The Commercial & Financial Chronicle

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BANKERS CONVENTION
SECTION

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AMERICAN BANKERS ASSOCIATION
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October 14, 1939

AMERICAN BANKERS CONVENTION

SECTION OF THE

Commercial and Financial Chronicle

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The Convention and the War

That the outbreak of European war, occurring as it did less than one month before the assembling of the American Bankers Association at Seattle, on Sept. 24, for its annual convention, was the uppermost consideration in the minds of the delegates, no one can doubt. But three or four weeks are too short a time for even the most discerning banker to envisage the duration of the conflict, its political and military consequences, or its economic repercussion in the United States. It may indeed be said that the series of incidents, since Germany invaded Poland on Sept. 1, gave little basis for conclusive judgment regarding the duration, probable character and longer results of the war, or regarding its repercussion upon our own markets, or regarding public judgment as to the manner in which the United States shall best preserve neutrality.

Actual news developments of the intervening period had been in all respects confusing. In Europe they had been made up of Germany's bloody subjugation of Poland, the beginning of an aggressive submarine campaign against British ships, invasion of eastern Poland by Russia (acting evidently under treaty arrangement with the German Government); the slow advance of the French army in the West into German territory guarded by fortifications. On these considerations were superimposed the enigmatic attitude of Italy toward Germany, which may or may not mean a rift in the paper alliance of those two countries—an attitude possibly forced by Herr Hitler's astonishing league with Soviet Russia—and, finally, Herr Hitler's own speech of Friday, Oct. 6, to the Reichstag. This came after the bankers' Convention had adjourned. Actual significance of that two-hour deliverance which, while asking for peace, conditioned it on Herr Hitler's having his own way with weaker States in Central Europe, has even now not been evident to American readers.

The course of events in the United States had been hardly less bewildering. At the outbreak of war in 1914 our own Stock Exchange, dreading the American market's complete collapse, had shut down for nearly five months. In September, 1939, it rushed at once into a wild carnival of speculation for the rise, based on prospective war orders, in which stocks, especially of companies manufacturing war materials, advanced 15 points or more under transactions which brought the monthly total of shares sold from almost the smallest August since the World War to the largest September since 1932. The low-interest Government bonds had temporarily fallen, under unprecedentedly large selling, below their issue price of par. Wheat had advanced in a week from 68½c. at Chicago to 89¼c.

Yet a few weeks later the stock market lost on the average nearly a third of its early impulsive gain. United States Government bonds had risen again above par; wheat had fallen from 89¼c. to 80c. The beginning of debate in Congress on proposed amendments to the neutrality bill at once introduced the widest imaginable cleavage of opinion as to what restriction on our sales to belligerents would decrease the probability of our own possible involvement in the conflict and what would increase that probability. It could scarcely be expected that even the most impartial and enlightened speaker at Seattle would have ventured, at such a moment, to suggest financial plans or policies, which must necessarily depend in large measure on the future progress of events.

Of necessity, then, the Convention's speakers and resolutions approached the war problem cautiously. They wisely applied their own analysis to the economic position in which the United States faces the shock of European war. The report of the Economic Policy Committee declared that the effects of a European war on our own economy "will depend on such unforeseeable factors as the duration of the conflict and the nature of the consequences to the participants." They warned that the huge volume of nearly idle deposits and the vast excess of reserves in our banks "might easily be used in ways that would produce unduly rapid price advances and foster undesirable forms of speculative activity." Therefore the Committee advocated a policy of "prudence and thoughtful care" in use of these resources. It thus regarded the question of our foreign trade, which had such remarkable vicissitudes in the war of 25 years ago:

> Probably the volumes of our exports will be increased, and our foreign trade with neutral nations will be expanded. These effects will be partly offset by the fact that large areas of our foreign trade have already been eliminated by the war, and that even those combatants which continue to purchase goods from us will limit their takings to war-time necessities.

But the burden of the speeches was much more emphatically to the effect that a policy should at once be adopted to put the United States in the proper position to meet an emergency. The Convention's own resolutions expressed belief that the present increase of business activity will continue throughout the year, and that the Nation's banking institutions are prepared to meet adequately and promptly all demands. But they added that "it is our belief that an approach to a balanced budget should be the primary object of our fiscal policy, to the end that sound national credit may be maintained." The retiring President of the Association, Philip A. Benson, declared to the convention:

> The least that we should accomplish is the end of disunion within our own borders. We have had our full measure of drastic changes imposed by legislation. It is necessary to have an opportunity to digest them. What we need now more than anything else is stability.

The new President, Robert M. Hanes, in his inaugural address took a more cheerful view:

> During the past decade the world has been engulfed in economic and political issues and panaceas. . . . Now there seems to be a turning of the tide. To those who have courage and are awake, a new day is dawning.

This may be so; it has always been the case that a real emergency, involving public safety, public resources and public credit, will compel an administration to surround itself with experienced financiers and men of affairs, even if it had theretofore taken its public policies from young idealists or class-room economists who had little or no experience with the realities of economic life. Yet the Convention's own feeling obviously was that something more than selection of an Advisory Commission, temporary or otherwise, will be required. Fred I. Kent told the bankers at Seattle what was absolutely essential:

> The great war that is now going on says to our Government and to our people, in no uncertain terms, that they must get together and take such action as is necessary to restore industry in the United States or we will be unable to hold our own in the world turmoil. This requires rescinding or correction and clarification of all laws that prevent the sound functioning of private enterprise that are in existence today.

Mr. Kent added that, while the passing of unwise war emergency laws because of fear that somebody may make a profit "is almost criminal," nevertheless "no right-minded person wishes to further the building of so-called war profits at the expense of a Nation." This is unquestionably the feeling which prevails throughout business circles. Few people wish to repeat the experience of 1916, when American manufactories of peace-time goods were converted on a prodigious scale to output of war material. Indeed, the sequel, when peace returned after 1918, must itself have taught its lessons.

Meanwhile the fact remains, and was cordially recognized at the Seattle Convention, that recovery in American industry is rapidly in progress. That recovery, though it may have been hastened by the events of September, did not result from European war. It was predicted and foreshadowed, both on the markets and in the reports from industry, many weeks before hostilities began. This recovery, not out of line with such advance predictions, has already brought the pace of industry back to what it was in the summer or early autumn of 1937.

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GENERAL SESSION

AMERICAN BANKERS ASSOCIATION

Sixty-Fifth Annual Convention, Held at Seattle, Wash., Sept. 24-28, 1939

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The Future of the Metropolitan Bank

By H. DONALD CAMPBELL, President The Chase National Bank, New York, N. Y.

President Benson, in introducing Mr. Campbell, said:

I have the privilege this morning of presenting to you a speaker who is well known in your city and needs no introduction to a Seattle audience. He came here, I am informed, some 33 years ago, after graduating from college and from law school, and made Seattle his home for a number of years. In 1912 he entered the service of a bank in this city whose officers have for many years been close personal friends of mine, the Washington Mutual Savings Bank. He was first elected Assistant Secretary in 1912, later becoming a Vice-President and director. Later, he had a call to come back to my City of New York, and he did so, to accept the Vice-Presidency with a New York banking institution. Since 1930 he has been an officer of one of the greatest banks in the world, the Chase National Bank of the City of New York. This gentleman is a leader in metropolitan financial affairs, and he actively participates in the commercial life of the country. He is well qualified to speak to us on this subject assigned to him.

Mr. Campbell's address follows:

I am asked in this short talk to you today to take a look into the future. Any attempt to forecast future events lies in the realm of prophecy, and the lot of prophets is not a particularly happy one. However, there are certain underlying truths which we can appraise, and certain forces which we can test. I shall attempt to do so, but will ask you to keep in mind the symbol sometimes attached to balance sheets—the letters E and O. E., certifying that the account is all right, except for errors and omissions.

At the outset, however, I should like to make one unqualified prediction. In my opinion, banks, both large and small, have a future in this country, and a future of such consequence and significance that the trials of the present will recede far into the background of our memories. Not as yet are the services we render so outmoded that we stand in danger of being relegated to some museum. The work in which we are engaged is much too vital and essential in the conduct of the business of the country.

Adaptability of American Banking

In the development of the United States from a fringe of sparsely settled communities along the Atlantic Seaboard to a great nation, banking institutions have made an indispensable contribution. Economic activity and growth have been financed, the use of savings facilitated, and funds transferred readily from one geographical area to another.

In the pre-Civil War period, the Suffolk banking system of New England, the commercial banks of New Orleans, along with many individual institutions in different parts of the country, established high standards in banking policies and practice. The post-Civil War period witnessed the continued development of State banking systems and the growth of the National banking system.

Through the entire history of this country, the banking system has been in a constant state of development. It has had to adapt itself continuously to changing economic conditions. It has survived severe depressions and deeply rooted political antagonisms. One hundred years ago, anti-bank sentiment was particularly violent. As serious as this animosity seemed at the time, it proved to be but a temporary barrier. In that situation, as in others, the importance of credit institutions to the country's well-being was soon realized.

In this process of constant adaption to environment, banks located in centers of industry and commerce grew as industry and commerce grew. Many had to be large in order to take care of the enormous financial demands of big enterprises.

Size in and of itself is not an iniquitous thing, nor yet a dangerous thing. It must always be borne in mind that size is relative to surroundings. In many respects the relation of the big bank to a large business is precisely the same as the relation of the country banker to the farmer or local tradesman. American banks, whether they be large or small, all take deposits, all make loans, when they can, all buy Government obligations, all buy bonds, many have trust departments, and most of them hold securities in safekeeping for their customers.

Services of the Metropolitan Bank

At the same time, the metropolitan bank has developed special functions as a wholesaler of credit for the purposes of the security and commodity markets, as corporate and personal trustee, as an agency of international payments and a provider of credit for foreign trade, and as a correspondent and depositary for banks throughout the country.

The process of growth and adaptation has been a continuous one. In recent years, investment service, oil and public utility departments have been organized. Personal and instalment loan departments and metered checking services have been provided. Branches have been opened for the convenience of neighborhood customers. These functions do not differ so much in kind, as in magnitude from the services which small banks habitually render to their customers. As a matter of fact, the facilities which a big bank renders to its banking correspondents places at the disposal of smaller banks and their customers the services of the metropolitan bank. This bank system of ours provides an extraordinary example, vastly beneficial to the development of the country, of local self-government in banking.

The financial power of the United States is held by the customers of some 14,000 banks, scattered all over the country, ranging in size from the neighborhood bank in farming communities to the metropolitan banks situated in the centers of industry and commerce. These big banks, while some of them compare in size with the largest financial institutions abroad, do not comprise a group of four or five great banks which, through their myriads of branches, make up practically the entire commercial banking strength of a country, as is the case, for example, in France and Great

Britain; but each compares in all respects except size with almost any one of the other 14,000 banks in the United States. We are all subject to rules and regulations, as every banker knows, but no one bank in the exercise of arbitrary power can choke off the flow of credit to a thrifty business man. This vast banking net-work with 14,000 outlets makes it possible in almost every year and almost every season for the worthy borrower, whether large or small, to get a loan when he needs it, irrespective of the bias or predilection of any individual banker. How much this has meant to the growth of American industry and commerce no man can ever justly appraise.

Common Future for Large and Small Banks

What I have said about the likeness between big banks and small banks in the services they render the public, suggests that we cannot speak about the future of the one without also speaking of the future of the other. Whether the institution with which we are associated is large or small, we live and work in a common economic and political environment. Whether located in industrial regions or in farming communities, whether primarily commercial or investment in the services rendered, all banks will be equally affected by those factors that make for progress or retrogression.

Each and every institution, whatever its size or character, will be subjected to the same stresses and strains, the same trends and developments. The work they both do—indeed, the work they have done—for the development of the country, is so similar that it is impossible to foresee the future of either the large or small bank without attempting to forecast the future of the banking system of the United States as a whole.

Present Conditions Not Necessarily a Guide to Future

Exclusive emphasis on present conditions could easily make one pessimistic as to the future of banking. The bare subsistence level of bank earnings, the legthened character of commercial bank assets, a decade of Federal deficits, the sub-normal level of economic activity, the vast numbers of unemployed, are ever present in our consciousness and could readily cause us to despair.

This brings me to the question which I think underlies our whole discussion. Will future conditions in the United States still demand services from banks in a volume sufficient to support the vast banking apparatus as we know it? Bad though the current situation is, the experience of the past has shown that prophecies based on current conditions are frequently wrong. Beyond our limited horizon lies a future that I feel will be far different from the dire predictions of some of our contemporaries.

The great American system of commercial banks has as its primary function the supplying of credit in response to the legitimate demands of business. While the field of credit has become immensely wider with the passing of the years, the extension of credit to business still remains the function to which we are most accustomed and which I believe will once again attain significant proportions.

In addition to the function of supplying credit, American banks have taken on innumerable services which they perform for the public. Those outside the banking profession are frequently as unconscious of the many services banks perform as they are of the air they breathe. American banks, more so than those in other countries, are generous in the multitude of functions performed for customers, which are indispensable to a smooth operation of business. They must be rendered by some organization. The commercial banks have done this work in the past and have the facilities to do it in the future.

Costs Incurred by Banks in Services Rendered

In serving as the bookkeeper of the country and as a source of credit information, the banking system is involved in heavy costs. The magnitude of these is little appreciated outside of our own ranks. However closely we watch costs and try to keep down operating expenses, the outlays for these specialized services press heavily upon us. In other days they were easily met out of the proceeds of lending deposits. What a mockery it is, in these days of ever mounting deposits, that we have come to look upon them, not as a means of revenue, but as an added item of expense! I know of one bank which pays Federal Deposit Insurance Corporation charges of many thousands of dollars a year on funds received last spring from nervous Europeans. And those deposits are merely lying alongside the rest of the excess reserves.

And now, in this same general connection, I want to say a word on a sensitive subject, that of service charges. In their efforts to meet the existing situation, many commercial banks have been forced to charge for services which they formerly did for nothing.

The imposition of these charges, although necessary and justified, cannot in itself, in my opinion, restore bank earnings to a reasonable level. Such charges are no substitute for an adequate return on loans and investments. At best, they can account for but a small proportion of gross earnings.

Lest I be misunderstood, I want to emphasize that I fully approve of the policy of making service charges. In the case of many individual institutions, they have made the difference between profit and loss. Cost analyses should be made carefully and the charges imposed should be related to the specific services rendered.

In this connection it is worth noting that service charges are practically universal among banks on the Continent of Europe. These are imposed despite the fact that those institutions have sources of income not open to American banks. Not only are activity charges imposed on accounts, but sometimes charges are imposed for inactivity also.

The Causes of Low Earnings

Earnings are low, of course, because the volume of normal bank borrowing is low. Average rates of interest on loans have this year reached the lowest levels in financial history, and yet low rates have not perceptibly stimulated increased borrowing. Business borrows money when it can use the funds profitably. Artifically low interest rates constitute one major cause of low bank earnings. Another is the widespread decline in commerce, both domestic and foreign, and a third cause has undoubtedly been the apprehension of war.

The large city bank, even more than the smaller institution, has suffered from the decline in loan and investment return. Interest rates in the financial centers respond much more quickly to changes in monetary policy than do those in the smaller communities. The deposits of the large bank turn over more quickly. Its assets must be of shorter maturities.

In consequence, to an extent greater than is true of smaller institutions, it has had to forego the return on long-term bonds, which, low as it is, is higher than the infinitesimally small return on short-term obligations.

Added to the handicap of low interest rates is the fact that to a varying extent all banks must face the competition of some Government credit agencies. I would not call attention to this competition unless at the same time I were to give full recognition to the effective work done by certain Government credit agencies in the matter of financial reconstruction during the great depression. To go beyond this and to make use of funds borrowed from commercial banks at rates of interest fixed at artificially low levels in order to compete with these same commercial banks, struggling desperately to sustain themselves, seems to me to be both unfair and short-sighted.

General Effect of Easy Money Policies

Commercial banks are not alone in experiencing the consequences of the present national monetary policies. The easy money policy has permeated the entire economy. The thrifty and prudent have been penalized through its effect on the return from their savings and investments. Millions of individuals are paying more money for life insurance which they carry to protect their families and dependents. Universities and endowed institutions have had to curtail essential services, increase charges and reduce salaries. The easy money policy has constituted a heavy tax upon all who possess capital, whether much or little.

In my opinion interest rates cannot remain pegged at their present levels. Existing rates do not represent an equilibrium between savings and the demand for long-term funds. For a time the true situation has been disguised by Government deficits, by the financing of these deficits through the banking system, by the swelling of bank deposits, and by the growth in excess reserves.

Until the beginning of September this made for an inflation in the bond market comparable to that of the stock market a decade ago. That this could not continue indefinitely has become strikingly evident to us in the past few weeks, and I have no doubt that interest rate, in time will rise to less artificial levels.

Low Bank Earnings a Matter of General Concern

The question of bank earnings concerns not only men like ourselves who are operating banks. It concerns the whole country. The reasons why earnings are a matter of national importance are easy to see, and I shall run over them briefly.

The first is one I have already touched upon. Banking services of a non-lending nature, which are so important to the business life of the country as a whole, do not pay their own way and are, therefore, dependent upon the general earning capacity of banks.

The second reason why bank earnings are important to the business public of the country is that net worth must grow if a suitable ratio of capital funds to rising deposit liabilities is to be maintained and if new banking capital is to be provided for the future. America has not stopped growing, and American business will need a strong and growing banking system. The need for adequate reserves against losses on loans has been amply demonstrated in the past, and national and international economic life has hardly become so stable that losses are not to be expected in the future. When this risk factor is taken into consideration, I sometimes wonder if in reality we are getting any interest today on our loans and investments.

I am not suggesting a mandatory capital-deposit ratio for banks. Such would be the height of folly. Whether a particular capital ratio is adequate or not depends upon attendant circumstances. The cash holdings of banks, which are very large now, must be taken into consideration as well as the quality of bank assets. All that I am suggesting is that a growing business, subject to unpredictable risks and uncertainties, should have a growing capital account. The present low level of bank earnings, a condition which tends to influence banks to assume greater loan risks, makes the building up of the capital account a difficult task.

In the midst of war uncertainties banks to an increasing extent will be obliged to revise their conception of the risk factors involved in fixing rates of interest on loans. Excess reserves or no excess reserves, we must have an insurance element of a substantial sort in our rates if we are to lend our depositors' money safely in the midst of a great war. In the last war both banks and businesses increased their surplus and undivided profits accounts while the boom was on—and those capital reserves were their salvation when the post war liquidation came. There may be more differences than resemblances between the course of the last war and the present war, but I have great confidence in the proposition that, sooner or later, we shall find a strong capital structure and an adequate liquidity exceedingly welcome in a time of readjustment.

New Lending Fields

As I suggested before, the banking system of the United States is a living thing. It has had to adapt itself to changing conditions in the past and will continue to do so in the future.

In searching for needed sources of income, commercial banks in recent years have ventured far into new fields of lending, sometimes reluctantly, sometimes tentatively, sometimes experimentally. One of the most important of these is that of term loans, which have come to occupy a significant place in the portfolio of the large bank.

A recent study by the Board of Governors of the Federal Reserve System revealed that the total of such loans comes to well over $1,000,000,000, or 25% of the total volume of commercial, industrial and agricultural loans of all reporting member banks. Over half the total volume of such loans has been extended by the New York City banks.

The growing competition for such loans has led to lower rates of interest, to longer maturities and to a concentration of payments in the latter part of the life of the loan. In view of the risk factor attached to long-term capital loans, such concessions are not reassuring. There are always possibilities of changes in management, in business conditions, or in the competitive situation of particular industries, any one of which would greatly alter the position of the borrower.

Existing conditions have also forced banks into the field of personal loans and retail instalment financing. So important has this activity become that the Association of Reserve City Bankers sponsored a very extensive study of this entire field.

The Commercial Loan Demand

Given an improvement in business conditions, commercial loans will experience a sharp revival. It will be remembered that the commercial loans of all member banks increased between June 30, 1936 and June 30, 1937—a period of marked business expansion—from $5,400,000,000 to $6,700,000,000, or by $1,300,000,000. This was one of the most rapid rises in bank loans ever experienced in a comparable period of time.

The recent trend of business activity has been encouraging, and I believe that it will not only continue to improve of its own momentum but that it will also receive a very decided impetus from the new conditions prevailing abroad since the early part of this month. I also have in mind the broader markets available to us in Latin America and other parts of the world because of the inability of the large industrial countries of Europe to devote as much attention to them as in the past.

Thus we may expect an increased use of our superabundant bank deposits, a quickening of productive activity, a rise in capital values, and finally, greater employment and a fuller utilization of existing plant and equipment. To set this sequence in motion complete recovery is not required; the improvement we are now experiencing should be sufficient. And I need hardly add that when business men can look forward with confidence to the future policies of the Government, the pace of the improvement will be accelerated perceptibly.

Already there is increased borrowing demand. Rates of interest have shown a rising tendency. Banks are going to have larger income from current operations than seemed probable six weeks ago. We should and will lend to all sound applicants for loans. If a war boom develops, we must remember to apply all those safeguards that bankers know how to apply in protecting the quality of bank credit—

we must do this in justice to our depositors and in fulfillment of our duties as trustees of the country's finances. Our vast excess reserves remove one of the great safeguards of sound banking—namely the necessity to watch our cash position every day. All the more reason for a rigorous application of credit standards.

The Alternatives

May I reiterate my faith in the future of banking for both large and small institutions? There will be hardships and difficulties to overcome. There will be inflationary dangers ahead of us. The way will not be easy. Yet I have confidence in the present generation of bankers to solve future problems. The fact is that the American banker, more than ever before, fully appreciates his responsibility to depositors and to the general public. He realizes that his office is a sacred trust, to be exercised diligently, prudently and competently.

It seems to me that the functions performed by the American banking system—both those that are paid for and those that are not paid for—are of such paramount importance to the economic welfare of the country, that they have to be continued. If there are no banks to do the work, someone else must do it. And that someone else is obvisouly the Government itself.

He is the alternative: Either a banking system with 14,000 outlets through which commercial credit is administered by the friends and neighbors of the borrower, or a centralized banking system operated according to rules and regulations prescribed in Washington and interpreted by employees of the central authority.

It does not matter for the purpose of this discussion whether the central authority is Republican or Democrat or something else. Opportunity for oppression or restriction or political misuse of the lending power would be identical whatever party might be in control; the only differences would be those inherent in the quality of the administrators.

Putting it very simply, the question is whether the American people want commercial credit administered by themselves, their friends and their neighbors, or whether they want it administered by political appointees. Does any American business man want to have the decision on loans controlled by district leaders?

Stated that way, there is no doubt which of the two systems the American business man wants. Stated that way, there is no question how the American voter would decide if the matter were left to his open and shut decision. The danger is that, through a process of attrition, the banking system as we know it may be worn away and before the American voter realizes it, the change from one system to the other will have become complete.

Is that possible? A couple of years ago, I should have answered yes. But since then there has come a change. Congress, not once but many times, has reasserted the powers granted to it by our forefathers. Little by little, the American people have re-learned economic laws, and have found that they cannot be set aside by legislative enactments or violated by Executive action without penalty.

The American Heritage

Surely, no nation ever established under the sun has realized in like degree the ideals to which we all aspire—liberty of thought and speech, freedom of action within the law, individual power to rise as high as the native capacity of each allows. Within this frame of law, our people—thrifty, industrious and self-reliant—drew upon the stores of our national resources, grew great and prospered. The material things that we regard as commonplaces, other nations look to as their ultimate hopes.

Despite the economic reverses of these recent years, despite the adverse circumstances in which not a few of our fellow citizens have been trying to carve out a livelihood, still the standard of living in America remains for the vast majority the highest yet attained by any nation. In these days of economic adversity, it is easy to lose sight of these accomplishments.

We still have new frontiers to conquer. Scientists tell us that we are on the threshold of revolutionary industrial change. In hundreds of laboratories, in a thousand drafting rooms, in the fertile and inventive minds of uncounted numbers of our citizens, there are fermenting and growing schemes and methods and new ways to increase wealth. Technology is still an active force and a dynamic people will always develop new techniques and better methods. The American people will not be satisfied with an illusion of economic security obtained through the pegging of prices, the limitation of output, the dissipation of savings and the loss of individual initiative. The present attitude of negation is but a passing mood.

Let us remember that no party, no group, no man, has any patent on an easy road to a land of plenty. Let us remember that phrases and symbols are dreams, unless they are keyed to the realities of life. Let us not be led into error by the oft-repeated slogan, "human rights before property rights." Property rights are human rights, built out of the sweat and toil of millions and tens of millions of our people who have labored all their lives long that they and their families might live each year a better and a more abundant life.

My own optimism as to the future role of banking rests upon my conviction that we shall return to conservative fiscal policies and that economic activity will surge forward in this country. My conviction that such will be the case arises from my faith in the spirit and temperament of the American people. I have great confidence in the ultimate good judgment and indomitable spirit of our people, and, in the long run, political and economic activities reflect a people's temperament.

It is my reasoned judgment, that the spirit and will that conquered a continent, that survived a civil war, that lived through past depressions to enjoy a richer and fuller life, will not die. The American spirit is the spirit of the pioneer, of the innovator, of the trail blazer. It is a spirit born of a vigorous and self-reliant people, who will not be content to rely for long upon the largess of a paternalistic government. Our pressing problems will be solved, in the future as in the past, through the combined efforts of a courageous, independent people.

The Economic Effects Upon This Country of the Present European Conflict

By Dr. Paul F. Cadman, President American Research Foundation, San Francisco, Calif.

In introducing Mr. Cadman, President Benson of the Association, said in part:

We are fortunate in the selection of our next speaker. He is an economist who has the happy faculty of making economics truly interesting. He received his early training at the University of California, earned a Doctor's degree at the University of Paris. He had been successively Executive Secretary of the San Francisco Stock Exchange, head of the Department of Corporate Finance and Investments in the University of California. Since 1936 he has been in private practice as a consulting economist. Since 1933 he has been an instructor in current economic events in the San Francisco Chapter of the American Institute of Banking. During the past summer, the students at the Graduate School of Banking at Rutgers had the privilege of listening to a series of interesting lectures that he delivered there. At present he is President of the American Research Foundation.

Dr. Cadman had kindly consented to talk to us this morning when we discovered that it would be impossible for Senator Pat Harrison to fulfil his engagement with us here. At that time we asked Dr. Cadman to discuss the subject which is on the printed program, "America's Stake in a Free Banking System." This all happened, of course, before the outbreak of the war in Europe, and since that subject was assigned to him, we have found it has been treated by other speakers at this convention, and in view of present world conditions, we have thought it wise to ask him to discuss instead of the topic in the printed program, "The Economic Effects upon this Country of the Present European Conflict." Dr. Cadman has been good enough to agree to do this. I know it is a subject that concerns us all, and I am sure that his address will interest us all intensely.

Dr. Cadman's address follows:

Mr. President, Ladies and Gentlemen: If I had not been so greatly sobered by the wise and far-seeing remarks of the two previous speakers, I think I would feel in a little facetious mood, for this is the first time that I have ever been called upon to pinch-hit for a United States Senator.*

Not so very long ago a good friend of mine, who is Vice-President of the Chase National Bank presented me to Mr. Campbell, and I was reviewing with him in his office

*U. S. Senator Harrison of Mississippi who had originally been scheduled to address the Convention.

one of my experiences in this regard, in which association and memory played me a very happy turn. I was supposed to be in a debate with the champions of the theory that you can generate wealth by spending money, and after a very elaborate and carefully prepared defense or, rather, explanation of the functions of money, my opponent in debate rose and said, "We are going to give away two and a half billion dollars. Do you want it, or don't you want it?" And I submit to you that that is an unanswerable argument.

However, when the audience was restive and the heckling began, there came to my mind a story which Ramsey MacDonald's son told some years ago when he was touring America. He said that the British students have really very little respect for public speakers, and that the Oxford Union, which should be the seat of everything that is sedate and conservative, frequently invited the politicians of the Empire to come down and address them.

On one occasion they had a very portly gentleman who was a candidate. It was a very warm evening, and he perspired profusely. He was not only very portly, but he was very sentimental. At a moment in his harangue he wished to say that his conscience was clear, so he struck a pose as best he could with his portliness, and he stretched out his arms to this student audience and said, or started to say, "If I should die tonight," but he waited just one fraction of a moment too long, and a very disrespectful student in the back of the audience put his hand up to his mouth and called out, "Then the fat would be in the fire."

It is patent that this is no time for pride of opinion or even for the exploitation of the special advantages which may have come either through experience or study on the part of any who attempt to analyze and review these difficult days.

I am feeling with you very deeply the fact that the overwhelming opinion of the American people, as expressed not only by their officials but by the polls, is the declaration that "we wish not to participate in this struggle." I think neutrality is perhaps an unhappy word, because it implies that we do not take sides, and that is not so. What we mean is that we do not wish to participate. Whether or not that opinion will prevail, only time can tell. But it is clear that at this moment we have expressed our will in an overwhelming degree that we do not wish to participate.

