of Berkeley and Spokane—had as much as $3,000,000 of loans outstanding. These two banks and the Central Bank for Cooperatives accounted for over 60 percent of the total volume of business.

(*g*) *Regional Agricultural Credit Corporation.*—These 12 corporations are now in liquidation, having been supplanted by the Production Credit Corporations and associations described above. Their stock is all owned by the Reconstruction Finance Corporation, which defrays their operating expenses. They are supervised by a divisional director appointed by the Governor of the Farm Credit Administration. The volume of loans outstanding on June 30, 1936,

was slightly over $36,000,000; the operating expense for the year ending on that date was $2,240,413.

(*h*) *Emergency Crop and Feed Loan Section.*—At the end of 1935 the Farm Credit Administration had 11 regional offices for the administration of emergency loans. The Director of the Crop and Feed Loan Section is responsible to the Production Credit Commissioner. Loans are made under authority of an act of Congress approved February 20, 1935, which authorized the Farm Credit Administration to make loans for the fallowing of land, the production and harvesting of crops, and the purchase and production of feed for livestock. Loans are restricted to applicants who have the necessary land and equipment for cultivating it, or livestock for which feed is required, and who are unable to obtain credit from commercial sources or from Production Credit Corporations. The loans are secured by a first lien on the crop which is to be produced or the livestock which is to be fed.

Loans of this general type were authorized by acts of Congress in certain years beginning in 1918 to meet local emergencies. The scope of the program was greatly enlarged in 1931; for the years 1931 to 1935, inclusive, the average number of loans per year was about 490,000. The peak was in 1933, when 633,586 loans were made; the number in 1935 was 424,216. The average size of the loans made in 1935 was $135. The balance outstanding on December 31, 1935, was about $107,000,000, representing 62 percent of the loans made in 1935, 42 percent of those made in 1934, and 29 percent of those made before that year. The administrative costs incurred in 1935 for 1935 crop loans amounted to $1,753,657, about three-fourths of which was covered by interest collections on the 1935 loans.

In addition to these loans the Emergency Crop and Feed Loan Section administers drought relief loans, authorized by an act of Congress approved June 19, 1934. Most of these loans have been secured by crop liens. These loans were made on very liberal terms, and collections were slow. On December 31, 1935, there were outstanding $65,000,000 out of a total of $72,000,000 loaned in 1934 and 1935. The administrative costs incurred for the 1934–35 operations were $1,527,832.

No drought loans were made in 1935–36, presumably because the responsibility now falls on the Resettlement Administration. The relation between the Farm Credit Administration and the Resettlement Administration lending programs are discussed below in the section dealing with the latter organization.

(*i*) *Joint-stock land banks.*—The organization of these banks was authorized by the Federal Farm Loan Act of 1916, in order to give privately organized companies the opportunity to handle farm mortgages in competition with the Federal land banks. The Emergency Farm Loan Act of 1933 prohibited their making new loans and provided for their liquidation. They are being closed out under the supervision of the Farm Credit Administration. There were 44 banks in existence at the end of 1935 (excluding three in receivership), with $205,000,000 of bonds outstanding and $265,000,000 book value of assets. The latter figure compares with $442,000,000 in assets at the end of 1933 and $337,000,000 at the end of 1934.

(*j*) *Credit unions.*—These are local cooperative credit organizations, urban as well as rural, which make small loans to their mem-

bers. The stock is subscribed by members, and the organizations are supervised by a sectional director under the supervision of the Governor of the Farm Credit Administration. No loan may exceed $200, and the length of maturity may not be greater than 2 years. As of June 30, 1936, loans outstanding amounted to $3,952,105. For the year ending on that date the unions reported a profit of $85,000, while the administrative expense of the Farm Credit Administration for supervising them was $113,000.

2. *Resettlement Administration.*—This organization is authorized to make rehabilitation loans to farmers who do not qualify for loans through production credit associations or national farm-loan associations. As of October 30, 1936, 384,731 such loans had been made, in addition to 467,064 outright grants. The total amount of the loans was $96,000,000; that of the grants about $19,000,000. These loans include, in addition to standard rehabilitation loans, emergency feed and crop loans, 1936 emergency drought loans, and a number of miscellaneous types of lending, most of them of a character closely akin to relief. The loans are secured by chattel mortgages on property acquired by the borrower from the proceeds of the loan, by assignments of the proceeds of the sale of products, and in some cases by liens on other assets of the borrower, including real-estate mortgages. Loans are also made to community and cooperative associations to establish, refinance, or extend the scope of cooperative facilities and services, and to individuals to enable them to purchase participating rights in community and cooperative associations. The total amount of loans in these two classes is slightly above $1,000,000; these are included in the total shown above.

As was noted in a previous section, the rehabilitation loans made by the Resettlement Administration are somewhat similar in character to those made by the Emergency Crop and Feed Loan Section of the Farm Credit Administration. Both are made only to farmers who cannot get credit from commercial sources or from production credit associations. However, the Farm Credit Administration now serves a somewhat better class of credit risks, loans of a strictly relief character having been left in large part to the Resettlement Administration since its lending activity started. In theory a Resettlement Administration loan is made only to a farmer who cannot satisfy the credit requirements of the Farm Credit Administration, though it is understood that there has been some competition in certain areas and some refunding of Farm Credit Administration loans into Resettlement Administration loans.

The principal differences are, first, that the Resettlement Administration loans are made for the purchase of equipment and for subsistence, as well as for crop and feeding operations; and, second, that the Resettlement loan is part of a larger program which includes farm and home management advice and direct grants for subsistence. Its representatives work out with the farmer a complete plan of farm operations covering a period of years. Instruction in home economics is furnished to farmers' wives. Because of the more intensive type of service rendered, the administrative costs of the Resettlement Administration are very much higher. One field representative of the Farm Credit Administration administers 12 or 15 times as many loans as does a representative of the Resettlement Administration.

3. *Commodity Credit Corporation.*—This Corporation was created in 1933 for the purpose of extending loans to farmers on the security of staple agricultural products held in storage. Its life as a Government agency terminates on April 1, 1937. It has a capital stock of $100,000,000, of which $3,000,000 is owned by the Treasury and $97,000,000 by the Reconstruction Finance Corporation. Additional funds are obtained by borrowing from the Reconstruction Finance Corporation. The bulk of the Corporation's loans have been made on the security of corn and cotton; a small amount has also been lent on turpentine and rosin. The amounts which the Corporation lends per unit of product are fixed by the President of the United States. In some cases loans are placed with commercial banks under commitments from the Commodity Corporation to take them over on demand. A charge of 1 percent is made for such guarantee. On April 10, 1936, the Corporation had outstanding loans of over $296,000,000.

II. ADMINISTRATIVE COSTS

(Year ended June 30)

1. *Farm Credit Administration and subsidiary offices*

	1936		1935	
	Number employees	Administrative expense	Number employees	Administrative expense
Washington operating divisions of Farm Credit Administration:				
Land Bank Division	221	$825,000	284	$946,000
Cooperative Credit Division	83	357,000	58	277,000
Intermediate credit	10	53,000	8	48,000
Production credit	24	135,000	26	152,000
Agricultural Credit Corporation Division	2	4,000	4	10,000
Regional agricultural credit corporations	10	65,000	15	72,000
Federal credit unions	28	114,000	7	26,000
Total, operating divisions	378	1,553,000	402	1,532,000
Emergency crop loans, field and Washington supervision	1,737	4,636,000	1,559	4,860,000
District banks and corporations under supervision of Farm Credit Administration:[1]				
12 Federal land banks	[2] 7,539	[3] 24,863,000	[2] 9,497	33,810,000
Less Federal Farm Mortgage Agency expense		9,123,000		19,899,000
Net		15,740,000		13,911,000
12 Federal intermediate credit banks [4]	[2] 722	2,003,000	[2] 884	2,578,000
12 Production credit corporations [4]	[2] 367	1,798,000	[2] 367	1,406,000
12 cooperative banks	[2] 215	762,000	[2] 191	848,000
12 Regional agricultural credit corporations [4]	990	2,240,000	1,741	3,718,000
Federal Farm Mortgage Corporation [4] [5]		[6] 9,880,000		21,104,000
Less Farm Credit Administration service expense		*516,000*		*619,000*
Total	9,833	31,907,000	12,680	42,746,000
Service divisions of Farm Credit Administration [7]	1,390	3,595,000	1,404	3,714,000
Grand total	13,338	41,691,000	16,045	52,852,000

[1] These figures do not include national farm loan associations and production credit associations under supervision of the Farm Credit Administration.

[2] Includes joint employees of these 4 permanent credit institutions.

[3] For 1935, includes $19,898,552, incurred by Federal land banks as agents of the Federal Farm Mortgage Corporation; for 1936, $9,123,333.

[4] Stock 100 percent owned by the United States.

[5] The Federal Farm Mortgage Corporation's affairs are being conducted on a service basis by the Farm Credit Administration, Federal land banks as agents, Federal Reserve banks as fiscal agents, and the Treasury of the United States.

[6] For 1935, includes disbursements for expenses on a service basis incurred by the Federal land banks as agents, in the amount of $19,898,552; and expenses on a service basis of $1,205,062 incurred by the Farm Credit Administration, Treasurer of the United States, and the Federal Reserve banks on behalf of the Corporation. For 1936, includes $9,123,353 incurred by Federal land banks, and $756,140 incurred by the other agencies mentioned.

[7] Includes financial, research, examination, and legal services.

2. *Resettlement Administration, rehabilitation program*[1]

	1936
Number of employees	8,831
Salary expense	$10,090,688

[1] Includes expenses connected with grants and other rehabilitation activities, in addition to the lending function which is discussed in this section. Comparable data for 1935 not available.

3. *Commodity Credit Corporation*

	1936	1935
Number of employees	84	85
Salary expense	$179,862	$167,704
Total operating expense	$554,827	$330,572

B. Home Loan Agencies

The principal agencies which extend or supervise the extension of credit to urban home owners are the Federal Housing Administration and the Federal Home Loan Bank Board.

I. SUMMARY OF ACTIVITIES

1. *Federal Housing Administration.*—The Federal Housing Administration was established by the National Housing Act (48 Stat. L. 1246), approved June 27, 1934, and amended by various acts in 1935 and 1936. It is directed by an Administrator, who is appointed by the President. Though the Administration is not a corporation in form, it exercises the most important powers of a corporation. Thus the Administrator in his official capacity can sue and be sued in a State or Federal Court, may issue debentures which are guaranteed as to principal and interest by the United States Government, and may pay his administrative expenses without regard to the provisions of law which in general govern the expenditure of public funds. His administrative expenses are paid out of funds made available by the National Housing Act, and do not require specific appropriation from year to year, though this will not be the case under the provisions of existing law after June 30 next. He reports his operating budget to the Bureau of the Budget, but it is understood that this is a voluntary arrangement on the part of the Administrator.

The more important activities of the Federal Housing Administration may be summarized as follows:

Modernization credit loans.—The Federal Housing Administration guarantees loans made by approved banks, building and loan associations, and other financial institutions for repairs and improvements upon real property and the installation of fixed equipment. The total liability of the Administration may not exceed $100,000,000. With respect to loans made by any one institution, the present limit of liability is 10 percent of the total volume of loans made by that institution; on loans made before April 1, 1936, it was 20 percent. The authority to make modernization loans lapses on April 1, 1937. The amount outstanding on June 30, 1936, was $395,882,687. The amount of claims paid under the insurance provisions up to June 30, 1936, was $2,249,035.

Mutual mortgage insurance.—The Federal Housing Administration administers a mortgage insurance fund in connection with the guaranty of real-estate mortgages on nonfarm residential properties. Apartment buildings housing more than four families are excluded. The loans are made by banks, building and loan associations, and other financial institutions, and must have a provision for amortization over a period not to exceed 20 years. The loans insured may not exceed 80 percent of the appraised value of the respective properties, and the total liability may not exceed $200,000,000. The Federal Housing Administration also guarantees mortgages of large-scale housing projects for low-income groups. The total liability limit is $10,000,000. One-half of 1 percent per annum is charged as insurance premium.

As of June 30, 1936, the Federal Housing Administration had 1,283 employees in its Washington office. The number of field offices was 90 and there were 2,337 field employees.

2. *Federal Home Loan Bank Board.*—The Federal Home Loan Bank Board consists of five members appointed by the President. It has supervision of the following agencies: The 12 Federal Home Loan Banks, the Federal Savings and Loan Insurance Corporation, the Home Owners' Loan Corporation, and the Federal savings and loan associations.

(*a*) *Home-loan banks.*—Each of these banks has under it a large number of member associations, including State building and loan associations, and also Federal savings and loan associations of the type described below. The home-loan banks make loans and advances to members on the security either of home mortgages or of United States bonds. Advances are also made to nonmember mortgagees on the security of mortgages insured by the Federal Housing Administration. Funds of the banks may also be invested in United States Government bonds.

The stock of the home-loan banks is in part owned by the United States Government and in part by the member associations. The home loan banks have authority to issue debentures and bonds, which may be either the obligations of the individual bank or consolidated obligations of the 12 banks.

(*b*) *Federal savings and loan associations.*—These are building and loan associations whose common stock is owned by private individuals. The number on November 30, 1936, was 1,106. The United States Government invests in their preferred stock up to a maximum of $100,000 for each association, subject to the provision that the subscription of the Government may not exceed that of the private shareholders. The United States also invests in full-paid income shares. Its total investment may not exceed 75 percent of the total share investment. On July 31, 1936, the investment of the United States in the two classes of stock was $49,213,000, most of it in income stock. The associations are under the general supervision of the Home Loan Bank Board.

(*c*) *Home Owners' Loan Corporation.*—The Home Owners' Loan Corporation was organized to refinance the loans of distressed home owners. The Federal Home Loan Bank Board is the board of directors of the Home Owners' Loan Corporation. The Corporation ceased to accept applications for new loans on June 13, 1936. The total amount of loans closed was $3,093,288,213. The Corporation

also had invested $63,142,700 in shares of building and loan associations. The principal task of the Corporation is now the gradual liquidation of the outstanding loans.

The capitalization of the Corporation is $200,000,000, all of which is owned by the United States Government. It has outstanding about $3,000,000,000 of bonds, most of which were issued in exchange for the mortgage obligations of borrowers. For the year ending June 30, 1936, the Corporation reports 2,212 employees in the home office, 5,117 in regional offices, and 10,729 in State and district offices.

(*d*) *Federal Savings and Loan Insurance Corporation.*—The purpose of this Corporation is to guarantee the share liabilities of building and loan associations and similar home-financing organizations. The Corporation has $100,000,000 capital, all of which was subscribed by the Home Owners' Loan Corporation. The members of the Home Loan Board are the directors of the Federal Savings and Loan Insurance Corporation. It is directed by a manager who is appointed by the Board. Federal savings and loan associations are required to insure their shares accounts with the Corporation, and State-chartered building and loan associations are permitted to do so. The maximum amount insured for any one shareholder is $5,000.

The Corporation also has authority to purchase the assets of insured associations or make contributions to restore them to normal operating capacity. The Corporation acts as conservator or receiver of all Federal savings and loan associations in default and may accept appointment as conservator or receiver of a State-chartered association.

The Corporation collects an insurance premium of one-eighth of 1 percent of the share and creditor liabilities of the insured associations. On June 30, 1936, the number of accounts insured was 1,023,511 in 1,363 associations.

II. INTERRELATIONS OF THE FEDERAL HOUSING ADMINISTRATION AND THE FEDERAL HOME LOAN BANK BOARD

Attention is called to the following ways in which the responsibilities and activities of the Federal Housing Administration and those of the Federal Home Loan Bank Board overlap, conflict, or are closely related to one another.

(*a*) *Contacts with mortgage institutions.*—Many of the institutions which have relations with the Federal Housing Administration as present or prospective purchasers of insured mortgages are also members or prospective members of the home-loan bank system. The Federal Housing Administration has an administrative unit which keeps in touch with associations eligible to purchase insured mortgages and makes contacts with other building and loan associations in an effort to promote the mortgage-insurance program. The Federal Home Loan Bank Board receives reports from building and loan associations and keeps files showing the condition of member associations. The 12 home-loan banks also must keep in touch with the activities of all member institutions. The Home Loan Bank Board has a staff of examiners which examines all associations members of the home-loan bank system, and also all insured nonmember associations. The Federal Savings and Loan System has a field force engaged in promotional work, which makes contact with many of the

same institutions that are visited by representatives of the Federal Housing Administration.

(*b*) *Appraisal.*—The Federal Housing Administration has a field force for appraisal of properties which are pledged under mortgages accepted for insurance. The Home Loan Bank Board has an appraisal force to appraise properties which are under the lien of mortgages that are pledged with the home-loan banks. It also appraises properties in connection with the examination of building and loan associations and in connection with the foreclosure of mortgages and the management of properties of the Home Owners' Loan Corporation.

(*c*) *Research and statistics.*—The Federal Housing Administration and the Home Loan Bank Board both have large organizations engaged in research and the compilation of statistics in the home-mortgage field. While there is a considerable degree of cooperation and division of labor between the research divisions of the two agencies neither has the full use of the results of research in the other organization and it is impossible to set up a well-organized joint program. Coordination of statistical and research work was one of the objectives in the establishment of the Central Housing Committee. This committee includes representatives of the two agencies under consideration and of other Federal agencies, such as the Resettlement Administration and the Federal Emergency Administration of Public Works, which are active in the construction of homes. The committee's accomplishments in this field are not striking. Little information goes to the Central Housing Committee that has not already been released to the public. Each agency has a large volume of information which it regards as confidential which would be useful to other agencies in the field, but never reaches them.

(*d*) *Field work.*—In the year ended June 30, 1936, the Federal Housing Administration spent $7,359,346 on its field organization, while in the same period the Home Owners' Loan Corporation spent $23,822,531 on its regional, State, and district offices. Moreover, the Home Owners' Loan Corporation has in Washington six assistant general managers supervising the field offices, each having an office staff, while the Federal Housing Administration has five deputy administrators, each with an office staff, supervising its field offices.

(*e*) *Home-building service.*—The Federal Housing Administration gives technical advice in regard to construction plans for all new building financed by guaranteed mortgages. The Home Loan Bank Board has recently announced a home-building service plan for houses constructed under mortgages purchased by approved members of the home-loan banks.

III. ADMINISTRATIVE COSTS

(Year ended June 30)

1. *Federal Housing Administration*

	1936
Number of employees	3,660
Salary expense	$8,023,375
Total operating expense	$11,337,849

(Not in operation for full year 1934–35.)

2. *Federal Home Loan Bank Board*[1]

	1936	1935
Number of employees	278	206
Salary expense	$858, 148	$654, 124
Total operating expense	$1, 040, 747	$858, 317

[1] Data do not include Home Owners' Loan Corporation and Federal Savings and Loan Insurance Corporation, which are shown separately, nor the 12 home-loan banks.

3. *Home Owners' Loan Corporation*

	1936	1935
Number of employees	18, 059	16, 958
Salary expense	$29, 331, 119	$27, 854, 155
Total operating expense	$35, 548, 136	$37, 426, 579

4. *Federal Savings and Loan Insurance Corporation*

	1936	1935
Number of employees	17	10
Salary expense	$40, 561	$23, 620
Total operating expense	$111, 238	$86, 546

C. Reconstruction Finance Corporation

The Reconstruction Finance Corporation was organized on February 7, 1932, under the provisions of an act of Congress which provides that it shall have succession until January 22, 1942, unless sooner dissolved by an act of Congress. Its powers to make loans lapses on February 1, 1937. The Corporation is controlled by a board of seven directors, consisting of the Secretary of the Treasury and six others. The capital stock of the Corporation, which amounts to $300,000,000, is owned by the United States Government. The Corporation has issued bonds and notes which are guaranteed by the United States Government. The amount outstanding on June 30, 1936, was $4,281,629,666.67, of which amount $4,030,000,000 was held by the Treasury. The Corporation has 32 field offices and a personnel of 1,635 employees in Washington, and 1,678 in the field offices (as of June 30, 1936).