That very fact alone makes it possible for us to do some analyzing and reasoning about our own state of affairs which otherwise would not be possible. If we were in a condition of emergency, if we had declared war, then all of us with any consciousness of the importance of national participation would temper our criticism and we would offer our complete support to whatever Government agencies had to be established, no matter how arbitrary they seemed. But since no state of emergency exists, we are in a position to discuss fully and freely and frankly the state of our own freedom and of liberty as it exists here.

Needless to say, we have not escaped the consequences of this war which has been in progress now less than a month, and already there have been the effects upon our markets. Sound cautions were given to us this morning regarding that, and I shall speak of this again in just a moment in the extemporaneous review which your President announced.

But before I do that, I feel very deeply the burden of saying that among the things that threaten our liberties most are the deliberate appeals to discontent, and that if as a people we are to escape the psychologies and the philosophies and the influences that have destroyed the liberties of 300 millions of people in Europe, we must be on guard against those persons and those agencies who deliberately stir up our people to discontent, for the appeal to discontent is the appeal to human weakness, to the sense of defeat, to inefficiency and ineffectiveness and futility in living. There are among all peoples at all times a segment, at least, who come under the classification of the failures.

Well, you and I have watched this appeal to discontent and it has come as a result of the operations of the workings of the great laws of supply and demand since the declaration of war. Four times in the last week I have turned the dials of my radio and listed to organized discussion quite obviously programmed and planned to persuade a large number of our people that any and all price rises in the American markets were due to racketeering, and nothing could be further from the truth.

There are racketeers in human society in every stage of history that has ever been known, and they are not at all economic racketeers. The political racketeers have vied for distention in this field.

But the deliberate attempt to persuade the American people that there are selfish men who deliberately sit down and propose to benefit by the sufferings of the people in a time of crisis like this is an outrageous thing, and it is high time that our people understand that these forces of supply and demand which are at work, even though they may be interfered with and even though they are from time to time curtailed, are so great that no government or no coalition of governments or no individual can interfere with their operations.

What you had in these recent weeks was a recognition that when 10,000,000 men are under arms, the production goods will be curtailed, and what you had also was a recognition that when the shipping of the world, both that of belligerents and neutrals, is either handicapped by hazards or is actually drafted for the exigencies of war, the transportation also becomes scarce, and you lift off from the surpluses and from present production the pressures, and you create by natural processes a seller's market instead of a buyer's market, and there isn't anything you can do about it.

We have been slow in recognizing that in this country we spend more than $500,000,000 a year for rubber. It is the largest single item of import into the United States in terms of money spent. The second commodity in that category is sugar. When you have these tremendous demands for these commodities and a recognition either that production will be curtailed or that transport will be difficult, immediately demand asserts itself, and not only nations but purchasing agents and individuals, yes, even the housewives, begin to lay in supplies, and what happens is that there is bidding for existing stocks, and the bidding for existing stocks is an influence on prices which can never be denied.

Some people say, "Does this mean that because there is a war, America is to have prosperity?" The answer is that throughout all time, since man has begun to produce and save in quantity, his estimates of value have fluctuated in a long sweeping wave length which we call the business cycle, and that reflects his reactions toward the existing stocks of the things that he most needs and that he most wants.

If America finds herself in the position where at the moment she has certain supplies which are wanted, not only the world around, but wanted in this country because of the threatened shortages and because 10,000,000 men are under arms and taken out of production, and because transportation is limited, then the price rises in America are not only inevitable but in the long run they are uncontrollable.

But this not mean that we are faced at this moment with the possibility of boom conditions. The bulge in the stock market has been misinterpreted by many, and there is the careless assumption that somehow we may have a repetition of what happened between 1914 and 1918.

I was deeply impressed with the wisdom and validity of the findings of your Committee on Economic Policy. I would like to add to those findings just this word of evidence which is already known to that Committee, namely, that there is a vast difference between the conditions which now prevail and the conditions which prevailed at any one of the epochs of the last war, either 1914-1915, or 1915-16, or any other of the epochs, because generalizations about that whole period are useless and averages for the whole period do nothing but conceal the facts. But if you take the conditions at the opening of that war and compare them with the opening of this war, you will find the evidence which appears at this moment to be strongly against our having a war boom. It is one thing to have a firming of prices—we have already seen that for the most part it was good, because as the price of money was too low, so the price of a great many commodities was too low in terms of the human effort that it takes to produce them.

What we witness today is a different set of conditions, and there is little likelihood that this market will suffer—and I use the term advisedly—a boom, even though it may enjoy a firming in its price structures. The reasons why it is not likely to enjoy a boom—if you think that a market does enjoy one—the reactions are usually too violent and too destructive. Let me trace for you very briefly the history.

In 1914, England and France were not ready for war. They were taken by surprise. They had to mobilize quickly, and they had to organize meager forces. In 1939, they had been preparing for war for more than 3½ years, and even though it is said they were not ready, their preparation was enormous.

In 1914, England and France had immense purchasing power, and their credit, so far as international credit was concerned, was at the peak.

In 1939, they, in common with all of the democracies, had extended their credit so far by processes said to be social and said to be for reconstruction, that that credit is impaired, which is not to say that it is destroyed, for it is not.

In 1914, England and France advances to their eastern allies, to Russia, to Serbia and others, $3,200,000,000, most of which was spent in America. No such situation today prevails.

In 20 years that have elapsed since the outbreak of the great World War, the productive capacities of the entire world have increased enormously, and the capacities of France and England have increased, as have ours, and there is in the world today not only stored up goods for this war activity but there is the immense capacity of a vast and developed and modernized industrial output.

I can see nothing in the present scene which indicates that type of inflation which reaches boom capacity. On the contrary, it seems to me that inflation at this moment is remote. One ought to reckon with the immense powers of production, one ought to reckon with the paralyzation of transport, one ought to reckon with the conditions in the money market which have been so accurately and helpfully presented to you this morning, and in the findings of your Economic Committee. One ought to see that the stage is not set for one of those furious periods of demand. The purchasing power which France and England have in terms of American securities which they hold and of their present gold reserve will no doubt be conserved, they will not be spent quickly but will be held in check against the emergency that may develop if and when this becomes a long war.

So we ought to be very sober in our reactions to this matter. One can never help the flurries of human hysteria in the stock market. The stock market itself may have been at levels in which there was a genuine reflection of the withheld demand in this country which was beginning to express itself when this catastrophe was announced. The boom in the "war babies" is a thing that you could expect, it is a thing that is very easy to understand, because the speculative mind is seldom analytical, it does not go down into the history, it does not consider the figures, it is not often concerned with a balance sheet. But that market will correct itself. It always has, and it has great strength within it because it has been heavily liquidated over a long period of time. I can see none of the forces that will unsettle our price structure nor can I see any of the forces that will bring it to boom proportions.

With the firming of these price structures, they will be immensely valuable, and one does not need to apologize nor listen to the shallow argument that we shall enjoy some advantage from the suffering of Europe. In this Western country of ours, there were vast quantities of fruit processed, in storage, and the growers and the producers and the brokers alike were facing heavy losses, which losses they have taken again and again through the past four or five years. The bidding for those stocks taking place not only in the countries that are affected by the crisis but within our own country, has strengthened the prices as little as one cent a pound in dried fruit and has changed the picture from anticipated loss to anticipated return.

There is evidence that the forces of supply and demand are at work and that somehow they transcend all of the desires and all of the ambitions of those who would dictate our economic life. This is not to say that the dictator does not have power over prices nor is it to say that an arbitrary Government does not and can not regulate prices, but it is to say that the great, sweeping forces of supply and demand are a reflection of what men want and a reflection of what men feel and think when they are faced with shortages of what they want. And so those forces are at work.

It seems to me that we ought to be very humble in their presence because they are an evidence of the thing that we wish to preserve, namely, that situation which is euphemistically called a free enterprise system. That free enterprise system is a part of the American way of life. It is not the selfish product of a group of men who have been classified or, shall I say, degraded by all of the language of abuse today, for no group of men ever met together at any moment in history and invented a thing called capitalism. It did not happen that way.

At some time in the history of the world, primitive man saved a little, and when he saved a little, even if it was only a handful of grain, in a rough brick kiln, that was lined with lime to keep out the rats, he had potential capital.

The interesting thing about the operation was two manifestations of constructive human activity—first of all, he exerted the effort to create that surplus, and, secondly, he exerted the sacrifice to save it. Out of those two things there arose a pattern of human behavior which has been badly named and which is badly called capitalism. It was that pattern of human behavior that gave us the vast stores of wealth that made possible the standard of living which we now enjoy. Nobody invented it and nobody forced it upon an unwilling society.

In the operation of that pattern of human behavior there came out this means of measuring value, which is to say, What are things worth to men? They are worth something to men in terms of their desirability and their scarcity, and you interpret that worth by a device called price.

I know there are racketeers, and I know that they operate in every stage of human history, but these great forces that are at work today are the natural forces of human behavior and as such we may recognize them and respect them as long as we do not abuse them, and this free enterprise system has significance for us for many reasons.

If I should have the opportunity to ask the American people one great, penetrating question in this hour, when we have declared ourselves against participation, but when we have taken sides with France and England, I should like to put this question: What is the outstanding and deepest issue which America faces today?

I believe it to be this: How far can they surrender their economic activities to a centralized Government without losing their political liberties?

Let that question be answered not by oratory and not by hysteria and not by emotional appeals, but let it be answered by the review of every free institution which we enjoy, and it is not a question of control or no control, because at all times we have submitted to reasonable regulation. It is a question of the degree of control, and at the heart of a free enterprise system there stands or should stand a free financial system, because the financial system is the manifestation of the modern working of the principle which I mentioned, namely, work and sacrifice determining values, and the financial system gives us the instruments to measure those values and helps us to conserve them, and helps not only in the development of every productive force, but acts as the sieve through which every project must pass to find out whether it has a reasonable claim upon the savings of the provident.

Therefore at the heart of every free system of enterprise there must be a free system of finance. And what is a free system of finance? How far is it possible to legislate concerning the activities of individuals who wish to invest? How far is it possible to fix the values of money by decree? How far is it possible to extend the credit structures, since credit and money go hand in hand and perform the same general function, namely, the facilitation of exchanges of goods between individuals and between groups? How far is it possible for us to establish those bureaucratic controls which never escape from political influence, in which bureaucratic controls we surrender the direction of our financial life to men who have not had experience? And what is the difference between the controlling influence that is exerted by men of experience and the controlling influence which is exerted by the politician?

It is all the difference in the world, because in one case you bring to bear the judgment of men who know what can be done and what cannot be done with safety, and in the other case you bring to bear the wills of men that are concerned only with the popular approval of their constituents.

Now somewhere in this moment, when we have time and when we are not yet in the period of emergency that stifles criticism, we must review the state of freedom in America, and this is not to say that we will not recognize social improvement when it was due, and that we will not accept the controls and the regulations which are legitimately put upon the selfishness of men, but it is to give in simple definition the meaning of a free bahking system and of a free enterprise system—and this is no recapitulation of classroom economics.

I don't have to review for you the extent to which Government control has now taken charge of our financial ininstitutions and functions, but I do say this, that whenever any Government, whether it calls iteself a democracy or not, embarks upon a policy of distributing wealth or redistributing wealth which has not yet been created, through issuing promises to pay or through the distribution of bounties, that Government has opened the door for disaster. And if there were on the ballots of 18 States last November the proposals to distribute wealth by increasing the velocity of money and if necessary by printing money of a spurious nature, it was because there had been years of the organization of discontent and the deliberate propagation of the illusion that you could get something for nothing. In my State we will shortly vote on a project. It has a dramatic sort of name, because it appeals to the appetite, but make no mistake, if that measure passes in California it will become an issue in the Presidential campaign of 1940; and if one million people vote for it in California it will be only a reflection of the millions throughout this Nation who have been led to the illusion that somehow the Government can take care of them, that somehow there is bounty to be distributed from a source which is never named, and they have been deliberately kept from the knowledge of the fact that wealth is produced by those who work and it is conserved by those who save, and that group alone is able to give any semblance of security.

Your afternoon program is on, and it is nearly 20 minutes after 12, and I am thumbing over these pages for just one or two paragraphs which I am eagerly anxious to bring to you. Let me repeat that at the heart of a free enterprise system there must be a free banking system, because no political agency can be trusted with the function of lending money. When any political power goes so far that it can fix the value of money and extend its credit, and when it can operate in the field of foreign exchange and influence the domestic interest rate and can itself engage in lending to private individuals and to public and private corporations, then it has the destiny of all industry in its hands.

There is a great meaning for a free banking system. The free banking system should serve those who operate a free enterprise system, who are willing to work and venture and save, and in the operation of that system is the liberation of their own personal powers of choosing and of selecting and of standing by their judgments whether they are bad or good, and in that activity is the heart of the thing that we call political freedom.

I listened to your President's closing remarks this morning with a deep sense of appreciation. There came to me while he was speaking a little phrase from the English prayer book on which I had the good fortune to be brought up, and since he appealed to us for a reassertion of our faith, I venture to bring it to you without any excess of emotion. In a very beautiful prayer which was repeated for centuries by men who lived in stress and strain, it was written: "Whose Service Is Perfect Freedom." One reason why this Nation rejoices in being Christian as opposed to the paganism of the totalitarianism of the modern world is because Christianity respected the individual and recognized in him a free, choosing agent, with the right to be what he would be and to standor fall by the consequences of his own judgment.

And so, my friends, we stand, as your President said, in a period of great emergency. Let us not be carried away by the forces which would influence our price structures temporarily with hysterias and bad judgment. Let us rely upon history ano look carefully upon the conditions and compare them line by line, for every bit of data is available as to what happened in 1914 and as to what is happening now, and if and when you and I are called upon to realize that the great, underlying issues in this conflict are the issues of human liberty, then let us put every safeguard about the free institutions of this country which are economic and political and the two go hand in hand and cannot be separated, and in that moment you will do well to guard your functions and your prerogatives as the representative of a free financial system at the heart of a free economic system.

The Future of the Country Bank

By Ernest L. Pearce, Executive Vice-President The Union National Bank, Marquette, Mich.

Had I been assigned the subject "The Future of the Country Banker" instead of "The Future of the Country Bank" it would be possible for me to dispose of it in short order by relating the experience of one of our fellow bankers. A young member of a 4-H Club, we are told, was interviewing his local banker in an endeavor to make a loan with which to purchase a heifer. The banker finally told the boy he was convinced that if he lived he would pay the obligation. "But," said the banker, "what will you do if you should die?" The lad thought a moment and replied, "Well, if I die and go to heaven I'll have to mail it to you, but if I go to hell I'll simply hand it over to you."

It's no wonder we are all headed in that direction, considering the job we are expected to do. Some country banker outlined his task in this manner: Bankers are expected to accept money from anyone who has any, pay too high a rate of interest for it, loan it without limit to everyone who wants to borrow any, at too low a rate of interest, and always be ready to return it to the owners without a moment's notice and to never lose a penny.

It is indeed fortunate for me that the future of the metropolitan bank was so impressively outlined by Mr. Campbell in his address yesterday. For I am convinced, and I know the great army of country bankers sustain me in the idea, that so long as the country banks train, develop and turn over such able and competent bankers to manage the big city banks, we may expect the very results Mr. Campbell predicted for them. And so long as there are successful metropolitan banks there is a need for and a future for the little old country bank.

When I speak of "the little old country bank" those outside of banking circles may possibly be inclined to associate it with the "horse and buggy" days. Despite the fact that there are but half as many of them as there were the 20's, the country bank is still just as important a cog in the banking wheel as at any time in banking history.

The Country Bank—Its Definition, Position and Traditions

A general definition used by many people simply classifies a country bank as one not located within a metropolitan area. In the Federal Reserve Act "country member banks" is meant to include all member banks located outside central reserve and reserve cities and, in addition, a number of banks in outlying sections of central reserve and reserve cities which are granted permission to carry the same reserves as are required to be carried by country member banks. In practice non-members are similarly considered in banking circles.

An analysis of the banking structure shows that of all the 15,000 commercial banks in the United States 91% are located in towns of under 500,000 population and thus qualify as country banks. These same banks account for approximately 47% of the total deposits of the system. The figures on Federal Reserve member banks show 94% to be country banks, with 29% of the total deposits.

These 14,000 country banks, 75% of which, we are proud to say, are under the banner of the American Bankers Association, with over 170,000 highly trained and trusted men and women, cooperate with the metropolitan banker to give the average American the best banking services on the face of the earth. Bradley, writing in a recent issue of "Banking," thus describes this service:

"In their various fields, within the limits of law and sound practice, they finance his birth, education, and marriage; build and furnish his home; cash his checks and collect his debts; clip his coupons and receive his dividends; safeguard his money and other valuable personal possessions; finance his funeral, execute his will and administer his estate.

"They help the American farmer buy equipment and stock his farm; plant, harvest, sell and deliver his crops and collect the proceeds. They furnish funds to help build, equip, maintain, and operate our American factories; supply raw materials; finance the manufacture, sale, shipment, and distribution of their products, and collect the payment therefor.

"They register and transfer the securities of American industry and faithfully administer the terms of their trusts in the interests of the American investor. They finance the shipments of our exports and imports and arrange the payments therefor in foreign and domestic currencies. They facilitate trade and commerce, serve producer, distributor and consumer. Through the purchase of their securities they furnish much of the money required by government."

This contribution to the social and economic welfare of the Nation is hardly in keeping with the picture of the "money changers" so often painted for the uninformed of the American banking system.

Surely there is a future for 14,000 country banks functioning today in such widespread and effective manner. These are the same institutions in type which set up and followed in the footsteps of the people who trekked in covered wagons along the Oregon Trail to this very ground on which we stand today, seeking farms and homes and stability. These country banks are the same institutions that followed in the steps of those who sought new frontiers in the gold rush of '49 on this same coast. The lofty ideals of these pioneers who sought the wilderness, unafraid, cannot be forgotten. These empire builders, these railroad magnates who linked the continent with iron rails; there steamboat pioneers who filled our mighty rivers with their craft—these actors in the living drama of American life—have for generations worked hand in hand with that rugged, conservative, helpful individual, the country banker, who has always been on the frontier of American progress.

The history of American business is written in the development of American banking. Had our banking system not marched forward in cadence with the almost incredibly rapid development of business, had it been less responsive to the needs of a new country, America would be far different than the America we know today. America would not have the far-flung frontiers, the intricate system of manufacture and commerce, nor the completeness of life and high standards of living that now prevail had banking not kept pace and met the demand which progress has placed upon it.

Surely there is a future for the country bank which has such a tradition and such a record of achievement.

The Country Bank—Home-Owned, Home-Ruled and Independent

The country bank we envision as a home-owned and home-ruled bank, an independent bank. We like that definition best, especially in this new era when we hear so much of branch banks, chain banks, and a central bank. We feel that the successful future of the country bank will be preserved if these new elements in banking are not permitted to supersede the long-established and typical American system of unit banking. We should carry the flag for independence in banking and local responsibility for the management of local financial resources as a matter of basic policy, for we believe that the path of centralization of power is away from Americanism and democracy whether it is in political or in financial fields. We know that when the local controls of credit and money are surrendered to the absentee interests, local social and political control are not long in following. He who controls the purse strings sooner or later usually considers it necessary, if only in self-defense, to control the political and economic life of the community as well. We should do what we can to prevent the development of any such banking concentration in the United States as has been developed in Great Britain and Canada.

"Country bank," "unit bank," "private bank" are almost synonymous terms. We often hear our American banking system incorrectly referred to as a private banking system with the implication that the banks are run by a few individuals and their friends for selfish interests. What we do have is a system of chartered banks under which authority is granted by the State or Nation to groups of individuals to render a banking service to the public under governmental supervision. Thus we have a dual chartered banking system which is one of the most democratic institutions in America. It is democratic in its origin, its ownership, its supervison, its methods and the number of people it serves. The democracy of our chartered banking system and the large number of locally-owned banks which we have in this country, as contrasted with the very few banks in the older countries of the world, constitute our greatest guaranty against monopoly of banking.

The country banker should be much concerned in the perpetuation of this system, especially in these times when, from the Administration in Washington, there is a growing propaganda for the further centralization of all government. The people of America, we are sure, are not in favor of branch banking on any large scale. Nevertheless the independent bankers should not leave to chance the measures with which they fight for public understanding of the system of home rule in money and credit of which they are the instrumentalities.

It will require the combined efforts of our 14,000 country bankers scattered throughout the United States, using every facility available, to combat this new trend. They should clearly and courageously express their views on this important matter. The branch banking issue is more far-reaching than the boundaries of a single State. There are individuals high in National Administration circles who would like to see nation-wide branch banking, with greater control over banking as a whole vested in Washington. The future of country banking will depend in large measure on the outcome of this attempt to effect concentration of control, especially the control of credit, which is the very heart of free enterprise. We confidently believe that such concentration is hostile to the fundamental philosophy of the American way.

Just one more comment while on this subject. We suggested that the country bankers employ every available facility at their command. We will never accomplish our end if we depend on legislation alone. We cannot expect to sit back and count on the American Bankers Association, our State organizations, or our banking leaders to pull us through. We must see to it that the country banks of this Nation keep abreast of the changing times and that our institutions render a service which will command the respect and admiration of the people.

In these days when we are in the spirit of the "World of Tomorrow," when the "horse and buggy" days are mentioned with derision, one must needs be courageous and optimistic to predict a successful future for the country banks. But we are convinced that the new frontiers which are on the horizon in this changing world require the country bank with its far-flung network of independent unit banks to the same extent as in the "good old days." Yes, indeed, there is a future, but it demands our constant and alert attention, for the banks of America are undergoing a fundamental evolution. We may expect elimination of those institutions, small and large, which fail to keep abreast of the changing times in meeting the community needs. We will get back to normal again if we maintain faith in a worthwhile future for the genuine America. Progress will come here as it has through the years, not from the top down, but from the bottom up. As in the past, banking will lead the way toward new horizons of progress in the upbuilding of America.

How, then, must we direct our activities to improve and preserve the country bank?

Streamline Our Banks

First, we should streamline our banks. We should perfect the functions we now perform. We must bear in mind that the banking business is selling, it is merchandising, just as in the commercial field, except that it has only one basic commodity to sell. The purpose of banks primarily is to buy and sell the use of money. We have credit and service to sell in much the same way the thousands of gas stations sell gasoline and service "to boot." Just recall the marvelous strides in the modernization of these stations, even in 10 years, and the manner in which service has been stressed.

A country banker in a business slump got a temporary job as a gasoline station attendant, and a customer, drawing up to the pump, requested 10 gallons of gas. Said the banker, "How far are you traveling?" The customer explained his journey in detail, whereupon the banker said, "Don't you think you could get along with five?" We can well reflect on this story in a comparison with methods pursued by some of our bankers these days.

Take a look at the methods of the chain stores in every community and witness first-hand what becomes of the country merchant who does not "streamline." But witness especially the alert progressive independent who "knows his stuff" and merchandises in the modern way. There are many examples of successful independents who have no fear of the "chains" because they have developed their merchandising technique in tune with modern needs.

Where would the railroad and the automobile industries have been today if in recent years they had not taken to streamlining, with all that term implies? Before the tracks of the abandoned street railways of our cities had been ripped up the buses which made the railways obsolete themselves became outmoded because streamlined Diesels became the rage. Similarly, the demand for faster, more flexible freight transportation has made a third of the $22,000,000,000 invested in steam railroads useless.

Can banking escape such changes? Decidedly not! If you feel that country banking is on the way out, just take a look at the experience in two very simple industries which have staged a comeback.

In 1921 some 100,000,000 phonograph records were sold in the United States. That was the peak. The next year the radio began to take hold. By the late 1920's, when all else flourished, the phonograph industry was given up for dead. Last year about 35,000,000 records were sold, equal to 1912, and all makers were far behind their orders. What did it? The combination radio-phonograph, the portable phonograph and "swing" music. Is the bicycle becoming passe? Back in the days of mutton sleeves, bustles and high gaiters, when the popular ditty, "On a Bicycle Built for Two," was the rage and it seemed that almost everyone had taken to wheeling, there were 400,000 bicycles in the country. It may cause a few eyebrows to lift when it is stated that nearly 1,300,000 were manufactured last year.

We must streamline our accounting and equipment, for this is a machine age. It would appear that many bankers haven't discovered this. It is important that the bank's products be properly manufactured; that is, that the banker keep abreast with improvements in the mechanics of banking. The old pen-and-ink method on ledgers, remittance letters and correspondence would have little change today in competition with the bookkeeping machines, the transit machines, the typewriters and Recordaks.

As merchandising today is devoting close attention to the packaging and display of a product it may be well for the banker to consider also the setting in which he works. Too often a bank's rooms, beautiful though they may be, create an atmosphere of austerity, of aloofness, even of unfriendliness. It may be that even some comparatively inexpensive alterations of the cages, of the check counters, the installation of air conditioning, remodeling or placing of comfortable chairs will aid in creating an air of cordiality, will help extend an invitation to the public to enter and feel at ease.

We country bankers should change methods—should change interior installations—should change the fronts—yes, should streamline and let the American public know that we intend to continue to grow in business for the next 50 years. We are encouraging and financing the restaurants, the retail establishments, the gas stations in our own communities to do this very thing. Why not do the same ourselves?

Make Banks Laboratories of Thrift

Second, to improve and preserve the country bank we should make our banks laboratories of thrift. The Government may regard the success of its cheap money policy as a triumph in Federal financing, but if it can take any pride in this accomplishment it is a hollow one, for it is at the expense of that great mass of people who have been brought up to believe thrift a virtue and who now find it difficult to derive a sufficient income from their savings on which they depended. It is indeed with keen regret that savings banks have been obliged to cut their interest rates to the bone.

The extent to which the so-called cheap money policy has gone is portrayed in a study of United States Treasury securities which reveals that interest rates have declined so low that an investor would have to own $100,000 worth of Treasury notes, maturing in a little over one year, to get enough return to purchase a newspaper every day. Worse than that! He would have to own $100,000 worth of the near-term Treasury bonds to obtain enough income to purchase a pack of cigarettes every day. But worse still! Had he purchased a million dollars of 91-day Treasury bills last December he could not from the entire income have purchased either a single newspaper or pack of cigarettes.

You may say these examples of yields on the short-term issues are not fair. Let's put it another way, using some comparisons with the '20's. To obtain an income of $1,000 per annum from Government bonds it would have required an investment of approximately $17,637 in 1920, $30,200 in 1933, or $42,735 in 1939.

And so it runs throughout the gamut of investments which heretofore had been designed to cater to the requirements of the thrifty. In the long run it will be the Government that will suffer most from its cheap money policy, for it is rapidly succeeding in killing off thrift, the real backbone of its security. We country bankers must be concerned, we must combat such tendency; we must meet the challenge and encourage thrift, and one way to do this is to make our 14,000 country banks "laboratories of thrift." Let us go slow in turning deposits away; let us be cautious before cutting interest rates further; let us find new ways to provide earnings which will permit at least respectable interest rates for the Nation's vast army of savers.

The banks and bankers of America throughout the history of our country's banking have persistently, consistently, and insistently preached the virtues of thrift, the economics of saved money or surplus. The deposits of all the bankers in the country on June 30, 1938, which amounted to $52,195,000,000, is something to think about. The remarkable picture of more than 44,500,000 thrifty savings depositors who in 1938 had accumulated savings of approximately $24,500,000,000, or $200 per inhabitant, is truly a wonderful achievement and reflects favorably on the country and the metropolitan bankers of America who encouraged this thrift and provided the facilities for its safe repository. The good they have accomplished in this direction has been illimitable, yet they have gone further in seeing that, so far as is humanly possible, idle funds are set to work in industrial and business situations which, by financial aid, would give employment and wages to millions of men and women who otherwise might have suffered hardship and want. This would seem to be the time of all times in American history when the virtues of individual thrift, instead of being sneered at in high places, should be extolled. All that the American public needs today is some assurance that the homely virtues of hard work, individual initiative and thrift are to be rewarded and not penalized. It is our own responsibility and privilege to help, to serve, to disseminate the time-tested doctrine that thrift and truth still are right and shall prevail.

The future of the country bank is linked with this doctrine.

Go in for Research

Third, to improve and preserve the country bank we should go in for research to carry the business of the country bank into broader and more useful fields. Scientific research in banking is just as necessary as in any other line of business or industry. It has saved the day for many of our large concerns and can do as much for banking. There is an imperative need for research as we face the opportunities and responsibilities of these changing times. Its development should not be confined to the activities of the American Bankers Association, which has not only early recognized the need and made remarkable strides in this direction, but should be carried on in State, county and local associations. We country bankers can do much to foster, promote and encourage research activities in these organizations.

There is not a country banker in the Nation who should not be going in for research in his own town, in his own bank, and in his own way. Nation-wide research, covering the whole of the United States and involving the cooperation of all banking groups, will also be necessary in order that the broad outline of banking reform may be determined. In order to find solutions to all the varied problems which arise from time to time it is apparent that each bank will need to study its own position individually in regard to earnings and costs of operation, as well as in regard to the service that it performs for the community in which it operates.

We are now in the midst of a period of the greatest increase in bank reserves, bank deposit expansion, and the accompanying forms of inflation that has ever been witnessed in a civilized country. All this has completely changed our banking environment. During the last quarter century there has been an almost revolutionary change in the factors influencing the profits of country banks. Banks themselves have undertaken a bewildering variety of new operations and instead of operating primarily in the field of working capital loans to business, have become the largest savings institutions in the country, an important factor in the market for investment securities and real estate mortgage loans, the leading fiduciary agent for corporations and individuals, and directly or indirectly an important source of instalment credit. During the same period many types of specialized financial institutions, both governmental and private, have developed and entered into competition with commercial banks, while significant changes have also occurred in the methods by which business enterprises finance their operations.

All these developments effect the profits of commercial banks, either by increasing costs of operation or by reducing the income derived from earning assets, and if profits are to be increased to a more satisfactory level in the future it is apparent that the commercial banking system must be modified in accordance with changes in business. This is the fundamental justification for stimulating research, since only by means of careful study is it possible to discover the precise nature of the change that will achieve the desired result.

It follows, therefore, that research directed toward an improvement in earnings will none the less have to take account of many problems. Naturally it will deal with earnings and operating expenses; with the income received from different types of loans and investments, and with the relative costs of different methods of doing business. But it will also involve careful study of the public demand for banking services, designed to find out to what extent and in what manner the needs of business and of the general public may be better served through improvements in banking structure and operations. Unless the practices of commercial banks are adapted to meet changing needs new competitive institutions will arise to serve the public as they have done in the past.

A worthwhile future for country banks, therefore, demands research.

Improve Our Banking Knowledge

Fourth, to improve and preserve the country bank we should improve our banking knowledge. This logically should be developed in three different directions:

Education of ourselves, with constant desire to raise the professional standards;
Education of employees, using every possible method to improve the efficiency and broaden the knowledge of the personnel;
Then the education of our customers and the improvement of our public relations.

If country banks are to have a worthwhile future we have the responsibility of giving the Nation a sound banking structure, which shall be at the same time adequate and modern enough to serve a progressive civilization. The degree of efficiency with which we do this will depend upon the intelligence of the 250,000 people who operate our banks and the manner in which that intelligence is applied. We are in a scientific age, and banking, or any other business, in fact, cannot be run successfully by hunches or by intuition. It requires an intimate knowledge acquired through accurate fact-finding and the proper application of those facts. There is no question but that by systematic persevering effort we can add immeasurably to our store of knowledge. As we survey our tasks we must realize it is time for deep thinking, for fresher viewpoints, for wider horizons.

As a result of wise leadership the American Bankers Association has for years shown phenomenal growth in making available to the bankers of America a program for self-education which has been in keeping with the times. We little realize that it was almost 40 years ago that the American Institute of Banking was launched, and it has continued with such success that there are today over 40,000 bankers improving their knowledge in an attempt to keep pace with its progress.

Outside of these activities the most important development in education in banking in recent years is a remarkable growth of banking conferences sponsored by bankers' associations. Further, there is the inclination to make all the national regional and State conventions avenues for dissemination of the best possible information on current banking problems. The country bankers should profit by attendance at these various meetings, where our associates give us in condensed form their studiously acquired knowledge. We must realize as we go about our daily tasks that scores of men engage in full-time research for us and make it available in the published reports of our commissions and committees.

Impetus for this increased education is probably to be found in the rapidity with which the nature of banking problems have changed in recent years. We have, for instance, the growth of investments and decline of loans; new kinds of loans, such as term, personal, and Federal Housing Administration; the whole foreign exchange picture has had its face lifted; managed currency has replaced the gold standard; the growth of Government agencies which compete with bankers for loans and investments; gold sterilization; deposit insurance. All these things and many others have kept the bankers on their toes to try to keep abreast the times. If they succeed in maintaining the pace it will be due largely to educational efforts along various lines.

If the country banks are to keep abreast of the times, in this changing world their executives, employees, directors, stockholders, and customers must be educated, must "know their stuff."

Cultivate Favorable Public Relations

Fifth, to improve and preserve the country bank we should cultivate favorable public relations. Last and by no means the least in providing for the future of the country bank is another phase of education—the cultivation of favorable public relations. We must constantly endeavor to interpret the science of banking and the necessity for our banking system to the public. We must educate the public mind to a proper understanding of the way in which banking serves business and industry and the way in which it contributes to the welfare of the community. We must arouse an unshakeable belief in the necessity for our banking system. We must educate the masses to the knowledge that business cannot survive without our banking institutions. We must create a favorable impression of the integrity of the system. We must so adapt the policies of our institutions and of our relationship to our public as to create these beliefs and impressions. In other words, we must make them real and tangible and easily understood.

We have still another and important job to do. Precisely it contemplates that our 14,000 country bankers in communities from the Lakes to the Gulf and from coast to coast assume the role of instructors who shall educate the public on economics as pertains to money and banking. Possibly they should assume the role of preachers, for it seems that we must soon return to the "old-time religion" of working and saving and living within our income. We must abandon the dream that the Government is all-wise and all-powerful enough to plan or control all agriculture, business and industry. We have learned by experience that the general standards of living cannot be raised by policies of scarcity and destruction of wealth. We must convince our people that they should get back to that American ideal of honest work and free enterprise through which this country has prospered and grown great.

We must speak in defense of the American system of private enterprise because its preservation is an issue that confronts every business man today; because it is a system that, under the Constitution, has made America, and because the chartered banking institutions of America have played an indispensable part in the functioning of that system. The bankers should be out in front in defense of a system of private industry and business which, although with faults, has, nevertheless, distributed more income to more people than any other system in the history of the world.

American enterprise, after all, is the primary source of employment, of production, and, in fact, of the revenues on which the Government itself depends. There isn't a job that wasn't born of individualism and created by enterprise. There isn't a home that isn't maintained and made possible by earnings and savings from those earnings. There isn't a church building or a hospital, a college or a school, that wasn't made possible by saved earnings. The very security of the home and Nation is reliant upon earnings. Why, then, isn't it a banker's job to lead the return to the sound policy of personal initiative and private enterprise with a minimum of government? It does not require a great program of legislation or of new governmental measures. The problem is rather to profit by the lessons which we have learned, to remove the handicaps which now prevail and release into new activity the pent-up forces of the Nation.

There is a simple formula outlined in a story concerning an old Negro. He was asked what he thought would cure this old depression. He replied that it was something they use in a golf game. It required just three putts. First, "Put your faith in God; put your Ford in the shed, and put your folks in the field."

We need not worry about the future of country banking if we can restore and preserve individual initiative and private enterprise, actuated by the ideal of a worthwhile service and the hope of a reasonable profit for meeting an unquestioned public need. These constitute the backbone of America's economic strength. Anything that weakens them weakens every institution whose financial welfare is in any way dependent upon them. Let us resolve therefore to lead in the fight to uphold and justify the American system of private enterprise—a system superior to any other yet devised, for giving the greatest number of people the most in material comforts and in liberty of action. The American way is our assurance of—Freedom, Justice, and Opportunity! Therefore,

Let us Defend it;
Let us Improve It;
Let us Preserve It.

The American Way

By Dr. Bruce R. Baxter, President Willamette University, Salem, Ore.

It would be a sad mistake for one who comes from a college campus to attempt to speak to bankers as if the speaker understood banking and were expert in it. I shall bear definitely in mind the fact that I am a layman. But every banker is a man before he is a banker, and it is of the man and to the man that I would speak.

Everyone understands that there are three forms of government now competing for ascendancy. This is probably the clearest fact that emerges from the European tangle. These three forms of government are communism, fascism and democracy. Naturally, our vote is cast for the democratic form of government. Democracy will succeed in the United States, or anywhere else, only when there is a sufficient number of good and intelligent men to participate in it and direct its activities. We in America are humiliated by the fact that even in the most stirring Presidential campaigns, thirty million qualified voters do not take enough interest in the issues at stake to cast a ballot.

I should like today to discuss certain attitudes and responsibilities which in our democratic form of government rest down in peculiar fashion upon bankers. This is because, by the very nature of their profession, they have assumed important responsibilities as community leaders. I think it is significant that in these last years one hears no more of the silly banker stories of the glass eye and ice water variety, no more of the wisecracks, or, as the Bostonians call them, sophisticated crevices, poking fun at the banking profession. This all indicates, it seems to me, a definite appreciation of the leadership that the banker gives to his community and of the burdens that he has carried for that community.

Now if the banker is to make his rightful contribution to the American Way, which is the application of the principles of democracy, he must, in the first place, be an intelligent world citizen—he must have the international, the world, point of view. One writer speaks of "the curse of the township mind," which simply means the curse of being unable to see beyond the limits of one's own community. On Sept. 27, 1938, a Paris newspaper sent a reporter out upon the street to interview 50 men chosen at random, asking them what they thought would come out of the Munich Conference. Number 17, a workman, replied, "I don't know anything about it at all. I live in the suburbs." This was wholly a foolish answer. It is a tragedy whenever, in relation to world affairs, one "lives in the suburbs."

Any man who merits characterization as a world citizen would understand something of the historical background of this present conflict, something of the racial antipathies that enter into it. His knowledge at this point would be in marked contrast to that of the school boy who wrote in his essay, "Martin Luther died a horrible death. He was excommunicated by a bull." The boy's understanding of church and secular history was very limited, but is no more limited than that of some who talk in glib fashion of the European war, with but meager understanding.

One who has the international point of view will comprehend that every normal individual passes through three distinct stages:

First, the period of dependence, which among humans in infancy means a rather long time.

Second, the period of independence, which comes with adolescent years and the desire to strike out for oneself.

Third and last, the understanding of interdependence, which realization goes far toward making a man a world citizen.

Truly, we are members one of another.

In the second place, the man who is going to do his share toward making democracy, that is, the American Way, must be an intelligent American citizen, interested far more in that which he owes the nation than in that which the nation owes him. Whenever a considerable percentage of citizens gives more attention to that which the government owes them rather than to that which they owe the government, we are headed for trouble.

There is a far greater demand for intelligent citizens today than was true in former and simpler times. In the year 1834 the City of Detroit had 24 civic functions; in 1900 it had 142, and in 1934, 306. Certainly the requirement for understanding of one's government in Detroit, or any other American city, demands far more intelligence in 1934 than it did a century ago.

This intelligent American citizen will understand that he is a citizen not only of his city and State, but of the entire nation, and he will vote and act accordingly. We recall the preamble to the will of George Washington, when he said, not "I, George Washington, a citizen of Virginia," but "I, George Washington, a citizen of the United States of America." The Father of our country had far more than a local, or even a State-wide point of view.

The intelligent American citizen will be scrupulously honest in all of his dealings with his government, for national integrity cannot rise any higher than the integrity of its individual citizens. This principle finds application not only in governmental relations but in faithfulness in all of a man's responsibilities. Bishop G. Bromley Oxanam tells of a night airplane flight when the pilot discovered that the landing gear of the plane had been so damaged as to be utterly useless. He brought the plane back to the home field and with almost unbelievable skill and daring landed it in such fashion that, although all the passengers were shaken up, none was seriously injured. The question that arises is just why, when he discovered the condition of the plane, he did not use his parachute and bail out and thus save himself. If a man were alone in a plane and such an accident occurred, he would, of course, do this, but the record of commercial aviation does not show one single instance where a pilot has ever bailed out and left his passengers in the plane. No man who takes his responsibilities seriously ever "bails out."

In the third place, this individual who makes his contribution toward the American Way will be an intelligent citizen of his community. I am impressed by the number of young men who, coming to college to prepare for a banking career, say that the choice is made because of the position of some banker whom they have known in their local community. Possibly all men in this profession do not realize how young people do look up to them. This banker who is an ideal community citizen will not be touched by any spirit of intolerance. Intolerance I take to be ignorance plus emotion, and ignorance is always a by-product of distance. I am greatly disturbed over that which I believe to be not only a wave, but a rising tide, of intolerance in the world today.

A recent writer in an American magazine points out that if a swindle is perpetrated and a Gentile is at the center of it, one does not label it a Gentile swindle, but places the blame upon the individual, where it ought to be placed. However, if a Jew is at the center of such unfair dealing, there are some narrow people who at once characterize it as a Jewish swindle, tarring an entire race with the misdoings of a certain individual. This is wholly unfair and wholly un-American

But this spirit of intolerance is not directed solely against the Jews. Louis Adamic, in his recent book, "My America," tells of a brilliant second-generation Scandinavian, now a college professor, who writes, "I think I have never quite been taken in. We second generation people can hand up the spices and the spoons but the old-stock Americans will still continue to do the cooking." I hope this is not a typical case but only an aggravated incident.

The American Way is the way of tolerance. Tolerance and indifference are not synonyms. Tolerance is the principle of active good will toward all races and all nationalities. It is a desire that all persons should share in the good things of life.

The ideal American citizen who, from a place of leadership such as is assumed by the banking profession, makes his contribution to the American Way, will be genuinely helpful in all his personal relationships. A New Zealand woman, writing of native birds which had been noted for the length and height of their flight, tells how they had been for so long so close to the feeding grounds that unknowingly they had lost the power of flight. Danger threatened and the birds were warned but they could not fly away. The poem ends, "Their wings had vanished—they had lost the sky." What of our contribution to men who in these difficult years have "lost the sky"?

Many there are who, discouraged over personal losses and unsettled world affairs, have felt that there was considerable point to the story of the country physician who sent a bill to a newly-made widow, reading, "Due, $50 for curing your husband up to the time of his death." Some feel that this foolish story represents the present state of world affairs.

Ian McLaren makes a character in one of his novels say, "Be kind—every person that you meet is fighting a hard battle." Well, if Ian McLaren could have that said a generation ago, how much more true it is today. I was called upon in the midst of the depression to speak at the memorial service for a young banker who had taken his life. Investigation showed that not one dollar had been misappropriated—his financial record was clear. I shall never forget the agony in the statement of the stricken wife, who said that she was not trying to excuse him for the enormity of his act. However, if only people could know that for weeks he had been scarcely able to sleep at all because of his worry over clients in that bank who needed money and who could not secure loans under the then stringent regulations—that perhaps if they understood the burden he was carrying they would not be too harsh in their judgment. "Be kind—every person that you meet is fighting a hard battle."

I take great comfort in the quotation by Robert Louis Stevenson just before his own untimely passing, in a remote South Sea Island, a victim of a dread disease which had made him an invalid for years, when he said, "I am bigger than anything that can happen to me."

I do not see how a community leader today can be of very much help to people who have lost their sky until he has an adequate philosophy of life and a standard of values for himself. He will then understand that the making of a fortune does not necessarily in itself bring contentment and recognize that other acquisitions must go with it. You older men will remember the school reader's story of the Oriental king who, in the midst of great depsondency, called in his philosopher to ask how happiness might be restored to him. The philosopher told him he might get it back again if he would wear the shirt of the most contented man in his kingdom. The problem then was to find that most contented man and when they found him, behold he had no shirt. Then the other day you went to see the play "You Can't Take It With You," and discovered that the wealthy man in the play learned from the old man in the tenement that the achieving of a fortune in itself does not necessarily bring happiness. This is nothing at all save the repetition of the old story of the unhappy king.

History has a word at this point. How many of you can give the name of the richest man in Greece when Socrates was writing and teaching, or the richest man in Rome when Justinian was preparing his legal code, or the richest man in France when Louis Pasteur was in his laboratory, or the richest man in the United States when Abraham Lincoln delivered his second inaugural address? History's judgment is sound, for unless there is something significant that goes along with the making of a fortune, genuine success is not attained.

That leader who has the proper relation to his fellow men is one who maintains his faith in others. As one writer says, faith is not a synonym for credulity. Faith is not believing something which you know is not true. Faith is reason grown courageous. A man does the best of which he is capable and then faith enters in. That one has lost faith in men does not mean that it is necessary for him to lose faith in man. And so, to those o represent a profession that is so largely based upon faith, remembering the foundations of a credit system—faith in the integrity of men and in their desire to meet their obligations—we make a plea for the maintenance of faith in one's fellows.

I would now offer two suggestions as to methods whereby one may be helped to attain that point of view and standard of values out of which can come the desire worthily to meet his responsibilities. The first lies in the development of one's cultural appreciation. The happiest person is the person who thinks the most interesting thoughts; therefore the necessity in active, busy days of building up reserves within oneself upon which he can draw in times of unusual stress or in days of retirement. Then only will the most interesting thoughts make for the happiest individual. In this same connection, it is significant that former Premier of France Leon Blum defines the truly free man as the man who dares to go to the end of his thoughts. This means that all of his thoughts are such that they could end in acts which would have only good results.

Is it not significant that the word amusement originally meant "away from the muses"—away from music, art and poetry? How many successful business men there are who have found in music an avocation, a release, that nothing else could give. Oliver Wendell Holmes speaks of those who "died with all their music in them." These are men who never gave any thought to the cultural side of life. Does any one suppose that Charles G. Dawes was a poorer Vice-President, or Albert Einstein a less able physicist, or Hendrik Van Loon a less capable author, or John D. Rockefeller Jr. a less able financier, because each played the violin rather well? Does anyone believe that Walter Hampden was less able to portray Shakespeare's characters because he played the cello, or that Dean Cornwall was a poorer painter because he played the cornet, or Charles Schwab less a financial leader because he had a pipe organ in his own home and played it rather well, or William Woodin a less efficient Secretary of the Treasury because he composed some good music? These are men who gain a measure of happiness because they think interesting thoughts based upon cultural appreciations.

My final suggestion is that every normal man must have a fixed point outside of himself and that fixed point I take to be his religion, his relation to his God, expressed through all his other relationships. A few months ago three British scientists, members of the Royal Academy of Science, went up from London to Oxford University and joined in saying to this present Oxford student body, "The youth of this present generation who are non-religious are non-scientific." These scientists spoke truly, for back of every fact is a cause and back of every cause is purpose and back of all purpose is God.

Some time ago I saw a letter that a small child had written to a friend of her father. It was the first letter that she had ever written to anyone outside of the immediate family. She was careful of its composition. The last sentence read, "And now I hope that you will live all of your life." The little girl spoke far better than she knew, for no philosopher could ever have written a more profound wish—to live all of one's life, to fulfill all of one's responsibilities worthily. It is entirely possible for a man to die never having lived. You and I have known men who have died never having lived. Merely to have lived a long life is not good enough, but to have lived a good life is long enough. May it be that each one of us shall live all of our life, being faithful to all of its responsibilities and obligations—that men upon whose shoulders are laid the responsibilities for the financial welfare of our nation, which involves the happiness or misery of so many of its citizens, may worthily make their contribution to the American Way, the way of democracy.

Immediate Task Constant Strengthening of Banks for Greater Service to Nation's Needs

By the President of the A. B. A., PHILIP A. BENSON, President of The Dime Savings Bank of Brooklyn, N. Y.

It is my great privilege this morning to formally open this 65th annual convention of the American Bankers Association and to bid you welcome to it. While I am grateful to each one of you for coming, the meetings are yours and it is your Association. We who serve you for a short time as your elected officers can only serve you effectively if we have your counsel and guidance. We have these to the extent that you actively participate in Association affairs. Your presence here indicates your real personal interest in our work, and this is indeed heartening.

Ten months ago you conferred upon me the highest honor within your power to give. In return I can say to you straight from my heart that it was the highest honor that has ever come to me. My year as your President has been an exceedingly interesting and gratifying year. It has offered opportunity for useful service, for as fine fellowship as ever a man can hope to experience, and for the making of freindships that will be forever treasured

Intimate contact with the affairs of the Association during the year have brought to me a greater realization of its usefulness and appreciation of the unique service it renders, not only to the business of banking but to the country as a whole. Finance touches the lives of nearly all citizens, and it is in their interest as well as our own that we unitedly strive for sound banks, improved banking methods, and intelligent public relations. It would be impossible for me to refer to the year's work without paying tribute to the headquarters staff. They are individually and collectively an able group of men and women. One and all they have my gratitude and my admiration. I cannot take time to name them, but I will always remember and value each one as a personal friend. Of course they have been under the influence of an inspiring leader. Indeed who among all of us has not felt the inspiration of Hal Stonier's personality and ability? To Hal, and all he has done as an educator and as an executive go our sincere thanks.

No name can do more than hope that at the end of his term of office the members find their organization as strong and effective as when that term began—and possibly a little better for his having served. You are, of course, the judges of that. I hope you will find some small contribution has been made.

In any case, I believe we have made progress this year. We have done so in one particular at least. That is in membership At the end of our previous fiscal year 76.62% of the country's banks supported our activities through membership in the A. B. A. On Aug. 31, the end of the immediate past fiscal year, that percentage had risen slightly to 79.76%. Since the latter date, we have welcomed five more new members. I can think of nothing more significant in our progress, for this indicates not only increasing recognition of the Association's services but recognition of united interest and a disposition toward common action with respect to common banking problems.

Our Association is a proof that banks of all types, State and National, can and do work together. There should be no issues that divide us, and we hope there never will be. The Association exists to serve the smallest bank as well as the largest. The banking needs of the country are being fully met by its 17,235 banks. There seems to be no present need for any substantial increase in the number of banks, nor is there any reason whatever to believe that there should be any change in our American banking system. I reiterate my faith in that system.

We can no longer go our individual ways. The problems that face our banks and the public they serve are no longer local problems. Whether for better or for worse, the issues introduced today are of a national character and they can be dealt with only through common action on a national scale. More than ever we need our national organization for crystallization of opinion and unity of program, and it is gratifying to witness recognition of this as evidenced by our figures.

If I were to express any regret over my year of official service it would be regret over my inability to meet all the members in person. But I shall have to remain dissatisfied on that score.

It would be ideal if all our members could come together for counsel and fraternity at a time like this. But we cannot really expect 100% representation at any one time. So we have tried various ways to take the Association to you, the members, in your own section of the country. Some of our officers have made appearances at your State Conventions and other meetings. A number of members of the headquarters staff have accepted invitations to speak at banker's gatherings. I myself have attended meetings in 13 States. I was greatly inspired by my experiences and felt an ever increasing regret over the fact that in what has been less than one year it was physically impossible to do more.

Twice during the winter we transferred the headquarters staff from New York to other centers. Early in February we conducted a successful regional conference at Columbus, Ohio, in cooperation with the Ohio Bankers Association. Later in the same month we conducted a similarly successful conference at Minneapolis in cooperation with the Minnesota Bankers Association. A third regional conference, held in New York City in March, enabled us to meet with 1,500 bankers from the North Atlantic States. Through these useful conferences we were able to meet with 3,500 representatives of our banks in three sections of the country, and we gathered strength and inspiration from them. I cannot tell you how greatly we appreciate the cooperation and support of the State associations in making these meetings successful. State Secretaries have been unfailingly helpful, not only in connection with these special meetings, but always. We acknowledge, too, the generous help of the associations of mutual savings banks, both National and State.

The activities of the Association have been intensified all along the line.

The several divisions, commissions, and councils have continued their researches and have produced a number of practical reports and studies of value to the intelligent management of banks, and have made definite contributions to intelligent thinking about banking. Let me compliment the officers of each division for their splendid work and cooperation during the year, and to express my thanks to them and to the members of all committees, commissions, and councils for their loyal service during my administration.

One of the first major activities of this administration was the consummation of the second step in our bank employee training program, the completion of the series on "Talk," designed to equip bank people to deal effectively with current questions about and criticisms of banking and related financial matters. Seven thousand sets of these booklets have been purchased by 3,000 banks and their use has made a real contribution to the understanding on the part of bank people of current popular opinions on economic and financial matters. It is hoped that many more banks will make intensive use of these booklets.

Time does not permit of a detailed exposition of Association activities. I shall mention but one or two of outstanding interest.

Through its Insurance Committee, the Association has effected another saving for banks throughout the country. During 1937 and 1938 premium reductions were secured on blanket and fidelity bonds which reduced the annual insurance costs of banks $2,735,000. Recently the Insurance Committee secured a reduction in the rates for forgery insurance which will save the banks an additional $300,000 annually.

May I call your particular attention to the work done through our Washington office? In mentioning this I wish to pay a tribute to the outstanding work of the Chairman of our Federal Legislative Committee, Lee Wiggins, President of the Bank of Hatsville, S. C. Mr. Wiggins has brought to this office an exceptionally intelligent, practical, and effective ability. He is a busy banker and merchant. Yet he has spent an extraordinary amount of time in Washington in behalf of all banks. His work and that of his Committee has been most effective. The Committee has been ably assisted in its work by our Washington office.

We were faced at Washington this year with two major items of legislation with far-reaching implications. One was legislation to broaden the powers of savings and loan associations to the point where they would virtually establish a third banking system outside the existing supervisory control now exercised through the Federal and State bank supervisory agencies.

Another dealt with the general idea of credit aid for small business. It was proposed in several measures, but the effort in that direction was concentrated on the Mead bill for insured loans.

In addition, there was a great deal of other legislation which occupied our attention.

Under the leadership of your Committee on Federal Legislation extended presentation of pertinent information was made to the appropriate committees of Congress, which we believe was helpful to the members of the committees and had a definite bearing on the disposition of the proposals in question.

In all that we have done the public interest was paramount. Our first job as bankers is to operate sound banks and to do all we can to see that they function in an atmosphere conducive to sound operation. To do less would be contrary to the public interest. It is in that spirit that the Association has expressed its views and presented data in regard to legislation.

Recently the A. B. A. has undertaken a new and effective step in its public relations program to deal with the misconception of the public regarding lending by banks. Up to now the only figures published on bank loans have been figures by governmental agencies on loans outstanding on a single date. These are static figures. They do not take into consideration seasonal trends or the fact that the same number of borrowers do not borrow the same amount of money one year as another. They do not give a true picture of bank lending activity, and they have been largely responsible for giving the public the impression that banks do not lend.

It is our job to correct this misconception. And we have undertaken to do it. Since the middle of July we have been assembling figures on the number and dollar volume of new loans and renewals made by banks, the amount of open lines of credit on their books, and the extent to which such credit is being used. We began with two States, Ohio and Pennsylvania. The significance of these new figures is indicated by the reception they have had in the press and especially by the editorial comment they have provoked. Our News Bureau has mounted some of its newspaper clippings on this subject on two display boards which are here. I suggest that you study them. And I urge that you give this most important program your full support. If you have not replied to our questionnaire, please do so as soon as you return home.

Our public relations work is our most important job, for public understanding of how we serve and how much we serve will determine our future, legislatively and every other way.

A sound public relations program involves sound banking, a sound attitude, and a readiness to inform the public concerning our services and our operations. We must develop an even greater sense of our responsibility. We must strive constantly for better management. We must endeavor to extend the usefulness of our institutions to their communities. And above all, we must run good banks.

A friend of mine who witnessed the launching of the new trans-atlantic liner America a few weeks ago told me he saw a bronze plaque mounted on granite in the yard of the Newport News Shipbuilding Corp. at Newport News, Va., bearing the following motto:

"We shall build good ships—at a profit if we can, at a loss, if we must, But always good ships."

We might adapt these words to our kind of service institutions.

We are meeting in the shadow of another great war. The lives of thousands, perhaps millions, of people are at stake. The economic structure of the world may be threatened. No people can completely escape its effects, not even we, 3,000 miles away from the scene of conflict. We must be prepared for whatever shocks may come.

Our immediate job in such a situation is the constant strengthening of the condition and the management of our banks for greater service to the nation's needs. In addition, we ought at all times contribute our share of intelligent opinion to the solution of such problems as arise.

It is to be hoped that in a time of developing crisis there may be an abatement of the conflict between the philosophies of business and government. The least that we should accomplish is the end of disunion within our own borders. We have had our full measure of drastic changes imposed by legislation. It is necessary to have an opportunity to digest them. What we need now more than anything else is stability. Labor, management, and government should act as a unit to rebuild our economy to meet the strains and stresses that the war will inflict on us

The struggle overseas may possibly drag down democracy in Europe. Perhaps it will be our mission to keep it alive in the world. In any case, we have it in our power to make this country the citadel of freedom, and we certainly ought to be about doing so

Again I want to reiterate my faith in true representative democracy and free private enterprise, the American political and economic system, and to express my abhorrence of Socialism, Communism, collectivism, and dictatorship in every shape and form. Let us have none of them here, nor even a mild approach to them. We have not been free from some of their baneful influences. What they are at heart, what they lead to has been made clear. Our strength and our hope lie in renewed faith in the God of our fathers and in a patriotic devotion to our favored land with its liberties, responsibilities, and opportunities.

Inability of Senator Harrison to Accept Invitation to Address Convention

President Benson announced the following communication from the Senior Senator from Mississippi who had been scheduled to address the Convention:

Again I want to express my disappointment and regrets over my inability to attend A. B. A. Convention. Appreciated deeply invitation to address meeting and only illness would have prevented my filling engagement. Be assured my every good wish for most enjoyable and successful meeting.
PAT HARRISON.