I. SUMMARY OF ACTIVITIES

1. *Loans to banks and trust companies.*—The most extensive financial operations of the Reconstruction Finance Corporation, aside from allocations to other governmental units, have been those necessitated by the banking crisis of 1933. The advances of the Reconstruction Finance Corporation to banks consist of two items: (*a*) purchases of preferred stock and capital notes and debentures of weak banks, most of which were made in order to prevent failures or to enable banks to qualify for deposit insurance; (*b*) loans to failed banks made in order to facilitate reorganization, or to hasten

the redistribution of funds to depositors. Loans to facilitate reorganization are now made by the Federal Deposit Insurance Corporation.

Of the preferred stock and capital notes and debentures of banks, $688,000,000 was outstanding on September 30, 1936, out of a total of $1,053,000,000 that had been disbursed since the beginning of the program. Since banks are required to retire these securities only over a period of 20 years, this investment will, in the normal course of business, be one of the last items in the portfolio of the Reconstruction Finance Corporation to be liquidated. Other bank loans, on the contrary, are being repaid rapidly, the total outstanding on the date mentioned being $228,000,000, out of a total of $1,966,000,000 which had been disbursed.

2. *Direct loans to industry.*—An item of considerable importance consists of the direct loans to industrial and commercial business, which were authorized by an amendment to the Reconstruction Finance Corporation Act passed in June 1934. These loans are intended to provide intermediate credit to sound borrowers who, for one reason or another, cannot get the credit they need at commercial banks. This service is very similar to one that is offered by the Federal Reserve banks.

3. *Loans to mortgage companies.*—These loans are chiefly for the financing of hotels, apartment buildings, office buildings, and similar structures which on the one hand do not qualify as industrial and commercial businesses within the meaning of the law authorizing direct loans to industry, and on the other hand do not qualify for credit at the home-lending agencies, which in general do not provide for the financing of residential buildings which house more than four families. At present, this business is chiefly concentrated in the RFC Mortgage Co., incorporated in 1935. All the stock of this company, $20,000,000, is owned by the Reconstruction Finance Corporation, and its personnel is practically all made up of employees of the Reconstruction Finance Corporation.

The RFC Mortgage Co. has the following authority: (*a*) To make loans secured by first mortgages on income-producing properties of the types referred to above, where financing is necessary and cannot otherwise be obtained on reasonable terms; (*b*) to make loans, under certain restrictions, to distressed holders of first-mortgage bonds; (*c*) to make first-mortgage loans in aid of the construction of new buildings. The company does not make direct loans to property holders who are eligible for modernization loans or mutual mortgage loans insured by the Federal Housing Administration, but it does purchase mortgages insured by the Administration.

4. *Other activities.*—The scope of the current lending operations of the Reconstruction Finance Corporation is indicated in the following tabulation of disbursements to and collections from governmental agencies during the third quarter of 1936:

Disbursements and collections of the Reconstruction Finance Corporation during the third quarter of 1936[1]

Debtor	Disbursed	Repaid
Banks and trust companies [2]	$15,515,978	$164,224,215
Building and loan associations		609,888
Insurance companies	4,000,000	802,269
Mortgage-loan companies	[3] 23,259,058	6,995,086
Credit unions		2,617
Agricultural financial institutions [4]	5,702,740	75,093,061
Railroads	9,202,667	48,374,144
State funds (insuring deposits of public moneys, etc.)		579,059
Fishing industry	21,200	3,261
Industrial and commercial business [5]	7,104,814	1,939,460
Self-liquidating projects [6]	16,232,748	291,647
Repair of damage from earthquakes, floods, etc	620,084	986,869
Drainage, levee, and irrigation districts	5,771,429	103,568
Mining industry	520,000	25,000
Total	87,950,718	300,030,144

[1] Excludes transactions arising from allocations to other Federal agencies.
[2] Includes purchases of preferred stock and capital notes and debentures.
[3] Chiefly to the RFC Mortgage Co. Includes subscription to stock of that company.
[4] Includes Commodity Credit Corporation.
[5] A considerable volume of industrial and commercial lending is included in the data for mortgage-loan companies given above.
[6] These are chiefly loans to municipalities and other local governmental units.

In addition to these lending operations the corporation acts as a financial intermediary in connection with certain operations of other governmental agencies. It purchases securities from the Public Works Administration for resale or collection. Up to September 30, 1936, such purchases had been made in the amount of $451,236,468, of which $310,758,918 had been resold or collected at maturity, leaving a balance of $140,477,550. It pays the expenses of liquidation of the regional agricultural credit corporations and the operating losses of the Federal Housing Administration and its credit losses on modernization (title I) loans.

Reconstruction Finance Corporation funds had been allocated and disbursed to other Federal governmental agencies, up to September 30, 1936, as follows:

Secretary of Agriculture for crop loans	$115,000,000
Capital of regional agricultural credit corporations	20,000,000
Governor of Farm Credit Administration	40,500,000
Regional agricultural credit corporations, for expenses	14,576,843
Secretary of the Treasury to pay for capital of Federal home loan banks	104,542,000
Secretary of the Treasury to pay for capital of the Home Owners' Loan Corporation	200,000,000
Land Bank Commissioner and Federal Farm Mortgage Corporation for loans to joint-stock land banks and to farmers	202,600,000
Federal Housing Administration	44,000,000
Commodity Credit Corporation, purchase of stock	97,000,000
Loans to Commodity Credit Corporation	95,808,924
For direct relief	1,499,998,176
Total	2,434,025,943

A condensed statement of the assets and liabilities of the Reconstruction Finance Corporation as of September 30, 1936, follows:

ASSETS

Loans to nongovernmental agencies:[1]	
Banks and trust companies	$929,976,420
Building and loan associations	3,377,810
Insurance companies	38,384,312
Mortgage-loan companies	149,108,259
Credit unions	298,033
Agricultural financial institutions	35,020,486
Railroads	349,260,577
State funds (insuring deposits of public moneys, etc.)	1,230,271
Fishing industry	620,776
Industrial and commercial business	57,690,456
Self-liquidating projects	[2] 184,417,834
Repair of damage from earthquakes, floods, etc	1,410,681
Drainage, levee, and irrigation districts	61,778,073
Mining industry	1,186,000
Relief advances to State and local governments	295,994,711
Securities purchased from Public Works Administration	140,477,550
Loans and allocations to Federal governmental agencies	[3] 2,434,025,943
Interest on funds allocated to Federal agencies	20,710,323
Preferred stock installment contracts	724,661
Cash	1,055,074
Collateral purchased	3,512,411
Accrued interest and dividends	31,015,075
Furniture and fixtures	542,621
Miscellaneous	2,486,771
Total	4,744,305,128

LIABILITIES

Liabilities for funds held as cash collateral and deposited with bids	3,293,656
Funds held for other agencies	5,941,100
Trust funds	33,687,142
Notes	4,011,749,667
Accrued interest	8,297,118
Stock	500,000,000
Surplus and reserves	141,487,720
Miscellaneous liabilities	39,848,725
Total	4,744,305,128

[1] Includes loans to Federal land banks and joint-stock land banks.
[2] Figure includes loans for financing repair of damage from earthquakes and other disasters in 1933.
[3] See preceding table.

It will be seen that something less than one-half the liabilities of the Corporation are covered by claims against nongovernmental agencies, the other half representing funds which have been disbursed for relief or used for the purchase of capital stock in other governmental corporations, to furnish them funds for loan operations, and to pay their operating expenses. The stock of the Corporation and $3,795,000,000 [1] of its notes are owned by the United States Treasury. The notes held by the Treasury are therefore in large part simply a bookkeeping offset against Reconstruction Finance Corporation nominal claims for funds which have been routed through the Reconstruction Finance Corporation and used for relief and other emergency purposes.

[1] As of July 31, 1936.

II. ADMINISTRATIVE COSTS

(Years ended June 30)

Reconstruction Finance Corporation

	1936	1935
Number of employees, Washington and agency offices	3,313	3,470
Administrative expense, Washington and agency offices	$9,097,879	$8,398,904
Expense of custodians	$1,776,679	$2,265,540
Total operating expense	$10,874,558	$10,664,444

D. Banking and Currency Supervisory Agencies

The three agencies which have primary responsibility for the supervision of banking, currency, and short-term credit are the Federal Reserve System, the Federal Deposit Insurance Corporation, and the Office of the Comptroller of the Currency. The Reconstruction Finance Corporation and the Secretary of the Treasury also have some authority in this field. We shall present first a summary statement of the activities of the three agencies first mentioned; then a classification of the functions which they have to perform, with notations of the way in which the functions are apportioned among these and other agencies.

I. SUMMARY OF ACTIVITIES

1. *Comptroller of the Currency.*[2]—The Comptroller's Office has five main functions. These are: (*a*) The chartering of new national banks, a task which has been lessened in importance by reason of the fact that the number of banks has been decreasing in recent years, whereas up to the middle twenties the trend was upward; (*b*) examination of national banks and enforcement of laws regulating their activities, which are now probably the most important activities of the Comptroller's Office; (*c*) issuance and redemption of the national bank notes, a task which is rapidly disappearing because of the calling of all the bonds which had the circulation privilege; (*d*) issuance to the Federal Reserve banks of the notes which they issue to the public; (*e*) appointment and supervision of receivers of failed national banks. This last task has been greatly changed with reference to future receiverships, because the law now requires that the Federal Deposit Insurance Corporation shall be appointed receiver of all failed national banks. However, there are still over 1,100 national banks with individual receivers who require detailed supervision. The Comptroller also exercises general supervision over the operations of the Federal Deposit Insurance Corporation as receiver of the banks which have failed since the present arrangement went into effect.

In addition to these duties, the Comptroller serves as a member of the board of directors of the Federal Deposit Insurance Corporation. He compiles operating statistics covering the operations of national banks, as well as the results of liquidation of failed banks, and collects from State banking offices data concerning operations of State banks. He exercises various administrative powers over

[2] For other agencies of the Treasury Department, see chs. III, XII, XIII, and XV.

national banks, including such matters as the establishment of branches, consolidations, retirement of stock, dissolution, and so on.

The Comptroller levies assessments on the national banks to cover the expense of examination, and, with respect to this part of the expenditures of his office, he is not under the supervision of the Budget Bureau nor audited by the General Accounting Office. The expenses connected with administration of closed banks are also reimbursed by the banks, as are part of the expenses connected with the issuance of Federal Reserve notes. Other expenses of the Comptroller's Office are covered out of appropriated funds.

2. *Federal Reserve System.*—The Federal Reserve System consists of 12 Reserve banks, 6,387 member banks (as of Dec. 31, 1935), the Board of Governors of the Federal Reserve System, the Open Market Committee, and the Federal Advisory Council. The capital stock of the Federal Reserve banks is owned by the member banks, but since the dividend is limited to 6 percent (an amount which is always earned and paid), and since the surplus is virtually owned by the Federal Government, the member banks have no financial interest in the operation of the system. The board of directors of each Reserve bank consists of nine members, of whom six are elected by the member banks and three are appointed by the Board of Governors.

The Reserve banks' most important functions arise out of correspondent relations with the member banks. The Reserve banks hold as deposits the entire legal reserves of their members. They are empowered to make loans to members under a variety of prescribed conditions. They also make working capital loans, of not more than 5-year maturity, to industrial or commercial businesses, either through the medium of financing institutions, or directly. In emergencies, when authority has been granted by at last five members of the Board of Governors, they may make direct loans to individuals by discounting secured notes. They are also empowered to purchase in the open market bankers' acceptances and bills of exchange and obligations of the Unitd States and certain other securities. They issue Federal Reserve notes, which constitute the most important element of the paper currency of the country. They examine State member banks and receive condition reports from them.

The Board of Governors of the Federal Reserve System consists of seven members appointed by the President, subject to confirmation by the Senate. The Board is empowered to "review and determine" the rates charged by the Reserve banks on all their discounts and advances, to regulate the amount of credit extended by banks on security collateral, and to fix the maximum rate of interest which may be paid by member banks on time and savings deposits. It also may, with certain limitations, change the requirements relative to reserves to be held by member banks against deposits.

The Federal Open Market Committee, which consists of the members of the Board of Governors and five elected representatives of Federal Reserve banks, controls the open-market operations of the Reserve banks. The Federal Advisory Council is composed of 12 members, one selected by the board of directors of each Federal Reserve bank. This council makes recommendations concerning policies and practices of the Federal Reserve Board and of the Reserve banks.

All of the activities of the Reserve System so far enumerated have to do with the control of the general credit situation, making money

abundant and cheap when it is desired to encourage expansion of business activity, and raising rates and making money scarce and dear when restriction is deemed necessary. This is the main function of the Board of Governors of the Reserve System. It is quasi-legislative in character.

The Board and the banks have in addition a number of administrative responsibilities, only a part of which have any necessary connection with the main task. The Reserve banks act as clearing houses and collecting agents for their member banks and as depositories and fiscal agents of the United States. The Board examines the Federal Reserve banks and requires statements and reports from them, and has supervision over their operations. It exercises a considerable range of administrative powers in connection with the relations between member banks and their affiliates; approves or disapproves interlocking directorates involving member banks; passes on applications of State member banks to establish out-of-town branches and on applications of national banks for authority to exercise trust powers, and operates a settlement fund for settlement of balances due between Reserve banks. The Board passes on applications of State banks for membership in the Federal Reserve System, but has no discretion regarding the entrance into the System of any bank which is granted a charter as a national bank by the Comptroller of the Currency.

The expenses of the Board of Governors are met by assessments on the Federal Reserve banks. The Reserve banks derive all their income from their own loan and investment operations. Neither the Board nor the banks come under the supervision of the Bureau of the Budget, and the General Accounting Office does not audit their records.

3. *Federal Deposit Insurance Corporation.*—This is a governmental corporation, its stock being owned jointly by the United States Government and the Federal Reserve banks. The stock is nonvoting and does not pay dividends. The board of directors of the Corporation consists of the Comptroller of the Currency and two appointed directors, one of whom acts as chairman and chief executive officer of the Corporation. The principal function of the Corporation is to furnish insurance to depositors in insured banks, which include all the member banks of the Federal Reserve System and approved nonmember State banks. The insurance covers deposits up to $5,000. The income of the Corporation is derived from two sources (*a*) the interest on investments of about $300,000,000 (U. S. Government bonds), and (*b*) assessments on insured banks, amounting to one-twelfth of 1 percent annually on their total deposits. The operating budget of the Corporation is submitted to the Bureau of the Budget (under an Executive order), but its accounts are not audited by the General Accounting Office.

The Corporation has authority to pass on the admission to the insurance fund of banks not members of the Federal Reserve System, but has no discretion as to the admission of any bank which is accepted as a member bank by the Federal Reserve System, or is chartered by the Comptroller of the Currency as a national bank. The Corporation examines nonmember State banks and receives reports of condition from them. It acts as receiver for closed national banks under the supervision of the Comptroller of the Currency, and may act as receiver for closed State banks, if appointed by the proper

State authority. The corporation has authority to make loans to banks in distress or purchase their assets in order to facilitate a merger with another bank and thus avoid the necessity of liquidation. It compiles statistics of the condition of all insured banks, and carries on a program of research on banking problems.

The Reconstruction Finance Corporation possesses a considerable degree of control over the banking system by virtue of its position as owner of preferred stock. The Corporation's activities in connection with banks are described in the section of this report which deals with our recommendations.

II. FUNCTIONAL CLASSIFICATION

In the following outline we show the relationships of Federal organizations for the control of credit from a different viewpoint, grouping together the agencies which are concerned with a specific function:

1. CONTROL OF THE FEDERAL STATUS OF BANKS

(*a*) *National banks.*—Chartering and forfeiture of charters, Comptroller of the Currency.

(*b*) *Membership in the Federal Reserve System.*—Board of Governors of the Federal Reserve System controls admission of State banks, but has no control over entrance through issuance of charter as national bank.

(*c*) *Membership in deposit insurance fund.*—Federal Deposit Insurance Corporation controls entry of State nonmember banks, but has no control over entry of banks either under national charter or as State member banks. The Corporation may, however, terminate the insurance of any bank. Such action in the case of a national bank leads automatically to receivership proceedings; in the case of a State member bank it leads automatically to suspension of rediscount privileges at Federal Reserve banks.

2. EXAMINATION AND REPORTS

(*a*) *National banks.*—Examined by the Comptroller of the Currency and file reports of condition with him. The Board of Governors of the Federal Reserve System and the Federal Deposit Insurance Corporation also have authority to examine, with the consent of the Comptroller, but in practice accept reports by the Comptroller.

(*b*) *State member banks.*—Examined by Reserve banks and also by State banking authorities; render reports of condition to both these agencies and also to Federal Deposit Insurance Corporation.

(*c*) *Insured nonmember banks.*—Examined by and file reports with the Federal Deposit Insurance Corporation; also State banking authorities.

(*d*) The Reconstruction Finance Corporation sometimes examines banks, by agreement with the bank, when it owns preferred stock of capital debentures, or proposes to buy such securities, though its general practice is to accept reports of the other Federal examining agencies.

(*e*) The Federal Deposit Insurance Corporation is authorized to review the reports of examination of member banks of the Reserve System made by the Comptroller and the Reserve Board, but cannot examine the banks except by permission of the Comptroller, in the case of a national bank, and of the Reserve Board in the case of a State member bank.

3. AID TO DISTRESSED BANKS

(*a*) *Reconstruction Finance Corporation.*—Purchase of preferred stock and capital debentures.

(*b*) *Federal Deposit Insurance Corporation.*—Purchase of assets of insured banks to facilitate merger.

(*c*) *Federal Reserve banks.*—Emergency loans.

4. RECEIVERSHIP AND LIQUIDATION

(*a*) *National banks which failed before the passage of the Banking Act of 1935.*—Receivers appointed by and responsible to the Comptroller of the Currency. (As of Dec. 31, 1936, there were 1,173 such receiverships.)

(*b*) *National banks failing since the passage of the Banking Act of 1935.*—Comptroller of the Currency must appoint the Federal Deposit Insurance Corporation as receiver. Comptroller supervises the activities of the Federal Deposit Insurance Corporation as receiver.

(*c*) *Insured State banks.*—Receiver appointed by State bank authority (possibly in a few States by the courts). In 30 States the Federal Deposit Insurance Corporation may be appointed receiver. As of December 31, 1936, the Federal Deposit Insurance Corporation administered 17 such receiverships.

(*d*) Reconstruction Finance Corporation loans to receivers secured by the assets of uninsured closed banks to hasten distribution of funds to depositors.

5. CONTROL OF GENERAL CREDIT SITUATION

(*a*) *Rediscount rates of Federal Reserve banks.*—Set by Federal Reserve banks, subject to review and determination by the Board of Governors. In case of dispute, final authority has been exercised by the Board of Governors.

(*b*) *Required reserve ratios of member banks.*—Fixed by law, but subject to change, within limits, by the Board of Governors.

(*c*) *Open market operations of Federal Reserve banks.*—Controlled by Open Market Committee, which consists of the members of the Board of Governors and five elected representatives of the Reserve banks.

(*d*) *Relations with foreign central banks.*—Subject to the control of the Board of Governors; usually conducted by the Federal Reserve Bank of New York.

(*e*) *Collateral lending by member banks.*—Board of Governors has special authority. Nonmember banks which make loans to brokers in registered security exchanges must agree to submit to similar regulation.

(*f*) *Margin requirements for advances to customers by stock-exchange brokers.*—Controlled by regulations issued by the Board of Governors of the Federal Reserve System; information necessary for enforcement of compliance is collected by the Securities and Exchange Commission.

(*g*) *Maximum interest paid by banks on time and savings deposits.*—(a) Member banks: Controlled by Board of Governors; (b) nonmember insured banks: Controlled by Federal Deposit Insurance Corporation.

(*h*) *Stabilization fund.*—Controlled by the Secretary of the Treasury, administered by the Federal Reserve Bank of New York.

(*i*) The Secretary of the Treasury also has in reserve the power to enter into agreements with the Board of Governors and the Federal Reserve banks for the purchase of not more than $3,000,000,000 of Government bonds by the Reserve banks from the Treasury; also in the event that the Reserve System declines to enter into such agreement, to issue up to $3,000,000,000 in greenbacks. He can also exert great influence over the credit situation by transferring United States funds between the Reserve banks and depositary commercial banks, or holding them in cash in the Treasury.