COMMITTEE AND OFFICERS' REPORTS—GENERAL SESSION

Report of Economic Policy Commission by the Chairman, Leonard P. Ayres, Vice-President of Cleveland Trust Co., Cleveland, Ohio

Two conclusions about the probable effects of the European war on our economy appear to be so clearly indicated that we may well regard them as being virtual certainties. The first is that the effects will be of major importance, although they will probably develop more slowly than we now assume, and some of them will prove to be unexpected. The second conclusion is that in the long run the results will be adverse to us, for great wars are immense calamities which impoverish not only the participants, but all the nations of the world.

During the early stages of the conflict American industries which produce goods or commodities needed by the belligerents will undoubtedly experience increased business and firming prices. It is not as yet possible to know which lines will be so affected. During the first year of the World War the groups of commodities which showed the most important price advances were grains, hides, nonferrous metals, and chemicals.

Our export and import businesses are already feeling the effects of conflicting influences of stimulation and restraint resulting from the advent of war. Probably the volumes of our exports will be increased, and our foreign trade with neutral nations will be expanded. These effects will be partly offset by the fact that large areas of our foreign trade have already been eliminated by the war, and that even those combatants which continue to purchase goods from us will limit their takings to war-time necessities.

The volume of commercial bank loans has been slowly expanding in this country since last February, and with the development of the war crisis there has come a much more rapid increase. This expansion of commercial loans may be expected to continue for some time to come. The banks have over five billions of excess reserves and they are amply able to take care of any demands for increased credit which may develop.

It may well prove to be the case that one of the important economic results of the outbreak of war will prove to be a definite downturn in the long-term trend of high-grade bond prices. This appears to have already happened and if that proves to be true, the development will be a highly important one for American banking, for business men, for investors, and for the National Government.

During our national history the prices of high-grade bonds have characteristically followed two sorts of movements. One of them has been made up of the relatively short wave-like fluctuations of expansion and contraction that have accompanied the business cycles. The other movements have been of much longer duration, and typically have continued through several business cycles.

Long-Term Trends

Bond prices reached their all-time low levels in this country in 1842, in the period of hard times which is often referred to as the Debt Repudiation Depression. Our only index of the prices of high-grade bonds which covers that period shows that in December of that year the best State bonds were selling at about 52. From that level bond prices advanced for nearly 22 years until in 1864, during the Civil War, they reached nearly 115. The long advance averaged about $2.90 per year on each 100 dollars of principal amount.

The next move was an abrupt decline lasting five and one-half years during which bond prices fell at an average rate of more than $7 per year. The bond price index stood at 75 at the beginning of 1870, and then its advances exceeded its declines from business cycle to business cycle during more than 28 years until the price was just under 163 by the middle of 1899. That was an average annual increase of almost $3.10 in each 100 dollars of principal during that long period. The index during this period is made from the very carefully compiled data of the National Bureau of Economic Research covering the yields of the highest grades of rail bonds capitalized at 5%.

During the next 21 years the general trend of bond prices was a declining one, and they fell from 163 in 1899 to only 91 in 1920. That was an average annual decrease of about $3.43 per 100 dollars of principal. The following advance has lasted for 19 years up to this past summer, and the index has risen at an average annual rate of about $4.24 on each 100 dollars of principal amount. That brings the record up to July of this year when the index stood at 172.

There are two features of these swings of bond prices which are of special significance. One of them is that they have charaeteristically been of such long duration that whole generations of bankers and investors have unconsciously come to accept them as representing permanent conditions in the conduct of their affairs. An upturn or a downturn in such long-lasting trends constitutes a most important change in one of the fundamental factors of business, and it is a change to a new set of conditions which is quite outside the experience of most of the policy forming executives.

The other important characteristic of these long trends is the wide amplitude of their swings. The average yearly change has been more than $3 per 100, which constitutes a most important leverage on the profit side during the long advances, and an even more seriously important one on the losing side during the declines. The operation of the leverage tends to increase both profits and recoveries from investment portfolios during the advances, and to increase losses and diminish recoveries during the long declines.

Federal Bonds

It is somewhat astonishing to find that the record of the Federal bonds during this latest long upswing of prices furnishes results that are even more extreme than those of the highest grade corporate bonds. The Treasury Department has recently compiled an index of the yields of all Treasury bonds having maturities in excess of 12 years. The index begins in 1919 and the highest yield is 5.67% in August of 1920. The lowest yield is 2.13% in June of this year.

If we capitalize these yields at 3%, the low price works out at just under 53 in 1920, and the high price in 1939 becomes almost 141. That is an advance of almost 88 dollars in a little less than 19 years, or nearly $4.70 per year for each 100 dollars of principal amount. In practice it has not been possible to realize on the appreciation in the values of the Federal bonds at so high a rate during the years since 1920 because the issues have been replaced by new issues at lower coupons, and because they were capitalized without assumed maturities, but even so somewhat comparable appreciations could actually have been realized.

An investor could have bought a Liberty Bond at 82 in May of 1920. The coupon was 4¼%. He could have sold his bond in March of 1923, and with the proceeds he could have purchased one of the 4¼% bonds of 1947-52, which he could have held to June of this year and sold for over 122. His initial investment would have been $820, and his selling price something more than $1,220, so he would have made a direct profit of $400.

He would have received interest amounting to $807 during the 19 years, or a total realization of $1,207 on his original investment of $820. This amounts to a return of $63.53 per year, or an income from a Federal bond amounting to 7.75% per year for 19 years. If the trends of bond prices were reversed so that the purchase was made at $1,220 and the final sale at $820, the income from the transaction would amount to about 1.75% per year. Clearly it makes a great deal of difference to bankers and investors whether they are doing business in a period of declining long-term interest rates, or in one of advancing long-term rates.

It should be noted that the precipitate decline in the prices of Federal bonds that has taken place since the outbreak of war in Europe is a most exceptional development, and one that should not be interpreted as being characteristic of the long-term trends that we have been discussing. Such long trends are normally made up of slow and persistent upward or downward drifts or tides which are made up of a succession of shorter wave-like fluctuations corresponding to the expanding and contracting phases of business cycles. We have at present such great amounts of nearly idle funds seeking investment that no long continuation of price declines at recent rates is to be expected. Our Federal bonds continue to be the soundest of all investments.

Two Reasons for Downturns

Normally there are only two fundamental reasons why the demand for high-grade bonds decreases sufficiently to bring about a downturn in the long-term price trend. One of them is the development of greater attractiveness on the part of competing investments. These might be stocks where the ordinary investor is concerned, or they might be commercial loans in the case of the banker.

The other factor which might cause a downturn in the long-term trend of the prices of high-grade bonds is a general realization on the part of investors that prices have mounted so high, and the returns from them have fallen so low, that the risks of making new investments have become great enough to outweigh the meager attractiveness of the income that can be realized from the coupon payments.

At the present time bond prices have turned downward because of a combination of both of these types of causes. Bankers have developed a preference for liquidity both because bond prices had mounted too high and returns from them had fallen too low, and because there has developed a recent sharp increase in the volume of commercial loans which may continue and furnish a more helpful and appropriate employment for bank funds. Individual investors have a diminished interest in bonds because they are hopeful for better returns from stocks.

These developments are not likely to be merely transitory for they are reinforced by conditions that were coming into being abroad even before the advent of war. Symptoms of monetary inflation have been coming into evidence in the economies of Germany, France, Italy, and Japan, and they may now be developing in England. If they make much progress they will result in advances in the prices of commodities and in higher interest rates abroad.

Clearly the nature and importance of the effects which the European war may have on our economy will depend on such unforeseeable factors as the duration of the conflict, and on the nature of its consequences to the participants. We have in this country huge volumes of nearly idle bank deposits and vast excess reserves. These monetary resources might easily be used in ways that would produce unduly rapid price advances, and foster undesirable forms of speculative activity.

Your Economic Policy Commission not only calls attention to the probability that we have just passed a new downward turning point in the long-term trends of bond prices, but it takes this opportunity to remind all bankers that the tragic outbreak of another great war marks the beginning of a period in which the granting of new credits and the expansion of existing ones should be conducted with special prudence and thoughful care.

Report of Official Acts and Proceedings of Executive Council, Presented by Richard W. Hill, Secretary of A. B. A.

President Benson: The Secretary of the Association, Mr. Hill, will report the Official Acts and Proceedings of the Executive Council since we last met. These are read to you for the purpose of information, and no action is needed on them. We will now hear from Mr. Hill.

Secretary Hill: Since the adjournment of the convention at Houston, Texas, the Executive Council has held meetings at Houston on Nov. 17, 1938, at Hot Springs, Virginia, on April 25 and 26, 1939, and at Seattle, Washington, on Sept. 25, 1939. At the Houston meeting on Nov. 17, the Committee, Commission, and other appointments presented by President Benson were approved.

At the same meeting favorable action was taken on the following items:

1 Budget report for 1938-1939 by the Chairman of the Finance Committee
2 Publication of a new edition of Paton's Digest with regular annul supplements
3 Revewal of lease for one year of premises occupied by the Association's branch office at Washington
4 Amendment to Association's By-laws bringing appointment of personnel of the Bank Management Commission in line with the appointment of other commissions
5 Employment of Harold Stonier as Executive Manager of the Association for a term of five years beginning Sept 1, 1938
6 Report of the Committee on State Legislation recommending a uniform statute covering bonding of bank officers and employees.

At the meetings at Hot Springs, Virginia, on April 25 and 26, favorable action was taken on the following matters:

1. Amendments to Association's By-laws establishing the Public Relations Council and the Graduate School of Banking as activities of the Association.

2. Recommendation of the Committee on State Legislation proposing a statement of principles governing the appointment of supervisory authorities.

3. Recommendation of the Committee on State Legislation proposing an escheat statute.

4. Authorization to the President of the Association to inform the Secretary of the Treasury that it is the sense of the Executive Council that Congress be urged to adopt such modifications of the revenue laws as will give relief to business and industry, thereby aiding the economic recovery of the Nation.

At the meeting in Seattle, Washington, on Sept. 25, favorable action was taken on the following matters:

1. Amendment to Association's By-laws consolidating the Insurance Committee and the Protective Committee, the new committee to be known as the Insurance and Protective Committee.

2. Recommendation of the Bank Management Commission raising the amount of no protest items from $10 to $50.

3. Establishment of the office of Director of the Public Relations Council, and the appointment of William T. Wilson thereto.

4. Authority to the Executive Manager to invest in, sell, exchange, or substitute obligations guaranteed by the United States for direct obligations of the United States, or to exchange securities of one type for securities of the other.

Report of Committee on Resolutions, by Chairman Robert V. Fleming—Banking and Credit Facilities, Taxation, &c.

Once more American business and American banking must revise their policies and readjust their plans because a great war has broken out in Europe. No one is wise enough to know as yet what the nature of the conflict will be, or how long it may last, and no one can forsee its outcome. There is only one certainty about its results for us, and that is that they will be detrimental, for wars are vast tragic calamities which impoverish not merely the participants, but all other nations as well.

Business activity has been increasing in this country since last spring, and it seems probable that the advances will continue through the remaining months of the year. Most harvests have been good in volume, but carry-overs are large and prevailing agricultural prices are still relatively low. Bank deposits have reached new high levels, and excess reserves are greater than ever before. Our banking institutions are prepared to meet adequately and promptly such demands for needed credit accommodations as may develop.

Most of the sudden expansion of business activity that has taken place during the present month has come because of the anticipation of war orders rather than as a result of orders that have actually materialized. There is as yet little evidence that a war boom is in the making, but if symptoms should indicate that one threatens to develop it will be prudent for us to remember that such periods always leave heritages of remorse and regret. The policies of American banking should be resolutely directed toward restraining and restricting any excessive war boom in trade, industry, agriculture, or the security markets.

The American Bankers Association and its members are fully cognizant of the dislocations which can occur in our national economy due to war conditions abroad, and the responsibilities which increasingly rest upon the shoulders of every banker as the custodian of the funds of the people of our country.

We pledge ourselves to spare no effort or means in our power in meeting conditions as they may change from time to time, to the end that our Nation may be able to maintain a sound and stable economy.

The American System

We reaffirm the action of previous conventions wherein the position of the Association was stated with regard to the dual system of banking, branch banking and the autonomy of the laws of the separate States with respect to banking, and opposing any proposal or device looking to the establishment of branch banking privileges across State lines, directly or indirectly.

Banking Supervision

With respect to governmental supervision of banking in the public interest, we believe this is wholly in keeping with the broad principle that the success and strength of democracy in America is largely due to the sound safeguards afforded by the wisely conceived checks and balances which pervade our composite governmental system.

We believe, furthermore, that as regards banking supervision this same principle of checks and balances, which now exists, should be maintained.

Bank Examinations

Various proposals are under consideration at Washington looking toward modifications of our present systems of bank examinations. The factors involved are too numerous and too complicated for discussion in these resolutions. There is, however, one principle concerning which the membership of this Association does desire to make record of its convictions, and that is that no attempt should ever be made to use bank examinations as instrumentalities of credit control. Bank examinations should be just what their designation implies, and no attempt should be made to use them for other purposes.

Banking and Credit Facilities

American banking is now meeting adequately the present needs of business and of individuals for credit accommodations, for facilities which encourage thrift, and for the financial mechanics which are essential to our national activities of production, exchange and service. The recent hearings before the Senate Committee on Banking and Currency produced abundant evidence that our banking system is now providing these facilities more fully, more flexibly, and at less cost to the customer than ever before.

Recent proposals for legislation by which bank loans to small businesses would be insured or guaranteed by Federal funds are fundamentally unsound and appear to be without merit. They involve the unsound principle of creating new forms of easy credit with resulting high percentages of losses which would be shared first by the banks and then by the Government. Under such programs the making of loans to marginal business men already close to insolvency should tend to maintain temporaily large numbers of inefficient businesses in destructive competition with the solvent and well managed ones.

Plans have also been under discussion of late for the creation of a system of capital credit banks. Most of these plans provide for the capital of the institutions being supplied by the Government. At present our most pressing credit needs, other than the ones relating to our governmental finances, are not those calling for additional institutions to make loans. Powers already granted existing governmental agencies to participate with banks in the extension of certain types of loans seem, in our judgment, to be wholly adequate. Our most pressing credit need rather is for better prospects for business returns so that investors may be encouraged to venture in productive enterprises the redundant amounts of credit already available and now being inadequately employed.

We urge again upon our members that they continue to explore fully every possibility of making their credit facilities available to all worthy borrowers. We also urge again that they continue to cooperate with applicants, where necessary, to put proposals, as presented, in bankable form, and to see that no sound and reasonable credit need is denied.

We reiterate our belief that an approach to a balanced budget should be the primary objective of our public fiscal policy to the end that sound national credit may be maintained. We take advantage of this opportunity to express to our fellow bankers, and to institutional and private investors, our continuing conviction that the bonds of our Federal Government are the safest of all investments. We are not disquieted by temporary fluctuations in their market prices, for these securities embody more fully than do any others the qualities of marketability and safety.

The Burdens of Taxation

The Congress and the Treasury now are studying our Federal tax laws with the announced intent of making them more equitable and their administration more efficient and certain. We commend this study and its objectives.

Federal tax laws should not be passed hurriedly, without thorough study of their economic effect upon all classes of taxpayers and upon the Government itself. They should be written with the aim of providing the necessary revenue and should avoid imposing controls or restrictions on business, or uncertainties in their assessment.

Preferably, the basic structure of Federal tax laws should be fixed and should remain unchanged for lengthy periods of time, with revenue requirements being met by changes of rate within this structure. Then taxpayers would be enabled to make future commitments with reasonable certainty.

Once the Federal tax structure is fixed, States and their subdivisions can adjust their laws so as to avoid the present maze of duplicate and overlapping taxes to which both the Federal and State governments have contributed. It should be possible, also, to clarify the laws so as to avoid expensive controversies resulting from uncertainties as to interpretation or conflicts between taxing jurisdictions. We are fully in accord with proposals for the creation of a commission to make a broad study of the problems here referred to.

We should particularly point out that not only are strict economies in Government operations essential to lessening the burdens of taxation, both State and Federal, but also the withdrawal of pressure on governments by special groups among our citizens urging the expenditure of huge sums for non-essential projects. A large volume of these demands for expenditures are made upon the Federal Government for local purposes which should be borne, if warranted at all, buy the State and political subdivisions to which they pertain. We recommend, however, a larger degree of restraint in respect to all such demands.

We again call the attention of the American people to the seriousness of mounting public expenditures, both local and Federal, and again remind them of the fact that the resulting indebtedness eventually must be repaid by all of the people.

Taxes should be paid by all who are able to pay them, but rates should not be so high as to stifle initiative or to hinder business activity and contribute to unemployment. The law of diminishing returns still stands. Also, full consideration should be given to equitable measures for progressively narrowing and finally closing avenues of escape from sharing the tax burden which still remain open in certain directions. Continuance of individual freedom in this Nation brings to every resident of the United States an obligation willingly to contribute through taxes to the financial support of our Government.

Resolutions of Appreciation

The American Bankers Association takes this opportunity of expressing appreciation to our retiring President, Philip A. Benson, for the splendid service he has rendered to our Association. By his character, integrity and personal conduct he has set a high standard of professional ethics which has enhanced the presitige of our Association and its members.

To Robert M. Hanes, our First Vice-President, and P. D. Houston, our Second Vice-President, go our appreciation and admiration for their fine teamwork, support and loyalty, and for their earnest endeavors on behalf of our membership.

To Harold Stonier, our Executive Manager, we desire to express our sincere appreciation for the able manner in which he is conducting the affairs of our Association. His unusual qualities of mind and character, his painstaking and thorough attention to all Association matters, which are handled with such broad vision, add to the strength of our Association and assure its functioning with the greatest efficiency and effectiveness at all times.

Our thanks are due also to the members of the staff of the Association for their loyalty and effective discharge of their duties.

To Mike H. Malott, our retiring Treasurer, who for so many years has generously given of his time, thought, and energies to the interests of our membership, we extend our heartfelt good wishes.

To the leaders in public life and the other speakers who have appeared before the various meetings of our convention, and given us the benefit of their time and counsel, we desire to express our sincere appreciation for their valuable contributions to the success of our meetings.

We also desire to thank most sincerely the bankers of Seattle, the local committees, the hotels, the press and the citizens of this beautiful city for their exceedingly hospital treatment throughout our convention. Pleasant recollections of our visit here will long remain in our memories.

Resolutions Committee

Robert V. Fleming, President The Riggs National Bank, Washington, D.C., Chairman.

M. A. Arnold, Chairman of Board Seattle-First National Bank, Seattle, Wash.

Leonard P. Ayres, Vice-President The Cleveland Trust Co., Cleveland, Ohio (Chairman Economic Policy Commission).

Roland E. Clark, Vice-President National Bank of Commerce, Portland, Maine (Vice-President Trust Division).

J. L. Dart, Vice-President Florida National Bank, Jacksonville, Fla. (Vice-President American Institute of Banking Section).

Paul S. Dick, President The United States National Bank, Portland, Ore.

William S. Elliott, President Bank of Canton, Canton, Ga. (Vice-President State Bank Division).

A. George Gilman, President Malden Savings Bank, Malden, Mass. (Vice-President Savings Division).

H. H. Griswold, President The Elmira Bank & Trust Co., Elmira, N. Y. (Chairman Bank Management Commission).

Rudolf S. Hecht, Chairman of Board The Hibernia National Bank, New Orleans, La. (Representative of Public Relations Council).

A. T. Hibbard, Chairman of Board and President Union Bank & Trust Co., Helena, Mont.

Fred I. Kent, Director Bankers Trust Co., New York, N. Y. (Chairman, Commerce and Marine Commission).

J. C. Klinck, President Kings County Savings Bank, Brooklyn, N. Y.

Francis Marion Law, President First National Bank, Houston, Texas.

F. Lee Major, Vice-President The Boatmen's National Bank, St. Louis, Mo. (Chairman Agricultural Commission).
V. H. Rosetti, President The Farmers & Merchants National Bank, Los Angeles, Calif.
Melvin Rouff, Vice-President Houston National Bank, Houston, Texas (Vice-President National Bank Division).
Charles E. Spencer Jr., President First National Bank, Boston, Mass.
C. C. Wattam, Secretary, North Dakota Bankers Association, Fargo, N. Dak. (Vice-President State Secretaries Section).
A. L. M. Wiggins, President Bank of Hartsville, Hartsville, S. C. (Chairman Committee on Federal Legislation).
O. Howard Wolfe, Cashier The Philadelphia National Bank, Philadelphia, Pa.

Remarks by Chairman of Agricultural Commission, F. Lee Major, Incident to Presentation of Placque to Oregon Bankers for Outstanding Banker-Farmer Projects

President Benson: I should like at this time to present to you the Chairman of the Agricultural Commission of the American Bankers Association, F. Lee Major, Vice-President of the Boatman's National Bank of St. Louis.

Mr. Major: *President Benson, Ladies and Gentlemen*: During the past year, 18 States have attained the 1,000 point goal of the Agricultural Commission.

The bankers of Oregon have made a remarkable record in agricultural achievement. For 10 consecutive years they have reached the goal of 1,000 points set by the Agricultural Commission of the American Bankers Association. Oregon is the first State to attain this record.

During each of these years Oregon bankers have peformed an outstanding job in banker-farmer projects. Because of this 10-year achievement, and for special recognition by the American Bankers Association, I have the pleasure, President Benson, of presenting to you, A. K. Parker, of LaGrande, President Oregon Bankers Association; George J. Greenwood Jr., Acting Secretary of the Oregon Bankers Association; T. P. Cramer Jr., Former Secretary Oregon Bankers Association; and Clyde E. Williamson, former Chairman of the Agricultural Committee and former President of the Association.

President Benson: This is indeed a notable occasion. I want to say that it was my happy privilege last year to have personally seen some of the work being done in the State of Oregon in banker-farmer cooperation. I had one of the most inspiring times in connection with my association with the American Bankers Association in attending one of their meetings at Corvalis, Oregon. Mr. Major and Gentlemen from Oregon, we want to recognize the achievement of your State, one in which I believe more than 90% of your banks have participated, and in doing that, we of the American Bankers Association have a great deal of pride in presenting to you a token of our appreciation.

In doing this we realize that your activities have had a wholesome and stimulating effect on bankers' agricultural activities over the entire country, not only in your State, but it has been an example and an inspiration elsewhere, which is indicated by the fact that during the past year 18 other States have followed your example, not having reached, however, as yet a 10-year record and that there are 15 other States well past the halfway mark.

We realize that your activities in Oregon have developed better and closer relations with the officials of your State College of Agriculture, with both State and county representatives of the Agricultural Extension Service. What particularly pleases us is the large number of farm people who are being contacted in a constructive manner, and that means more and better customer relations, and that is a subject in which the American Bankers Association and all of its members are deeply interested. So you set a splendid example. We appreciate your record, what you have done. And now, Mr. Parker, as the President of the Oregon Bankers Association, will you accept this token of our appreciation for your splendid work?

[Presentation of Plaque.]

A. K. Parker: President Benson, the Oregon Bankers Association appreciates this trophy and the 10 years of continuous effort which brought this award. For the visiting members who might not be familiar with Oregon finances, we have 144 banks which carry in excess of $300,000,000 in deposits. We have enjoyed our work with the American Bankers Association through your efficient Director of the Agricultural Commission, Dan Otis, and at this time I wish to extend our appreciation for all of the courtesies you gentlemen have extended to us. I thank you.

Remarks of Andrew Price, Chairman of Committee of Bankers at Seattle

President Benson—The convention is indeed fortunate to be able to come to a city like Seattle, here in the Pacific Northwest, for its annual convention. I am sure that those of you who have been here for a few days have enjoyed the beauties as well as the hospitality of this great city. It is most favorably situated geographically. At the foot of snow-topped Mount Rainier, on that lovely body of water known as Puget Sound, Seattle has become the port of call of ships from all of the seven seas. It has had a remarkable growth and development, and is destined, here in this Pacific Northwest, to be one of the great, the mighty cities, of our land. In fact, it has grown from the 150th city in rank to, I believe, the 19th in a short period of 30 years. So we are very happy to have the privilege of coming here.

The committee of bankers of the city and all of the committees have done perfectly splendid work in preparing things for us. The Chairman of that committee is a member of the Executive Council of the Association. He has been active in Association affairs and in banking affairs for many years. He is President of the National Bank of Commerce in Seattle and General Chairman of the Convention Committee.

It is with a great deal of pleasure and with deep appreciation for what he has done for us that I present to you Andrew Price.

Mr. Price—It was just 82½ years ago that the first speech of welcome, I suppose you might say, was extended on this ground. It was on March 27, in 1852, when Dr. Maynard, a pioneer from Vermont and a college graduate, arrived and established a fishing camp about where the King Street Station now stands. He was urged to do this by Chief Seattle, for whom the new town was eventually named.

Dr. Maynard at first settled down on Puget Sound near Olympia, but Chief Seattle, hearing of him there, went to call upon him and urged upon him the advantages of this particular location, where he said he knew there was a good bay and which location would be particularly favorably served from the standpoint of trade, because there was a secret pass right back over there where friendly Indians from eastern Washington, too, would come to trade, and that he could assure him (Dr. Maynard) that these tribes would welcome him, that they wanted to trade and of course they wanted a medicine man in their midst.

So Chief Seattle, with these friendly Indians, in March, 1852, spoke a word of welcome to Dr. Maynard as he arrived on the waterfront. True to his word, Chief Seattle brought his friendly Indians with him and these Indians immediately set to work with Dr. Maynard and set up a fish cannery. They actually packed fish that first year. For ready money they cut piles or timbers and sent them to San Francisco, all with the aid of these friendly Indians.

Dr. Maynard was essentially a man of trade, a well-educated, progressive man. He wanted to build a city. Some of the other early settlers who followed him wanted to be farmers, but he wanted to build a city, a friendly city where friendly tribes could come and meet, and he prevailed. But he had a lot of things to do.

He was the first merchant. He naturally performed the first major operation. He ran the first store. He built the first home. He was the first Justice of the Peace. . . .

But enough of this history. I mentioned it only to show you that Seattle was conceived in a friendly spirit and has been so ever since. There have been lots of welcomes extended, but none, I can assure you, more truly from the heart than the welcome which the Seattle bankers have extended to you at this time on this occasion.

Remarks of President-Elect Robert M. Hanes—Task of Association to Be Built Around "Banking and Business Development"

My first words as President of the American Bankers Association are spoken in appreciation of the service rendered by Philip Benson as head of our organization during the past year. His intelligent, kindly and effective handling of Association affairs has been a source of inspiration to us all—officers and members alike. I am happy in the thought that he will serve us for another three-year period on the Administrative Committee of the Association.

Realizing the scope of Association work, the men who formed this organization years ago allotted certain functions to sections and divisions, each presided over by a President. I know you will have outstanding service from these men in their various fields, and I shall depend on them for help during the year. I am glad of the opportunity of presenting them to you tonight.

The incoming President of the Division having to do with the work of National banks—Melvin Rouff, Vice-President of the Houston National Bank, Houston, Texas.

The man who will preside over the destinies of the Savings Division—A. George Gilman, President of the Malden Savings Bank, Malden, Mass. The conduct of the work of the State Bank Division, with which many of our members are associated, will be entrusted to William S. Elliott, President of the Bank of Canton, Canton, Ga.

The chief officer of the Trust Division will be Roland E. Clark, Vice-President of the National Bank of Commerce, Portland, Me.

The head of our educational section, the American Institute of Banking, during the coming year will be Harry R. Smith, Assistant Vice-President of the Bank of America National Trust & Savings Association, San Francisco, Calif.

The gentleman who will represent the State Secretaries Section as its President will be C. C. Wattam, Secretary of the North Dakota Bankers Association.

In an organization such as this, spread over a vast nation, it is to be expected that we should have various interests represented in our membership. It is logical, therefore, that divergent points of view should be expressed and even fought for at times. As a result, throughout the history of the organization we have had many internal struggles regarding the structure and operation of our banking system. No doubt similar situations will prevail at times in the future, for the Association has never attempted to curtail expression of thought. The Association has been, rather, a vast forum where our many points of view have been presented.

Despite these periods of general internal controversy, however, the Association has grown in strength and prestige through the years. It is stronger today than at any time in its history. Why? Because there is an Association loyalty that transcends all else and challenges us to give the best we have to the end that American banking, with the help of the Association, may meet the responsibilities put upon it in the interest of public welfare. As your President, may I remind you that the Association will continue to need that kind of loyalty.

Our first duty as bankers is to serve the interests of our depositors, who have faith in us and in our institutions. We must be true to that faith, or chartered banking will fail and fall. During my term of office I shall mobilize every force in the Association to help our members better serve the legitimate needs for bank services on the part of the general public. More people today are interested in banks as service institutions than ever before. We must continue to meet our responsibilities in this regard.

The work of the Association this year will be built around two phases. The first is "Banking and Business Development." Through our regional conferences and other public contacts, we shall show our banking serves business and makes for employment of men and services. Banking attains its greatest usefulness in times of normal business development. Business achievement results when economic sanity prevails. During the past decade the world has been engulfed in economic and political issues and panaceas. Men have lost their heads, false gods have been worshipped, a doctrine of something for nothing has lured people to chase economic rainbows—all to no avail.

Now there seems to be a turning of the tide. To those who have courage and are awake a new day is dawning. Those who have great followings in pursuit of false illusions are losing ground. Reckless spenders and careless debt creators are on the defensive. I see evidence that economic sanity is returning, and as it comes bankers can again be useful servants of business development.

The second aspect of our work will have to do with the internal management of our institutions. "Know Your Bank" is a pharse you will hear often during the next 12 months. The work of our educational section, the activities of the Bank Management Commission and of the Research Council will be focused upon ways and means of helping to know our banks better.

Their problems, opportunities and responsibilities will be viewed from many angles. Studies will be made, conferences will be held, results of our findings will be published and studied to the end that we as bankers will better understand how our banks can meet the need of the public for banking activities that are at once sound and serviceable.

The interests of the depositors and of the borrowers are not incompatible when economic sanity prevails. But even in times of prosperity banks cannot be sound unless bankers know their banks and how to run them. American banking has had a long and honorable record. Individuals have made mistakes during the past 120 years of which we are all ashamed. Banking like Government is founded in law and served by men—neither is divine, both have erred. Government as an institution is not to be blamed if some of its servants prove weak, inefficient, or dishonest; neither is banking. Government and banking, on the other hand, are constantly trying to improve their services and raise the standards of their office-holders and personnel.

No business in America has a finer record in educational effort than has banking. But we cannot be content with our records; we must establish new ones. The phrase, "Know Your Bank," has a challenge in it for every man in the fraternity in every bank—small or large—in the lands.

This is neither the time nor the place for an extended address. So may I conclude by again expressing my gratification for your confidence in conferring on me this great honor and by reminding you that the accomplishments of the year ahead will be largely determined by our willingness to work together for the advancement of banking as it undertakes to serve the common welfare of the people of the nation.

Report of Committee on Nominations—Newly Elected Officers

President Benson: The next report is that of the Nominating Committee. Will that report please be made at this time by the Chairman, H. Lane Young, of Atlanta, Ga.

Mr. Young: Mr. Chairman, a regularly called meeting of the Nominating Committee was held at the Olympic Hotel on Wednesday, Sept. 27, 1939. The unanimous recommendations of that Committee are as follows:

For President, Robert M. Hanes.
First Vice-President, P. D. Houston.
Second Vice-President, H. W. Koeneke.

President Benson: Thank you. The report of the Nominating Committee is that Robert M. Hanes, President of the Wachovia Bank & Trust Co., Winston-Salem, N. C., has been nominated for the office of President of the American Bankers Association for the ensuing year. Are there any other nominations?

[Upon motion regularly made and seconded, it was voted that nominations be closed and that the Secretary be instructed to cast the unanimous ballot of the Convention for Mr. Hanes for President.]

President Benson: I have a ballot bearing the name of Mr. Hanes, and I do now declare him elected President of the American Bankers Association for the coming year.

The Nominating Committee's report included the name of P. D. Houston, Chairman of the Board of the American National Bank of Nashville, Tenn., for First Vice-President of the Association for the coming year. Are there any other nominations for that office?

[Upon motion regularly made and seconded, it was voted that nominations be closed and that the Secretary be instructed to cast the unanimous ballot of the Convention for Mr. Houston for First Vice-President.]

President Benson: I have before me a ballot bearing the name of Mr. Houston, and I therefore declare him elected First Vice-President of the American Bankers Association.

Henry W. Koeneke, of Ponca City, Okla., has been nominated for the office of Second Vice-President of the Association for the coming year. Are there any other nominations?

[Upon motion of M. Lathrop, of California, regularly made and seconded, it was voted that nominations be closed and that the Secretary be instructed to cast the unnanimous ballot of the Convention for Mr. Koeneke for Second Vice-President.]

President Benson: I have before me a ballot bearing the name of Mr. Koeneke, and I do declare him elected Second Vice-President of the Association for the coming year.

The newly elected officers have agreed to serve in the offices for which they have been elected for the coming year. The constitution requires that they be installed at the close of the last day's session. While this formal inauguration takes place tonight, in order to comply with the constitution, I hereby declare the newly elected officers installed in their respective offices, and as evidence of that fact I now hand the symbol of authority, the gavel, to your newly elected President, Mr. Hanes, who will adjourn this session.

President Hanes: Does anybody have any matter he wishes to bring up? If not, I declare the meeting adjourned.

[The meeting adjourned at 12 o'clock, Sept. 28, 1939.]

NATIONAL BANK DIVISION

AMERICAN BANKERS ASSOCIATION

Seventeenth Annual Meeting, Held at Seattle, Wash., Sept. 25, 1939

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Social Implications of Banking Changes

By Dr. Howard H. Preston, Dean and Professor of Money and Banking, School of Economics and Business, University of Washington, Seattle, Wash.

Some years ago a well-known American periodical published an article entitled "The Habit of Going to the Devil." The purpose that the authors hoped to achieve was to allay the public's fear of change. The method was to bring together a series of forceful quotations showing the iniquities of the rising generation and the perils of progress. The statements sounded very frightful until one read the date line. Practically all had been within a century or more earlier. In spite of the dire forebodings of the prophets of the early nineteenth century the world had not gone to the devil. Even a cursory glance at history shows us than change—political, economic and social—is normal, and that seldom have conditions remained static for many years. Bankers who today are confronted with trends or changes that are perplexing may find some comfort from the fact that American banking has survived many such periods.

Banking history has always held a great interest for me. In recent years it has been my privilege to delve into the history of banking in this Commonwealth. As you are aware, we are a young State, celebrating this year our Golden Jubilee of Statehood. Our earliest banks were founded only seven decades ago, but even in that relatively brief period banking has undergone marked changes. When we became a separate territory in 1853, incorporation of banks was barred by the Organic Act creating the territory. For more than three decades this law remained unchanged. Since territorial banks were illegal, our earliest banks were private, i.e., unincorporated institutions. Only a few of the larger towns could maintain a National bank whose capital requirements were high and scope of operations too restricted to permit them to serve the needs of pioneer communities. In 1886 we legalized territorial incorporation of banks. In 1907 we created a State Banking Department; in 1909 we prohibited branch banking, and in 1933 again authorized it. By 1915 private banking, which 40 years earlier had been the sole form of banking in Washington, was ended by legislative fiat. From 1917 to 1921 we experimented with deposit guaranty. In 1923 we granted to the supervisor for the first time discretionary power with respect to bank chartering. These are only a few of the major changes affecting the State banks of Washington.

In the national arena the changes have been no less striking. National banks were essentially institutions of discount, deposit and note issue until after the turn of the century. Savings were taken only on time certificates of deposit; bond departments were non-existent; trust business was not lawful; the only real estate mortgages had been taken to secure debts previously contracted.

In 1903 savings departments were first officially recognized by the Comptroller. The Federal Reserve Act first authorized trust departments of National banks. The same legislation permitted five-year farm mortgage loans and one-year loans upon urban real estate, with a proviso that such loans should not be made in the central reserve cities of New York, Chicago and St. Louis. It may fairly be stated that the decade which closed with the establishment 25 years ago of the Federal Reserve banks was a highly dynamic era in American banking.

The years that followed were not less so. The Federal Reserve banks had not opened for business when the World War with all of its disturbing effects upon our existing financial organization was upon us. Stock exchanges closed in a panic, the gold standard was universally abandoned, prices soared, bank assets doubled in six years. Post-war years saw the rise and fall of the investment affiliate, broadening of loaning powers, expansion of foreign banking facilities by American banks, a great merger movement, the development of group and branch banking systems, and the wave of stock speculation which culminated in 1929.

Banking has not been static and the great bankers have been those who boldly faced and overcame the problems of their day. I have recently been fascinated by reading the story of "The Growth of Chicago Banks" by my friend Cyril James. As one turns its pages, he finds portrayed the achievements of Wm. F. Coolbaugh, Lyman Gage, John J. Mitchell, George and Arthur Reynolds, James B. Forgan, Melvin Traylor, and many other giants of former days. We in the Northwest recall with pride the contribution of Wm. S. Ladd, Dr. D. S. Baker, Dexter Horton, Jacob Furth, A. L. Mills, Manson F. Backus, and other pioneers who built well the foundations of our banks. I commend to the perplexed banker of today that he seek inspiration for the solution of his tasks by reading the story of how the leaders of other days met their problems.

The title I have selected for this paper does not impose any time limitations upon the banking changes to be considered. It is my purpose, however, to center attention primarily upon those changes that have grown out of the catastrophe of 1931-33 and subsequent years. The discussion will deal principally with the public or social implications of these changes.

Of the many changes, only a limited number have been selected for analysis. The first of these have to do with the structure of our banking system. Most noteworthy structural changes are the decline in the number of banks and the spread of branch banking. We have today only half the number of banks that served the American public at the post-war peak. Mergers, failures, voluntary liquidations, and the spread of branch banking explain this 50% reduction in a little over a decade. True, the decline in the number of banking offices is not as drastic as the reduction in the number of banks. Two decades ago branch banking was in its infancy; at present (June 30, 1939) there are 3,607 branches in operation. But even with all branches added, the net reduction in the number of banking offices is more than 12,000.

Conditions in Washington may be assumed to be somewhat typical of the country as a whole. In 1933 there were 75 bankless communities in this State in which a bank or banks had been in operation subsequent to 1920. Banking service has since been reestablished in some of these towns by chartering new banks, by moving existing banks, by reopening banks under stabilization, by the establishment of branches. Intercommunity mergers and voluntary liquidations—we have had no failures for six years—have about kept pace with the creation of new banks. As a result we still have approximately three score and ten towns without banks which once boasted a local bank. It might be expected that local pride would be stung and some residents of the community inconvenienced by this situation. Improved highways and the automobile have made unnecessary and uneconomic a bank at every cross-roads town. My own analysis of the conditions in Washington leads to the conclusion that there are now few bankless towns in this commonwealth in which a bank would prove economic.

While part of the reduction in number of banks has come about through the elimination of small institutions in one-bank communities, some of it is due to a reduction in the number in those towns and cities where banks still operate. In many cases this has merely corrected a grossly overbanked condition. A striking example is found in the Chicago area. In Cook County, Illinois, only 98 banks were operating in 1935 out of 479 which had been in existence some time during the years 1921-35.

May we conclude that the reduction in the number of banks has been in the public interest? In general, the answer is yes. Fewer banks has made possible better banks. No serious inconvenience has resulted from cutting down the number.

Is there greater danger that the evils of monopoly will manifest themselves with 15,000 banks than with 30,000? If so, what are the correctives? For two decades supervisory authorities pursued a very lax bank chartering policy. It was easy for any faction in the community which felt the existing institutions were not giving adequate service at moderate cost to launch a new bank. Some of these banks were "spite institutions" and many of them were uneconomic, but the existence of this right effectively prevented any charge of banking monopoly. In recent years we have adopted a policy of rigorous birth control in banking. As a consequence existing banks have what amounts almost to a franchise for carrying on the banking of their communities.

A usual condition of exclusive franchise, for instance in the field of public utilities, is regulation of rates and services. In banking rate regulation has been limited principally to fixing maximum rates of interest on savings deposits. Bankers have chafed at the lower earning power of their loans and investments and have sought means to recoup their declining earnings through various types of service charges for checking privileges, cutting interest on savings accounts, and similar measures. Bank patrons will pay reasonable service charges and accept lower interest rates on savings deposits rather than have the banks try to build up earning power through making hazardous loans. Bankers, on the other hand, must exercise moderation in their policies, must be able to fully justify any new charges, and must be prepared to accept moderate profits. Critics have pointed to clearing house agreements, relatively high rates to borrowers who have only limited access to banking facilities, the failure of the over-the-counter loaning rate to fall as low as the open market rate on commercial paper, as evidence of monopolistic elements in commercial banking. An examination of the data shows that thus far there is little ground for this criticism. As bankers eagerly seeking new business and harassed by the competition of new credit agencies, these charges may seem to you little less than fantastic. The reports of the Comptroller of the Currency show that dividends paid by National banks in recent years have not been unreasonably high. On the other hand, the net profits of the years since 1936 represent a fair return upon the investment.

The spread of branch banking is also causing changes in the structure of banking in certain sections of our country. Visiting delegates from the East and Middle West may not be aware that the Twelfth Federal Reserve District is the Nation's largest branch bank area. All of the seven States in this district permit State-wide branch systems.

Branch systems in the Pacific Northwest have evolved in most cases from earlier group organization. The transition has been gradual. The local bank was acquired by a holding company. The existing management was unchanged; the bank was still known by its former name. Later it became a branch. Policies of management were modified gradually, if at all. As a consequence, the bank's patrons have scarcely been conscious of the change that was taking place. The retention of local management has allayed public opposition to the growth of branch banking. In some cases the branch bank is able to give a wider variety of services and to extend larger lines of credit.

The coming of branch banking seems to me to have rather broad social implications. It is an evidence, not a cause, of a changing economic order. A half century ago business units were local. Today they cover trade areas, States or even the entire Nation. An illustration drawn from any typical Western Washington community will illustrate what I mean. A generation ago each community had a local power plant, a creamery, locally-owned sawmills, grocery stores operated by individual owners. Today the picture is changed completely. The local lumber mills have been sold to some of the larger timber interests which hauls its logs a considerable distance to its large and efficiently equipped mill. The local power and light company has become part of a large system with headquarters in the larger cities. The creamery has become a branch of a cooperative organization. Of the retail stores in the average small town an increasing number are chain institutions. The gasoline which furnishes the motive power for hundreds of local autos and replenishes the supply of tourists along the highways is sold from service stations controlled by the great oil companies. The farmers sell their produce through cooperative associations with headquarters in the more important cities of the State.

What is the effect upon the country banker? A generation ago the local mill owner, logger, dairy man, merchant, and power and light company were all valued customers of the bank. They were independent business men operating on a small scale, borrowing their money from the local banker over the counter at the regular rate of interest. The banker practically never looked outside of his community to invest his funds. Today these same lines of business maintain an account in the community bank. With what effect? The local manager is a salaried official. The borrowing to meet the needs of the entire organization is done in the financial centers. The big corporation can get the best terms available on over-the-counter loans. It can also go into the open market to sell its paper through the commercial paper houses.

Bank deposits increase, but instead of loaning the money to the business interests of the community the banker is forced in ever-increasing amount to seek for an outlet for these growing deposits. The bond account of the country banks has grown to a large figure. It makes loans at call in the New York market. It buys the commercial paper of the corporations whose branches are absorbing the local business. The bank becomes less and less a purely local institution from the credit-granting point of view.

In the three Pacific Northwest States excellent unit banks may be found. Progressive bankers have adapted themselves to changing conditions. Our laws have protected existing banks from the pressure of branch bank competition by providing that branches can be established in communities with adequate banking service only by purchasing on an existing bank. My observation on the whole, therefore, is that the extension of branch banking has been carried on in a wholesome manner without creating an over-banked condition or engendering bitter hostility between branch and unit banks. Progress has been made gradually, and the absorption of new units appears to have taken place in a normal manner. Although branch banking has developed rapidly in this section in the past five years, it is safe to predict that we will continue to operate branch and unit banking side by side for many years to come, if not indefinitely.

Deposit Insurance

Deposit insurance has, to my mind, a number of interesting implications. In the first place, its adoption shows how impredictable important changes in banking may be and how dependent they may be upon existing economic conditions. A decade ago State deposit guaranty programs had collapsed. All eight, including our own in Washington, had been dismal failures. The general conclusion was that these experiments had demonstrated the fundamental unsoundness of deposit insurance. The conservative banker felt that he had been vindicated in his conclusion that insurance of bank deposits could not succeed. But he had a rude awakening!

More far-seeing was a shrewd American economist, Professor F. W. Taussig, who wrote more than two decades ago:

"The course of legislation on this matter, as on others, is likely to be much affected by actual experience. A succession of conspicuous bank failures, bringing great loss to depositors, would immensely strengthen the movement for deposit guarantee."

Subsequent experience had seemed to belie his prophecy. Then came the "succession of conspicuous bank failures." The movement for deposit insurance proved irresistible. It was accepted reluctantly by many bankers and welcomed by others as a means of restoring public confidence. There is evidence that this result has followed. Deposits returned to the banks in 1934, and they stayed through the recession in 1937.

The Panic of 1907 gave us the postal savings system. This was a city of refuge for timid depositors, but its facilities were little used before 1930. As a consequence of the depression, postal savings jumped from $150,000,000 to $1,200,000,000, an eight-fold increase. But postal savings pleased neither the banker nor the depositor. The banker saw his deposits drained away by bank-shy depositors just when he needed them most. The average depositor prefers to deal with his regular bank. I am of the opinion that the public will insist upon protection for deposits. If deposit insurance is discontinued it is probable that even more far-reaching changes will be demanded in order to assure safety of deposits.

A second consequence of the adoption of deposit insurance is that bank failures must be kept at a minimum. The eight State systems had all broken down in the comparatively calm days before 1930. The present resources of the Federal Deposit Insurance Corporation are not sufficient to withstand a crash like that of 1931-33 without Government aid. In the present temper of the depositing public, I hazard the prediction that Federal insurance will not be allowed to go the way of the State systems.

How may this be prevented? The best way is to assure the solvency of the Insurance Corporation through sound banking, fostered by rigid supervision. Insured banks have everything to gain by supporting supervisory policies that will minimize failures. Not only will this contribute toward stability of the insurance program, but it may ultimately reduce the insurance premiums which you are called upon to pay. It is well also to recognize that the incidence of the cost of deposit insurance is upon the depositors.

In an analysis of the Banking Act of 1933, immediately after its passage the writer stated:

"In the long run, if the Federal insurance plan works, the cost will be passed along to the beneficiary—the insured depositor—which is entirely proper." *

This has in effect taken place. Increased service charges, compulsory elimination of interest on demand deposits, reduction of interest on savings accounts are methods by which bank patrons are helping to defray the expenses of deposit insurance. As I stated six years ago, this is entirely proper. It would be even better if depositors were conscious that they were paying the premiums. Indirect taxes encourage extravagance. Unconscious payment of insurance premiums tends to make the depositor indifferent to the burden which unsound banking may impose upon the insurance corporation.

It has been suggested that we must permanently maintain a Government-owned corporation—perhaps a bigger and better Reconstruction Finance Corporation—to aid the banks in the next crisis. The Federal Deposit Insurance system was instituted with the cooperation of the RFC. The capital of thousands of banks was so badly impaired in 1933 that the sale of approximately a billion of preferred stock to the RFC alone made possible the inauguration of the insurance program. Without extensive use of preferred stock the alternatives would have been:

(a) Admission of thousands of weak banks with heavy potential losses to the FDIC; or (b) denial of insurance to a large number of banks which probably would have precipitated heavy runs on Jan. 2, 1934.

After six years the RFC still owns hundreds of millions of preferred stock of banks. Must we continue its existence as a public fire department to save the banking system in case there is a general conflagration? I don't know the answer, but I do not believe the system will be allowed to collapse as did the State systems. If the Government is forced to absorb heavy losses, the next step may be to take over the banks. Business men, and in fact I believe the majority of voters, will join in your desire to preserve the private ownership of banks. I am hopeful, therefore, that improvement in the quality of bank supervision will so reduce the number of bank failures that a fire department may be unnecessary and public ownership averted.

An important result of deposit insurance having broad social consequences is greater uniformity in banking supervision. There were many who wanted Congress to seize the opportunity to bring all insured banks under Federal supervision. Senator Glass gave up his opposition to deposit insurance when the bill provided for compulsory Federal Reserve membership of all insured banks in two years. Early amendments removed this requirement from small banks (deposits under $1,000,000), and postponed the date when the larger banks were required to enter the fold. The requirement was swept away entirely by action of Congress last spring.

Nevertheless, the supervisory powers of the FDIC have had a marked effect in unifying bank regulation. Insured banks are subject to annual examination. State examiners have adopted part or all of the revised examination procedure put into effect a year ago by the Federal Reserve, the Comptroller, and the FDIC. For the time being at least, the steps taken toward uniformity are to be preferred to enforced Federal Reserve membership by unwilling State banks or the complete abolition of State commercial banks. This, I note, accords with your own declared policy.

There are certain implications of deposit insurance that may appear to you to be highly theoretical. To my mind they may become quite practical. The first of these is a belated recognition that deposits are not ordinary business debts. They constitute an important part of our medium of exchange, greater by far in volume than the coin and paper money in circulation. Depositors and bankers have looked upon a bank deposit in quite different ways. To the banker, deposits are liabilities; to the depositing public, they are "money." Which is right? At least with respect to demand deposits, our verdict must be that the depositor is correct.

The view, long vaguely held and poorly understood, that, to use the words of a prominent monetary economist, banks are "creators and guarantors of money" † is now finding expression in the literature of money and banking. "Keynes Treatise on Money" includes bank deposits. Laughlin's "Supply of Money" also deals with deposits.

A century ago the notes of banks were a liability differing in form but not in substance from the deposit liabilities. New York, under the safety fund system, first provided for mutual insurance of bank notes. This method was superseded by a system of bond-secured note issue, first adopted in New York in 1838 and carried over whole-cloth into the National Banking System, where it was used for more than seven decades.

My college generation was taught that holders of bank notes were deserving of special protection since notes circulated widely. Depositors, on the other hand, were assumed to be able to select sound depositories and to exercise a restraining influence upon bank policy by their right to withdraw funds from an unsoundly managed bank. The result has been bank runs, hoarding, deflation, and heavy losses to loyal depositors. Today, a conservative economist writes:

"Deposits are deserving of the same measure of protection which the Government has long accorded in connection with bank notes." †

Lest you think his statement radical, I hasten to add that it is made in connection with a masterful appraisal of the 100% plan, in which he opposed the adoption of that proposal.

A hundred years ago exchange charges were customary when out-of-town bank notes were received in payment or taken on deposit. For decades bank notes have been received everywhere at par. Under the Federal Reserve system of check collection, par remittance is universal. No further steps looking toward abolition of all collection charges seem to be imminent. It does not necessarily follow that bank deposits will pass through the same evolution as bank notes. It is safe to assume, however, that the public will demand that the banks must provide a safe form of bank "money." If deposit insurance is discontinued, it is possible that even more far-reaching changes may be made in order to assure safety for the country's money. Of the reforms currently advocated having this objective the 100% reserve plan seems to be most widely discussed. It would, if adopted, put deposits in the position of bond-secured bank notes. My personal view is that the adoption of this plan would require such a drastic overhauling of our banking system as to make it an undesirable reform.

The argument that deposit insurance is a belated recognition that bank deposits are "money" does not account for the inclusion of savings deposits in the insurance program. Economists and bankers who accept without cavail the concept that demand deposits are "money" will ordinarily balk at putting savings deposits in that category and yet savings deposits are insured. In fact, pains were taken to make mutual savings banks eligible for insurance before the law was originally enacted. It is interesting to observe, however, that only 48 mutual savings banks, with approximately one-tenth of the deposits in this class of institutions, are

* American Economic Review, Volume 23, page 598.

† Watkins, Leonard L., "Commercial Banking Reform in the United States."

now insured. Is this evidence of a recognition of the difference between "money" in the bank and a savings account? In my opinion, it is not. It is rather a tribute to the splendid record of mutual savings banks. It does, however, suggest that the oft-proposed programs for segregation of demand and time deposits is based upon an actual difference in the nature of these classes of deposits.

The definition and classification of deposits has been a troublesome problem for the supervisory authorities since the passage of the Banking Act of 1933. It is a stumbling block for advocates of the 100% reserve plan who generally choose to treat savings deposits as investments.

A final implication of deposit insurance is its effect upon the stability of the volume of bank deposits. In the past, bank failures have been a serious deflationary factor. Purchasing power is tied up in failed banks; hoarding increases; banks feel compelled to maintain high liquidity; loans are called or not renewed. The indirect social losses from bank failures may well exceed the direct losses to depositors. If deposit insurance allays the fear of the depositor, the banker may be expected to adopt a bolder policy. To the extent that deposit insurance mitigates the deflation caused by hoarding and the banker's fear of his depositors, it will achieve a real social gain. There is some evidence that it has contributed toward this objective.

Most striking change in the functioning of banks is revealed by an examination of the asset accounts. A West Coast banker, famous for his ability to coin terse epigrams, has said that a modern bank is a "combination of an investment trust and a pawn shop." He did not explain that the investment trust has not diversified its portfolio very extensively. Examination of the loans and investments of all member banks reveals that in recent months two-fifths of the assets and two-thirds of the investments of member banks have been United States Government securities, direct or fully guaranteed.

The "pawn shop" activities have been evidenced by making of modernization credit loans on electrical equipment and the creation of personal loan departments. Modernization credit gave banks an opportunity to participate in the Government's drive on unemployment and enabled them to make new lending contracts in a field which they had previously been hesitant abount entering. The expansion of personal loans should give bankers an interest in better regulation and control of consumer credit. It is possible for them to render a social service by supporting the movement for sound small loan legislation. With their conservative traditions, bankers should keep an eye upon the aggregate volume of consumer credit. Overextension of credit is bad for the borrower and economically unsound.

Present indications are that commercial loans will not regain their former place in the banks' portfolios. Bankers may be forced to seek still further outlets for funds. The progressive banker may thereby contribute toward economic progress and improved methods of financing business enterprise.

A discussion of the implications of banking changes would not be complete without some consideration of the place of the Government in our credit system. It is with considerable temerity that I approach a question so full of dynamite. The entry of the Government into the loan field was largely to meet the emergency. Participation is through loans made by governmental corporations and credit agencies; through the ownership of stock in State and National banks, savings and loan associations, agricultural credit institutions and other lending institutions; and by the insurance of certain classes of loans made by banks. Governmental corporations and credit agencies reported $8,500,000,000 of loans and preferred stock on June 30, 1939. At the head of the list stand the farm credit agencies and the Home Owners' Loan Corporation.

The most important example of insured loans are those under the Federal Housing Administration. Title I loans were made by all classes of commercial banks. National banks are the largest single holders of insured FHA mortgages. Aggregate holdings of Title II mortgages by National and State banks are well in excess of half a billion.

Possibilities for the future are that governmental participation in the loan field will be gradually terminated. Many existing agencies were created to meet the emergency. It is obvious, however, that even those institutions that were presumably temparary are liquidating slowly if at all. The same is true of insured loans. The period of Government guaranty of modernization credit loans (Title I) was at first to terminate in 1936. It was twice extended with some modifications, lapsed for a time, and was revived in 1938 to meet the recession. The Government guarantee of insured mortgages under Title II was at first limited to those insured prior to July 1, 1937, and it, too, has been extended. Viewing the record of the past six years does not offer much prospect for the early withdrawal of the Government from the loan field.

At the other extreme stands the possibility that the Government may take over all lending operations by outright ownership of the commercial banking system. I do not see any strong probability that this will take place. Business men are generally opposed to Government ownership of banks. Thie history of Government credit-granting shows the dangers of political influence and stands as a strong deterrent to a complete transfer of the control of credit from private institutions to public hands. The eagerness with which banks seek to adapt their credit policies to changing economic conditions will have a significant bearing upon future developments. It must be conceded that the public interest is paramount. It is the continuing responsibility of the bankers to show that this interest can be best served by retention of the private administration of credit. I have already suggested that the breakdown of deposit insurance might result in Government ownership of the banks. This means that the banks must vigorously support sound administrative policies to the end that failures may be minimized.

The outlook for the future, as I see it, is for a continuation of the present system of privately-owned banks with supplementary governmental agencies. I expect to see an extension of the use of insured loans, but believe they should be restricted to loans that banks are willing to hold for their own account. I observe that banks, loaded with idle funds, are making FHA loans in the higher loan-to-value ratios or with longer maturities with the expectation of selling them to the Federal National Mortgage Association. This practice is likely to bring repercussions. Should banks make loans that they believe to be unsound? Will the Association long permit itself to be the dumping ground for the weaker loans without expecting to have a proportionate share of good loans to average its losses?

A banking change frought with great possible social significance is the increased powers of the monetary authorities. Legislative changes and the great influx of gold have given to the Treasury and Federal Reserve increased powers. Acting together, they are in a position to dominate the money market. The Board in its annual report for 1938 has concluded that the power of the Treasury "to influence the volume of member bank reserves under existing conditions outweighs that of the Federal Reserve System." The whole problem of credit control and the possible conflict of policy between the two monetary authorities is one of primary social importance. It appears, however, to be beyond the scope of this paper and deserving of more careful analysis than is possible in the time allotted to me.

May I briefly summarize some of the points raised in this discussion? In the first place, we have undertaken to show that change is normal and that banking leadership has always proved adequate to meet changed economic conditions. In fact, the success of the leaders of other eras has been due in large part to their ability to pilot their institutions through uncharted seas.

Having the number of banks and the restrictive policy with respect to charters to new banks has given a sounder banking structure. Limitation upon the number of banks makes possible development of monopolistic practices in commercial banking. At the present time there is little, if any, evidence of the evils of monopoly. The public stands ready to pay a fair price for banking service. The banker on his part must accustom himself to more moderate profits than those prevailing in the boom days of investment affiliates, mergers and stock split-up. If earnings are reasonable and service adequate, existing banks need not fear pressure in favor of letting down the bars for creation of new banks or the possibility of more rigorous regulation of rates and service.