6. COMPILATION OF BANKING STATISTICS

(*a*) *Operations of national banks and receivership data for national banks.*—Comptroller of the Currency.

(*b*) *All member banks.*—Board of Governors (data for national banks are drawn from the Comptroller's reports).

(*c*) *All insured banks.*—Data compiled by the Federal Deposit Insurance Corporation, using reports of the Comptroller of the Currency and of the Board of Governors for national banks and State member banks, respectively.

(*d*) *All State banks, including insured banks.*—Comptroller collects data from State banking supervisors, consolidates and publishes them.

(*e*) *Miscellaneous banking and financial data.*—Statistics concerning bank operations collected by a number of agencies are published by governmental agencies. For example, the New York City Clearing House collects clearing data and these are republished in the annual reports of the Comptroller. Federal Reserve Bank of New York collects data on the turn-over of bank deposits and publishes them in its Monthly Review. Data on interest rates collected by various agencies are published by the Board of Governors in the Federal Reserve Bulletin, also information on gold holdings of central banks and other foreign banking data. Data on production and industrial consumption of gold collected and published by the Director of the Mint. The Survey of Current Business publishes banking and financial data compiled by other agencies. The Bureau of Agricultural Economics publishes some data on interest rates paid by farmers.

7. RESEARCH ON PROBLEMS OF BANKING CONTROL AND CREDIT POLICY

(*a*) Extensive research is carried on by the Board of Governors; by some of the Federal Reserve banks, especially that of New York; by the Federal Deposit Insurance Corporation; and by the Division of Research and Statistics of the Treasury.

8. SHORT-TERM LENDING

(*a*) *Direct loans to industry.*—The Federal Reserve banks and the Reconstruction Finance Corporation offer a duplicate service in working-capital loans; Reconstruction Finance Corporation also makes mortgage loans of a type not made by the Federal Reserve banks.

(*b*) *Loans to agriculture.*—See section A above.

9. CURRENCY

(*a*) *Federal Reserve notes and Federal Reserve bank notes.*—Issued to the Federal Reserve banks and paid out by them. These are obligations both of the issuing Reserve bank and of the United States Government. The credit operations which give rise to the assets back of the notes are supervised by the Board of Governors. The engraving, printing, and issuance of notes are the responsibility of the Comptroller of the Currency, who is reimbursed by the Federal Reserve banks for the expense incurred. The Bureau of Engraving and Printing prepares the notes.

(*b*) National-bank notes originally issued by national banks under the supervision of the Comptroller of the Currency; now in process of retirement, all the bonds which underlie the notes having been called for payment.

(*c*) *United States notes.*—Amount fixed by law; redemption and reissuance under control of the Secretary of the Treasury.

III. ADMINISTRATIVE COSTS

(Year ended June 30)

1. *Comptroller of the Currency*

	1936	1935
Number of employees	850	920
Salary expense	$2,446,024	$2,219,703
Total operating expense	$3,248,308	$3,056,678

(For 1935 $2,792,810 and for 1936 $3,017,630 paid from assessments on national banks.)

2. *Board of Governors of the Federal Reserve System*

	1936	1935
Number of employees	345	343
Salary expense	$1,080,125	$995,095
Total expense	[1] $1,881,064	[1] $2,137,242

[1] Includes new building expense; $773,271 in 1935 and $318,567 in 1936.

3. *Federal Deposit Insurance Corporation*

	1936	1935
Number of employees	750	738
Salary expense	$1,817,830	$908,037
Total operating expense	$2,592,288	[1] $1,332,210

[1] For 6 months ended June 30, 1935.

PART II. RECOMMENDATIONS CONCERNING CREDIT-GRANTING AGENCIES

The proper organization of lending agencies which have ceased, or practically ceased, to make new loans and are engaged simply in the collection of debts due them and the liquidation of securities owned, presents a problem which is very different from that involved in the interrelationships of agencies that have a permanent lending function, or of temporary agencies during the period of their principal lending activity. We shall consider first the allocation among governmental agencies of the work of collecting loans and liquidating investments of types which are no longer being made, or are scheduled for early discontinuance. The organization of the agencies which have permanent credit functions in connection with agriculture will be discussed next; then the permanent home-loan agencies.

A. Liquidation of Temporary Agencies

The two most important agencies which have substantially completed their task of credit extension and are now engaged in liquidation are the Home Owners' Loan Corporation and the Reconstruction Finance Corporation. Other agencies which are in liquidation or, under the provisions of existing law, are shortly to cease lending, include the Commodity Credit Corporation (lending authority expires Apr. 1, 1937), Public Works Administration (lending authority expires June 30, 1937), and the joint-stock land banks and the regional agricultural credit corporations, which are already in liquidation. There may also be mentioned the notes held by the Farm Credit Administration evidencing advances made from the revolving fund created under the Agricultural Marketing Act ($115,712,244.32 on Jan. 31, 1936) and some odds and ends of securities left over from wartime financial activities, such as securities received by the Secretaries of War and of the Navy on account of the sale of war supplies, the assets of the War Finance Corporation, and the railroad obligations acquired under provisions of the Transportation Act of 1920.

It seems obvious that the liquidation of outstanding obligations requires much less specialized ability and experience than does the task of extending credit wisely to institutions whose needs and credit standing vary as widely as do those of the different classes of borrowers with whom these agencies have been dealing. The present is, therefore, an especially appropriate time to consider reduction in number and simplification of organization of lending agencies.

Alternative methods of procedure.—Two alternative lines of procedure suggest themselves. One way to attack the problem would be to set up a comprehensive liquidating agency to which would be assigned all of the assets of the agencies that no longer have any substantial lending function. The sole task of this agency would be to make collections or sell the assets as expeditiously as might be deemed consistent with public policy.

The other plan is to split up the task of collection, and assign to existing permanent agencies such parts of it as are closely related to their tasks, leaving to the central liquidating agency only those

assets whose administration does not tie in with the work of a permanent agency.

The most important differences between the two plans concern the liquidation of the Home Owners' Loan Corporation, the joint-stock land banks, the regional agricultural credit corporations, the securities obtained from the use of the Agricultural Marketing Act revolving fund, and the preferred stock of banks.

Under the first plan responsibility for all these operations would fall to the central liquidating agency. Under the second plan the Home Owners' Loan Corporation would remain with the Federal Home Loan Bank Board or, as is suggested below, with a consolidation of that agency and the Federal Housing Administration. Liquidation of joint-stock land banks and regional agricultural credit corporations would remain with the Farm Credit Administration. The central liquidating agency would have the remaining assets of the Reconstruction Finance Corporation, together with the securities held by the Emergency Administration of Public Works at the close of its lending period, and various odds and ends resulting from past lending operations which do not fit in well anywhere else.

To the extent that the task involved is purely one of liquidation, there are economies and other administrative advantages in centering the work in a single agency, and there can be little question that the idea of centralizing the task of liquidation is feasible and desirable, insofar as the business relationships involved are with institutions and individuals which do not have continuing close relations with permanent Government agencies.

On the other hand, in cases where a permanent Government agency exercises continuous supervision over the debtor institutions, and must maintain a field agency in contact with them, we believe that greater economy is likely to be effected by turning over the task of collection to such an agency than through concentrating it in a liquidating agency. Moreover, since the problem is not merely one of getting the Government's money out, but of insuring that the original purposes of the loan are fulfilled, the governmental agency responsible for supervision or support of the debtors has a vital interest in the administration of the collections.

Finally, the plan of liquidating discontinued activities through permanent agencies rather than through a temporary liquidating corporation has the advantage that it minimizes the temptation to the liquidator to prolong the work in order to protect his own job. Observation of receivership and reorganization procedure leads one to the conclusion that this is an important consideration. In any agency which is only a liquidating agency, the better the job the employees do the more quickly they must find other employment. In a permanent agency which has been assigned a temporary task, the same consideration applies to certain employees, but in less acute form. At least the management at the top has more incentive to wind up the temporary jobs and employees engaged in those tasks have some prospect of continued employment in other phases of the agency's work.

We believe, therefore, that the sound principle is to leave with the permanent agencies, or turn over to them, such liquidation tasks as are closely related to their own operations, and to concentrate in the general liquidating agency the collection only of such loans as do not tie in closely with the work of permanent agencies.

Under either plan there must be some general liquidating agency for collecting loans and selling securities of types in which other existing agencies have no special interest. For this work two agencies have been considered: First, the Reconstruction Finance Corporation; and, second, the Reserve banks, acting as fiscal agents for the Treasury. The Reconstruction Finance Corporation already has a personnel experienced in dealing with a very wide variety of types of borrowers, and the contraction or elimination of its lending activities releases personnel which might be employed in the liquidation of assets taken over from other agencies.

However, we believe that there is no real reason for continuing the life of the Reconstruction Finance Corporation as a dwindling agency after its lending operations are over. The Reserve banks are already custodians of its securities and notes and the collateral which has been deposited under them. The work of collection involves constant handling of this material, releasing and exchanging collateral, recording and releasing liens, returning instruments to borrowers, and so on. Much communication and interagency accounting between the Reserve banks and the Reconstruction Finance Corporation is necessary. As was shown above, about one-fifth of the total operating expense of the Reconstruction Finance Corporation consists of payments for custodians' services. The Reserve banks have permanent staffs which are well fitted to undertake the additional responsibilities that would be involved in making the actual collections. Moreover, the work of their staffs has been considerably lightened by the virtual cessation of the rediscounting of commercial paper for banks. They already act as fiscal agents for the Treasury and are familiar with the accounting problems involved in custody of Treasury funds. In a number of cases the regional offices of the Reconstruction Finance Corporation are housed in Reserve bank buildings, so that no space problem would be created in taking over the Reconstruction Finance Corporation's records and such of the Reconstruction Finance Corporation personnel as might be needed.

We recommend, therefore, that the Reconstruction Finance Corporation be speedily liquidated following the cessation of its lending activities, which under present law will take place on January 31, 1937. All its assets except those specified in later sections should be turned over to the Treasury, which would make payment for them in Reconstruction Finance Corporation bonds. Even if it should be decided to continue the lending functions of the Reconstruction Finance Corporation beyond the date now fixed for their termination, we recommend that its assets and liabilities be assigned to the Treasury as indicated above and arrangements for routing funds to Federal governmental agencies through the Reconstruction Finance Corporation discontinued. The Reconstruction Finance Corporation would then act as fiscal agent for the Treasury in making new loans to the public and the Federal Reserve banks in collecting them.

Federal Emergency Administration of Public Works.—The securities of the Public Works Administration should be handled in the manner just suggested in connection with the Reconstruction Finance Corporation, that is, transferred to the Treasury for collection or sale through the Reserve banks. This involves no radical innovation, as present practice is for the Public Works Administration to sell its securities to the Reconstruction Finance Corporation, and the Reserve banks perform custodian service for both agencies. Up to Septem-

ber 29, 1936, $448,000,000 out of a total of $599,000,000 Public Works Administration bond purchases had been sold to the Reconstruction Finance Corporation; $243,000,000 had been resold to the public or collected by the Reconstruction Finance Corporation up to September 1, 1936.

Regardless of the decision as to whether the Reconstruction Finance Corporation or the Treasury and Federal Reserve banks should be the general liquidation agency, the following recommendations are offered concerning the liquidation of certain types of loans through other agencies.

Transfer of preferred stock of banks from the Reconstruction Finance Corporation to the Federal Deposit Insurance Corporation.—The Reconstruction Finance Corporation held on September 29, 1936, $702,151,215.66 in preferred stock and capital notes and debentures of banks.[3] This is by far the largest item in its portfolio, with the exception of advances and allocations to other Federal governmental agencies. This stock was issued in connection with the Government's program for the rehabilitation of the banking structure after the banking holiday of 1933. Since the end of 1934 retirements have exceeded new investments by more than $150,000,000. The banks are required to amortize the investment over a period of 20 years and may retire it more rapidly if they are able to do so without jeopardizing the interests of depositors. Up to September 29, 1936, $364,912,317 had been retired.

It is recommended that this entire investment be transferred to the Federal Deposit Insurance Corporation, the Government purchasing additional stock in the Corporation and retiring a corresponding amount of the Reconstruction Finance Corporation bonds now held by the Treasury. Thereafter all funds collected by the Federal Deposit Insurance Corporation from the redemption of preferred stock and capital notes should be used to retire the Government's investment in Federal Deposit Insurance Corporation stock, except for a reasonable reserve for the purchase of additional preferred stock. Dividends on preferred stock and interest on capital notes and debentures in excess of the direct cost of management of the preferred stock investment should also be used for the retirement of the stock of of the Federal Deposit Insurance Corporation.

The basic reason for this recommendation is that the problem of administration which arises in connection with the preferred stock is not simply one of getting the money, but rather of preventing the soundness of the banks' capital structure from being impaired by too rapid a liquidation. Essentially the whole program of issuance of preferred stock has precisely the same objective as has the program of deposit insurance administered by the Federal Deposit Insurance Corporation. The system of bank examinations now administered by the Comptroller of the Currency, the Reserve banks, and the Federal Deposit Insurance Corporation also has the same objective, namely, that of protecting the monetary supply of the country and the individual interests of depositors against bank failures. The responsibility for the maintenance of bank solvency rests on the banks' supervisory agencies just mentioned.[4] The Government

[3] Capital notes and debentures are issued by State banks in cases where the State law does not permit the issuance of preferred stock. The figure given above includes $13,636,159.59 loans secured by preferred stock.

[4] Pt. III of this report deals with possible redistribution of functions or consolidation of the supervisory agencies.

has invested $300,000,000 in the Federal Deposit Insurance Corporation for the purpose of protecting bank depositors and has made an investment of $700,000,000 in preferred stock of banks through the Reconstruction Finance Corporation for precisely the same reason. Both agencies have to maintain close contact with the banks. While there is apparently satisfactory cooperation between the two agencies, the splitting of the function creates confusion in the minds of the public and a divided responsibility on the part of bank officers. Moreover, on the assumption that the Federal insurance of bank deposits is a permanent arrangement, cases may arise long after the lending activities of the Reconstruction Finance Corporation and other emergency agencies have ceased, where it will be advantageous to purchase preferred stock in banks rather than close them and pay off the depositors. The Federal Deposit Insurance Corporation is the logical agency to exercise this function.

While the Reconstruction Finance Corporation in most cases accepts the examination reports of the Comptroller of the Currency, the Federal Reserve bank, or the Federal Deposit Insurance Corporation, it also maintains an examining staff and makes supplemental examinations, with the consent of the bank concerned, in cases where it is not satisfied with the report of the regular examining agency.[5] The Reconstruction Finance Corporation reports that on June 30 it had 34 employees (with total annual salaries of $165,790) in the Bank Administration Section of its Examining Division. This is a larger number than were employed in reviewing bank reports in the Federal Deposit Insurance Corporation. The figure given does not include the costs of the secretary's office, the treasurer's office, the legal divisions, and the other overhead expenses of controlling Reconstruction Finance Corporation's relations with open banks, nor does it include secretarial and other assistants.[6]

The Federal Deposit Insurance Corporation is empowered to purchase assets of banks to facilitate consolidation and prevent failures and to make loans upon assets for the same purpose. Purchases of preferred stock by the Reconstruction Finance Corporation are frequently negotiated by the Federal Deposit Insurance Corporation or by the Comptroller of the Currency, with a view to restoring solvency. Thus a bank with impaired capital may be taken care of by any one of three procedures. First, the Reconstruction Finance Corporation may purchase preferred stock or capital debentures, in which case the bank goes ahead without change of organization; second, the Federal Deposit Insurance Corporation may purchase undesirable assets, or lend on them as collateral, arranging for the purchase of the acceptable assets by another bank, in which case the two banks are consolidated; or, third, the bank may be closed and the depositors paid off by the Federal Deposit Insurance Corporation. In any case the loss resulting from the deterioration of assets, if the bank does not regain solvency, finally falls on the banks which contribute to the insurance reserve fund of the Federal Deposit Insurance Corporation. And the Federal Deposit Insurance Corporation is the agency which has the responsibility of safeguarding

[5] The Chairman of the Federal Deposit Insurance Corporation said in 1935: "In the capital rebuilding program, in better than 90 percent of the cases they have always taken our examination." (Hearings before House Committee on Banking and Currency, 74th Cong., 1st sess., H. R. 5357, pp. 135–136.)

[6] It does, however, include expense incurred by the Reconstruction Finance Corporation in connection with loans to closed banks, which are recommended for transfer not to the Federal Deposit Insurance Corporation but to the Treasury.

against bank failures, and is best equipped to decide when a given bank is able to retire its preferred stock. Now that the great mass of bank lending operations of a salvage character has been completed, no good purpose seems to be served by separating the functions of lending to effect consolidations from that of lending to avoid the necessity of consolidation or receivership.

Reconstruction Finance Corporation loans to closed banks and receivers.—In the light of the facts set forth above it might seem logical to transfer from the Reconstruction Finance Corporation to the Federal Deposit Insurance Corporation, the loans to closed banks, amounting to over 95 million dollars, now held by the Reconstruction Finance Corporation. Consideration has been given to this suggestion, but in view of the fact that the necessity for such loans no longer exists, in the case of failure of an insured bank, such transfer is not recommended. Recommendation is made elsewhere that the Federal Deposit Insurance Corporation be made receiver for all closed national banks now in receivership. If this recommendation is followed, it seems better that the Federal Deposit Insurance Corporation should not be the holder of the outstanding loans to closed national banks, since there is a possibility of conflict of interest between the holder of the loans as a preferred creditor and the depositors. These notes are therefore included in our recommendations for transfer of assets to the Treasury for collection by the Reserve banks.

Direct loans to industry.—On June 19, 1934, there was passed an act (48 Stat. L., 1105) amending the Federal Reserve Act and the Reconstruction Finance Corporation Act, which authorized both the Reserve banks and the Reconstruction Finance Corporation to make direct loans to industry. The accompanying table presents a comparison of the terms under which the two agencies are authorized to lend.

Legal qualifications and conditions for direct loans to industry, Federal Reserve banks and the Reconstruction Finance Corporation[1]

	Reserve banks	Reconstruction Finance Corporation
Type of business	An industrial or commercial business	An industrial or commercial business, including the fishing industry.
Age of business	An established business	Established prior to Jan. 1, 1934.
Financial status		Solvent, in the opinion of the board of directors of the Corporation.
Credit position	Unable to obtain requisite financial assistance on a reasonable basis from usual sources.	"When credit at prevailing bank rates for the character of loans applied for is not otherwise available at banks."
Purpose of loan	For working capital	For maintaining and increasing the employment of labor.
Maturity of obligation	Not over 5 years	Not over 5 years.
Security required	"On reasonable and sound basis"	"Adequately secured, in the opinion of the board of directors of the Corporation."
Amount of funds available.	$139,299,557	$300,000,000.
Amount of any one loan		Not over $500,000.
Form of transaction	(*a*) Direct loan; or (*b*) discount for or purchase from financial institutions; or (*c*) advance to financial institution on the security of such obligation; or (*d*) commitments with regard to such loans or advances to financial institution; ((*b*), (*c*), and (*d*) require 20 percent participation of financial institution in the risk).	(*a*) Direct loans; or (*b*) loan in cooperation with bank; or (*c*) purchase of participation.

[1] Charles O. Hardy and Jacob Viner, Report on the Availability of Bank Credit in the Seventh Federal Reserve District, p. 30.

It will be noted that there is very little difference in the scope of the direct-loan operations of the two agencies. Businessmen are free to place their applications with whichever agency they think is likely to be more liberal. In a number of cases concerns have applied simultaneously to both, and in other cases applicants who have been refused at one have applied at the other.

On November 18, 1936, the Federal Reserve banks had outstanding $26,859,000 of these advances and had commitments involving an additional $22,138,000. On September 30, 1936, the Reconstruction Finance Corporation had disbursed $65,675,968 on account of these loans, of which $7,985,512 had been repaid, leaving $57,690,450 outstanding.

It seems obvious that the duplication of administrative work in the making of these loans involves unnecessary cost, confusion in the minds of the public, and the possibility of undesirable differences of standards between the agencies. Whether such loans are continued indefinitely or not, the entire function should be concentrated in one place or the other.

Our recommedation depends on the policy of Congress as to the permanent or temporary character of this lending function. If such loans are to be continued indefinitely, we believe that the entire block now held by the Reconstruction Finance Corporation should be transferred, at an appraised valuation, to the Federal Reserve banks. If, however, direct loans to industry are regarded as an emergency type of operation suitable for discontinuance whenever the general program of emergency loans is terminated, they should be transferred to the Treasury and handled by the Reserve banks as fiscal agents, as recommended above, and the making of such loans by the Reserve banks discontinued.

Regardless of whether any of the recommendations made in the preceding paragraphs are adopted or not, we recommend that the industrial advisory committee which now serves in connection with these loans, both at the Reconstruction Finance Corporation and the Federal Reserve banks, be abolished. In this connection the following passage from the report of our Treasury investigation is relevant:

> We are not convinced that the industrial advisory committee is a necessary or desirable feature of the system of Reserve bank, direct lending. This statement in no wise reflects on the ability or public spirit of the individuals who compose the committee which advises the Chicago Federal Reserve Bank. Members of the committee are taking a great deal of interest in their work and giving it a very large proportion of their valuable time. Unquestionably in a number of cases their advice has been extremely helpful. However, the work of the committee is essentially a duplication of the work of the lending officers, and results in an undesirable division of responsibility. It also makes it incumbent on the applicant to plead his cause, if he presents it in person, before two tribunals.
>
> The Reserve bank officers whose responsibility it is to see that the funds are disbursed in accordance with the law seem to give to each application that is reported favorably by the industrial advisory committee the same careful scrutiny as they would give if the advisory committee had not already investigated. The bank has, in fact, declined a number of applications which have been favorably recommended by the advisory committee. In the majority of instances this was due to the fact that investigations made by the bank's examining force uncovered facts which had not come to the attention of the advisory committee. In other cases there was a genuine difference of judgment.
>
> On the other hand, it appears that when the judgment of the advisory committee is negative, though the case is reviewed by the Reserve bank officials, the finding of the advisory committee carries more weight than when it is

favorable. This is not surprising, since an outstanding unfavorable feature brought out in the report of the industrial advisory committee may suffice to debar the application without further detailed study. To a considerable extent, therefore, the advisory committee, which was intended to bring into the picture a nonbanking viewpoint, and probably to bring about greater liberality, works out as one more hurdle which the applicant must clear. In any case the advisory committee, unless it provides itself with a staff of trained investigators comparable to that of the Reserve bank, cannot be expected to take final responsibility for the decisions.

Moreover, the tendency is for the advisory committee, in dividing up its work, to place the initial responsibility for reporting on a given loan upon that member of a committee who comes from the State or city, or general area, in which the applicant's place of business is located, and in some cases the unfavorable judgment of this one committee member seems to have been nearly decisive. Such an arrangement can easily give rise to the accusation that the decision of the committee is affected by the committee member's political or business connections in the applicant's community. Representatives of the survey came across a considerable number of rumors of this sort. Regardless of the merits of these accusations (and we have no real evidence that there was any basis for them), we believe that such complications would be minimized and the work of the Reserve banks put on a sounder basis if the work of appraising loan applications were unified and professionalized.[7]

Other recommendations concerning certain types of temporary loans are made in sections B and C of this report, which deal relatively with farm credit and home-owners' credit.

B. Farm Lending Agencies

In general the farm-lending program of the Federal Government is well organized, as a result of several years' of effort in the consolidation and coordination under the Farm Credit Administration of the work of miscellaneous agencies. We shall consider first the liquidation of the outstanding farmers' loans of types that have been or are shortly to be discontinued; second, the organization for administration of agricultural credit activities that are relatively permanent. The Farm Credit Administration is charged by law or by Executive order with administrative responsibilities in connection with the following types of loans which are no longer being made: (*a*) Loans of the Regional Agricultural Credit Corporations; (*b*) loans made from the Agricultural Marketing Act revolving fund; (*c*) loans of the joint-stock land banks.

Regional agricultural credit corporations.—These corporations were created by the Reconstruction Finance Corporation and that organization owns their outstanding stock. By the terms of Executive order dated March 27, 1933, all the administrative functions connected with the operation of these corporations, except those relating to expenses, were transferred to the Farm Credit Administration. Because their principal functions had been taken over by the production credit corporations, the regional corporations were placed in liquidation early in 1934. As of December 31, 1935, their loans remained outstanding to the extent of $43,400,186, or 14.1 percent of the amount that had been lent. On June 30, 1936, the amount outstanding had been reduced to $36,026,384. Of the repayments to December 31, 1935, $35,866,363, or 24.4 percent, had been effected through transfer of loans to the production credit associations. The

[7] The same, pp. 37–38. It is perhaps appropriate to point out that the staff member who is primarily responsible for this section of the present report was the Administrator in charge of the survey of the availability of bank credit in the seventh Federal Reserve district and joint author of the report quoted.

Farm Credit Administration collects the loans chiefly through the services of agents who are paid on a per diem basis. For the year ended June 30, 1936, the total administrative expenses was $2,240,000, which was paid by the Reconstruction Finance Corporation.

We suggest that in order to eliminate unnecessary accounting and transactions between agencies, and to facilitate liquidation of the Reconstruction Finance Corporation, the stock of the Regional Agricultural Credit corporations be sold by the Reconstruction Finance Corporation to the Production Credit associations of the respective districts at an appraised valuation; with the Government purchasing stock in the Production Credit Corporation and paying off indebtedness to the Reconstruction Finance Corporation in amounts corresponding to the valuation of the loans.

It would appear that, since the loans are of a character similar to those made by the Production Credit associations, economy might result from the use of the services of the Production Credit associations in the servicing of Regional Agricultural Credit Corporation loans. We are advised that the Farm Credit Administration has already done this to the extent that it seems economical; however, we believe that transfer of the responsibility for the costs of collection from the Reconstruction Finance Corporation to the Production Credit corporations would exert a wholesome pressure in the direction of further efforts along this line.

Joint-stock land banks.—No recommendation is offered concerning the liquidation of these agencies as it seems to be properly located in the Farm Credit Administration.

Commodity Credit Corporation.—We recommend that the liquidation of the Commodity Credit Corporation be placed under the supervision of the Cooperative Credit Division of the Farm Credit Administration, which will be in position to utilize the facilities of the cooperative banks and the Production Credit associations as they may be required to facilitate collections. This division already has charge of the collection of loans made under the Agricultural Marketing Act of 1929, which were still outstanding at the end of 1935 in the amount of $115,858,541. Of this amount, $71,425,775 consisted of loans to the Grain Stabilization Corporation. The remainder were loans to cooperatives. Of the latter, $33,919,345 were classed as "effective merchandising" loans, $8,677,735 were facility loans, and $1,835,686 as commodity loans. These loans are now being administered by the Cooperative Division of the Farm Credit Administration. Agents are sent out directly from the Division to contact the borrowers. There is no separate allocation of funds and no data in the reports indicating the cost of the operations involved.

It has been pointed out that the Farm Credit Administration does not now have facilities and personnel to deal with the sale of commodities involved in dealing with loans without recourse. However, it will not be difficult to absorb these facilities now existing in the Commodity Credit Corporation, and it should be possible to economize materially in the collection of loans from the agencies and areas where the Farm Credit Administration already has extensive facilities for collection and contacts with the borrowers involved. The collection of Regional Agricultural Credit Corporation loans has involved the taking over of a line of grain elevators so that the

problem of disposing of properties is already involved in the administration of the loans.

Banks for cooperatives.—Since the intermediate credit banks now rediscount practically all loans made by these banks, consideration has been given to the possibility of amalgamating them with the intermediate credit banks. Part of the work of the banks for cooperatives consists of the making of commercial loans of a type similar to those formerly made by the intermediate credit banks. The remainder, however, consisting on June 30, 1936, of $14,823,672 in facility loans, represents an illiquid type of advance which probably could not be made directly by the intermediate credit banks without impairing their present excellent credit standing. Consideration should be given to the feasibility of reducing the number of these banks. Of the 13 banks, only 3 had outstanding at the end of 1935 as much as $3,000,000 in loans. However, the cost of maintaining the separate organizations is not much greater than would be the cost of branch offices or field representatives of a smaller number of banks. This is true because of the well-developed system of joint facilities and joint supervision which the banks for cooperatives share with the farm land banks, the intermediate credit banks and the production credit corporations.

Emergency crop, feed, and seed loans.—As was noted in part I, the work of this division of the Farm Credit Administration is similar to that of the Rehabilitation Division of the Resettlement Administration. Both make loans on the security of chattels to farmers who cannot qualify for needed credit from the production-credit associations or from commercial banks. There has been, undoubtedly, an undesirable overlapping of activity between them. Nevertheless, there is probably justification for the continuance of crop-loan agencies in both divisions, assuming that it is the policy of the Government to continue a program of the present scope. The Farm Credit Administration crop loans (as distinguished from the old drought loans) are business operations conducted on the basis of reasonable security, though they involve higher risks than local banks are prepared to assume. The Resettlement Administration loan program is closely related to its program of relief grants and rehabilitation. What is needed for the present seems to be a better delimitation of the respective fields, so that there may be no competition, or refinancing of the loans of one agency by advances from the other. Progress appears already to have been made in this direction. We recommend that any future drought loan activities which may be necessary be centered in the Resettlement Administration. We do not believe that the lending activity of the Resettlement Administration could advantageously be transferred elsewhere until the completion of its general rehabilitation work. Nor are we prepared to recommend that the crop loans of the Farm Credit Administration be transferred to the Resettlement Administration until the permanent character of that agency's future organization and work are more settled.

Land-bank commissioner loans.—Consideration has been given to the suggestion that the so-called land-bank commissioner loans made by the Federal Farm Mortgage Corporation be transferred to the Resettlement Administration on the ground of its quasi-relief character. It seems clear to us, however, that the balance of argument is decidely against such action. The bulk of these loans are secured by

second mortgages on properties on which a farm-loan bank has a first mortgage. The actual work of collection of a land-bank commissioner loan is done by a Federal land bank, and in many cases it is able to use the facilities of a national farm-loan association for this purpose. Interest and amortization payments on these loans are scheduled to fit in with the farmer's payment on his land-bank loan, and much would be lost, both from the standpoint of the Government and from that of the farmer, if administration of the two classes of mortgage loans were separated.

C. Home Lending Agencies

In another section of this report we have described the home lending agencies of the Government, and have commented on the extent of overlapping and duplication between them. We offer here our recommendations with regard to the future relationships of these agencies. In formulating these recommendations it has been assumed that the functions performed by all these agencies are to be continued with the exception of the Home Owners' Loan Corporation, which is already in liquidation.

Home Owners' Loan Corporation and the Federal Housing Administration.—It was noted in a previous section of this report that in the last fiscal year the Federal Housing Administration spent over $7,000,000 on its field organization and the Home Owners' Loan Corporation over $23,000,000. The work of these field organizations is very similar, and the similarity will grow greater as the Federal Housing Administration grows older and is confronted with a larger volume of defaults on its guaranteed loans. Both agencies have the same problems of property management and resale of properties. Their legal staffs are specialists in the same field of law. Their research staffs collect very extensive data concerning the trend of real-estate values in the same communities. The same questions of policy as to the treatment of delinquent debtors will arise in both agencies. No important public purpose is served by keeping them separate, and we have no hesitation in recommending that they be consolidated.

However, the best method of effecting the consolidation is a question of some difficulty because of certain differences in the character of the assets and the liabilities of the two organizations. The Home Owners' Loan Corporation may direct loans; the Federal Housing Administration guarantees mortgage loans made by approved private lenders. Consequently the Federal Housing Administration has a large and growing contingent liability while the liabilities of the Home Owners' Loan Corporation are direct obligations incurred in raising the funds which it used to make loans. The Home Owners' Loan Corporation owns a portfolio of about a million loans, the great majority of which are believed to be good.

The Federal Housing Administration owns no mortgage loans but comes into the possession of properties which are foreclosed by private agencies. Hence the two agencies have similar problems in the management and disposal of properties. They each engage in effecting the transfer of foreclosed properties of the respective agencies. In the one case the Home Owners' Loan Corporation is the mortgagee while in the other a private agency is the mortgagee and the Federal Housing Administration acquires title after fore-

closure, if carried out by a private agency as mortgagee. However, the Federal Housing Administration does exercise some supervision over loans which have not been foreclosed. It receives reports of delinquency and gives advice and assistance to mortgagees in servicing loans that are in arrears.

We have given consideration to a suggestion that the Home Owners' Loan Corporation should sell in the open market, without recourse, such of its loans as command a market, using the proceeds to retire its bonds. If this were done, the remaining work arising in connection with the bad loans could be turned over to the Federal Housing Administration, as a service agency, and the field force of the Home Owners' Loan Corporation consolidated with that of the Federal Housing Administration.

If all the Home Owners' Loan Corporation loans were either good enough to be sold in the open market without recourse and without discount or else bad enough to be foreclosed immediately, this plan would be very satisfactory. The properties taken over could be turned over to the Federal Housing Administration for management and sale. The Home Owners' Loan Corporation would become a mere financial holding company which would pay the costs of administration of its bad loans and gradually pay off its bonds as funds were made available. This arrangement would be similar on a larger scale to that which now exists in the liquidation of the Regional Agricultural Credit Corporation.[8]

In fact, however, an uncertain, and probably large, proportion of the Home Owners' Loan Corporation's loans would fall between the two classes mentioned. They would not find a ready market, neither would they be in default. The collection organization of the Home Owners' Loan Corporation would have to be kept alive in some agency to service these substandard loans until they either rose into the salable class or fell to the class of defaulted loans. There would be a financial gain in the amalgamation of the servicing and property-management work of the two organizations, but there would be no economy in the sale of the good assets, for the simple reason that the Home Owners' Loan Corporation would be able to sell, in general, only those loans on which it was most likely to make a profit and would still have to keep up its overhead and field organizations for collecting the rest.

Moreover, there is considerable doubt as to the willingness of financial institutions to purchase the loans, and it is certain that debtors would resist the transfer. All the Home Owners' Loan Corporation loans were made to borrowers who were, or appeared to be, in distress, and the purpose of the loans was to relieve this distress. Borrowers are certain to feel that they are entitled to somewhat more lenient treatment, if their distress recurs, than they would be likely to get from a commercial lender who had no recourse to the Government. And whatever the merits of this plea, prospective buyers of the mortgages are certain to take it into consideration.

If, on the other hand, the loans are offered under the guaranty of some governmental agency, so that the new lenders and the debtors

[8] See sec. B above. It will be remembered that the actual work of liquidation is done by the Production Credit Corporations, while the Reconstruction Finance Corporation as owner of the stock of the Corporation pays the costs of administration. Proceeds of loan collections are used to retire the stock.

can hope to compose their differences with the aid of the Government, the loans can probably be sold without difficulty. In that case we see no reason to confine the experiment to the high-grade loans. The whole block, except those foreclosed, or threatening foreclosure, can be sold under a guaranty similar to that offered by the Federal Housing Administration. The servicing, legal, and property-management organizations can then be amalgamated with similar divisions of the Federal Housing Administration.

We recommend, therefore, that the Federal Housing Administration and the Home Owners' Loan Corporation be consolidated, and that the entire block of Home Owners' Loan Corporation loans which are not already in default be insured by the new corporation under a guaranty similar to that given to holders of the so-called title II mutual mortgage loans and then sold in the open market. The new corporation organized to take over the assets and liabilities of the Federal Housing Administration and the Home Owners' Loan Corporation would have an authorized capital regarded as sufficient to meet title I claims (now paid from funds furnished by the Reconstruction Finance Corporation) and any additional claims arising under title II which the equity contributed by the Home Owners' Loan Corporation and the reserve fund of the Federal Housing Administration might be regarded as insufficient to cover. The Treasury could subscribe for an amount regarded as ample to meet title I claims and at a later time increase the subscription if the equity of the Home Owners' Loan Corporation and the title II reserve should prove insufficient to meet all losses arising from the guaranty of mortgages. Since the new corporation would realize a large sum from the sale of Home Owners' Loan Corporation mortgages, the title II plan of issuing guaranteed debentures could be suspended, the mortgage insurance corporation paying off the holders of these foreclosed loans at the time when the properties were taken over. The costs of administration would be greatly reduced by the changes suggested. There would be some loss of profit on the good loans, but there would be an offset in that the entire cost of foreclosure would fall on the buyer of the securities.[9] In spite of this item, buyers could afford to take this risk in exchanging Home Owners' Loan Corporation bonds for guaranteed mortgages since the mortgages bear a much higher rate of interest. Indeed, in many cases these guaranteed mortgage loans might be exchanged for HOLC bonds with some premium on the mortgages.

The funds obtained from the sale of Home Owners' Loan Corporation mortgages would be used for two purposes—first, to provide funds which may be needed to pay off holders of defaulted mortgage loans insured by the Federal Housing Administration, thereby obviating or reducing future issues of Federal Housing Administration debentures; second, to retire Home Owners' Loan Corporation bonds. So far as practicable, Home Owners' Loan Corporation bonds should be taken in exchange for the newly issued mortgages, and any premium obtained would furnish coverage for losses on Home Owners'

[9] Under Federal Housing Administration guaranty the holder of a mortgage is required to foreclose before he has recourse to the Federal Housing Administration, and his claim for reimbursement of foreclosure costs is subordinated to the Federal Housing Administration's claim against the property for principal and interest.

Loan Corporation loans and protect the Government's equity in the stock of that Corporation.

In summary, the advantages of this plan would be—

(*a*) Elimination of the collection service of the Home Owners' Loan Corporation insofar as good loans are concerned.[10]

(*b*) Elimination of foreclosure costs.

(*c*) Consolidation of the property-management and the loan-servicing divisions of the two organizations.

(*d*) Substitution of private capital for public ownership of a large mass of mortgages, and retirement of a large volume of outstanding bonds.

(*e*) Use of funds derived from the sale of mortgages to provide for future financial needs of the Federal Housing Administration program, thereby avoiding the necessity of simultaneously retiring Home Owners' Loan Corporation bonds and issuing Federal Housing Administration debentures.

(*f*) Consolidation of research activities and legal work of the two agencies.

(*g*) Avoidance of conflicting policies, divided responsibility, and confusion in the minds of the public with respect to the Government's program for the financing of housing.

(*h*) Reduction of general overhead through the elimination of one major governmental unit.

Organization of Federal home lending agencies.—It is not necessary, in order to carry out the recommendation made in the preceding section, that either the Home Owners' Loan Corporation or the Federal Housing Administration should absorb the other. What is suggested is the merger of the Federal Housing Administration and the Federal Home Loan Bank Board into one Federal home-loan agency, to be administered by a board or an administrator, as the Congress might determine. Within this organization there would be a mortgage-insurance corporation which would take over the assets and liabilities of the Federal Housing Administration under its title I and title II guaranty and the assets and liabilities of the Home Owners' Loan Corporation. No new capital stock need be subscribed by the Treasury at the creation of this corporation except to meet title I claims, since the equity represented by Home Owners' Loan Corporation stock and Federal Housing Administration reserves should be sufficient to cover probable losses under title II after the merger. It is important, however, that the new agency should be brought under the supervision of the Federal Home Loan Bank Board or of some other coordinating agency exercising supervision over all the home lending institutions.

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[10] The profit on good Home Owners' Loan Corporation loans under the present arrangement will tend to become a vanishing factor from year to year, since a new loss factor will soon appear. As the principal is paid down the profit margin arising from the difference between the interest received on mortgages and the interest paid on bonds will decline by over 6 percent per annum, on an average, because of a similar decline in the unpaid principal. At the same time the number of installments to be collected is always equal to the number of loans. Hence costs of collection will not decline as fast as the profit margin between interest paid and interest received. Service costs will decline to some extent as the number and principal amount of loans declines, but there will soon develop, after the bad loans are foreclosed, a more steady cost of servicing which will not decline as the income from these loans declines. Hence, deficits will steadily increase, especially in the latter half of the life of the Home Owners' Loan Corporation, because the Corporation will not be in a position to replace the principal of loans as it is paid off. This consideration will not apply to institutional buyers of the mortgages, under the plan suggested above, because they will be reinvesting the principal as it is collected.