Branch banking is changing the structure of banking in some sections, notably in the area. It has come, in part at least, in response to changes in economic conditions, especially the tendency for business units to operate over wider areas. Observation of the trend in the Pacific Northwest leads to the conclusion that the public is primarily interested in having branches manned by men with an interest in the local community. Unit banks are safeguarded from branch competition in their own field. Indications are that we will have a combination of unit and branch banking at least in the proximate future.

Deposit insurance has been a major banking change growing out of the depression. Its adoption was a surprise to most bankers and students of banking and was due to a "succession of conspicuous bank failures." It was the answer to the public's demand for banking safety. Eight State systems have broken down and disappeared. The Federal program may be preserved by rigid supervision. If this proves inadequate the Government will probably step in either through a Government-owned corporation or outright assumption of the bank's liabilities. It is to the interest of the banks to support rigid supervision to the end that this contingency may be averted. A consequence of insurance has been the tendency toward greater uniformity in banking supervision. This is a desirable outcome and is preferable to enforced Federal Reserve membership or complete abolition of State commercial banks.

A broad implication of the adoption of deposit insurance is the recognition that demand deposits are "money" and not ordinary business liabilities. As such they are deserving of special protection. Less than one-tenth of the deposits of mutual savings banks are now insured. This does not indicate any conscious recognition that deposits of this class are an investment whereas demand deposits are "money." It does suggest, however, that the current attempts to differentiate the two classes of deposits rests upon a fundamental difference.

Instability in the volume of bank deposits contributes to deflation. If deposit insurance results in more confidence on the part of depositors and bankers and thereby mitigate deflation it will achieve a real social gain. The basic argument in favor of the 100% reserve plan is that it will prevent violent changes in the total quantity of "money," including bank deposits. This proposal would entail such a drastic revision of our banking system that its adoption is not favored. It may come in some form, however, if existing machinery is unable to achieve greater stability.

The changing function of the commercial banks is evidenced by the decline in commercial loans, the growth of new classes of loans, and the expansion of bank investments. Nearly half of the earning assets of the member banks are Government securities or bonds or loans guaranteed by the Government.

The future place of the Government in our credit system is a moot question. There is little reason to expect the early withdrawal of governmental agencies from the loan field. On the other hand, outright Government ownership of the commercial banking systems is undesirable and unlikely to come unless the present system breaks down in some future crisis. A growth in the use of insured loans of the type of those used by the FHA is anticipated. Bankers should use their influence to see that they are basically sound.

The increased powers of the monetary authorities is a change fraught with great possible consequences. This responsibility is divided between the Treasury and Federal Reserve System. Policy is not clearly defined and the boundary line between the field occupied by the two bodies is still undetermined.

The National Banking System

By PRESTON DELANO, Comptroller of the Currency, Washington, D. C.

President Cook in introducing Comptroller Delano said:

In presenting to you the next speaker, gentlemen, let me tell you that it affords me great pleasure. I am proud of his record which has been most successful and most active in the country's service. He served in the World War as an officer of the United States Army and in various other official capacities, in each one rendering the best of public service, and on Oct. 24, 1938, became the Comptroller of the Currency.

Mr. Delano's address follows:

The traveler leaving the National Capitol is confronted by a quotation from the Spanish, cut in stone on the facade of the Union Station. This particular legend has always interested me for its colorful presentation of a truth applicable in its broader aspects not only to travel but to other lines of human endeavor, whether they be government, business, banking, or any of the many activities of civilized man. The quotation reads:

"He who would bring home the wealth of the Indies must carry the wealth of the Indies with him."

The inscription goes on to explain that it is thus with travel, a man must carry knowledge with him if he would bring home knowledge. To my mind this principle holds true of all enterprise, and it is certainly true in our chosen field of banking.

It can properly be said that the National Banking System, now 76 years old, has met the requirements of this old Spanish proverb. Since its inception in 1863 it has brought home the wealth of the Indies, but it also has carried the wealth of the Indies with it and has given richly in return. It is difficult to overestimate the contribution made by the national banks to our civilization while that civilization was developing from a rude frontier, an agricultural community, to the intricate and involved industrialism which is today both our boast and a plague to us. It requires study and reflection to understand the vast difference which exists between the America of the 1860's and the America of 1939. Students of social and scientific progress insist that the pace and momentum of change within these years is without precedent.

In 1862 the "Washington Standard," a four-page weekly newspaper published at Olympia, served as the official United States paper for this Washington Territory, which then contained about 12,000 inhabitants. On Jan. 4 of that year the subscribers noticed a new advertisement headed "Olympia Wagon Manufactory," which made the following announcement:

"STUART & BLACKSHEAR

Would inform the citizens of Olympia and the surrounding country that they are now manufacturing WAGONS, CARRIAGES, and BUGGIES of all descriptions . . . for which wheat will be taken in exchange, delivered at the Tunwater mills."

It was at this period, when barter was still an accepted means of trade in a progressive, growing community, that the National Banking System was born. Let us look for a moment at what sort of a country ours was at that time, and notice how much has disappeared, changed, grown, and come into being.

Until shortly before the Civil War man traveled only on horseback or by stage coach. He transmitted messages only by courier or by such crude devices as signal fires. In the realm of medicine, anesthesia was unknown and Pasteur had not yet startled the world with his discoveries. In all other lines of the applied arts and sciences quite as great a discrepancy exists between that era and our own. When we attempt an examination of the social and economic organization we are again struck by the wide gulf between these two periods. You will search in vain for any 76 years of history which even remotely compares in this respect.

When the National Banking System was inaugurated in 1863, there were 34 States in the Union and the population of the United States was some 32,000,000. Of this total, some 27,000,000 lived on farms or in small towns of less than 8,000. The steam railroad was in its very early development, there being some 30,000 miles of trackage in the United States providing a service which we would regard today as primitive. The telegraph was still a curiosity and there were, of course, no electric lights, no telephones, no automobiles, no radios, no airplanes. There was also a lack of so many of the conveniences and ingenious devices by which we live that it is practically impossible for us to mentally project ourselves back that far—and it is only 76 years ago.

The economic and financial problems which confronted the nation were so widely different in character from our own that they again illustrate this great gulf between the two eras. It was largely because of one of these financial problems that the National Banking System came into being, and this particular problem would appear fantastic to us today. Whatever may be our financial and economic troubles, and they are many and serious, we do not have to wrestle with the difficulties created by 7,000 different kinds of bank notes, ranging in value from par to a few cents on the dollar, and so heavily counterfeited that an expert is required to tell what, if anything, each bill is worth. It was precisely this condition which was responsible for the creation of the National Banking System. In 1863, when the Senate was deciding whether the Federal Government should throw its power into the confused banking and currency field, its leading financial expert, John Sherman of Ohio, later Secretary of the Treasury, said:

"There are 1,642 banks in the United States established by the laws of 28 different States, and these laws are as diverse, I was about to say, as the human countenance. We have every diversity of the bank system in this country that has been devised by the wit of man, and all these banks have the power to issue paper money. With this multiplicity of banks, depending upon different organizations, it is impossible to have a uniform national currency, for its value is constantly affected by their issues. . . . There is no check or control."

To assist in meeting this situation, an enterprising house started a weekly publication known as the "Banknote Detector." This publication attempted to carry advice as to the validity of various notes and the standing of the issuing banks. Sumner, in his "History of Banking," says:

"The 'bank note detector' did not become divested of its useful but contemptible function until the National Bank System was founded. It is difficult for the modern student to realize that there were hundreds of banks whose notes circulated in any given community. The bank-notes were bits of paper recognizable as a species by shape, color, size and engraved work. Any piece of paper which had these came with the prestige of money; the only thing in the shape of money to which the people were accustomed. The person to whom one of them was offered, if unskilled in trade and banking, had little choice but to take it. A merchant turned to his 'detector.' He scrutinized the worn and dirty scrap for two or three minutes, regarding it more probably as 'good' if it was worn and dirty than if it was clean, because those features were proof of long and successful circulation. He turned it up to the light and looked through it, because it was the custom of the banks to file the notes on slender pins which made holes through them. If there were many such holes the note had been in bank and its genuineness was ratified."

"I ask you, Sir," said John Sherman, in the Senate, "How is it possible to have a currency—and how is it possible for any honest man to detect the genuine from the counterfeit, when he has to select from 7,000 different kinds of bank bills, and the bills of those banks have been counterfeited?"

The newspapers supplemented the bank note detectors with fresh tips on the latest counterfeits. For instance, the "Washington Standard" in January, 1863, informed its readers that large numbers of new counterfeit bills were in circulation in California and that some had found their way into the Territory. "The five's," it announced, "are being extensively counterfeited, and being good imitations are most dangerous," and the citizens were advised that a slight difference in shade was almost the sole reliance for distinction. On the other hand, it said, "the counterfeit ten's are easily recognized from their imperfect execution. The female figure, which is on the right of the spurious bill, has five toes on the left foot and four on the right. In the true bill there are four toes on the left foot and three on the right."

The National Currency Act was passed on Feb. 25, 1863. The national banks grew slowly but steadily during the early years of their authorization. The problem of counterfeited and unstable currency was met. The Federally chartered institutions, with their sound note issues, gradually assumed a greater importance and wielded a larger influence. In 1874 there was a revision of the National Currency Act bearing the title, "The National Bank Act." From this time forward, with its first important job well done and behind it, the Nnational Banking System assumes more the character which we recognize and becomes the dominant factor in the field of commercial credit.

From the close of the Civil War to the great panic of 1893 there was an ever quickening pace of expansion and commercial development in these United States. There was a great surge forward in the field of science and invention. These were the years of the winning of the West—one of the most romantic periods in our history, and the national banks did much to steady it and give it financial sinew. By 1890 the national banks had grown in number to 3,500, with deposits of practically $2,000,000,000 and with total resources of $3,000,000,000. The population had grown to 63,000,000; the number of States had increased to 45, and that significant shift from agriculture to the communities of great cities was already taking place. Of the 63,000,000 population, over 18,000,000 now lived in the larger cities, and we were beginning to feel the impact of the business cycle and of the difficulties of industrialism.

The crisis of 1893 first called attention to a defect in our fiscal organization which was later to be emphasized by the so-called "Paper Panic" of 1907. This was the inelasticity of the nation's currency. No attempts were made in the 1890's to meet the growing demand for a less rigid system of note issues, due probably to the fact that the silver question drew away men's minds from consideration of this question. There was some recognition of the necessity for at least more currency in the Act of 1900, permitting the organization of smaller national banks and a larger proportionate circulation. The taxation on circulation was reduced. The privileges thus granted led to a marked increase in the establishment of banking institutions and in their circulation. From 1899 to 1913 the number of national banks doubled from 3,595 to 7,492. The circulation nearly trebled between 1900 and 1911, from $254,000,000 to $759,000,000.

This period, which extended from 1890 through the controversy over silver and bi-metalism and into those years of the Twentieth Century just prior to the World War, saw the practical completion of the industrialization of our country. The progress of science and invention, the growth of population and of wealth, the shift to urban centers, the changes in standards of living brought about by the introduction of the automobile, the radio, the airplane, and, above all, the economies effected by mass production, all served to accentuate the metamorphosis taking place in both the social and economic organization. The large increase of national banks during this period and their effort to keep pace with ever increasing financial demands were supplemented in 1913 by the introduction of the Federal Reserve System. The panics of 1893 and 1907 had finally resulted in the establishment of machinery to provide an elastic currency and a central banking system able for the first time to exercise some control over the expansion and contraction of credit.

One year later—in 1914—the world was plunged into war. The last few weeks indicate clearly that the years which make up the epoch from that fateful decision to the present day must be treated as constituting a quarter century of great significance. Technological development and the change in habit and method continue apace, but there is added a clash over social and economic organization greatly imperiling all those intangible but precious things which make a civilization. This war which started in 1914 and which we thought ended with the armistice in 1918, is again breaking into flames. The events of those 25 years since 1914, culminating in the recent resumption of hostilities between the major European Power., are all too fresh in our minds to need review. Their significance is another matter, which, because of the lack of perspective, it is very difficult to appraise. What may all this mean to banking, and in a norrower sense, to the national banks of the United States? It would seem that we are witnessing the beginning of a fundamental struggle between economic and social regimentation on one hand, and the forces of an individualistic society and a free economy on the other.

These are questions which are too deep, and is too rapid a flux for us to properly plumb. However, I would like to digress for just one moment at this point to most informally answer a number of questions that I have met, and which members of my staff who are here tell me are being asked in the corridors and which, of course, are very pertinent to this situation. That is the attitude of the Comptroller's office toward the Government bond portfolios of the National banks. I think we should make it clear that there is no contemplated change in the policy or the regulations which the Comptroller's office has now had in operation for some time on this point. But it seems to me the fundamental thing we are witnessing here goes much deeper than mere questions of technique or policy, because we are witnessing what seems to be the start of a great struggle between economic and social regimentation on one hand, and the forces of an individualistic society and a free economy on the other. This is a bettle of great moment to all of us.

Whatever role may be reserved for this young republic in the grim drama now unfolding both to the east and to the west, there will be heavy responsibilities placed on all leaders of men. Banks are the nerve centers in the intricate and involved system by which we live, and there will be need for steady hands. America is equipped for the job. Whether we consider wealth in terms of the necessities and conveniences of life or in terms of gold and banking assets, we have it. The national banks have held and still hold their all important position and influence in this greatest of free societies. Their resources today exceed thirty-three billions of dollars.

Never in your history, gentlemen, have you been collectively so strong to play your part in the great decisions which ie ahead.

COMMITTEE AND OFFICERS' REPORTS—NATIONAL BANK DIVISION

Address of President H. E. Cook, President The Second National Bank, Bucyrus, Ohio

Performance of every character of helpful service within its power to furnish to its members continues to be the policy of the National Bank Division of the American Bankers Association. Essential to the success of such a creed is a recognition of the nature of member banks' needs. Therefore, to supplement the general understanding of the ends toward which banks are always striving, and the needs which arise from major changes which command wide attention, the Division has sought, through its various committees and State Vice-Presidents, to keep informed of the pecial problems of banks in different localities, as well as throughout the entire United States. Thus it has been able to study questions which ordinarily might not come to its attention, and it feels that this collective consideration of such questions has been advantageous. Special emphasis is laid upon this proffered aid to single banks in the solution of their individual problems, and it is limited only by their needs. It is available to all members.

In a category differing not at all in its general purpose, but with a broader application, the Division likewise watches constantly developments which affect all members as a group This serves a much larger section of the Division and deals with their more important common problems. It embraces such items as concern earnings and expenses of National banks, legislative developments, regulations under which member banks operate, and suggestions for improvements in practices common to all banks. The advice and assistance of officers and committeemen and members of the division at large have been drawn upon freely in this work, and the degree of success attained in its performance is traceable in a very considerable measure to the cooperative attitude and prompt response to appeals for expert guidance.

Expenses and Earnings

The latest tables prepared by the Division on earnings and expenses of all National banks showed some progress toward the goal of more satisfactory bank operations. However, to even the casual observer it is apparent that some additional improvement must be made. With deposits at the highest peak in banking history and bolstered by a capital structure greater than ever before assembled, the lessened opportunities for employment of bank funds present problems most difficult to solve. The additional vast sums in private hands, seeking but unable to find investment, add materially to the seriousness of the dilemma. However, despite the diminished total of loans and investments in National banks reported for the year, the more recent slight increases are mildly encouraging, and give rise to the hope that the decline, which was almost continuous from 1929, will be reversed.

Recent developments abroad—particularly the outbreak of war in Europe—has given stimulus to business activities in our own land, and while these developments are so recent that sufficient time has not elapsed to accurately gauge the ultimate effect upon American business, temporarily at least in all likelihood banks will experience an increased demand for loans, firmer money rates, with consequent increased earnings.

By closer analysis of operating expenses, the curtailment of costly and unnecessary service, thorough analysis of commercial accounts and services rendered to patrons, and the application of proper and equitable service charges, substantial additions have been made by most banks to their operating revenue. An analysis of out banking operations has pointed out to us not only a substantial saving in operating costs but new sources of revenue which many banks have found to be advantageous, as well as broadening their services to their clientele.

Bank Loans

As conditions now exist there are ample bank funds available for loans, nor is there any doubt that banks not only are willing, but eager to lend. This Division has investigated this subject to learn something of the degree of determination with which new loans are sought. In some cases lack of continued effort to make loans brought about the result of lack of response on the part of the borrowers to use bank funds to expand their businesses. In communities in which constant efforts to place additional funds have yielded no results, there is in evidence a lack of that aggressiveness which is always found to underlie expanding business activity. This may be accounted for in some measure by the type of local business which, because of its nature—either because of the type of industry or agriculture—does not find that bank credit under existing conditions can be profitably employed.

On the other hand there are many outstanding cases of gratifying results attained by demonstrating to borrowers the advantages of dealing with banks. Banks know they can offer more satisfactory loan plans, and a considerably greater percentage of the curtailed total lending may be within the reach of banks if borrowers who find ways to use additional funds can be convinced of the superior services offered by banks. A great number of our banks, particularly the larger institutions, have found it advantageous and profitable to install personal loan departments under the management of experienced and capable executives, thereby serving a source of credit demand which is essential in our present system. It meets the requirements of a large number of people, is profitable for the banks, retains borrowers as potential patrons in other departments of our organizations, serves to stabilize and maintain fair and equitable rates of interest, and is altogether a very necessary development of modern banking.

Assignment of Proceeds of Government Contracts

The inability of banks to obtain assignments of proceeds of Government contracts as security for loans, makes impossible in many instances the granting of loans which under other circumstances would be highly desirable. Seemingly, the most that can be done at the present time is to file instructions with the Government to have the contractors' checks sent to the banks, though in many cases this is unsatisfactory. The desirability of an amendment to the statute was studied by the Division's Executive Committee, which sought also to determine the probable difficulties which might be encountered. The advantages of such a move were suggested also to certain other organizations which have an obvious interest in it. A satisfactory solution, including the method of accomplishment, has not been found, but there still appears to be merit in the proposal and the Division is seeking ways to have further consideration given to it.

Double Security for Deposits

Protest against the requirement that they provide collateral security for certain deposits protected by the Federal Deposit Insurance Corporation coverage also, is being made by an increasing number of banks, particularly the smaller banks. Their contention that all banks should be freed from this double burden is sound. However, there are only three types of deposits on which the collateral security ordinarily required may be omitted to the extent that such deposits are covered by the FDIC insurance. They are postal savings deposits, bankruptcy funds and moneys belonging to certain National banks being liquidated by the Comptroller of the Currency. These exceptions are statutory.

Postoffice accounts cause much of this dissatisfaction when they do not exceed $5,000 each. Though they are under FDIC protection, they still require a pledge of securities when carried in banks designated by the Security of the Treasury as Federal depositories. Furthermore, such funds must be placed in such depositories if one exists in the town or city.

Figures gathered recently reveal that approximately 400 banks throughout the country have postmaster or postoffice accounts amounting to less than $5,000 each. The collateral requirement is more or less vexatious also to the Treasury Department, because of the fluctuations in amounts and the inability of the Department to know at all times the exact sums on deposit in the various banks. The Department is as liberal as it feels it can be in dealing with such deposits.

However, the lack of justification for this double security is so apparent that the Treasury Department is considering a pain under which it would cancel the designation of small banks as Government depositories when requested by them to do so, in order that they might avoid the requirements of collateral security, especially for postoffice accounts. The Postoffice Department cannot demand such security and the Treasury Department can do so only if the banks are designated depositories. Therefore, the cancellation of such designation would remove the necessity of posting collateral, but would not affect their right to subscribe to future issues of Government securities and pay for them by book credit.

Federal Legislation

To a group of banks chartered and regulated by the Federal Government, changes in Federal banking laws and enactment of new laws are matters of deep concern, whether they apply to such banks exclusively or to others as well. Therefore the Division had a direct interest in many bills proposed in Congress during the year just closed.

One of them, affecting all members of the Federal Reserve System and enacted into law, was the measure extending until 1944 the time in which executive officers' loans may be repaid to their banks. Another bill of vital and continuing importance to National banks extended the provisions of the Social Security Act to include such banks and State member banks, as well as a number of other organizations. The extension and revision of the National Housing Act was important also. Likewise, some of the amendments proposed to the Fair Labor Standards Act, had they been enacted into law, would have simplified compliance with some provisions of the statute.

The Glass bill—Senate 2150—extending the time under which interlocking bank directorates might be continued, was vetoed. The Social Security amendments of 1939 were passed by Congress, and now National banks are subject to the provisions of the Social Security Act.

Of importance to our entire banking system is the authority given to the Banking and Currency Committee of the Senate to conduct an intensive study of the monetary and banking policies of the Federal Government.

To the National Bank Division the Governmental Reorganization bill has given much concern, for the reason that the office of the Comptroller of the Currency was not exempted from its provisions. The measure known as the Brown bill, which would have had a vital effect on the office of the Comptroller of the Currency, failed of passage.

We make mention of these in particular for the reason that all this is indicative of a definite trend toward centralization in banking and monetary control. Legislation broadening the powers of the various governmental agencies to compete with banks of all classes has given much concern and has been given diligent attention by those of our organization responsible for our legislative endeavors.

The Washington office of the American Bankers Association, under the leadership of D. J. Needham, General Counsel of the American Bankers Association, in continual cooperation with A. L. M Wiggins, Chairman of the Legislative Committee of the American Bankers Association, has served loyally and well the interests, not only of the National Bank Division, but of the entire American Bankers Association.

Robert M. Hanes, First Vice-President of the American Bankers Association, and Robert V. Fleming, past President, have continually given of their time and their abilities to safeguard the welfare and the stability of the banks of the Nation.

Inactive Officers

From time to time the Division directed attention to the seemingly unwarranted hardships which resulted from the lack of distinction between active and inactive officers whose borrowings from their own banks were limited by statute. Normal borrowings were prevented, and good loans to some of the most desirable customers could not be made because they were officers, though sometimes with no voice in the granting of credits and with no part in the determination of policies or actual management of their banks.

Small Business Loans

The Division has given much attention and sounded sentiment toward several proposals to give effect to that considerable volume of Congressional thought which assumed that a liberalization of loans was the element necessary to unleash the forces of business development. The Division approved heartily the principle of ample credit extensions upon the sound bases evolved through years of lending experiences, and also upon any modification of those bases which will not jeopardize the safety of depositors' funds. The Division members are in complete accord with the desire to encourage business through any safe means, but they cannot agree that either local or National interests would be best served by disregarding rules found to be requisite to proper credit extension. The dangers inherent in unwise and unwarranted expansion of credit to those whose capacity for the proper employment of such credit is limited would eventually create a situation which might readily jeopardize the soundness of our banking structure.

The President of the Division, representing it before the Senate committee, expressed his approval of the ends sought to be attained, but insisted that removal of some of the deterrents to business revival, rather than encouragement of questionable practices which likely would break under the weight of their operations, would be the wiser course to follow. The eagerness of member banks to expand their loan totals is well known to all actual and potential borrowers, but the accomplishment of that purpose by ignoring vital lending experiences cannot be expected either to generate or to quicken the recovery movement so sorely needed in the United States.

Capital Fund Requirements

Throughout the country the high capital and surplus funds National banks are required to maintain are imposing an increasingly heavy burden, particularly in the smaller communities The $50,000 minimum capital for a new bank plus the same amount of surplus which ultimately must be created make a total capital structure too high to be supported by the volume of business available in many places Almost as burdensome in other instances is the minimum of $25,000 capital and a final like surplus for a bank in existence prior to passage of the Banking Act of 1933 In recent years and continuing to the present there has been a tendency for National banks to surrender their charters and operate under State charters instead, and it is believed that the occasion for this trend may be attributed to the severity of capital fund requirements. While ample capital funds to support the deposit structure is absolutely essential, just as necessary is capable, honest management, which in the final analysis is the greatest safeguard for depositors' funds and profitable operations.

From 600 National banks, each with a capital of $50,000 or less, picked at random in all of the States, it was found that the capital and surplus equals 15.32% of the deposits. Ratios in individual banks show both extremes. One hundred and fifty-four banks in this group have a capital and surplus of less than 10% of deposits, while 57 banks each have a capital and surplus of between 25 and 50% of deposits.

The Division recognizes in this problem a number of elements which are difficult to correct. A weakening of the stability of banks is something to be guarded against zealously. A relaxation out of which would develop speculative organization of National banks would be undesirable. Likewise laws which would require adjustment of capital to deposits at frequent intervals would impose unsatisfactory and impracticable demands. The Division looks upon this situation, aggravated as it is by abnormally high, though perhaps unstable, deposits, as meriting some adjustment, but adjustment of such character as would avoid diminution of the strength of individual banks or of the National system as a whole.

The Division is expected soon to be able to announce completion of its Bank Survey Handbook, which is intended to be a guide to a periodic check upon practices followed in bank operations. The necessity of guarding constantly against avoidable wastes and undue expansion of costs prompted the search for some formula which might refine or make more effective the efforts being expended constantly in all banks to hold costs at reasonable levels and to maintain the required high degree of efficiency.

A series of questions directed to the details of operating practices, supplemented by miscellaneous suggestions, seemed to meet the need. Through them the performance of each feature of work may be brought into review to test its effectiveness and for such subsequent improvement or elimination as may seem proper.

The Handbook also will emphasize the importance of budgetary control. Likewise it will refer to numerous publications of banking reports and statistics which are looked upon a shelpful guides in bank management.

The Office of the Comptroller of the Currency

The authority granted to the President of the United States to reorganize the Executive Branch of the Government within stated limitations, and carrying no restrictions upon changes in the office of the Comptroller of the Currency, focussed attention upon the possible future of the oldest bank supervising agency in the Federal Government. Orders issued in pursuance of that grant of authority so far have had little effect on the Comptroller's office, and there is no public knowledge that other changes in its status are in contemplation. However, until some assurance is given there can be no confidence that the present position of that office, which has won so much respect, will be preserved.

Only last year, in a number of cities throughout the United States, appropriate exercises commemorated the 75th anniversary of the creation of the office of the Comptroller of the Currency. Those demonstrations reflected a recognition of the high type of public service rendered by that office through the many years of its existence Bankers participated with other folks in acclaiming its accomplishments, and the cross-sections of National banker opinions gathered from time to time support that attitude by indicating practically unanimously an insistence that the influence and the effectiveness of the office of the Comptroller of the Currency be not diminished.

Therefore, the National Bank Division is opposed strongly to elimination or curtailment of the work of the Comptroller of the Currency. The Division insists that there should be maintained an independent office for chartering and for the examination and the supervision of National banks alone; that it should be allowed, not only to retain the independence it now holds, but that there should be restored to it the fullness and the independence of action which characterized its administration in other years. These functions should be centered in one agency which would be the sponsor and the champion of National banks, the same as State bank commissioners are the partisans of banks under their control.

At its spring meeting in April of this year the Executive Committee of the Division expressed by resolution its faith in the ability and the efficiency of the Comptroller's office Becuase it is completely attuned and thoroughly responsive to the needs of the public and to banking alike, the Division expressed its conviction that the strongest possible efforts should be made to show whatever unsoundness and undesirability may appear in any movement which may develop to curtail or abolish the Comptrollers' exclusive supervision over National banks.

Appreciation

The Executive Committee of the Division was assembled but once during last year, though smaller groups were called together upon several occasions to consider matters of importance. In addition, through correspondence their views were gathered upon other subjects, and in each instance the promptness and the thoroughness with which the members responded made work with them a distinct pleasure. The same type of cooperation was given by the State Vice-Presidents and members of the Division at large. Their willingness to contribute a full measure of assistance to the Division in the work it undertook gave practical assurance of the attainment of its objectives.

Particularly do I pay tribute to Edgar E. Mountjoy, Secretary of the National Bank Division, and Deputy Manager of the American Bankers Association. His loyal, efficient service in the interests of the Division, capably directed to its welfare and its efficiency, has lightened the burden of responsibility of your officers, and again to him I pay this tribute of appreciation and respect.

Then the official staff of the American Bankers Association—Phil Benson, President of the American Bankers Association; Robert M Hanes, First Vice-President; P. D. Houston, Second Vice-President; Hal Stonier, Executive Manager—all have given of their abilities and their efforts to the strengthening of the organization of the American Bankers Association of which this National Bank Division is a part. So to these men who have given devoted service when the uncertainty of the times demands great minds and understanding hearts that the business of banking, an absolutely essential factor in the economy under which our Nation operates, may fulfill its responsibilities and do its full share to serve the needs of the Nation, we give our fullest measure of appreciation.

The privilege of serving as President of the National Bank Division is one which I have prized highly. It has given me inspiration and pleasure. And the opportunities afforded for closer association and a better acquaintance with the splendid members of the Division have filled my memory with the choicest experiences to be called up and enjoyed in the years to come.

Remarks Before National Bank Division of Incoming President of A. B. A., Robert M. Hanes, on Wagner Resolution for Study of National Banking Policy

In response to a request from President Rouff, newly elected President of the National Bank Division for a few remarks, Robert M. Hanes, speaking as First Vice-President of the A. B. A., spoke in part as follows:

Mr. Hanes: Thank you, for myself and my running mates here, for this opportunity of breaking into your program this afternoon to tell you if I should be elected President of the American Bankers Association—in that I shall have to have a lot of help from you, too—I hope I may expect from you the same loyal support you have given Phil Benson.

This is a great Division of the American Bankers Association, very influential, a fine membership, hard working and intelligent, and certainly the success of all the work of the Association depends in large degree upon the work of the National Bank Division.

I wonder if I might just say a few words about the Wagner Study Committee that has been set up in Washington and will probably start hearings some time in the next 30 or 60 days. That has tremendous imports, in my opinion and the opinion of my associates, for the future of banking in America. It may change the whole trend of banking. Certainly, it puts a large responsibility on the American Bankers Association to properly present in testimony before this committee the bankers' viewpoint. In our connections and our relations in Washington, we have gone there and sat down with the various members of the Congress and the committees and told them our story as honestly and frankly as we knew how, not trying to bring any pressure but, feeling our contentions had merit, that they would list to them. If they didn't have merit, we couldn't expect them to see it from the same viewpoint as we did.

With this spirit in view and mind, we are now making certain studies which we shall hope to present before the Wagner committee. But in this we are going to have to ask for help from bankers throughout the country in offering the testimony, in preparing the testimony, and I sincerely hope the National Bank Division will give us that support and help which we are going to need.

I might say there is nothing, no matter how serious it is in your bank, that should surmount in importance this investigation, so far as the future of your bank is concerned. So if you are called on for help and assistance, I hope, no matter what you are engaged in, you will drop it and help with this most important work we have before us in the next 60 or 90 days.

[The Wagner resolution providing for a study of National Monetary policy by the Senate Committee on Banking and Currency, was passed by the Senate in August last.—Ed.]

Report of Committee on Nominations

President Cook: I will call on Francis Marion Law, Past President of the American Bankers Association, who comes from Houston, Texas, to give us the report of the Committee on Nominations. Mr. Law is Chairman of this committee.

Mr. Law: The report of the Nominating Committee of the National Bank Division is as follows: We beg leave to submit for your consideration the following nominations:

For President of the National Bank Division—Melvin Ruoff, Vice-President Houston National Bank, Houston, Texas.

For Vice-President of the National Bank Division—Andrew Price, President National Bank of Commerce, Seattle, Wash.

We have four members for the Division's Executive Committee: The Second Federal Reserve District, the Fifth, the Seventh, and the Twelfth. These are for three-year terms.

Second Federal Reserve District—F. Raymond Peterson, President First National Bank, Paterson, N. J.

Fifth Federal Reserve District—James D. Harrison, Vice-President First National Bank, Baltimore, Md.

Seventh Federal Reserve District—John J. Anton, Vice-President First National Bank, Chicago, Ill.

Twelfth Federal Reserve District—O. A. Houglum, Vice-President First National Bank, Eugene, Ore.

[The reported was duly adopted and the officers installed.]

STATE BANK DIVISION

AMERICAN BANKERS ASSOCIATION

Twenty-Third Annual Meeting, Held at Seattle, Wash., Sept. 25, 1939

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What Profiteth It a Nation?

By Wood Netherland, Vice-President Mercantile-Commerce Bank & Trust Co., St. Louis, Mo.

In view of certain economic situations in the world and political situations, I have taken the liberty of departing from the usual custom to speak to you briefly with respect to the political philosophy of our time.

Humanity is on the move. It is one of those great periods in history. . . . When the pages of history have been written with respect to this age, no doubt it will be as important as the Dark Ages, followed, we hope, by the Renaissance. Certainly people are as emotional now as they were when the great Crusades were made. We have dictatorships all over the world; religion banished from many countries. Certainly, in Europe, the Four Horsemen of the Apocalypse ride again. Once more, back and forth across those plains that have known so much bloodshed, swings the long engaging scythe of death—only this time with increased tempo, and with much more effective instruments of destruction. The culture of the ages is in danger. Civilization itself seems to be tottering.

Again tens of thousands of the flower of youth, friend and foe alike, are blended in one great red burial. Little children, whose pinched faces blanch at the road of new monsters of the air, are scuttled into underground holes like so many rats. Behold man at his worst!

Surely He who wept over the city of Jerusalem must now be bowed down in grief.

As we stand helpless and aghast, and contemplate the destruction that may be wrought before the world concludes this struggle and current civilization lies desolate and prostrate from its effects, we somehow sense its utter uselessness.

With our progress in science and invention, with a productive plant capable of supplying an abundance of life and happiness to every family on the globe, we grow sick at the thought that the strife which now engulfs the world may end in such a crucifixion of mankind that the resurrection may be a matter of centuries.

Faced with such an imponderable, and seeking to grope our way out of the depths that threaten us, would it not be well to recheck our figures, to retrace our steps, to examine the route along which we have come, to re-read the markers past which we have driven too fast, so that if possible we may discover how, when and where we have lost our way?

So it is, in a spirit of reason and logic, that I am attempting now to go back to origins to find some light on the question, if I can, as to why man, conscious of the oneness of the human race, even after centuries of experience and the lessons of history, seems unable to work out and accept either a moral or legal code which will enable him to enjoy in peace that abundance of life which is so freely at his disposal.

Currently we hear much of Nazism and Communism, supposed to be new and opposing ideologies which offer a complete solution to the manifold difficulties that confront the human race. As a matter of fact, both are no more or no less than the modern version of an ancient doctrine advocated by many philosophers, including Spinoza, Bentham, and especially the German philosopher, George Friedrich Hegel, over a hundred years ago. His philosophy was but a restatement of the doctrine of absolute and supreme power of the State over the individual, as opposed to the democratic theory that man is older than the State and possesses certain personal or inalienable rights as so forcibly stated in the Declaration of Independence by the American colonies.

According to Hegel, the State is an impersonal supreme being, possessing absolute power. It is the highest form of the universal reason and will, and all dutiful citizens must live and act according to its needs and demands. Hegel says: "The State is the realized ethical idea or ethical spirit. It is the objective spirit, and the individual has his real existence and ethical status only in being a member of it." In short, the individual has no rights whatever, even the right to live, unless the State so decrees. Thus it may be observed that the present National Socialist regime in Germany presents nothing essentially new in so far as this brand of philosophy is concerned, but represents a social theory that appears to be inherent in the German nation. Obviously such a doctrine opens the door to absolutism and tyranny, cuts its people off from any right of appeal, and deprecates the value of human life. The full answer to such a doctrine is found in the famous encyclical letter on the reconstruction of the social order by the late Pope Pius XI, whose whole life was devoted to the uplifting of the proletariat, and who yet had a fine conception of the necessity for harmony among all ranks in the social order. Keenly conscious of the obligation of men of wealth toward society, especially as regards their superfluous income, he nevertheless strongly condemned the contention of socialists that economic production must necessarily be carried on collectively. "Society, therefore," he said "as the Socialist conceives it, is on the one hand impossible and unthinkable without the use of compulsion of the most excessive kind, on the other it fosters a false liberty, since in such a scheme no place is found for true social authority."

As opposed to the theory of absolutism is the doctrine embraced by most civilized nations, democracies in particular, that the individual possesses certain rights that cannot be surrendered at all, even to his own government. These are called inalienable because they cannot be taken away from the individual without doing violence to his personality. They include the right to live, the right of self-defense, and religious liberty. From this point of view a human being is valuable for himself apart from any other human being or the State itself. In a democracy, "a human being retains his value because it is intrinsic to him." The reason . . . is to be sought in certain inner endowments. . . . These endowments are the powers of intelligence and free choice. They are the endowments of a human person, whose principal element is a spiritual soul.

"The powers of intelligence and freedom of choice are possessed by man alone, and are not found in any being in the world outside of man. These possessions invest man with the quality of intrinsic value. By means of them he is enabled to act intelligently and freely in deciding between right and wrong. Obviously, he could not merit happiness if he did not understand what he was doing, or if he were not free in his actions. Because of his intrinsic value, every person possesses the quality of inviolability. This quality forbids others to harm or injure his person in any way."

Wars will not cease until governments acknowledge and respect the inviolable nature of the individual, whether he be friend or foe. There exists no moral law under high heaven which gives a nation the right to take human life of other nationals for material considerations.

Now, the transition from a form of government which confines its prerogatives to the protection of these rights to a form of government which imposes a planned economy on its nationals may be quite as unnoticeable as it is insidious. Although at its climax it may break forth in the form of revolution, it is brought about often with the full, though unwitting, cooperation of the people themselves. It has its genesis usually in the necessity of some economic crisis within the State, or by the fear of war from without. In either case, realizing that prompt action is necessary against a common foe, citizens of a democracy intrust their leaders with certain emergency powers "to provide for the common defense"—and thus in a spirit of patriotism voluntarily forego rights which under normal circumstances they reserve sacredly unto themselves. At the time of this foregoing there is no thought of giving up inherent natural rights indefinitely, but usually, to use the stock phrase, it is "for the duration of the emergency." The grave danger of this departure from these basic tenets of a free people is that either the laws voted in an emergency are seldom repealed, or the period of the emergency is so prolonged that the restrictions which tend to stifle fundamental rights become a permanent and accepted part of our political economy. This unfortunately provides legal processes whereby an ambitious Administration actually may vest in itself certain dictatorial powers which the electorate never intended should be lodged permanently in any one branch of the Government.

Moreover, the regimentation to which we have been subjected in the past few years arises from the idea just mentioned as to the divine right of the State, which theory, it seems, unfortunately must be tried and disproved at frequent intervals in the history of nations. This condition invariably has for its basis the concept of reformers, who would have us believe that government should occupy not only the position of arbiter or umpire, but also should enter into the game as quarterback. This is graphically illustrated by the National Labor Relations Board, which becomes prosecutor as well as judge and jury. Such a government, impressed with its own omniscience, becomes intolerant and vindictive, and all too often must use force to impose its will upon its citizens—and gradually its people pass from the status of free men to that of slaves.

A president, legislator, or government bureau executive is, after all, merely a human being like his fellow men. Of himself, he has no right to oblige others to do things which they prefer not to do. All human beings are essentially equal, for each has the same intrinsic worth and importance as every other. Hence a public official, in his personal capacity, has no right to bind the wills of his fellow men, and can do so only as they have, through statute, clearly and unmistakably given him the official right to do. Under our concept of government, where this right is not positively and affirmatively given, such a right is specifically reserved either to the individual or to the several States. The manner of administration of the National Labor Relations Act presents a dangerous threat to freedom of contract, any in my judgment will in the end prove to be unworkable. Its machinery is too intricate, too detailed, and will never prove an effective substitute for tolerance and understanding between employers and employees. Morality cannot be established by government fiat.

This is not to say that the State should not be concerned with respect to the economic welfare of all its citizens, particularly the low income groups, nor to say that capital should be permitted to reduce labor to a condition of economic servitude. The story of the factory women and children of the first dark days of the industrial revolution pictures a situation which should be avoided now—machines had been perfected, steam had come in, coal was at a premium, hand labor was doomed and hand laborers were starving. No regulation of labor, no protection, no homes prepared, no concern for physical or spiritual welfare. Children worked from six in the morning to seven at night. A generation of factory women grew up who had never been in a home, could not cook, sew, or keep clean. The bodies of the poor were exploited for dividends without regard to the future. Time and education have cured much of this, as has the formation of labor unions capable of collective bargaining, so every government, whatever its form, is to be regarded as an agency to supplement the efforts of its citizens. If a government attempts to do more than supplement or assist, and assumes to do for its citizens what they themselves could do better, it becomes paternalistic and stifles natural initiative, the life-blood of national welfare. If a government does less than supplement or assist, and shows itself indifferent to injustice or oppression, it opens the door to anarchy and its own destruction.

I have tried here to suggest the line of demarcation between personal liberties and civil liberties, in the full realization that this line of demarcation is an intangible and abstract boundary which changes constantly with progress. But America in its beginning instituted a system of checks and balances designed to redefine this boundary from time to time, in so far as it is humanly possible to do, and he who would destroy this system, however cumbersome it may be, strikes at the heart of this republic. That is the danger inherent in any proposal that the executive, legislative, or judicial branch of our Government has an undue influence on either or both of the other branches. That is the danger inherent in any proposal that States shall continue to yield their sovereignty to the Federal Government. That is the compelling reason why the American dual banking system must be preserved lest there be a further creation of instruments of power in Washington, and the ultimate end of State autonomy, toward which we are drifting slowly but surely.

Since the advent of the Federal Reserve System and the Federal Deposit Insurance Corporation some State Banking Departments have surrendered their independence of thought and action. Let, so long as both the State and National banking systems exist, they serve as a check on each other and at the same time cooperate in their work. Grant, for the sake of argument, that we might have a more economical and efficient banking system by consolidating all supervisory and regulatory authority in one agency, we would provide the most powerful weapon for economic and political control that can possibly be imagined. While the FDIC machinery is a step in the direction of concentrated power, yet so far it has been splendidly managed and, so long as a bank may, if it meets certain requirements, convert from the State to the National system, and vice versa, and membership in the Federal Reserve System is voluntary for State banks, a measure of checks and balances is maintained. What little is left certainly should be preserved.

I have said that the transition from a form of government which limits its interference with private initiative, to one which dictates a planned economy, often steals upon us ere we are aware. You are too familiar with the history of our past few years for me to detail the various specific measures that have been enacted which have tended to weaken gradually States rights and lodge more and more power in our National Government, nor can anyone fail to note the proportions to which the power of the executive branch of the Government has expanded, while that of both the legislative and judicial branches has declined. This does not augur well. Its repercussions have been somewhat mitigated by the prodigious and lavish expenditure of money from the public treasury, and yet we found ourselves this spring with more unemployed than we had in 1932, and facing a debt of $44,500,000,000 by the end of the fiscal year of 1940—with an annual interest charge, even at low rates, of over $1,000,000,000. This one item is more than three times the amount of the entire cost of the annual budget in the Administration of President McKinley. Some four to six million people are directly or indirectly indebted to the Federal Government through its labyrinth of leading agencies. Thus either through legal or economic means the Federal Government becomes more and more dominating.

Nor am I one of those who believe that all of the blame for our difficulties attaches to those in high places, for in a democracy at least leaders are usually responsive to popular demands. But the fault, it seems to me, lies with the average citizen who has forgotten, or who has not yet learned to think in terms of the general welfare. No better proof of this could be manifested than the attitude almost generally shown in our country with respect to the so-called recovery measures which have been initiated during the past seven years. While holding to the view that indiscriminate spending and large deficits are both dangerous and ineffective—a view now substantially proven by experience—most of us have at one time or another joined pressure groups in demanding of the Administration local expenditures or costly activities which only added to the mounting debt we so bitterly assailed at the same time.

A favorite news release, and unfortunately a most effective one by a member of Congress standing for reelection, is a recapitulation of the expenditures which the Federal Government has made in his district, and a favorable comparison of them with the amount of taxes collected therein. I do not need to enumerate to you the many instances wherein the citizens of this country have either supported, or have been adamant with respect to unwise and fantastic proposals simply because they themselves were the beneficiaries. As one member of Congress so aptly suggested, what we need, and what we must have if we are to retrieve our position, is representatives in Congress who can think in terms of "my country" rather than in terms of "my district," and constituents who will approve their stand. Moral rearmament cannot begin at the top. It must first find its place in the heart of the individual citizen.

Illustrative of what I mean, I often recall a visit I had at the close of the last war with my good friend the late Senator Joe Robinson, who unfortunately like the rest of us some years later became charmed with the emotions and largess of the New Deal. After a separation of some two years, during a part of which I had been completely out of touch with what was going on in this country, I called to pay my respects as we were then both citizens of the same State. During the conversation I shared with him the pride he evidenced as he old me of the sacrifices and self-denials Arkansas had made during the war in the conservation of sugar, flour, and other commodities called for by the Food Administrator, and other economies the State had practised in order to help carry through in the emergency. Other States showed a similar spirit of self-denial. This was then the badge of honor, and I say to you that when the time comes that we can revive that which is the soul of America, think a little more about our duty and what sacrifices we as citizens can make for the sake of national recovery, rather than what we can get from the national Treasury while recovery is being attempted, then we will begin to construct a way out of this confusion and avoid this unmistakable trend toward concentration of power before it is too late.

I have also said that the transition from a democratic form of government to one which dictates a planned economy, usually makes its greatest strides during periods of national emergency. A pertinent case in point is the necessity for national unity now confronting us as a result of the war in Europe. No one of us desires to criticize or to hamper the President unduly in discharging the tremendous responsibilities that are his in this difficult and critical situation, and thus normally all would be quite willing to forego many of our personal rights in the interest of collective defense and security. We would be less than frank, however, if we failed to say that the complete confidence which should obtain in such a situation does not now exist. It will be difficult for those substantial elements of our population who have been the victims of Mr. Roosevelt's bludgeoning, and on whom he must now rely for assistance, to trust him implicitly with sufficient power to deal with the critical issues that now confront him. Because of his record he is now faced with the necessity of convincing a large segment of the population that such additional powers as may be granted him will not be abused, and that these powers will not be permanently appropriated after the emergency has passed. Only time and Mr. Roosevelt himself can create an atmosphere of confidence so necessary to the best interests of the United States in the present condition of world affairs.

It seems to me we have gone a long way on this transition from our original conception of a free government to one which dictates a planned economy, and that it is high time we pull over to the side of the road, shut off the engine for a while, and have a look at our compass. I feel confident that the appalling tragedy in other lands will bring us back to our senses and draw us closer together than we have been for a decade. If, as one writer has suggested, the Angel of Humility will but wing his way through the White House and bring the realization that no one has a monopoly on patriotism in this country, "the moral and political atmosphere in the United States would be instantly transformed. There would come to the people a feeling of confidence altogether lacking today, and they would face the future without anxiety, in a calm spirit and cool courage." I have the feeling that the recalcitrant members of Congress who declined to repeal the neutrality legislation at the last session did so not because they objected so much to the repeal itself, but because they have reached the end of their tether in risking the dangers of a one-man government. If this be true, it is a happy omen, for whatever may be the emergency, there is none so important that it justifies further trends in the direction of autocratic power.

As other men have emotional experiences, so I have mine, and not the least of these occur at times when I am privileged to visit the city of Washington. It is always an inspiration to stand for a few moments in silence beside the tomb of the unknown soldier at Arlington. From there I like to return to a spot some hundred yards from the Capitol and observe Crawford's statue of Freedom, which mounts the dome of the building. As I stand there in reverie, I am oblivious to all about me, and through the mist before my eyes the events of our history pass in review. It is not the great figures in our national life that I see, but rather visions of my forebears, simple folk who led unostentatious lives and were motivated by love of country. I see them with Washington at Yorktown, with Grant and Lee at Appomottox. They were silent companions in that somewhat nebulous late venture to make the world safe for democracy. Unconsciously, almost audibly, I murmur, "That is my own, my native land," and as I go from that spot a voice invariably leaves with me the words of a great thinker, which I would like to leave with you:

> Freedom has a thousand charms to show,
> Which slaves, howe'er contented, never know.

Some Constructive Worrying

By R. E. Gormley, Superintendent of Banks, Atlanta, Ga.

I have been requested to talk to you on banking as viewed from the outside, or as affected by outside influences.

I accepted this assignment with some hesitation for the reason that I regard myself as being primarily too much a banker to present properly the viewpoint of an outsider.

I recognize, however, that a lack of knowledge of the purposes and functions of banks, together with certain other factors, largely governmental, which have developed within recent years, threatens to warp if not actually destroy the American system of banking as we have known it.

Without boring you with even a summary history of banking, and of the grief which has befallen us, we find ourselves at the present time in this position: In a land of plenty, with unmeasured natural resources, with a plethora of agricultural and manufactured products, with an amount of available credit at an all-time high, and, at least as far as banks are concerned, with a profit position which might be worse, we have an economic system apparently badly out of kilter, and there is a great deal of dissatisfaction and unrest in the land.

Whether these conditions can be attributed to the type of banking which has served the American people, whether conditions would have been different had banking resources been controlled by a few large groups, as advocates of multiple banking contend, or whether the trend would have varied greatly under a system of Government-owned banks, or banks the control of which was dominated by the Government as the present trend seems to be, are questions which, with your permission, I shall discuss briefly, though necessarily somewhat abstractly.

Now, in regard to multiple banking, we have had branch banking with us for a number of years, and it has, I believe, increased recently. Its record of accomplishment does not serve to offer a solution to our economic ills. I do not believe the American people, accustomed to social and economic liberty, will accept a system of banking contrary to the very plan on which this Government was founded, one which permits of absentee control and the monopolization of a factor so vital to our financial welfare. Yet there are powerful influences at work undertaking to overcome public opposition to such a system. Even now there is under way a study by the American Economist Council for the study of branch banking, its stated purpose the dissemination of information about branch banking. It is interesting to note that the Chairman of this Council, in addition to being a professor in one of the leading universities, is also economic adviser to Bank of America N. T. & S. A. of California. It does not take a seer to prophesy to the nature of propaganda which will be disseminated by this Council. It will be interesting to learn just how they propose branch banking will cure our economic and business ailments.

It is rather difficult at the present time to foresee a possibility of the Federal Government's commandeering all banking. Certainly such a possibility seems remote, unless there should occur another breakdown of private banking—the possibility of which seems equally remote.

Yet we have noted an increasing disposition on the part of our legislative forces to create additional factors competitive to private banking, and to increase the powers of such factors already established.

It is seemingly inconsistent that under a condition which, according to your political affiliations, you may designate as an over-supply of credit, or a subnormal demand for loans, that some of our legislative forces and at least one of the Federal agencies, should be critical of banks for their failure to make loans, when at the same time there is a hue and cry from two of the Federal examining agencies for standardization of examining practices and uniformity of method of valuing assets, with the policy of at least one of these agencies, as well as the minds of its examiners, becoming so mechanicalized, it would seem their purpose to occupy a position more managerial than supervisory.

It is not difficult to understand the purpose which motivates our legislative forces. There is a demand from a large number of individuals for freer credit as a means to easier money, and from business men for a more liberal spending power. It is in answer to these popular demands that politicians are seeking the establishment of additional credit agencies and a liberalization of the loan policy of those already established.

We as bankers realize we can only afford to make such loans as will be repaid. When we consider that loans are generally repaid from earnings and that such repayments, whether made by the individual borrower or through a form of loan insurance provided by the Government, can only have the effect of reducing spending power in the future, we cannot but question the soundness of a loan policy for the purpose of creating spending power, rather than for legitimate production.

Granting it possible, it might be a fine thing if we could develop a control which would assure economic stability—an intricate system of checks and balances, magnificently geared to operate in response to a lever pushed or pulled in Washington, which would result in uniform prices, production to take care of unemployment, and the necessary demand to absorb such production.

The Federal Reserve System, with its extraordinary powers over banking and money, has unquestionably been a stabilizing influence. Yet in spite of the facile system of currency which it has provided; its power to expand and contract credit through open market operations by discounting and by raising and lowering reserve requirements; its influence over capital funds and speculatino by reason of its control over margin requirements, business conditions continue to fluctuate, prices rise and fall, and booms and depressions come and go in pretty much the same cycles as in the old order.

It has been suggested the Board of Governors of the Federal Reserve System has been hampered in its efforts to further economic stability by restrictive examination policies, and that examination and investment policies should be more closely allied with monetary control.

While there may be some merit to the criticism that examining policies of certain agencies are too restrictive and that certain classes of banks are being unduly badgered and harassed by such policies, I regard it dangerous for examination and investment policies to be made a part of monetary control.

Personally I have reached this conclusion: The advocates of a so-called managed economy have reckoned without certain phases of human nature, which are as old as the hills and which will continue to exist until the end of time. At best the most we can hope to do is to administer purgatives and sedatives to business. Basic conditions will continue to be governed by fundamental laws over which we have no control.

Now, on the question of bank examinations: I think that all supervisors had just as well come to a material realization of a fact which we all admit, but which we don't all practice, and that is that we cannot manage or direct the operation of the banks of this country; that as long as we have privately-owned banks (which I hope will be always) we cannot accomplish uniformity of management. I have never been able to get two or more bankers to see everything through the same hole in the wall. This very diversity of management has, in my opinion, made for that latitude in credit which has been responsible for the rapid development of this country and which is so necessary to our business life.

The hue and cry which has been raised by some of the Federal agencies for uniform examination policies, standardization of forms, &c., and which has been taken up by some of our State Supervisors, can only result in one thing, and that is the elimination or shelving of State Banking Departments. What will be the purpose of the several States continuing to make examinations, call for reports of condition, &c., if we are to accept forms devised by the Federal agencies (which they admit are not perfect), and if we are to permit our minds to become so dominated that our thoughts and ideas as to examination policies, methods of valuing assets, &c., are attuned to the beat of a pendulum, the stroke of which is controlled in Washington?

There are peculiar factors and conditions pertinent to the operation of banks in Montana which do not apply in Georgia. Likewise, similar variations exist, even within separate States. A supervisory policy which undertakes to enforce uniform regulations, without regard to peculiar local circumstances, in large banks as well as in small, in banks located in agricultural sections as in banks located in industrial centers, cannot but hamper their operation and curtail the service which they have customarily rendered.

It is true that there are certain basic principles which all supervisors should recognize and enforce. And, after all, it is only these basic principles we, as Supervisors, can hope to enforce. The responsibility of determining loan policies, soundness of investments, &c., must necessarily rest with the management of the bank.

I tell you, gentlemen, if you permit your State Banking Departments to be eliminated or their authority to become subrogated or overshadowed by that of any Federal agency, you have gone a long way towards accomplishing centralization of banking, with its accompanying possibility of monopolization of credit control or the abuse of such control for political purposes.

This brings us to the question of centralization, or a unified banking system.

For approximately 75 years this country has been served by a dual system of banks, State and National. I believe I may add it has been well served. The creation of the National system led to the development of a school of thought in banking, advocating the conversion of all banks into National banks. This sentiment for a unified system has gained and waned successively through the years. Advocates of retention of control of State banks by the separate States have remained consistently in the majority, and the number of State banks has at all times exceeded that of Nationals. The course of operation of the two systmes has pretty much paralleled each other. At the present time, I would say, the possibility of nationalizing all banks, as such, is farther away than at any time in the past quarter century.

In passing, and as an advocate of State banking, I would like to say I have the greatest respect for the Comptroller's office, and I am for it 100%. It has gained a wealth of experience by reason of its 75 years of existence. It is a well-seasoned and efficient department. While it may have dabbled in politics from time to time, as we State Supervisors sometimes do, it has in the main kept remarkably free from political influences. To transfer its function to or merge its independence in some other newly-created agency, or agency whose then dual functions would be at cross purposes, would, in my opinion, be detrimental to the service which National banks render.

In the operation of the Federal Reserve System, with its functions, as its name implies, to hold reserves of member banks, to provide an elastic currency, and to exercise supervision over member banks, &c., advocates of centralization saw an opportunity to accomplish Federal control over substantially all banks. In its 25 years of existence only a comparatively few State banks have deemed it advantageous to become members. To the contrary, smaller banks in a number of States have regarded membership in the System a disadvantage.

Yet I have a most wholesome regard for the system and what it has accomplished. The relations between my department and the Federal Reserve Bank of our district are and have been all that I could ask. I would say the Federal Reserve System has justified its creation many times over.

As a result of disturbed conditions and as an aftermath of the banking holiday, another factor entered into banking. The National Congress created the Federal Deposit Insurance Corporation.

Deposit insurance was not a new thing, but had been attempted by various banking groups and by several States. In each instance it had proved unworkable, and the idea was generally regarded by bankers as impracticable. With the prestige of the Federal Government and its seemingly superior capitalization, contributed by the Federal Treasury and the Federal Reserve banks behind it, it has impressed even a large number of bankers. Its present plan of insuring deposit accounts up to $5,000, while of no direct consequence to larger banks, has had the effect of placing smaller banks on a better competitive basis with larger banks. There is no question but that it has been a stabilizing influence.

Yet in the creation of FDIC, with the extraordinary powers vested in its Board of Directors, together with the popular appeal which the idea of deposit insurance has (and there is no question but that it has), I see the only means of ever accomplishing a unified banking system.

My conception of the purpose of FDIC, and I believe the intent of its original advocates, was that it should function as an insurance agency and not in a supervisory capacity. I do not believe we can expect banks to function to meet the needs of American business, as they have in the past, with supervisory control vested in an organization whose primary concern will be its hazard as guarantor, rather than the efficient operation of banks.

Title I of the Banking Act of 1935 vests in the Board of Directors of FDIC the power to make such rules and regulations as they see fit; the right not only to make examinations and cancel the insurance of any bank, but also to issue call for reports of conditions and to require publication of same, to assess fines and penalties, and, in the event of failure of any bank, to comply with any direction given by the Corporation, to publish any or all portions of reports of examinations and of correspondence between the Corporation and such bank.

Thus we see an insurance agency vested with the unusual authority to make such rules and regulations governing the operation of banks as it may see fit; the power to enforce such regulations with punitive provisions, such as fines, penalties, imprisonment of officers, and threats to crucify any bank in the eyes of its depositors by advertising unfavorable information.