The reorganization suggested would proceed along lines similar to those which have been worked out in the Farm Credit Administration, where the Federal land banks, the Federal intermediate-credit banks, the banks for cooperatives, and the production credit corporations use common buildings for their field offices and maintain jointly legal staffs, statistical, auditing, control, and accounting services, and are governed by joint boards of directors. Joint service agencies also are maintained in Washington to service the various operating divisions. Coordination of home lending activities under a single supervisory agency would make it possible to amalgamate the legal, accounting, statistical, and research services of the various housing credit agencies, and in the field to consolidate the offices of the Federal Housing Administration with the Home Owners' Loan Corporation and those of the home-loan banks. This would eliminate the present necessity for two separate organizations to keep informed as to the financial condition of building and loan associations, since the proposed home-loan corporation and the Federal Savings and Loan Insurance Corporation would have access to the reports of examination and the files of condition reports of associations which are members of the home-loan bank system. One appraisal division would supervise the appraisal of mortgages insured under the mutual mortgage system and of mortgages offered as collateral at the home-loan banks. A single agency would serve the Federal housing institutions, and they would have full access to the research work done in connection with one another's work, which now is not the case. And a single agency would furnish technical advice and assistance to home builders, which is now offered by the Federal Housing Administration and by the Home Loan Bank Board.

It will be noted that we do not suggest that the work of the home credit agencies should be amalgamated with the home-building program of the Public Works Administration or the Resettlement Administration or any agency which may be set up to coordinate work in the field of housing construction. We have considered suggestions for such amalgamation, but it is our judgment that the work of these agencies in the low-cost housing field is more closely related to that of agencies responsible for relief and improvement of living conditions in urban areas than it is to that of the home credit agencies; hence it is recognized that such projects can be better tied in with some agency responsible for welfare work in urban communities.

RFC Mortgage Co.—To facilitate the operations under titles I and II of the Federal Housing Administration, the RFC Mortgage Co. purchases guaranteed mortgages, both regular home mortgages and large-scale housing mortgages. With the consolidation of the Federal Housing Administration and the Federal Home Loan Bank Board, it is suggested that this function of purchasing or holding guaranteed mortgages be transferred to the home-loan banks. This action would not only facilitate the operations under title II of the National Housing Act but might also be of value in connection with the liquidation of the Home Owners' Loan Corporation. To facilitate such operations by the Federal home-loan banks they should be authorized to issue debentures against insured mortgages as collateral.

If it is desired to continue the making of loans on other types of property which are now made by the RFC Mortgage Co. (chiefly office and commercial buildings and apartment houses with more than 4 families) it is recommended that the RFC Mortgage Co. be transferred to the supervision of the newly constituted Home Loan Bank Board [or Administrator].

D. Summary of Recommendations

1. That the preferred stock of banks be transferred from the Reconstruction Finance Corporation to the Federal Deposit Insurance Corporation, the Government buying stock in the Federal Deposit Insurance Corporation to cover the investment. Payment by the Government to the Federal Deposit Insurance Corporation for new stock, and payment by the Federal Deposit Insurance Corporation to the Reconstruction Finance Corporation for the preferred stock of banks, to be made with Reconstruction Finance Corporation bonds now held by the United States Treasury.

2. That the direct loans to industry, made by the Reconstruction Finance Corporation be sold to the Reserve banks if the latter are to continue making direct loans, or sold to the Treasury in the event that direct loans are presently to be discontinued.

3. That regardless of the disposition made of the outstanding direct loans, if the making of direct loans to industry is to be continued, by either the Reconstruction Finance Corporation or the Reserve banks, the industrial advisory committees be abolished.

4. That the production credit corporations purchase the stock of the regional agricultural credit corporations from the Reconstruction Finance Corporation and the Government purchase stock in the production credit corporations in corresponding amount, payment to be made in both cases in Reconstruction Finance Corporation bonds now held by the United States Treasury.

5. That all the assets of the Reconstruction Finance Corporation, other than those provided for in the recommendations listed above, be transferred to the Treasury, and a corresponding amount of Reconstruction Finance Corporation bonds held by the Treasury be canceled.

6. That the assets of the Reconstruction Finance Corporation be taken over by the Treasury and its outstanding liabilities assumed by the Treasury. In the event that it is desired to continue the Reconstruction Finance Corporation's lending activities beyond the date now fixed for its termination, it is recommended that it make future loans as fiscal agent of the Treasury.

7. That the balance of Public Works Administration loans which has not been taken over by the Reconstruction Finance Corporation be purchased by the Treasury.

8. That the collection of assets taken over by the Treasury under these recommendations be entrusted to the Federal Reserve banks as fiscal agents.

9. That the Commodity Credit Corporation be put under the control of the Farm Credit Administration and its loans liquidated through the Cooperative Credit Division.

10. That the Federal Housing Administration and the Federal Home Loan Bank Board be amalgamated.

11. That in the new agency suggested in the preceding recommendation there be created a new corporation which shall take over the assets and assume the liabilities of both the Home Owners' Loan Corporation and the Federal Housing Administration.

12. That the outstanding loans of the Home Owners' Loan Corporation for which foreclosure is not imminent, be placed under the protection of mortgage insurance of the type now offered by the Federal Housing Administration, commonly known as title II loans, and that these loans be sold to the public.

13. That the funds obtained by this operation be used in part to retire Home Owners' Loan Corporation bonds and in part to create a fund out of which losses on guaranteed loans shall be paid in cash, thereby obviating or postponing the necessity for the further issuance of Farm Credit Administration debentures.

SPEECHES

Mr. Hersey

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Mr Coyle

THE EFFECT OF GOVERNMENT LENDING AGENCIES ON BANK MANAGEMENT POLICIES AND PRACTICES.

Address of I. J. Roberts, Assistant Cashier of The Riggs National Bank of Washington, D. C., before the Departmental Conference on Bank Management of the Convention of the American Institute of Banking, Seattle, Wash., June 9, 1936.

In order to intelligently discuss the effect of Government lending agencies on bank management policies and practices, it is essential that we first know what these agencies are and what lending functions they perform. A "Survey of Government Banking" made by the American Bankers Association disclosed that 36 Federal and quasi-Federal agencies are authorized to furnish credit to industry, commerce, finance, the farmer and the home owner. Through these agencies credit of almost every description is available at low rates of interest. The loans are usually made against specified security, payments in most cases being required in monthly or yearly instalments extending from a few months to 40 years.

The outstanding loans of Government corporations and credit agencies exceed the total outstanding loans of all member banks of the Federal Reserve System in 101 leading cities. These loans, as of March 31st, aggregated $8,317,000,000, represented by:

Loans to financial institutions	$ 578,000,000
Home mortgage loans	2,952,000,000
Farm mortgage loans	2,943,000,000
Other agricultural loans	707,000,000
All other loans	1,137,000,000

These figures do not include the investment of the Reconstruction Finance Corporation in preferred stock, capital notes and debentures of banks and trust companies, amounting to $856,000,000.

The entry of the Government into the lending field dates back to 1917, when the United States Railroad Administration, the United States Shipping Board-Merchant Fleet Corporation and the Federal Land Banks were established.

The lending functions of the Railroad Administration were confined to the extension of credit to federally-controlled carriers for the purpose of raising funds for maturing obligations or for reorganizing railroads in receivership. Total loans originally amounted to over a billion dollars.

The United States Shipping Board-Merchant Fleet Corporation was originally intended as a War emergency agency, but its activities became more or less permanent. The Corporation made loans for the building and reconditioning of merchant ships, but lending operations have been suspended pending the determination by the Government of a new shipping aid policy.

FEDERAL LAND BANKS

The Federal Land Banks were originally organized in March and April of 1917 under authority of the Federal Farm Loan Act of 1916, to relieve the difficulties of farmers who desired to secure long-term credit at reasonable rates of interest and whose principal sources of credit up to that time were insurance companies and private mortgage concerns which charged high rates of interest and in addition imposed heavy renewal charges every few years. Federal Land Banks make loans only upon security of first mortgages covering farm lands and the improvements thereon. The loans are made direct or through national farm loan associations for agricultural purposes only and are repayable on an amortization basis over periods as long as 34-1/2 years.

WAR FINANCE CORPORATION

The next venture by the Government into the lending field was the creation on April 5, 1918, of the War Finance Corporation, which was designed originally to finance industries whose operations were necessary for the prosecu-

tion of the War. Its functions were extended in 1919 to include railroad financing, and in 1921 to permit advances for agricultural purposes due to distress conditions growing out of the collapse following the post-war boom. The influence of the War Finance Corporation in stabilizing credit conditions helped to restore the confidence of farmers and bankers alike and greatly relieved the financial stringency. Total advances made by the Corporation before it entered into liquidation in 1925 amounted to $690,431,000.

RECONSTRUCTION FINANCE CORPORATION

The sharp reduction in values which took place during the depression period beginning in 1929, with the resultant demoralization of our credit structure, led to the organization on February 2, 1932, of the Reconstruction Finance Corporation, through which funds were provided by the Federal Government for direct aid to agriculture, commerce, industry and financial institutions. The Corporation was also authorized to furnish funds to other Governmental agencies. Since its organization the Corporation has disbursed over eight billion dollars, of which roundly three billion dollars was for the benefit of the banking business, $1,933,000,000 for loans to banks and trust companies (including receivers), $1,057,000,000 for the purchase of preferred stock, capital notes and debentures and $11,841,000 for loans on the assets of closed banks. The extent of the operations of the Reconstruction Finance Corporation directly affecting banks and trust companies is shown by the fact that loans were authorized to 7464 banks and trust companies; authorizations were made for the purchase of preferred stock, capital notes and debentures of 6719 banks and trust companies; 1121 loans were authorized to be secured by preferred stock, and loans were authorized for distribution to depositors in 2675 closed banks.

There can be no doubt that the activities of the Reconstruction Finance Corporation have greatly strengthened our banking structure and have been generally

helpful to business, and the affairs of the Corporation have been conducted in a highly efficient and business-like manner.

The loans and investments of the Reconstruction Finance Corporation outstanding as of April 30th amounted to $2,482,020,000, distributed as follows:

Loans to financial institutions	$ 410,383,000
Loans on preferred stock of banks and insurance companies	46,053,000
Preferred stock, capital notes, and debentures	851,620,000
Agricultural loans	8,623,000
Loans to railroads (including receivers)	394,168,000
Loans for self-liquidating projects	164,891,000
Loans to industrial and commercial businesses	50,194,000
Loans to drainage, levee, and irrigation districts	54,713,000
Other loans	3,587,000
Securities purchased from Public Works Administration	143,838,000
Total loans and investments, other than interagency	$2,128,071,000
Loans to Federal Land Banks	34,365,000
Loans to Commodity Credit Corporation	291,961,000
Capital stock of, and loans to R. F. C. Mortgage Co.	17,623,000
Preferred stock of Export-Import Banks	10,000,000
Total all loans and investments	$2,482,020,000

From 1933 to 1935 there was a rapid increase in the number of Federal and Federally-controlled agencies which were established for the purpose of extending credit over a wide range of activities. It is not possible in the time available to us to discuss each of these agencies, many of which are limited in scope and are of a temporary nature. I think it will be well, however, for us to inquire into the functions of some of the larger agencies closely related to the banking business.

HOME OWNERS LOAN CORPORATION

The Home Owners Loan Corporation was established June 13, 1933, to provide emergency relief for home owners by enabling them to refinance their mortgages and prevent the loss of their homes through foreclosure. Up to March 26th of this year the Corporation has closed 1,000,749 loans, in an aggregate amount of $3,031,168,924, estimated at one-sixth of the present entire American urban home-

mortgage debt. The Home Owners Loan Corporation has stated that by helping to put the private mortgage structure of the country on a firm foundation, the exchange of over two and one-half billion dollars of liquid HOLC bonds for frozen mortgages has protected the savings of some 50,000,000 people invested in real estate loans directly or through bank deposits, shares in home-financing institutions, life insurance policies, mortgage bonds and other investments which depend on the stability of real estate values.

FEDERAL SAVINGS AND LOAN ASSOCIATIONS

Federal Savings and Loan Associations are chartered by the Federal Home Loan Bank Board under authority of an Act approved June 13, 1933. The loanable funds of an association are received through payments on shares, of which there are four types to provide for the savings of all classes, from those who can make systematic savings as low as fifty cents a month to persons who desire to invest larger sums through the purchase of fully-paid shares. Each saver or investor is a member of the association, and participates in its profits and management. An important source of funds for the associations is the purchase by the United States Government of fully-paid shares. Accounts are insured up to $5,000 each through the Federal Savings and Loan Insurance Corporation. The loans of the associations are limited to first mortgages on homes, or a combination of home and business property, and are repayable in monthly instalments in not less than 5 nor more than 20 years. These associations have had a rapid growth, the total number reported on April 30th being 1102 with resources aggregating $570,351,261. The purpose of the Federal Savings and Loan Associations is "to expand the services of local thrift and home-financing institutions operating with private funds" and the enabling Act stipulates that

> "No charter shall be granted except to persons of good character and responsibility, nor unless in the judgment of the Board a necessity exists for such an institution in the community to be served, nor unless there is a reasonable probability of its usefulness and success, nor unless the same can be established without undue injury to properly conducted existing local thrift and home-financing institutions."

FEDERAL HOUSING ADMINISTRATION

The Federal Housing Administration, created under authority of the National Housing Act, June 27, 1934, while not primarily a lending institution has had a stimulating effect upon the loaning policies of banks through its insurance functions. In its insurance activities it operates under two Titles. Under Title I approved lending agencies are insured up to 10 per cent of their total advances for modernization and repairs, and mortgage loans made by approved lending agencies up to 80 per cent of the appraised value of the property and on an amortized basis up to 20 years are insured for their full amount under Title II. In making these loans banks are performing a public service, as there is no field of business which can do more to stimulate employment and contribute to the stability of the country than the building industry. Banks have been glad to cooperate with the Federal Housing Administration in its activities, and the total of modernization and repair loans made up to May 7th amounted to $371,000,000 represented by 1,033,294 loans, of which 42 per cent were handled by national banks and 26 per cent by state banks and trust companies. The total of mortgage loans actually insured as of May 7th was 66,562 for a total of $262,329,258.

FARM CREDIT ADMINISTRATION

The banks most directly affected by Government lending agencies are those in the agricultural sections where the farmer is provided with a wide variety of credit by the agencies of the Farm Credit Administration, which was created by Executive Order on March 27, 1933, to provide a coordinated credit system for agriculture. The permanent institutions operating under the supervision of the Farm Credit Administration are the Federal Land Banks, National Farm Loan Associations, Production Credit Corporations, Production Credit Associations, Federal Intermediate Credit Banks, and Banks for Cooperatives, including the Central Bank for Cooperatives.

The first task which confronted the Farm Credit Administration upon its creation was that of stopping farm foreclosures by refinancing the burden of debt which had accumulated as the result of the depression. During the first two and one-half years more than a million applications for mortgage loans were received, and approximately 700,000 individual loans, aggregating nearly $1,900,000,000, were made.

Farm Mortgage Loans are divided into two groups, namely, Federal Land Bank loans, which are made on first mortgages only, and Land Bank Commissioner loans, which were made available to farmers who were most heavily in debt and unable to qualify for Federal Land Bank loans. Commissioner loans may be secured by first or second mortgages. Farm Mortgage Loans outstanding as of March 31st amounted to $2,877,876,000, of which $2,059,978,000 were made by the Federal Land Banks, and $817,898,000 by the Land Bank Commissioner.

Another task confronting the Farm Credit Administration was the building of a Production Credit System. About 560 production credit associations have been established, their purpose being to connect farmers with the investment market in order to obtain from it the funds used in operating their farms. Production credit associations obtain their loan funds principally by discounting the notes of their borrowers with their Federal Intermediate Credit Banks, which in turn sell their debentures to obtain loanable funds. Production credit association loans outstanding as of March 31st amounted to $116,392,000.

The Farm Credit Administration also made emergency crop loans and drought relief loans to farmers who had no other source of credit, to enable them to carry on their farm operations. Funds for these loans were appropriated by Congress and amounts outstanding as of March 31st were $104,113,000 for crop loans and $63,713,000 for relief loans.

Farmers cooperative associations generally obtain their credit requirements from the District Bank for Cooperatives or from the District Federal

Intermediate Credit Bank. Loans to Cooperatives outstanding March 31st amounted to $87,463,000.

All permanent units of the Farm Credit Administration which lend directly to farmers are cooperative in principle, each borrower owning stock in proportion to his loan. Government subscription to the capital of these units is somewhat similar to the purchase of preferred stock in commercial banks by the Reconstruction Finance Corporation.

FEDERAL CREDIT UNIONS

Federal Credit Unions, which operate under the supervision of the Farm Credit Administration, are cooperative associations of persons having a common bond of occupation or association, organized for the purpose of promoting thrift and of creating a source of credit for provident and productive purposes. Members are required to purchase shares, payable in cash or in small instalments. Savings may be withdrawn as desired, and fully-paid shares draw dividends, the average rate being four to six per cent. Funds are loaned to members only, for periods not greater than two years. Loans in excess of $50 must be secured, and may not exceed $200 or 10 per cent of the unimpaired capital of the union, whichever is greater. Interest must not exceed one per cent per month on unpaid balances. The number of Federal Credit Unions as of March 31st was 1396, with total savings of $3,000,000 and outstanding loans of $2,650,000.

EFFECTS OF GOVERNMENT LENDING OPERATIONS

From my study of the Government lending agencies, Ihave become firmly convinced that they have rendered a distinct service in helping to stabilize our economic structure at a time when it was rocked to its very foundations by the greatest depression in the history of our country, and that the Government, by providing a source of credit to the home owner, the farmer and to business in general during a period when the established financial institutions were unable to meet the extraordinary demands upon them, enabled millions of citizens to

save their homes and their farms from loss by foreclosure, and also made it possible for thousands of industrial organizations to weather the storm, saving the investments of their bond and stock holders and keeping millions of workers on the payrolls. In the main, the effects of the operations of the Government lending agencies were beneficial to the banks, by relieving them of frozen assets and even by providing them with capital funds to carry on their business. In determining whether the Federal lending agencies have been competing unfairly with the banks, the reasons which impelled the Government to undertake large-scale financing must be borne in mind, and I believe this study has shown us that there was an urgent need during the period of emergency for the establishment of practically every one of the lending agencies closely related to the banking business.

LIQUIDATION OF GOVERNMENT LENDING AGENCIES

It seems to me that bankers in general recognize these facts, but there is a growing impression that while the entry of the Government into the lending field was justified by emergency conditions, these conditions no longer exist and the Government should withdraw from those fields of endeavor which naturally belong to the privately owned banks.

The attitude of the Government with respect to retiring from the lending field was expressed by President Roosevelt in his address to the American Bankers Association in Washington in 1934, in the following language:

> "I find almost general agreement among bankers that the agencies must continue until such time as the banks and other private credit agencies are themselves able and ready to take over the lending functions; and when that time comes, I shall be only too glad to curtail the activities of these public agencies in proportion to the taking up of the slack by privately owned agencies."

The American Bankers Association is now making a study to determine whether or not some emergency organizations of the Government have not fulfilled their function and should be liquidated, and how banks may assist in such liquidation.

It is encouraging to note that the process of retrenchment in Federal lending activities has already set in. The Home Owners Loan Corporation has discontinued accepting applications and its lending functions will end on June 13th of this year. The power of the Reconstruction Finance Corporation to make new commitments will expire on February 1st, 1937, unless extended by law, and the lending functions of several other agencies will cease during 1936 and 1937.

However, events of the past few years have brought about permanent changes in our economic system and some of the lending agencies created to meet the new conditions are here to stay. Therefore, it seems to me that the best way to hasten the withdrawal of the Government from credit fields which can best be served by the banks is for the bankers to demonstrate that they can do a better job.

One way in which the banks can hasten the liquidation of Governmental agencies is by taking over some of their desirable assets. For example, the Reconstruction Finance Corporation has many loans which can be acquired by commercial banks on an attractive basis. The Comptroller of the Currency recently stated that a survey has been made to ascertain how many receivers' loans held by the Reconstruction Finance Corporation are available for banks, and it was found that there are 173 loans which are deemed suitable for banks, amounting to over $33,000,000. The Comptroller expressed the hope that every one of these loans will be taken over by banks in the vicinity of the receiverships.

EFFECTS ON BANK POLICIES AND PRACTICES.

Interviews and correspondence which I have had with bankers from all sections of the c ountry have failed to disclose that the activities of the Government lending agencies have had any material effect on the policies and practices of the city banks. The agencies of the Farm Credit Administration, however, have seriously affected the country banks by reducing the available amount of loans and discounts and making it necessary for them to find an outlet for their funds

in the investment market, particularly in Government securities. The low return on high-grade securities as compared with the rates which they were accustomed to receive on loans has so reduced the income of many of the smaller banks that they have been compelled to reduce expenses and curtail activities in every way possible, and I am told that many small banks, particularly in the South, would not be able to exist if it were not for the charges they are now compelled to collect for services which in the past were rendered free to their customers.

I believe the principal effect the Government lending agencies have had on the policies of banks in general has been to make them more aggressive in seeking new fields for credit and in trying to render a greater variety of services to their communities.

Mr. Robert V. Fleming, President of the American Bankers Association, in referring to the possibility of taking over facilities now offered by Governmental agencies, said in a recent address:

> "I do not advocate the making of unsound loans, or engaging in any practice contrary to sound banking principles, but I do believe that with the broadened facilities now available through the Federal Reserve System, and the fact that public confidence in the safety of banks has been restored, there is no longer any need for banks maintaining a high percentage of liquidity and bankers can adopt a broader, long-range viewpoint in dealing with their customers.
>
> "I do not propose that we should not always have in mind the need for maintaining an adequate degree of liquidity and the soundness of the credit extended, but I have seen statistics recently, which I believe to be accurate, showing that these agencies of Government at the present time are extending credit in a volume in excess of one quarter of the total loans made by all the chartered banks in the country. Where the Government has to continue to function in such capacity, it must be financed, and to a great extent it is the banks which must do the financing; hence, we find the situation where the Government is extending credit to the public at a reasonable rate and, on the other hand, is financing itself, largely through the banks, at the lowest rates of interest we have ever known in our history.
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> "I am sure you can see how this strikes at the heart of bank earnings. It is my belief that the people prefer to deal with chartered institutions, carefully supervised by national or state

authorities, rather than directly with Government agencies which cannot function as elastically as private organizations. Therefore, I believe bankers should explore the possibility of handling these credits at a reasonable rate of interest to the public, thereby helping the government to reduce its expenses and, in turn, augment bank earnings."

The experience in making loans under Title I of the National Housing Act has been so satisfactory that many banks are now making modernization and appliance loans on an amortization basis both with and without the cooperation of the Federal Housing Administration. There is also an upward trend in the extension of credit on real estate security, a rapidly increasing proportion of these loans being amortized over periods of ten, fifteen and twenty years. While probably the larger amount of these loans are made under Title II of the National Housing Act, there is a marked tendency on the part of banks and trust companies to make loans of this character without insuring them under the Federal Housing plan.

Many banks are also making instalment loans of every character, including automobile loans and personal loans, and there is a widespread belief that the field of consumer credit is a sound one that can be cultivated by the banks to their own advantage as well as to the benefit of the consuming public.

So far as country banks are concerned, I believe the outlook is much brighter for an increasing demand for credit. While the banks cannot hope to compete with the Government in the matter of low interest rates, information brought out at the recent Conferences on Banking Service conducted under the auspices of the American Bankers Association, indicates that there is a large volume of desirable loans available to banks which are willing to go after the business vigorously and to adjust their interest rates to a level in keeping with existing conditions.

I believe the situation with respect to agricultural loans was well expressed in a recent address delivered by Hon. W. E. Myers, Governor of the Farm

Credit Administration, when he said:

> "The Farm Credit Administration has neither the resources nor the desire to monopolize the field of farm credit. Our job, as I see it, is to supplement and not to supplant existing private agencies. Although our job is one of supplementing, our credit institutions are going to be somewhat competitive. I don't deny that. With the return of private agencies to the farm loan field this competition has become more evident. I am very glad to see private agencies return, for it bespeaks improving conditions in agriculture and improving confidence in the welfare and the future of the industry. *** Commercial banks certainly have a vital part to play in the financing of those types of farm production which they choose to handle. However, it seems to me that there is a need and a place for both private and cooperative agencies in the farm financing field and that reasonable competition on a proper plane will result in better service to farmers and will be in the public interest. It is very easy to overemphasize competition, especially when just recovering from a depression. There will be a greater volume of credit business for all credit agencies as recovery continues and becomes more broadly extended."

In conclusion, I feel that such competition as does exist between the Government lending agencies and the privately owned banks offers a challenge to the bankers of the country to demonstrate that they are both able and willing to extend sound credit at fair rates of interest to meet every reasonable demand. I believe the bankers will accept this challenge in a spirit of helpful cooperation and that the younger generation of executives who have the good fortune to secure their training through the American Institute of Banking will play a large part in developing our banking structure and in placing it on a higher plane than it has ever occupied before.

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OLD AND NEW CREDIT FIELDS FOR BANKS

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Presented at Executive Session
Kansas Bankers Association
Kansas City, Mo., May 5, 1936
by A. G. Brown, President,
The Ohio Citizens Trust Company,
Toledo, Ohio

Credit sources and credit needs are as old as business itself. Through the years the credit needs of the average community have been handled mainly by the commercial bank, which gathered the savings and surplus funds from those who had an excess and loaned them on the security of real and personal property, or on financial statements of business, to those who could profitably use them. Thus, through the natural and intelligent utilization of credit, backed by its own resources, the American community has been securely builded as the foundation stone of our own great Nation; - and the American banker's contribution to this ideal state has not been small.

Things have gone astray from this ideal and now we find the banker facing many competitors in the credit field. The United States Government is the largest, with thirty-six owned or sponsored lending agencies. Business itself is another competitor, for practically every line of industrial endeavor now includes hundreds of companies whose capital structure has been built sufficiently strong to finance open accounts or long term credits for all the productive and distributing processes of industry from the manufacturer to the retailer. Figures are not available to show how much of the credit of the country, formerly handled by banks, is now carried by business itself, but it would run into hundreds of millions of dollars.

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Consideration of new credit fields might be divided into three categories:

1. Credit fields in which the Government is now lending money.
2. Those fields of Government credit activity in which the credit needs can be met in whole or in part by commercial banks.
3. New credit fields in which the Government is not engaged in the lending of money.

Since bankers generally have been so confused and perplexed about the Government's participation in the credit business, I consider this phase of my subject the most timely, and justify, in my own mind at least, the need of reversing the sequence of my discussion.

Bankers' magazines and periodicals are filled with the favorable experiences of many bankers throughout the country who have installed Personal or Character Loan Departments and who are successfully handling automobile finance paper. Heretofore the feeling has prevailed that such business could not be reconciled with the operation of the conservatively managed commercial bank. Bankers have been reluctant to consider that they held any responsibility to the public to take care of this class of business. From the record made in the handling of this type of credit, it would appear that we, as bankers, have not kept pace with changing conditions. Only a few years ago most banks refused to purchase collateral notes of finance companies, for, as they termed it, they did not want to contribute to unsound credit practices. Whether or not this business might have been developed as an integral part of commercial banking to the degree of efficiency with which it is now handled is open to question. Obviously our attitude then as to the soundness of such credit was wrong. If we are to meet the legitimate and sound credit requirements to the fullest extent in our own communities, are we not justified in thinking in terms of changing business and a changing public, and adapting our business to such change?

The wonderful growth of the Credit Union, with 4,000 units serving 400,000 people through a cooperative plan of saving and lending to their members, should remind us of the truism that "Labor is the basis of all wealth" and that commercial banks, to serve the maximum credit needs of their communities, must take cognizance of the desire and willingness of the people to save and spend in proportion to their labor. This record should also impress us with the seriousness of purpose and thought of these average folks, who, as producers of wealth, have instinctively spoken through the Credit Union plan and said "We shall not be denied the opportunity of saving and borrowing."

Some have stated that few commercial banks are so constituted that they can profitably handle the savings of individuals in small sums; that they are limited by law to a rate of return which makes a loan of $500 or less an unprofitable transaction. Perhaps Credit Unions will supplement the functions of commercial banks, rather than duplicate them. Maybe finance companies, as now constituted, will continue to extend the major portion of personal or character loans. It may be desirous to have big business continue to carry most of the processing credits of industry. If, however, the bankers of this country are to conduct a business which has heretofore been thought of as indispensable to the needs of the public, they must adapt themselves to new conditions and gear their operations to the modified economic system that now exists. Only to the extent that private banking recognizes its obligation to serve the community by meeting the legitimate credit demands of the people at all times can it expect to be free from Government interference of one kind or another.

The subject of Government competition with private enterprise is one that concerns not only the commercial banker, but every thinking American, who cannot help but be alarmed about the many activities of our Government which touch those of our individual businesses. You know when I go about the country and meet business men, especially bankers, I find they are a little disturbed. That isn't strange when you analyze general conditions. The cause of this disturbance, I think, is brought out by what a Kentucky judge said to a fellow who had come up to stand an examination to practice law. On inquiring what he had read, the old judge mentioned Blackstone and two or three other authorities in law and the fellow hadn't read any of them. The judge said to him, "You're going to be a lawyer and you haven't read any of these; what did you study?" The applicant replied "Ive specialized on the statutes of Kentucky. I've studied them hard and I think I can answer any question on any important statute of Kentucky." The judge thought a little while and then said to him, "I'm going to tell you frankly what's going to be the trouble with you as a lawyer; that Kentucky legislature may meet next winter and repeal every damn thing you know."

So, a lot of bankers in this country are disturbed because they are afraid that they will wake up some morning and find that the Government has repealed their right to do business.

Surrounded by Government sponsored credit agencies, which obviously have acquired an irresistable desire to make their services indispensable and themselves perpetuated, and circumscribed by a regulatory system referred to as one of the most complex ever imposed upon any business of Government, there is little wonder that the banker has moved slowly toward an aggressive program of lending. In a fog of fear and confusion, his program has necessarily been a negative one; but in spite of some clouds that still prevail, I have the confidence that under the virile and intelligent leadership of men like Robert V. Fleming and Tom K. Smith of the American Bankers Association, and your own President Bryant of the Kansas Bankers Association and Mr. Allendoerfer of the Missouri Bankers Association, the clouds are lifting. In fact, you folks here in the territory served by this great city where the "West begins", are fortunate to have such leaders in progressive banking thought as Fred B. Brady, President of the State Division and Carl Allendoerfer, President of the National Bank Division of the American Bankers Association, both of whom have contributed so much to a positive program of our great A.B.A., - - a program that, when undertaken and applied by the individual banker in his own community, will result in the general acceptance by the people of America that an aggressive, stable, independent, chartered banking system is essential to the continued economic development and welfare of the Nation.

Marriner S. Eccles, Chairman of the Board of Governors of the Federal Reserve System, made a very significant statement at the American Bankers Association Convention in New Orleans when he said:

> "I feel that you have every reason in the world to have confidence that the system of private industry and the system of private banking has a future, if you will but profit by the lessons in the past, if you will but do your part and step out into the field and extend not the type of credit that you prefer to extend - 90 days or 6 months credit - but the kind of credit that there is a demand for in your community."

In other words, it seems to me that if the bankers of the country want the Government to get out of the lending business, it is up to them to demonstrate that they are not only able but willing to take over as much of the available sound credit risks as possible. It may be that we have reached a point where, as Governor Eccles points out, we are facing a demand for different types of credit than those to which we have heretofore been accustomed. Certainly the small volume of short-term credit, as compared with the large volume of long-term credit, would indicate the existence - for the present at least - of a very different type of demand from that which has heretofore existed. The question whether this is a good thing and whether it is permanent remains to be demonstrated. In the meantime, it is a fact to be confronted and an indication of the necessity for a change in commercial banking as practiced today.

In considering the credit fields in which the Government is now lending money, and how much of the credit needs in these fields can be taken over by commercial banks, we are interested mainly in the activities of the major agencies: - the Reconstruction Finance Corporation, the Home Owners' Loan Corporation, the Farm Credit Administration with its Federal Land Banks, Federal Intermediate Credit Banks, Production Credit Associations and Banks for Cooperatives.

The Reconstruction Finance Corporation, since its organization in 1932, has made loans aggregating three billions of dollars to the banking business, - one billion through the purchase of preferred stock and debentures, one billion through straight loans to open banks and one billion to closed banks for distribution to depositors. At present it is the country's largest bank, with resources on January 31, 1936 of more than Five Billion Dollars. However, its lending operations cease February 1, 1937.

In contemplating ways and means by which the banks of the country might assume much of the credit load carried by governmental agencies, might not consideration be given to a program involving the liquidation of the Reconstruction Finance Corporation through the purchase by banks, under prescribed conditions, of assets now held by it in

the form of loans, bonds, etc., and perhaps the purchase of other of its assets by privately financed agencies organized for the purpose? Mr. George E. Anderson, in a recent issue of "Banking", suggests the possibility that banks, through the revival of the National Credit Corporation, could take over the RFC's advances to banks and trust companies. The record of the National Credit Corporation in earning 3.35% on the $188,000,000 which the banks put into it, would justify consideration at least of such a program that would assist the government to get out of the lending business to this extent.

I know that many feel that the RFC has not completed its work, - that the railroad program, real estate mortgage problem, drainage and irrigation situation, - all affect the sane progress of business to the extent that the Corporation should stay in the picture until these additional questions are solved. If that is desirable, bankers should say as much and say it now, and assist in every way possible in the securing of desirable commitments from the Corporation, so that these unfinished credit matters could be on their way and the feeling once and for all eliminated that the Government is preempting private rights in insisting upon handling this type of credit.

According to a recent report, the Home Owners' Loan Corporation received, from the time it began operation in 1933, to January 31, 1936, - 2,000,000 applications and closed 1,000,000 loans, for a total amount of $3,000,000,000. Commercial banks, as the recipients directly and indirectly of hundreds of millions of dollars of these loans, appreciate the great contribution which the HOLC has made to the credit needs of the mortgage situation. Now that the emergency has passed, and with increased interest manifested by private lending agencies in this field, it is hoped there will be no reason for extending the loaning activities of the Corporation, which cease by law June 1, 1936. With the rediscount facilities of the Federal Home Loan Bank available to qualified Building and Loan Associations and Savings Banks, and with the cooperation of the FHA

making sound real estate loans attractive investments for insurance companies, trust companies and commercial banks, it would appear that ample provision is thus made for those standing in need of this type of mortgage credit.

The agencies of the Farm Credit Administration, dealing exclusively in the credit of farmers, have a direct influence upon the business of country banks. Possibly these organizations, more than any other, are the ones referred to by bankers in registering any complaint about the Government continuing to be in the credit business.

It is well to be reminded that following the enactment of the Farm Mortgage Act of 1933, most of the commercial banks joined every class of creditor dealing with the farmer and called upon the Federal Land Banks to take over all of their farm paper - secured and unsecured - that could be refunded by mortgage, and to do it quickly. The Federal Land Banks, after sixteen years of operation, held but 12% of the farm mortgage debt on July 1, 1933, or $1,100,000,000. In the thirty months following, in order to meet the requirements and demands of banks, life insurance companies and individuals, as well as the farmer-borrower, Federal Land Banks and the Land Bank Commissioner loaned practically two billions more, bringing its total holding of farm mortgage debt to more than one-third of the whole.

In order to meet the tremendous responsibility these figures suggest, the Federal Land Banks, organized as farmer cooperatives in 1917 and wholly owned by them until 1932 - became the beneficiaries of a generous Government which now owns more than 50% of their Capital. The fact that in six of the twelve banks the borrowers still own a majority of the Capital Stock is a basis for the hope that the Government may ultimately be repaid for its advances, control returned to farmer-borrowers and the banks again assume the role of real cooperative institutions.

In the meantime there is the opportunity now offered to bankers, particularly country bankers, to interest themselves actively in the Land Bank System by directing straight thinking and giving active support to those of its real friends who want to see it preserved as the great stabilizer of long-time mortgage credit, - governor, so to speak, of the whole farm mortgage situation, guaranteeing fair rates and terms but not

usurping the business to the exclusion of every other farm mortgage loaning agency.

There is a fear generally prevalent that all Government sponsored lending agencies are attempting to dominate their fields by promulgating interest rates that cannot be justified by actuarial experience. Lowering of interest rates, especially on agricultural credit and home mortgage loans, has been a policy of the Government for several years, culminating in the arbitrary lowering to 3 1/2% of the rate on mortgage loans of the Federal Land Banks by action of Congress, which authorized it as a temporary measure of relief. If such a rate were made permanent, as it is proposed, it would not only further demoralize private farm mortgage lending, but would also mean the subversion of the Land Bank System. The present situation is wholly artificial, made possible only by Government subsidy, and any attempt to found a permanent policy upon it is bound to result disastrously not only for the private mortgage lending business but also for the farmer, whose best interest would be served in having every form of private finance, including commercial banks and Land Banks, competing for his security. On this subject Dr. W. I. Myers, the very able Governor of the Farm Credit Administration, made this rather reassuring statement recently to a group of representatives of National Farm Loan Associations:

> "In my judgment there will not be a continuing subsidy. The temporary subsidy that has been made available to borrowers from the Federal Land Bank to enable them to get on their feet has been helpful, but we must not expect a continuing subsidy after this is over."

I know he believes that the most effective way of reducing interest rates, as far as Federal Land Banks are concerned, is to make and keep the institutions sound, and this goes for commercial banks as well.

It is heartening to note that life insurance companies and banks are renewing their former interest in farm mortgages and that in the first half of 1935 they made mortgage loans totaling $306,000,000, a gain of 27% over the same period in 1934. With the liberal provisions of the Banking Act of 1935, bankers should explore the possibilities

in the real estate mortgage field, of obtaining liquidity and ever-increasing security in loans properly amortized and on farms properly appraised. The development of the amortization principle in the lending of funds will probably constitute the distinguishing feature of the banking business in the years just ahead. It seems to me that the application of the principle of amortization on a monthly, quarterly or semi-annual basis, has been too long neglected by commercial banks, although they have stood by and furnished loaning funds to instalment credit agencies whose success is due primarily to the intelligent use of this principle. Bankers have been too content, so long as they had what they felt to be a sound loan, to permit the borrower to renew from time to time, without any provision being made for amortization or repayment on any sort of a program. Consequently we entered the depression with a vast amount of credit, much of which could have been liquidated without the assistance of a Government credit agency if a definite paying plan had been provided therefor. This applies not only to real estate mortgage credit, but to a large proportion of so-called commercial credit as well. In fact it would be a good axiom for bankers to place over their desks that "If a credit need cannot be amortized over a reasonable length of time, the loan should not be made." Or, to put it rather curtly, "Let every loan have a pay day schedule." Someone has said that the railroads have "muffed" their job because they overlooked the value of amortization; they should have at least provided a payment plan that would have refunded a less amount each time a new bond issue was made.

In the intermediate or short-term credit field, Production Credit Associations, of which there are now five hundred scattered throughout the United States, are a real potential source of competition for the country bank in the future. Their funds are obtained from the Federal Intermediate Credit Banks which are Government-owned and which in turn, secure their funds from the sale of debentures to the investing public. The Intermediate Credit Banks are authorized to discount farmers' short-time notes for Agricultural Credit Corporations, commercial banks and other loaning agencies, as well as Production Credit Associations, but they do not loan directly to the farmer. They are in reality a federal reserve for handling the operating credits of farmers.

Commercial banks might well consider the advisability of qualifying for the rediscount privilege with the Federal Intermediate Credit Banks. While it is not likely that such facilities will be needed in the immediate future, good use of them could have been made back in 1930, 1931, 1932 and 1933. At least here is an agency that is providing a market for farm paper, thereby adding to its desirability as a proper and liquid investment for commercial banks.

While it seems unjust for our Government to provide a subsidy, as it has. to the extent of a hundred million dollars, in setting up the initial Capital of the Production Credit Associations, these organizations seem to meet the theoretical plans and aspirations of a lot of worthy and capable people who believe that they provide an opportunity for farmers to set up their own cooperative credit institutions, farmer-owned, farmer-managed and always an insurance against the time when they might not be able to borrow from any other source. They are here and they are going to stay a while and, in the meantime, we might justifiably acquaint ourselves with their procedure and requirements, which I believe are sound and which, if added to the more personal interest and attention which the country banker can give to the farmers' needs, will insure a quality of credit that the banker can provide that will outsell the Production Credit Association or any other Government sponsored agency. Personally, I cannot appreciate the need for Production Credit Associations. Having been intimately acquainted with the banking facilities of Ohio, Indiana, Illinois, Kentucky and Tennessee, it is my judgment that the commercial banking machinery - at least for that section of the country - is entirely adequate and capable of caring for the legitimate credit needs of the people. If there is any section of the country, however, where unconscionable interest rates prevail, as formerly in the one-crop country, or where too limited banking facilities exist, then there can't be any "kick" if Production Credit Associations insist upon meeting the requirements of that particular locality. The smart banker, however, will see to it that his worthy borrowers do not obtain their credit from these Associations.

Banks for Cooperatives were established to make loans to farmers' cooperative business organizations, - the kind formerly made by the old Federal Farm Board. In my judgment the type of credit which they consider would not come into competition with a commercial bank. They are, however, contributing to a most worthy effort on the part of farmers to provide successful cooperative business organizations and should have the good will and support of commercial banks.

While the agencies of the Farm Credit Administration are anxious to explore every possibility of appeal to farmers to utilize the various sources of credit under their supervision, they acknowledge that they cannot reasonably expect any farmer to go to a National Farm Loan Association, or a Production Credit Association for his credit unless the Association can extend to him as good or better service over a period of years and at as low or lower cost than he can borrow of his local bank.

Government influence in the field of private lending will be halted, in my estimation, only after it is generally acknowledged that there is no need for its participation. The banker, - particularly the country banker - has a real opportunity to "nail" its progress on a cold-blooded business appeal, - (1) by assuming a more aggressive attitude with respect to the procurement of loans, (2) by a lowering of interest rates to meet the competition of governmental agencies, and (3) by providing a proper quality of credit to meet the farmers' need, including a plan of payment commensurate with the ability of the borrower to repay.

True, the Government may be in a favored position, so far as taxes, costs and low interest rates are concerned, but we must not forget that interest rates heretofore charged were primarily based upon the borrower's footing the entire banking income, including a fair return to stockholders, as well as all expenses, which included the expense of handling the depositors' money. Interest rates on deposits have been reduced, service charges have been installed, and it would seem that banks should give the borrower the benefit of reduced rates. Perhaps Capital has been obtaining too large a share of its earnings at the expense of the borrower. Banks may be obliged, - for a

time at least, - to meet this situation by being content with lower rates, in order to meet the competition offered by the Government in its endeavors to alleviate the distressed conditions that have existed.

A banker friend of mine in Indiana met this competition of the Government in business by using a little salesmanship. In the first place he reduced his interest rate, even on small loans, from 8% to 6% and, incidentally, he has made more money this past year (1935) than he has made in six years, and is paying his regular 6% dividend to stockholders.

One of his farmer-customers who had a six month loan of $200, at 6%, at the bank took notice that corn loans could be obtained through the Commodity Credit Corporation at 4% interest. In due course he got a loan and paid off the bank, and then this banker called him in one day and secured the following information concerning the amount of out-of-pocket expense that he had incurred in getting the $200 loan:

$4.00	Six Months' Interest @ 4%
3.00	Sealer Fee
1.00	Recording Fee
.20	Releasing Fee
.50	Stamps
1.50	Insurance
$10.20	TOTAL COST.

Of course, you know what the farmer did.--He secured a new loan from the bank, paid off the corn loan, and will undoubtedly do a little figuring and thinking before he again borrows from anybody else except the commercial bank of that community.

When checking with his customer as to the total cost - expense and interest - in obtaining a cattle loan from a Production Credit Association, a Kentucky banker discovered that the cost to the farmer for one of these 5% cattle loans was actually 6 3/4%. The banker's rate is 6% and he is getting all the desirable cattle loan business in his community.

A few weeks ago I visited a bank in Central Ohio where the President, an elderly, white-haired man, showed more vim and fire than any younger banker that I have seen in a long time. He says "We're always ahead of them. I cut my interest rate on time money to 1%, a year before the Federal Deposit Insurance Corporation came into existence. My regular rate on real estate loans is 5%, but before I'll miss a real one, I'll make the rate 4%. I've made $100,000 in cattle loans in the last two months and the rate was 5%. I didn't lose one to a Production Credit Association." While other bankers whom I visited have not cut their rates as low as this, some reductions have been made and enough experience had to assure them that the farmer is perfectly willing to pay 6% for cattle paper, as compared to 5% to the Production Credit Association, and that 5% is a satisfactory rate on farm mortgage loans.

Speaking of the barrier of interest rates, one commercial banker, in whom I have a lot of confidence, made this statement:

> "We have been used to generous money rates so long that I find it awfully hard to convince the country banker that he can afford to do business on a much narrower margin as regards interest rates. One factor, of course, that is against it is that a lot of them are still paying interest on too large a proportion of their deposits."

In the December issue of the Northwestern Banker is an article by R. R. Schroeder, Cashier of the Iowa County Savings Bank at Marengo, Iowa, entitled "$202,000 Loan Increase in One Year." I commend that to all country bankers, who, when they have read it, will agree that each of us might have had the same experience if we had exercised like energy and interest in going over our county, visiting our farmers, checking the Court House records and having our people know that we are interested in taking care of their legitimate financial requirements.

In talking with the Dean of the College of Agriculture of one of our great Universities just recently, he made an observation that should impress all commercial bankers with the need of checking up on themselves, when he said:

"There seems to be an apathy on the part of many bankers, which makes it rather easy for an aggressive, low-cost-of-operation organization like the Production Credit Association to get a good deal of business even though it would appear that the bank could give the farmer a rate equally as good or better."

One of the country's greatest students of agricultural finance, Dr. E. C. Young of Purdue University, recently pointed out some practices of Production Credit Associations that might well be used by commercial banks. He said:

"It seems to me there is real merit in the policy of Production Credit Associations, which have insisted that their Secretary-Treasurers be intimately acquainted with the actual operating problems of the farmer and able to sit down with him and work out an operating budget. As these men gain experience, undoubtedly they should be of real service to farmers in helping them to develop their farms along more profitable lines and, at the same time, keep their operations within the limits of financial safety. Likewise, commercial banks will have to come more to a basis of lending on a borrower's operating statement, rather than on his balance sheet. This means, of course, that the banker must follow to a greater extent than he has in the past the policy employed by these Production Credit Associations."

A recent experience in our bank impressed me with the need of knowing more intimately the financial standing of our own customers. An operator of a small grocery store in an outlying residential district of Toledo, who has had an account at our bank for several years, recently mustered up enough courage to come to my desk and to make a rather negative application for credit when he said "I don't suppose you would loan me $300, would you?" Upon questioning him, I found that he owned his store, his own business property and residence, all valued at approximately $10,000, with no current debts excepting a $300 obligation to a loan company, which was being paid out monthly at an interest cost of 36% per year. Having seen some press reference to a statement I had made that banks wanted to be helpful, he came in and sprung the question referred to. Naturally, I was very happy to avail him of the $300 on banking terms and, after reporting the matter to my Committee, we all agreed that likely there were scores of such cases in our city, and hundreds and thousands throughout the country, who, for lack of assurance that commercial banks would be helpful in such instances, were paying the price and joining the followers of the Demagogue, whose rantings run to "driving the money changers from the temple."

You Kansas bankers, ever alert to your responsibilities as custodians of the credit requirements of your communities, have really pioneered, in a State-wide movement, under the direction of your own State Association, to create an improved public attitude regarding the services and usefulness rendered by banks. Other State Associations are taking your cue, which is "To the degree that we bankers have the public with us, we will be in a position to make legitimate profits and be free from the threat of destructive legislation."

The Ohio Bankers Association, speaking through four great meetings addressed by Doctor Harold Stonier of the American Institute of Banking, and attended by seven thousand employees, officers and directors, is embarking upon a positive program of public relations that has for its goal increased good will, loans and earnings for the banks of that State. Fortified with inspiration and facts which they will use, these seven thousand

Buckeye bankers have the militant conviction that when the public understands the extent of services actually rendered by the bank and how the bankers make their profits, the politicians and the demagogues will change their tune.

The time has come for aggressive action; mere opposition and criticism will not suffice. It is not enough for the bankers of the country to say that the granting of credit must be restored to private instrumentalities and that phase of the Government's business relinquished. It is their obligation to do the job and to begin now.

The Reconstruction Finance Corporation, with its subsidiaries, and the Home Owners' Loan Corporation, are approaching the legislative limits of time wherein they can take on further business. Let us not only aid them in orderly liquidation, but lend every reasonable assistance to the end that there will be no need for the enactment of any legislation that will grant them the right to solicit additional loans.

The Federal Land Banks, Federal Intermediate Credit Banks and Production Credit Associations, being set up as permanent organizations, will continue to extend their facilities just in proportion to the quantity and quality of sound credit service rendered to worthy farmers by the commercial banks of this country. As aggressive banks and intelligent bankers, let us assist the agencies of the Farm Credit Administration to limit themselves to their main job, which Governor Myers says is to supplement, rather than supplant, existing private sources of credit.

The announcement a few weeks ago by the President of the United States that authorization of one billion dollars for lending by Governmental agencies was to be immediately cancelled, is significant of the desire which the Chief Executive undoubtedly has for privately owned agencies to provide full financial support for the economic life of the country. A year ago, in Washington, the President, in addressing the Convention

of the American Bankers Association, said:

> "I find almost general agreement among bankers that the agencies must continue until such time as the banks and other private credit agencies are themselves able and ready to take over these lending functions; and when that time comes, I shall be only too glad to curtail the activities of these public agencies in proportion to the taking up of the slack by privately owned agencies."

These words, supported by his action, are indeed a challenge to the bankers of America to do their part in taking up the slack, in order that the President may justifiably further "curtail the activities of these public agencies."

* * * * *

PUBLIC RELATIONS INBANKING

C. H. Wetterau, Vice-President and
Trust Officer,
American National Bank, Nashville,
Tennessee.
Before the Illinois Bankers Association
Convention in St. Louis, May 26, 1936

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~~PUBLIC RELATIONS IN BANKING~~

This is a broad subject that lies at the very foundation of the successful operation of banks, for banks have no rights except those granted them in their charters for supplying certain recognized needs of the public under the authority of the law-making bodies representing the people; thus banks, as we know them, serve in a semi-public service capacity as chartered banks privately capitalized.

I am sure that we all agree with my belief that the rapid development of this country to its present standing of world leadership may be largely attributed to our present type of bank operation. Whether we are to be allowed to continue this type of privately capitalized chartered banks through the years ahead may in large measure be determined by the manner in which the Public Relations Problem of our banks is handled now.

#15

So widely read an historian as H. G. Wells in his "The New America; the New World," published in 1935, is quoted as offering this comment:

"A multitude of people....declare that the general process of private banking is unfair and dishonest and socially destructive. The banker replies that this indictment comes from sheer ignorance. But he does not volunteer the information that would remove this ignorance."

And Mr. S. Sloan Colt of the Bankers Trust Company of New York City is quoted as saying:

"A learned and respected member of the Federal judiciary, in a recent utterance before a meeting of bankers, made this very pertinent observation: 'Gentlemen, your acts over the next ten years will determine whether banking shall continue to be conducted by private interests, or become a function of the National Government.' This is the considered opinion of a man of wide

experience in public affairs and with a strong prejudice in favor of the capitalistic system."

Also Herbert Agar, co-editor of the recently-issued "Who Owns America?" and quoted as a nationally recognized authority on political economy, declared in a lecture at Vanderbilt University on May 1st that if America is to succeed as a democratic nation, it must re-examine and re-build its capitalistic system.

Said Mr. Agar "We are going to live through a period when the principles on which this country has been operating will be re-examined and re-defined."

Mr. Agar closed his lecture with the assertion that Americans should figuratively "wake up" and devote some honest, constructive thought to the changes taking place in government in order to aid in the retaining of a thoroughly democratic country.

You may not agree with all I have to say on this subject, but if some of my comments are sufficient to challenge your interest and induce you to think seriously and constructively on Public Relations as it may affect each of our banks now and as it may affect the future of banking as we know it, then this discussion will be well worthwhile.

I feel sure that most of us sympathize with the railroads in the problems that have been confronting them for years, resulting largely, I feel, from the "Public be damned" attitude which they pursued at the height of their greatest prosperity, making it difficult for them to change to a more intelligent Public Relations Program in these later years. That, coupled with their slowness in meeting changing conditions, has been an almost insurmountable problem for them. Yet we need railroads; they have their proper function and should be allowed to survive and prosper, but it is a difficult task for railroad operatives, bred in the old type of operation, to bring them-

selves to a recognition and acceptance of changing conditions requiring modern Public Relations. I grant there are exceptions and that the present generation of railroad executives seems to be honestly endeavoring to meet the problems of today. How much more difficult their problem has been made, however, by having to live down the attitude of their predecessors, which has brought about discussions of government ownership.

I have injected this illustration simply that we may understand the problems which face banking if we do not recognize the importance of and act intelligently in handling our Public Relations Program. After all, we hold our charters at the will of the American public, and it is to that public we have to account. The problem of Public Relations has been with banking since its inception, but never in the history of American banking do I believe that bankers have appreciated its importance quite as fully as at the present after having survived the last depression.

Public Relations is something that has to be worked at - and worked at intelligently - year in and year out - in the days when least needed, as well as in the days of stress, for it is not something that can be kept in a closet and brought out for use on special days and occasions, but must be kept constantly in the foreground of daily operations. Changes of plans or policies in days of stress merely incite suspicion and have the opposite to the desired effect.

As bankers, we all know that during the depression, many honest and conscientious bankers lost their all and many made extreme personal sacrifices of their fortunes in an attempt to save their depositors from the hysteria which swept the country, aggravated as it was by the sins of the few, ~~and a press to which only the bad was news and the good ignored~~

AN IMMEDIATE PROGRAM

As bankers then, we are interdependent and must recognize our responsibility each to the other, as well as to the public. It is patent that the first thing for each institution to do is to place its own house in order, and by that I mean that its policies and operations should be such as to justify the confidence which it asks the public to bestow upon it.

If you are a good banker, when you lend your customer money, you ask the borrower to furnish you with an intelligent statement that you may year by year note the progress that the borrower is making and the ratio of his holdings to compare with the accepted standard of what a borrower's statement should show, for loans to be justified. In recent years, you have come to understand that it is also important for you to have a year by year operating statement to assist your judgment in passing on the loan. Would it be out of line, when your customer is lending you money on deposit, for him to ask to see your yearly statements to note the progress you are making in operating your bank, and also to have the privilege, if desired, of being furnished an operating statement in order that he might judge whether your bank was being operated upon an accepted standard set for privately capitalized chartered banks. Only a properly operated bank could meet such a request.

With our policies in order, the next thing to be considered is the operation of the bank or the service we furnish the public. Here develops our responsibility for training our employees who contact the public, whether officers or tellers, so that our customers may be served in a manner most pleasing to them and intelligently in the customers' interest. While we must never lose sight of our stockholders and our bank in serving the public, yet in the long run it is my belief that the ~~Rotary~~ slogan ~~holds good, "He profits most who serves best." It~~ of a well known international organization holds good, "He profits most who serves best." It is the province of our bank, insofar as practical, to make our Customers' Relations with our institution profitable to them.

It is an indisputable fact that the customer gets his impression ~~We cannot overlook the fact that our employee, rendering a particular~~ of the bank from the employee who serves him, ~~service to a customer - to that customer is the bank,~~ whether that employee be an officer, teller, telephone operator or floorman. ~~and the impression which that employee makes upon the customer is the impression that customer acquires of the bank.~~ If you have not as yet instituted a program of training for your employees, I could not do better than recommend to you the publication "Constructive Customer Relations," published by the American Bankers Association, in collaboration with the Financial Advertisers Association, together with a more recent publication of the Public Education Commission of the American Bankers Association issued as a manual of procedure.

Having fortified the organization with the proper training in the part it plays in this matter of Public Relations, we have something of value to sell to the public, and here advertising is brought into play. This is the type of publicity which can be controlled, for it is the paid space you use in your newspaper or advertising you do by mail or on the air.

In handling your advertising, there are a few things which it would be well to remember.

First, that you are not merely competing with other bank advertisers, but with all the advertising appearing in the same publication for attention; that it is not necessarily what the banker wants to write that the public wants to read, but that we should incorporate in our advertising what the public wants to read, as the banker would write it, yet so worded that it could be understood by the layman.

It has always been my feeling that a bank's advertising in its appearance, illustration, layout and interest should compare ~~compete~~ favorably with the best advertising produced by any other type of business, and I would rather do less advertising ~~better~~ than more advertising of a poor ~~quality.~~ of outstanding quality type, even though the same cost was involved.

With your advertising to assist in educating the public and to open the

doors for your salesmen, with your business development executives and contact employees as your sales force and your personnel officer to see that the service is rendered and the manner in which it is rendered satisfies and justifies the patronage of the public, you have then developed a Public Relations Program for your individual bank.

You might say to me "Well, what's the use of all this to my bank? We are on friendly relations with our customers," and that may be true by and large, but I challenge you to one test. Take an average list of accounts on your books, employ a professional investigator, give him the list, let him call from door to door as an outsider and ask each of those customers a series of questions with reference to your institution, and have him bring you the result. I am confident that much of the information you would receive would challenge your interest and convert you to a Public Relations Program for your particular bank.

IN ACTION

Assuming then that you have an interest in a Public Relations Program for your bank and wish to do something about it, you might be interested in knowing a few things which our bank does in the interest of better Public Relations.

Our institution holds conferences with contact employees, as well as officers.

Our officers and employees call on present customers, as well as new business prospects and report to the Business Development Department, where records ~~are kept of interviews.~~ of interviews are kept.

At 8:30 each morning, our officers meet for 30 minutes to discuss customer relation activities, new business, new accounts that have opened and those that have closed, make reports on calls and interviews, and also to discuss

other matters considered important by officers in charge of specific departments.

Semi-monthly, a mimeograph bulletin goes to all officers and employees and the executive committee, showing the new business solicited and produced by each officer and employee, describing its type.

We consider it important that the proper morale be maintained in the organization, and at least twice a year a meeting is held in which the family spirit of the group is emphasized, entertainment provided, and a short talk is usually made by one of our executive officers, stressing the importance of securing and holding business for the bank.

We also publish a house organ called "The American," principally for the interest of our officers and employees. Our material for the publication is mostly inspirational in character, and a listing of those personal items referring to our employees, which is of interest to the entire group. In this publication, we also stress the importance of securing and holding business for the bank, and include articles showing the progress of our institution.

One of the recent plans for improving our relations with our customers and the public was a letter soliciting loans, which I believe to be unique and the results worthwhile. This letter was sent to 8,000 citizens of Nashville who rated good credit or better, and the reaction over and above the loans which it produced was most favorable for our bank.

These are just a few of the things which we do in the interest of better Public Relations in our immediate program.

A LONG RANGE PROGRAM

This subject though is larger than one bank or one hundred banks for that matter. It has to do with the entire system of American Banking as we know it - its development, or May I say, its survival. From the individual bank, let's turn our thoughts to the consideration of a national program.

First, I would ask this question, "Is there any one of us who would be willing to insure banking against the risk of another depression in the years ahead?" Since 1899, when I entered the service of my bank, I have seen these recurring periods of prosperity and stress, after each of which some legislative action is generally taken, which is heralded as an insurance against such a happening in the future, and while successive periods have not always resulted from the same causes, yet they have come.

Will it not be well to start now the building of a Public Relations Program with all banks cooperating, not alone for immediate benefit but as a backlog for days of future economic stress that we cannot now foresee. If we would do this, we must think in terms of a long range program to win for banking a more favorable public sentiment.

Some bankers are chafing under the new rules and regulations that have been imposed upon them by recently enacted laws. What many don't seem to fully understand is that this new legislation has resulted from the demands of the public.

Have you been addressing your advertising publicity to those who earn $5,000 or more a year? Do you know that it is said that only about 2% of the adult population of the United States earns $5,000 or more a year? If we are to win a more favorable public sentiment for banking, is it not logical for us to address ourselves to the other 98% of the adult population, which earns less than $5,000 a year, who, being qualified to vote, have a tremendous influence

upon the laws of the land under which we operate, as well as upon the attitude of the public towards banking.

The politician usually addresses himself to the 98%. If he is a successful politician, he keeps closely attuned to the wishes and thinking of this majority group in the enactment of laws. Doesn't this simple fact indicate a need by banking for a National Public Relations Program, taking this majority group into consideration?

While the public has never understood banking and probably never will, and I do not feel that it is essential to better Public Relations for the mass of the public to be so informed as to qualify each individual as capable of serving, in an official capacity, some financial institution, yet the public is interested in the results that accrue to them and affect their welfare. In other words, we must sell the public on what banking has done, can do and is doing for the welfare of each individual in this country.

#4 & 5

There are some simple things which can be done now, which I believe to be of major importance. Every state should enact as a law, and give authority to the banking superintendent of each state for enforcement, that the words "bank, banks and banking" shall not be used by any individual or organization not qualifying for supervision by some banking authority, (Tennessee enacted such a law in 1935). We all know that commercial banking suffered tremendously during the last depression from the bad press accorded investment banking, as well as commercial banking, and the public was not sufficiently informed to differentiate between investment banking and commercial banking.

It might be well also, if it could be legally done, for the word "Trust" to be reserved for institutions having trust functions under supervisory authority of some banking department. Without doubt, the fact that in the State of New York it is unlawful for any institution to use the word "Savings" except the savings banks, and the further fact that those savings banks cooperated in

an intelligent Public Relations and Advertising Program, had much to do with that type of institution weathering the storm without a failure.

While we can all aid in a Public Relations Program by the intelligent operation of our individual institutions, I cannot but believe that the most rapid accomplishment of the results desired would come by banks getting together in a cooperative program.

I believe that the different banking associations wish to do for banking what banking wishes them to do, and fully realize that those in authority cannot bring such a program to banking until the demand for it arises from the membership, but I believe that in the American Bankers Association, the Reserve City Bankers Association, the Financial Advertisers Association, American Institute of Banking, the State Bankers Associations and other groups are men fully capable of instituting and carrying on such a program, and that when bankers have come to fully appreciate its importance and to indicate sufficient interest, there will be found someone to carry the torch.

On April 28, 1915, at a meeting of the Tennessee Bankers Association, Elbert Hubbard made a talk on "Getting Together." Leaving the Convention, Mr. Hubbard went to New York, sailed on the Lusitania and was drowned when it sank on May 7, 1915, his speech in Nashville being his last. Mr. Hubbard told this story, which is probably old to you and which was probably old then, but I think it appropriate for closing my remarks:

Mr. Hubbard said, "Now the other day I was at the classic town of Kalamazoo, Michigan, the home of the State hospital for the insane, the insane asylum, and I walked across the beautiful grounds, a half mile from the main building, and I saw a young man out with a lot of patients out for a walk and, you know, I suppose there were twenty-five of those patients and only one man in charge. I just kind of slipped in with the bunch and nobody noticed me,

and finally I worked my way up alongside of the little fellow in charge of these men, and I said to him "Are you armed?" And he said, "No, why should I be armed?" I said, "You have all these men in your charge; what is to hinder their getting together, setting up a job on you, giving a signal and putting you out of commission?" And he looked at me and said, "You belong here all right." He thought I was qualifying for a degree. He said, "You belong here all right. You ask why those fellows don't get together?" I said, "Yes." He says, "They can't, that is why they are sent here." He says, "There is only one reason for sending a man to the insane asylum, or the penitentiary, and that is because he cannot or will not work with other people." He says, "Sanity lies in the ability to do team work, and the more people you can work with and for, the bigger and better are you." I said, "You will have to give me time to Fletcherize on that." But you know, when I got home, it came to me like this; he says, "If you don't get together they will send you to the insane asylum," and it came to me all at once that if you do, they will send you to the penitentiary. So we stand, you see, in a peculiar position; but as a general proposition, I will give you this, that the more men you can work with and for, the bigger and better are you, and the bigger your reward will be."

The language I have quoted is exactly as expressed by Mr. Hubbard, and I feel that there is an opportunity for bigger and better things for banking if we can get together on the proper program of Public Relations.

Had you realized that while the recent insurance law is costing banking 1/12th of 1% insurance premium on its deposits, that for as little as 1/200th of 1% or 5¢ per one thousand dollars of deposits per annum, if there are fifty billion of deposits in the country, banks could raise a fund of $2,500,000 to handle a cooperative Public Relations Program? If your bank

has one million dollars on deposit, would you not be glad to pay $50.00 per year as an additional insurance against the type of hysteria which we have seen in this last depression, with the possibility that by the use of such a fund banking may be so interpreted to the public as to win greater acceptance and appreciation and lay up a backlog of public goodwill against the days of future stress and future challenge of the chartered bank with private capital?

This is just a thought to leave with you in the hope that it may start you thinking.

Abraham Lincoln is quoted as saying "In this and like communities, sentiment is everything; with public sentiment, nothing can fail; without it, nothing can succeed; consequently, he who molds public sentiment goes deeper than he who enacts statutes and decisions; he makes statutes and decisions possible or impossible to be executed."

The subject "Public Relations" is now being discussed before every meeting of bankers, and discussions are fine for they serve to provoke and srystalize thought. What will be the result of our thought? Shall we merely agree that these are things that should be done and then let this matter slide, following the course of least resistance, or will we bestir ourselves with an immediate program for our separate institutions - and - at the same time lend our influence and support to the promotion of a long range, cooperative program for the creation of a more favorable public sentiment for chartered banks privately capitalized? I ask you! !

Off
Circulate

Speech of Mr. Lon R. Smith
(First Vice President of ABA)
before Oklahoma Bankers Assn
May 18, 1936

4/3/2

I stated at the dinner last night, that my business hours are spent in a banking institution that teems with the traditions of this Oklahoma country. Some of your earliest settlers were our customers, and their descendants still carry accounts with us. It is therefore interesting for me to spend those days with you and to discuss some of the things in which we have a common interest.

I regret that President Fleming could not find the time to make this trip. Some of you were privileged to meet him at the recent banking conferences, and I am sure you were impressed with his sincerity in approaching our common problems. "Bob" Fleming has served the bankers of this country so long that we hardly think of anyone else when we visualize Washington. One of these days he will retire from the official family of the American Bankers Association, but remember it will be just too bad if he is not succeeded on the firing line by some outstanding banker in or around Washington to whom we can turn for consultation and advice. My close observation of President Fleming's work has impressed upon me the importance of being properly represented in Washington. I have such regard for what he has done that I consider it a great privilege to substitute for him here.

noted

During the course of the depression with the increasing number of bank failures, there developed a growing demand for drastic banking legislation. In answer to this popular feeling, several bills were introduced into the Congress of 1931 and 1932 and finally culminated in the Banking Act of 1933, which made a definite attempt to remodel the banking structure. Two years later another banking act was passed, now known as the Banking Act of 1935, which is probably the most important piece of banking legislation enacted by Congress since the passage of the Federal Reserve Act twenty-three years ago.

During this four-year period of legislative activity concerning banking, there were ever present those active individuals who were determined to socialize banking and to take advantage of the opportunity afforded to urge their pet "isms". I

shudder to think of what might have happened if Congress had been without the information and assistance furnished by the bankers of the country, for it must be remembered that banking and tax legislation are the most difficult kinds of law making which come before the House of Representatives and the Senate.

The various legislative committees working on this legislation during that period were desirous of having the bankers' point of view, and, as a result, ~~the~~ bankers went to Washington from all sections of the country--representatives of small banks and of large banks--and were ready and willing to discuss banking problems with congressional representatives whenever necessary. I am convinced that these bankers, giving as they did facts, figures, and first hand information of business conditions in their various territories, set up a bulwark against the group which considered banking a governmental function and believed that the end always justifies the means. Even in the late days of the 1935 session, when it became apparent that banking legislation would not take the radical form that these agitators demanded, they nevertheless felt that they could stop any movement toward sound and workable laws. After the conferees had agreed on the final form of the Banking Act of 1935, one of these gentlemen told me that the bill would not pass, for he had hopes of blocking it in an attempt to introduce more radical banking legislation later. An acceptable bill was nevertheless passed and signed by the President.

The act has nearly fifty sections which provide for enforcing regulations by federal authorities. Some of these regulations are of paramount importance, and it has been necessary for the American Bankers Association to keep in constant touch with all the agencies having to do with the drafting of these rules and regulations. For the past several months we have tried to be helpful to government authorities. They have exhibited a spirit of cooperation and openmindedness, and, as a result, we believe that sound, workable regulations have for the most part now been effected which will be helpful to bank officers in carrying out the provisions of the Banking Act of 1935.

In recent months we have also directed our attention toward pending tax legislation affecting banks. Representative officers and staff members of the American Bankers Association are in touch with government officials, ready to furnish information when desired to any branch of the government and, if necessary, willing to appear before the committees of the Congress to give concrete information that will enable them to pass sound tax legislation which will provide an adequate income for the government but which will not at the same time work an injustice on the banks.

The executive officers of the American Bankers Association now believe that legislation of a national character affecting banking is behind us, at least for the time being. However, every intelligent banker knows that we have many perplexing problems ahead of us which will require study, experience, and everlasting cooperation to solve.

In speaking of the problems ahead of us, S. Sloan Colt, president of the New York State Bankers Association, in a recent address before his association, stated the need for more careful analysis of the problems of commercial banking so clearly that his words will bear repetition here. He said:

"...I think we will all agree that there are some major unsolved problems in our commercial banking system. Many of the laws which have been enacted affect the general regulation and supervision of banking policy but leave untouched some of the fundamentals of banking structure and banking operations. Deposit insurance on a national scale is a new experiment and while it may have its effect in preventing the spread of withdrawals in time of trouble it can in no way be accepted as a substitute for good banking. Supervision can limit the scope of bank operations, but the ultimate decision as to the kind of assets to be held in the portfolios of the banks rests with the bankers.

"One of the most important questions which bankers face is this: Are we going to have a banking system which will stand up in future periods of depression, or shall

we have a system that will accentuate the difficulties and lend itself to excessive liquidation in periods of stress?"

The New York State Bankers Association has recently published an exhaustive study of what it thinks should be done in the empire state to solve some of our present-day banking problems. I suggest that you read this document if you have not already done so. I hope it will be possible for other state associations to do a similar piece of research work in their states. It is well for us to know the character of the problems confronting us and something of what we must do to solve them locally.

We cannot rely on law alone. In fact, while recent legislation helped us clear up some of our perplexing questions, these very cures have brought on problems which we must face today and tomorrow. Suppose we think of the Federal Deposit Insurance Corporation as an illustration of what I mean. It is designed to insure depositors against loss; yet we all know that the F. D. I. C. could not withstand a wave of bank failures such as swept this country a few years ago. The fact that deposits are insured is no invitation to loose banking. The presence of the F. D. I. C. in our banking structure places on bankers, on the Federal Government, and on the public an obligation which did not exist a few years ago.

With the F. D. I. C. in effect, every banker is truly his brother banker's keeper. We cannot sit idly by and see things done which we know will wreck the insurance corporation. Furthermore, the Federal Government has a responsibility it did not have before. It cannot, on the one hand, insure the solvency of chartered banks and, on the other hand, permit governmental agencies in the banking field to take from these chartered banks their sources of strength and usefulness by cutting rates or indulging in unsound banking practices. The presence of the F. D. I. C. also puts an obligation on the public to see to it that they do not permit the chartering of too many banks in the future. We cannot have a sound banking structure if we have more banks than bankers.

Recently I heard a half dozen banking superintendents discussing the subject of bank chartering, and they all agreed that overbanked communities are a serious menace to the banking structure of the country. Herman B. Wells, secretary of the department of financial institutions of Indiana, said in a public utterance in Chicago recently: "The continuance of our banking system in its present form depends in a large measure on the development of a sounder chartering policy than we have had in the past."

State bankers associations may render an outstanding service by impressing upon the people within the states and upon the state authorities the importance of this question. It is not a problem for bankers alone; the public must be made to understand its responsibility in view of the F. D. I. C. It means that in order to carry this message to the public within your state you must take advantage of every opportunity to impress upon schools, clubs, and colleges their responsibility for a sound banking structure by not permitting too many banks to be formed in the future.

Have we this? Last year the American Bankers Association published a study under the title, "The Bank Chartering History and Policies of the United States." This is a comprehensive statistical analysis of bank chartering in this country and it should be of great value to the various state organizations in their efforts to carry this story to the public. The American Bankers Association will be glad to send a copy of this study to you if you have not seen it.

Yes

During the past four years there has been one fundamental change which affects our problems in the field of bank management in a very definite manner. That change has been brought about through the organization of agencies of the Federal Government which today affect every bank--whether it be chartered under state or national law. There was a time in banking history when Federal agencies were of interest to national banks only. That day is past. Such instruments of the government as are represented in the Reconstruction Finance Corporation, the Federal Deposit Insurance Corporation, the

Federal Housing Administration, the Home Owners' Loan Corporation, and the Farm Credit Administration now present national problems and possibilities in the management of our banks wherever they are located and under whatever charter they operate.

While I have not been associated in an official way with the American Bankers Association for a very long time, I have had impressed upon me the importance of its work on behalf of both state and national banks in dealing with Federal agencies. Day by day, through our office in Washington as well as in New York, the Association is in contact with all these agencies regarding laws, rules and regulations, many of which affect trust institutions and state banks just as vitally as they do national banks. If some rule or practice of any one of these agencies adversely affects the interest of sound banking in your community, we want you to report it to us at the American Bankers Association, for we desire to be your servant and to exert every effort to bring about fair play in every instance where continued injustice exists. You must remember that in dealing with the Federal Government you are meeting the largest business organization in America at the present time, and if we are to be effective agents for you, we must be able to speak with authority for all of you all the time.

In spite of the fact that the American Bankers Association must contact all these Federal agencies in the interest of its membership, it is not a political organization and cannot engage in partisan controversies. Regardless of what political party is in control, the Association must exert its efforts in behalf of sound banking in the interest of bank depositors. This means that the Association must direct its efforts along two lines of activity. First, we must aid banks in improving the services they render to the public and, second, as a national association we must represent chartered institutions in their dealings with Federal agencies.

In the interest of helping banks to improve banking service, the Association has in recent years through the Bank Management Commission, which represents all kinds of banks, completed a series of eighteen studies on ways and means of increasing the

Lets see all of these together

efficiency of banks, at the same time adding to their earning power and hence their stability. These studies have been of interest to thousands of bankers and have aided in the solution of many of their problems of bank operation. All the studies are based on the experiences of institutions that have found ways and means of bringing about practical results through study and research. You will not find any of these studies abstract or theoretical. They are written for bankers by bankers and in banking language. Scores of bankers throughout the nation have given liberally of their time and ability in preparing these documents, which are of tremendous importance in helping solve problems common to us all.

On the other hand, there are problems affecting bank management which cannot be solved within the bank itself. These problems arise from the impact of governmental agencies upon our chartered banking system. It is at this point that the American Bankers Association has been found to be of such great value to the banks in presenting their point of view to governmental authorities. One such problem of interest today in this section of the country has to do with the Postal Savings System. Please bear in mind that this is not a political question in a partisan sense of the word. As you know, the Postal Savings System was established by a Republican administration in 1909 and has come to its greatest development under a Democratic administration in 1936.

The Banking Studies Committee, of which I have the honor to be chairman, is making an exhaustive study of this question at the present time. When we arrive at our conclusions, we will present them to the Federal authorities in an impartial manner and not in the heat of political controversy. We will give the Federal authorities, the public, and each member bank, as well as the state associations, the benefit of our findings. We have faith in the American people and in the government representatives they have selected and believe that they will act fairly when they have the facts before them.

In the course of this study we are making a series of maps of the various states in the Union, indicating the present-day practice regarding the Postal Savings System with the idea of showing where it can be helpful and where it is unnecessary in that it duplicates the service now being offered by regular chartered banks either state or national. Among other questions we are desirous of answering the following:

1. Is there a need for the Postal Savings System today along the lines of its original purpose when it was established twenty-seven years ago?

2. Should the Postal Savings System be continued in those areas where banking facilities now are adequate to meet the demands of the public? As a result of our survey we hope to find out where the banks are ready and willing now to take over deposits and continue to do so in the future for those desiring to establish small savings accounts in banking institutions, assuming that the Postal Savings System would be curtailed ~~in certain areas~~ or abandoned. It is obvious that if the banks are not willing to take such deposits, it would be foolish for us to urge Congress to curtail the services of the system. Our scientific approach to this problem will give us the answer.

3. Is the Postal Savings System making it difficult for members of the F. D. I. C. to pay the corporation assessments and maintain earnings sufficient to keep them in a sound position to serve the needs of their community in various sections of the country? The more we study this question the more it becomes apparent that we must have all the facts from all the banks where the Postal Savings System is in operation if we are to render a satisfactory report to the Congress, the banks, and the public. If we are to represent you in a national way, it becomes apparent that we must have word from you as to what you want. It may be that we cannot satisfy every one, but I am certain that you will be content with the attitude of the majority upon which the findings of the Banking Studies Committee will be based.

The President and others in authority have said that many of the emergency loaning agencies would be curtailed whenever and wherever chartered banks were willing and able to take up the task. We have no desire to urge chartered banks to undertake

unsound loans. Here again our approach to the solution of this problem must be based on no narrow partisan conception. For that reason we have undertaken a study of the various Federal lending agencies in Washington. We are studying the ways and means by which these agencies operate, with the idea of passing along the information we obtain upon this important problem to all the banks of the country. We shall place before you the names of these agencies, the laws back of them, and the time limitations within which they are supposed to operate, as well as the extent and scope of their operation. We shall study the question of whether or not some emergency organizations have now fulfilled their function and should be liquidated, for we believe that it is useless to continue emergency organizations if the emergency for which they were established has passed away. As we obtain our information we shall file it in loose leaf form with the secretaries of the state bankers associations, so that it will be available for all the bankers of this country.

Under the heading of permanent agencies let us consider the Farm Credit Administration. The very able Governor of that agency has said that the F. C. A. is to supplement and not to supplant other credit agencies in the field of farm credit. We must admit that the Farm Credit Administration, through its various banks and corporations, has done a splendid piece of work in meeting the emergencies which existed a few years ago in the field of farm credit. As a result of the work of that agency, many banks and insurance companies are in a better position today than they were formerly. We are now interested in seeing to it that the Farm Credit Administration continues to supplement and not to supplant banks and other legitimate credit agencies in agricultural credit. It is evident to all that if a permanent agency like the F. C. A. should take business away from chartered banks, these banks would have difficulty in remaining sound and in paying their taxes to help support both state and federal governments. The government and the banks are interested fundamentally in maintaining the soundness of the Federal Deposit Insurance Corporation, and the more sound banks we can have in that

system the better it will be for the Federal Government and for the public at large. In other words, we wish to impress upon the Federal Government the necessity of looking at this problem as a whole. The various agencies affecting banking must be coordinated and must work toward common objectives.

In conclusion, gentlemen, may I impress upon you the fundamental fact that many of our banking problems today and in the future are problems of a national character, whether you happen to be connected with a state bank or with a national bank. It means, therefore, that you must have a strong national organization representing you in Washington. This organization should not be a lobby. The American Bankers Association has not supported a lobby. Neither should this organization be enmeshed in partisan politics. Whatever the political competition or whatever the party in power may be, we shall always treat our problems as business problems of an economic character affecting all the people, and it has been long established in business that scientific study and research are the only sane approach to a solution of any business question. Political questions may be surrounded with the heat of oratory where there isn't much light, but the national problems which you and I as bankers must contend with are problems of vast economic importance which only study and research can solve.

If the Association is to protect the interest of the chartered banks and their customers in dealing with the government, we must have the support, both moral and financial, of all our banks, because we can be most effective when we can assure Federal agencies and committees of the Congress that we represent in our membership all the chartered banks of the country. The American Bankers Association is the only means of expression which we have in dealing with economic questions of a nationwide character. Let's give it the support which its record of performance and promise of future effort so well deserve.

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