The authority of State Supervisors has been subrogated to or is in conflict with that of the FDIC. In numerous instances its examiners have been kind enough to undertake to relieve me of the responsibility of enforcing provisions of our State banking law—and in cases where such violations admittedly created no condition of hazard to the Corporation.

A great deal of pressure has been brought to bear to accomplish the adoption of a uniform examination form, and the acceptance of FDIC reports in lieu of examination by State Departments. I know of no surer way to accomplish centralization of banking. If we surrender our individuality to the extent of relinquishing our right to devise forms and supervisory practices best suited to the needs of our respective States, what will be the purpose in retaining State Banking Departments? Without enforcement authority vested in someone in the State, what will be the purpose of State banking laws? What kind of State banking system will you have?

Now, I have no fuss with the gentlemen in charge of formulating and enforcing the policies of the Corporation. I am personally acquainted with most of them and count them my friends. It has been a source of some satisfaction to me to hear, within the past year, several of these men declare in favor of a dual system. Yet I can't help but remember that the Chairman of the Corporation is on record in testifying before the Senate Banking and Currency Committee on the Banking Act of 1935 as being in favor of centralized control of banking, and stating he did not believe bank losses could ever be eliminated until we had a unified banking system.

I am wondering whether the dual system to which he refers as favoring is not a system of National, State, and State member banks, the primary or sole supervisory control over which shall be vested in the FDIC.

I am personally very much interested in the FDIC and its success as an insurer. I am opposed to increasing the Corporation's potential liability by raising the maximum coverage. I am opposed to decreasing the Corporation's income by lowering the present premium charge, though I recognize the present method of assessing premium cost to be unfair to large banks. In short, I want to see this thing given a fair trial. The only question between the FDIC officials and myself is just what kind of a dual system do they favor?

I was frankly amazed at the apparent apathy with which State bankers accepted the provisions of Title I of the Banking Act of 1935, yet looking back at the disturbed conditions through which we had passed, and the uncertainty as to the extent to which Government would go in undertaking to control business, and especially banking, it is not difficult to understand their failure to protest more vigorously.

Which brings to mind this: The reason, in my opinion, for the unholy fear which bankers and business have of government is that business has paid too little attention to government in the past. Of course, I realize that as our population increases and the country becomes more congested we must naturally expect more regimentation, as the cattle, which formerly roamed the Western plains in all the glory of their long horns, as their number increased were forced to surrender their most cherished natural possession, even to the extent of being behorned.

Now I sincerely trust we will not permit ourselves to be completely dehorned; that at most we will only suffer knobs to be placed on our antlers, so that we may still butt with some authority. And please keep this is mind: There is no other class of people with the potential influence of bankers.

Econimists will tell you that the trend of population is towards larger industrial centers and that the day of the country bank is numbered. This concentration has, in my opinion, been a potent factor in our persent unsatisfactory economic situation and the seemingly unsolvable condition of unemployment. Economic laws will force an adjustment of these concentrations. There will never come a time when you can't sell credit, even in the more remote sections. The independent, privately-ownd bank is worth fighting for. If the bankers of this country will get their heads out of the trough and look forward, take time out to study and analyze legislation and Government policies—certainly those which may affect their business—exercise and coordinate the influence which is theirs, a vast influence can be wielded on Government policies in the future—certainly on those related to business.

I believe the time will come again when banking will be done on a basis of personal confidence. I am probably one of the few who believes the course of banking since the holiday would not have varied greatly regardless of deposit insurance, preferred stock, or other Government assistance and control. I like to believe the bankers of today are capable of operating their banks in a manner to warrant public confidence. I believe that with the assistance which we supervisors can lend in guarding against an overcrowded field by not permitting the creation of banks which are economically unsound, and for which there is not a permanent, profitable operating basis, we can maintain a banking system which will withstand the ravages of time. It seems to me there is a great deal more at stake than just the matter of your jobs, your investments, and your life's work. In protecting an independent dual system of banking you are maintaining what I believe to be the greatest single factor in assuring the liberty of a democratic people.

Now some of you may have begun to wonder where the connection lies between the thread of my talk and the title chosen, "Constructive Worrying."

I have been charged by some of those connected with the Federal agencies with being narrow in my views; that I do not have the broad, general outlook which they have. In short, I am provincial—for which I am thankful.

In turn, some of my fellow Supervisors accuse me of being an alarmist, say that I shy at imaginary "boogies," and that I worry too much about things which are of no consequence.

COMMITTEE AND OFFICERS' REPORTS—STATE BANK DIVISION

Address of the President, Henry W. Koeneke, President, Security Bank of Ponca City, Ponca City, Oklahoma

Independent Banks Meet Public's Banking Needs

This is our annual round-up. Ten months ago we gathered in Houston, Tex. At that meeting you honored me with the Presidency of your Division. You bestowed a great honor upon me and gave me an opportunity for useful service and pleasant association that have been among the outstanding experiences of my lifetime. Each administration has built upon the experience and achievements of its predecessors. So have we. The administration now closing has attempted to carry forward the tradition, service, and principles of the Division, adding something original of its own. If the Division has been strengthened in some degree because of our service, that contribution will be or own reward.

The program for the year ended today was set forth in a statement of principles adopted at our Houston meeting. Your officers and Executive Committee have sincerely endeavored to carry it out.

Throughout the year we have tried to maintain close contact with our Division's State Vice-Presidents in each State, keeping them informed of our activitities and seeking their advice and guidance. We plan while we are here, to hold a joint meeting of State Vice-Presidents and our Executive Committee for an intimate exchange of ideas and for the planning of a future program. This increased mutual assistance has been one of the significant developments of the Division's year. Our Division is the machinery through which the State chartered banks express themselves and it is appropriate for them to do so through their representatives, the State Vice-Presidents, in our councils.

Your Committee on Federal Legislation has been most effective this year. It can point to one great achievement alone which justifies its existence and your support. Under its leadership the compulsory Federal Reserve membership provided in the Banking Act of 1935 for banks with deposits of $1,000,000 or more was repealed.

This effort on our part and this step taken by Congress and the President is in keeping with the spirit of the dual system of banking and the original conception of the act creating the Federal Reserve System as a voluntary federation of regional Federal Reserve systems coordinated through the Federal Reserve Board.

We cannot look with favor upon the current efforts to centralize control of the banking system. The establishment of the 12 Federal Reserve banks was the culmination of an historic struggle between two schools of thought dating back to the establishment of the first bank in the United States in 1791. This struggle continued right up to the time of the debates over the Reserve system under the Wilson Administration. The triumph of the conception of a federation of 12 central banking systems was a recognition of the diversified nature of American economic fabric and a reflection of the most fundamental characteristic of American life which is local, regional, economic, and social development.

Compulsory Federal Reserve membership and current efforts to center financial control in Washington represent an attempt to undo and reverse the principle that has prevailed through 150 years of struggle.

Such a centralization cannot be justified by a "horse and buggy" allusion to the past. America did not grow up in Washington or Wall Street or any other single city. America grew up in the Northeast, in the Southeast, in the Middlewest, in the Northwest, and the Southwest. Each section developed its own economy and habits, its social life and customs, even its own accent and sometimes its own vocabulary. Each contributed its strength to the Nation. It is a new idea that each must depend for its strength on Washington.

We expected to be able to report success to you in our efforts to have extended the time limit of the Clayton Act amendment prohibiting directors from serving on the boards of two banks. While both houses of Congress passed the extension, the President vetoed it.

Of greater legislative concern to us, however, was the Mead Bill, providing for insured loans to business and supplementary proposals to establish government banks. The alleged purpose of the Mead Bill was to make low-rate loans available to marginal business enterprises in competition with better established and better managed enterprises. A great barrage of publicity was released in support of this project. The Association made an effective presentation of constructive information at hearings on this measure, in which your President had a part. While this measure was defeated we may expect its reappearance in some form at the next session of Congress.

A great onslaught was made on the banking system this past year under the guise of efforts to provide credit and capital not available through the normal channels. The proposal for insured loans was but a small phase. A larger objective seems to have been the establishment of a system of Government banks. Government witnesses appeared before Congressional committees with a new theory.

Briefly, the theory held that the country had achieved economic maturity, that there no longer is room for great industrial development and expansion, that industry no longer offers opportunity for investment. Therefore, capital is not being invested and the economic machine is slowed down. Hence the Government should undertake to assure economic activity by taking savings and investment capital and investing it in industry and public works. Thus would discredited pump priming be made permanent.

It was confessed by one Government official that under this program the Government would ultimately come to own most of the productive units of the country. That means the end of free enterprise.

Under the Wagner resolution passed by the Senate, hearings will be scheduled on the entire banking set-up. There is no doubt but what a challenge will be made against the dual system of banking, seeking exclusive Federal control. These hearings are expected to get under way sometime during the month of October. This Division must consolidate its efforts and be prepared to present factual information to this committee.

One can readily see that socialized lending can easily stifle private enterprise. I am sure that the American people are not ready for this.

One of the leading daily papers of Oklahoma recently had an editorial which illustrates the viewpoint of some of the thinking American business men, which is as follows:

"*Two Sure Signs*—Until there is more demand for money, all persons may be sure that recovery is not here, although they may hope that it is on the way. Today money is going begging. Banks continue to remain full with but little demand aside from routine financing. Interest rates are low for all types of loans, especially low for those favorably secured. From the viewpoint of money, there probably never was a time in the country's history of pay investments when financing was easier. But few persons are asking for loans.

"When one borrows money, he not only must make enough to pay back interest and principal, but also give him whatever profit he is entitled to make. The only inducement to borrow beyond actual needs is the profit motive. When that is absent, people just don't borrow, and it is apparent that the profit motive is lacking now and has been for a number of years. It is possible that the cracking down one hears so much about from Washington and the growing burden of taxes have something to do with diminishing profits.

"The American people are individualists, full of initiative, willing to adventure. Is our initiative killed? Have we lost our confidence to see a thing through successfully? Are we lacking in courage and the spirit of adventure as applied to business? We believe not but must admit that for some reason we have been greatly subdued.

"There are two sure signs that business is picking up, that recovery is on the way. These are when interest rates begin to increase and loans to pick up. One may then know that business men are regaining confidence in themselves and in the country. When this occurs we shall be catching up with that corner which we have been trying to turn since the depression hit."

Our Committee on State Legislation has actively cooperated with the American Bankers Association's Committee on State Legislation and has supplied all officers, members of the Executive Committee, and the State Vice-Presidents of the Division with copies of the 1937 program of State legislation, together with the 1939 supplement which provides the following recommendations:

(1) Uniform principal and income Act.
(2) Holiday bank transaction statute.
(3) Model banking board statute.
(4) Model bank chartering statute.
(5) Model bank employees bonding statute.
(6) Reporting violations of banking law.

Their continued cooperation with the State Secretaries Section made it possible to keep the States informed through the secretaries of the various associations as to what bills were being introduced in other States.

Our Committee on State Banking Departments is directing its attention toward the greatest possible degree of cooperation with the supervisors of State banking departments in the 48 States. The commiteee's purpose is to strengthen the State banking system through close contact with State bank supervisors, and to unite with them in achieving the chief objectives for the betterment of State banks.

For many years, at five-year intervals, the Division has conducted its survey of the status of State bank supervision as a means of determining the progress made in improving the state of State bank supervisors in the various States. The material for their survey, which includes information on qualifications, appointments, term of office, salaries and duties of commissioners, banking boards, bank examiners, desired bank legislation, chartering banks, liquidation of banks, is obtained from the State bank commissioners. These five-year surveys have been compiled and codified so as to permit comparison between States and to show progress that is being made throughout the country as a whole in State bank supervision. The fourth such survey is being made and will soon be ready for distribution. It will be found exceptionally valuable by legislative committees in the respective States in recodifying their State laws.

Our Committee on State Bank Research has gathered and compiled valuable statistical data of State charted banks in the 48 States and the eighth annual survey of resources and liabilities and the fifth annual survey of earnings and expenses of State supervised banks have been published. If you will take the time to study this report, you will be well repaid.

The Committee on Public Relations of the State Bank Division has cooperated with the Public Relations Council of the A. B. A., in the distribution and use of the valuable information contained in the talks which have been and are being prepared by the Public Relations Council for use of bankers and others in addressing public gatherings, in an effort to bring about a better understanding of banking by the public.

In dealing with this issue, we must always act from the public interest standpoint. The independent credit system will not survive if we defend it only from a selfish point of view. The future of independent banking rests in the last analysis on the degree to which we serve the public. But defense of the independent credit system does require a united front. This is no time to revive intra-family quarrels. The waters are muddied enough. Besides, a great war is in progress which tends to obscure issues and may bring new difficulties to us.

In these circumstances it is unfortunate that one segment of the banking business should reopen the branch banking issue. At the moment a highly publicized campaign is being carried on for the extension of branch banking by a group of university economists whose letterhead indicates affiliation with the branch banking interests.

In any such campaign, we believe motives should be clearly stated. We should like to see our branch banking contemporaries in the West state clearly their relation, if any, to this campaign. Likewise, we should like to see the economists state clearly the nature and purpose of their relationship, if any, to the branch banking interests.

But whether they do this or not we regard centralized control of banking as opposed to the democratic American way of locally owned and managed credit institutions.

The State Bank Division stands on this question as it did two years ago when the American Bankers Association restated its position on the branch banking question.

At the Boston convention the Association adopted a resolution supporting the autonomy of the States with respect to banking, and declared itself "definitely opposed to any proposal or device looking to the establishment of branch banking privileges across State lines, directly or indirectly."

At the risk of being trite, I would remark that the dual system of independent locally owned banks has proved its value to the welfare of the country. It has been through considerable alteration in the last several years and on its own initiative it has greatly widened its services to people.

The country itself has been kept unsettled for a long period of time by means of endless legislative innovations. What we need now is a resting period in which to absorb the changes that have been made.

I am old fashioned enough to believe that deep down in the hearts of every thinking American rests an attitude of loyalty to our democratic form of government and that we are all willing, as individuals, to accept our responsibilities as we understand them. While business men are reluctant to participate in partisan politics, if we wish to enjoy to the fullest extent the heritage left us by our forefathers, we must accept responsibilities and make personal sacrifices. I am sure you will agree with me when I make the statement that we should become more active and assist in shaping the policies of our Government by familiarizing ourselves with the problems confronting the Nation, and be willing to accept the responsibility of leadership and go down the line for sound principles without regard to party affiliations.

Europe is at war. Who can say that we will be able to keep out of it, or what trials we shall have to face in the years immediately ahead? Instead of tearing our structure apart and introducing new conflicts among ourselves, we ought to be builidng it up to render the greatest possible service and to contribute the greatest amount of stability to the country.

Remarks of President-Elect William S. Elliott

President Elliott: I realize that the acceptance of an honor of this sort involves responsibility of the highest order. The two speakers, as well as the retiring President of our Division, have told you something of the difficulties that confront banking today. Perhaps at no other time has the future of privately chartered banking, as we have known it for many years in this country, been more seriously threatened or obscured with clouds of doubt and uncertainty. Apart from the threat of war which hangs over the world today, we find economic conditions have produced suggestions for change from various quarters, some of these suggestions emanating from high places in the Federal Government. We do not know what the future may hold for chartered banking, nor do we know definitely what efforts may be made to change the dual banking system and the powers and authority and usefulness of State banks throughout the Nation.

We do want to dedicate ourselves to the task of meeting these new problems as they arise with courage and fortitude, and with the common intelligence born of close cooperation and loyalty to the principles which have underlaid the banking structure of our country during the many years when it has wrought so well for the advancement and progress of the American people. We do not want the emergencies and the exigencies that exist today to obscure the great fact that the fundamentals of the American way of living and the fundamentals of our economic system must be preserved at all costs if we are to enjoy the freedom which was bequeathed to us by the founding fathers 150 years ago, and which has been maintained and preserved down to this good day by the sacrifice and, oftentimes, by the blood of our forefathers.

To this task we can very well dedicate ourselves and, in a spirit of cooperation, strive to meet the issues that confront us in the days to come.

It shall be my purpose to keep you advised, as members of our Division, as to the changes that occur, as to the dangers that threaten, as far as we can discern them, from time to time, and to ask your cooperation as we present a common front toward a common enemy.

I want to bespeak the cooperation of our Executive Committee and the cooperation of every member of our State Bank Division. We want you to write to us if we can serve you. We want your suggestions from time to time, because the organization which we maintain within the Constitution of the American Bankers Association and the By-laws of the State Bank Division is primarily for your benefit and to preserve and foster the principles of State banking and the rights of State banks to continue to exist and perform the useful functions of which they are capable for the benefit and the prosperity of our common country. To this end we can very well dedicate ourselves, and I ask your consideration and your patience with us as we enter upon and pursue our way along the new Association year. I believe we will succeed in the measures we will properly undertake to preserve the rights and the life of the State banking system as we have enjoyed it for so many years.

Report of Committee on Nominations

President Koeneke: We will now call on M. H. Malott, President of the Citizens Bank of Abilene, Kansas, who is Chairman of the Nominating Committee, for a report. If Mr. Malott is not in the audience, we will call on M. Plin Beebe, President of the Bank of Kimball, Ipswich, S. D., for a report.

Mr. Beebe: Mr. Chairman and Members of the State Bank Division: The Nominating Committee offers the following names for the ensuing year for our Division:

For President—William S. Elliott, President, Bank of Canton, Canton, Ga.

For Vice-President—Harry A. Bryant, President, Parsons Commercial Bank, Parsons, Kan.

For Member of the Executive Committee, term expiring in 1940—L. C. Palmer, President, Citizens State Bank, Arlington, Wash.

For Members of the Executive Committee, term expiring in 1942—Wood Netherland, Vice-President, Mercantile-Commerce Bank & Trust Co., St. Louis, Mo.; Frank P. Powers, President, Kanabec State Bank, Mora, Minn.; James M. Shackleton, President, Saginaw State Bank, Saginaw, Mich.; Peter G. Cameron, President, West Branch Bank & Trust Co., Williamsport, Pa.

Respectifully submitted,

M. H. Malott, President of the Citizens Bank, Abilene, Kan., *Chairman*,
Raymond H. Beyer, President of The First State Bank, Guthrie, Okla.,
M. Plin Beebe, President of the Bank of Kimball, Ipswich, S. D.

President Koeneke: You have heard the report of the Nominating Committee. Are there any nominations from the floor? If there are no nominations from the floor, I will entertain a motion to accept the report of the Nominating Committee.

[The motion was duly carried and the officers installed.]

President Koeneke: You have elected a new set of officers and additional members of the Executive Committee. So you may be thoroughly familiar with the government of your Division, we elect four new members to the Executive Committee each year to serve for a three-year term. The reason for the odd one this year is that one of the members of the Committee, Charlie Laird, of Moorestown, N. J., is in ill health and asked to be relieved of this responsibility.

SAVINGS DIVISION

AMERICAN BANKERS ASSOCIATION

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Good and Bad Money

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During the past two years, while attending State banker conventions, I have had the privilege of meeting many bankers, including Past Presidents of the American Bankers Association and State Associations, some of whom indicated by their inquiries they were unaware of the duties and responsibilities of the United States Secret Service.

Coming from bankers, these inquiries have been a bit perplexing, and I have since wondered why bankers know so little about us when our interests are so closely related. However, it has occurred to me that perhaps it is our fault that we are not better known in the banking field. May I say that this is one of the reasons we are on your program today, for we want you to know that the Secret Service as a division of the Treasury Department is one of the oldest investigative agencies in the Government structure. In fact, we are this year observing our seventy-fifth anniversary. Briefly, we are charged with the responsibility of preserving the integrity of the currency and coinage and other fiscal obligations of the Government, as well as the great responsibility of protecting the President of the United States and members of his family, and the person elected to be President. We are called upon occasionally to protect visiting royalty, our most recent responsibility being their Majesties, the King and Queen of England, who visited the United States in June. This additional duty taxed our resources to the limit, but I am happy to say the arrangements connected with this dual task were successful in every particular.

Since the Nation's banks are our first line of defense in combating the counterfeiter, your tellers occupy the front line trenches and you must depend upon their judgment and discrimination in determining the quality and character of the money passing through their hands.

Tellers perform a splendid service through their general efficiency in detecting counterfeits included innocently in customer deposits. Many new counterfeits first come to our attention in this manner. I feel that our efforts in suppressing counterfeiting would be retarded in great measure if we failed to receive this assistance from our banker friends.

With a comparatively small field force scattered at strategic points, the responsibility of keeping our money clean rests squarely upon the Secret Service. Bankers share with us a common interest in this responsibility, and we rely upon them in coping with a problem which in recent years has developed into an organized racket with underworld connections extending throughout the country, and even into foreign countries. We value highly your cooperation, and it is Chief Frank J. Wilson's desire that all bank employees shall regard themselves as unofficial Secret Service agents, always on the qui vive for that shady commodity which is the spawn of the criminal engraver and the criminal printer.

The average teller daily sees the portraits of Washington, Jefferson, Lincoln, Hamilton, Jackson, and perhaps Grant and Franklin, hundreds of times. They pass before him in rapid review and it is impossible for him to stop and examine minutely the portrait on each note. He must accept or reject the notes instantly and, incidentally, he makes few mistakes. An experienced teller can spot instinctively the strange, or "unfriendly," face on a counterfeit note as quickly as he can spot the face of a stranger before his cage.

Through long years of training your teller acquires a sort of sixth sense in separating the chaff from the wheat—a sense enabling him to distinguish between good and bad engraving and printing. But what about the butcher, the baker, the candlestick maker? Why are they usually the victims of the counterfeiter? It is because they are not familiar with the quality and character of our currency and coinage, and it follows that the counterfeiter makes capital of this ignorance by distributing his worthless wares.

The finished product of the Bureau of Engraving and Printing in Washington, D. C., surpasses in excellence the currency output of all other nations, because our genuine notes are printed from steel plates superbly engraved by hand by the finest craftsmen in the world. Except for the serial numbers and Treasury seal, which are surface printed, every line, every dot, every dash on a genuine note stands up clearly and distinctly and the composite design presents a challenge which the counterfeiter cannot meet. The paper is impregnated with tiny red and blue silk fibers to increase its durability and tensile strength. These distinctive fibers are difficult to discern at first glance and, contrary to popular belief, they are not intended as a protective feature.

In this fast-moving age the average person does not take time to consider our money seriously in terms of quality appreciation. He is inclined by habit to identify currency by the large denominational numerals appearing in the corners of each note. He is not impressed by the artistic workmanship, superb engraving and printing values and general high-class appearance of our paper money.

I have in mind a grocer who catered to a clientele which demanded the best of everything the market afforded. Fully aware his customers inspected his offerings for freshness and quality, he visited the wholesale dealers daily before sun-up to replenish his stock, shopping at various booths in an honest effort to obtain the choicest items of his list. One day, when his display of strawberries attracted more than usual attention, a stranger purchased six baskets with a $20 note. The grocer knew most of his customers, but occasionally a stranger patronized his store, and this strawberry sale to a neatly-dressed man, whom he did not know, failed to register with him until a few minutes later, when he sent the bill by one of his clerks to a nearby bank for change. His indignation reached lofty heights when the clerk returned with the announcement that the bank had retained the note after labeling it counterfeit.

In common with many other people, this grocer was unaware that counterfeits are passed by strangers in 95 out of 100 instances, but I hazard the guess he will exercise as much care hereafter in handling his money, in particular money proffered by strangers, as he displays in selecting his fruits and vegetables. He will scan his currency a second time to reassure himself it does not reveal the tell-tale distinguishing marks of the "phony" bill.

Current counterfeits cannot be compared in deceptive quality with the issues which circulated many years ago. Since the processes of engraving and printing have been simplified in recent years, it is unnecessary that the counterfeiter shall be a hand engraver skilled in the graphic arts. It may surprise you to know that most present-day counterfeits are made by persons who have learned just enough about photo-engraving to build up a zinc or copper plate suitable for their purposes. However, the counterfeiter who turns to photo-engraving finds a serious impediment provided by this process, which is incapable of transferring to metal plates the delicately-cut hand-engraved lines and shadow values which distinguish genuine notes. For this reason, fidelity to detail is generally lacking, particularly in the portrait in which the facial features are reproduced coarsely and the eyes lack expression and vitality. Because of this inferior workmanship, faces on counterfeit notes are obviously strange and "unfriendly," echoing the base character of their unworthy sires.

Counterfeiters unwittingly transfer to their work the label of their own individuality. Just as an art connoisseur can identify an original Raphael, Rembrandt, or Remington, so can experienced Secret Service agents recognize the technique of known skilful counterfeiters.

New York agents a few months ago apprehended Peter Terhorst, a German, who applied himself seriously to home-study of photo-engraving and became one of the most dangerous counterfeiters with whom we have contended in recent years. This man's criminal career began in 1930 in his home town in Krefeld, Germany, when he was arrested for embezzlement and gigantic frauds. While awaiting trial he swallowed a needle and was transferred from jail to hospital. After a few days Terhorst took "French leave" and fled to the United States. Visualizing an easy road to rapid wealth by imitating United States currency, he turned to study of photo-engraving and produced a fairly deceptive $10 note after six months of diligent preparation. This note circulated in the larger Eastern cities until our agents arrested Terhorst under the name of Henry Braun in New York City. He was sent to Atlanta Penitentiary for three years and deported in 1935. Before his departure, however, he made certain underworld contacts upon which he depended for aid in returning to the United States.

Soon after his deportation he obtained a passport under the name of a son of his former employer in Krefeld and, as Hans Neuwerth, he returned to the United States through the port of New York. Within a few months new counterfeit $1, $5 and $10 notes began to appear in New York City and elsewhere. There were eight varieties, each of which flashed certain characteristics which convinced agents they originated from the same source. Agents believed they identified in these counterfeits the imprint of Terhorst's personality, and investigation was conducted on the theory he had returned to New York. This theory was partly confirmed when our New York representatives arrested the deportee in October, 1938. Unfortunately, there was no direct evidence to connect him at this time with any illegal activity, since it could not be proved beyond a doubt he was responsible for the flood of new notes with which hundreds of innocent people were being defrauded in many sections of the country. He was then surrendered to immigration officials, in as much as he reentered the United States illegally. He was held under $5,000 bond for a hearing, at which he failed to appear.

Undaunted by our failure to connect Terhorst with these new counterfeits, Chief Wilson assigned a specially picked corps of agents to concentrate their whole time and attention in New York in an effort to re-locate him in an atmosphere providing the evidential background necessary to involve him. After five months of intensive investigation, during which agents worked night and day with inspired enthusiasm, Terhorst was recaptured March 6 in a Greenwich Village apartment surrounded by an elaborate counterfeiting outfit, which included approximately $50,000 in complete and incomplete counterfeit notes. Simultaneously, agents arrested six other persons closely identified with the conspiracy. Terhorst confessed fully, naming other important figures who for many months had been under surveillance, including a group of gangster Italians long on our suspect list. This group acted as distributors, or wholesalers, and maintained connections with other dealers in various sections of the United States. They were arrested promptly and convicted largely upon Terhorst's testimony. Capture of Terhorst removed from the scene a most dangerous character whose activities in his chosen field resulted in the arrest by our agents of approximately 250 persons as distributors and passers.

With the issuance of the small size currency notes, the Government curtailed materially the activities of another type of counterfeiter who does not concern himself with the detail and expense of assembling a photo-engraving and printing plant. This swindler is a specialist in his own right. He tampers with genuine currency, erasing the corner numerals and denominational lettering, and substitutes in paint or ink the artistic flourishes necessary to increase, for his purposes, the original value of the note. He may even tear off the corners of $5, $10 or $20 notes and paste them over the corners of notes of smaller denomination. Genuine notes are issued in 11 denominations, each carrying a standard denominational portrait. Irrespective of other identifying characteristics, a note should be recognized only by the portrait it bears. If one will remember the portraits on genuine notes, he will not be deceived by the note-raiser, notwithstanding the fact the swindler may display amazing skill in converting a note of small denomination into a note purporting to be of larger denomination. The following portraits appear on the various denominations: Washington, $1; Jefferson, $2; Lincoln, $5; Hamilton, $10; Jackson, $20; Grant, $50; Franklin, $100; McKinley, $500; Cleveland, 1,000; Madison, $5,000; Chase, $10,000.

Counterfeiting of coins seems to attract criminally-minded persons of meager means. For the most part, counterfeit coins are made of lead or babbit metal in plaster of paris molds. Some "coiners" treat their products with a silver plating bath to increase their deceptiveness. These coins are generally light in weight and produce a dull sound when dropped on a hard surface. They tarnish quickly and have a greasy "feel" when rubbed between one's finger tips. Molded coins fail to reproduce accurately the parallel crevice lines on the rim erge. This feature, often identified in error as the milling, is known as the reeding. Probably the surest test of a doubtful coin, unless the coin be counterfeit with genuine silver content, is application of a solution of nitric acid and nitrate of silver. A drop of this acid on a coin made of base metal will produce a black spot. A silver plated coin should be scraped first and the acid applied at the point of abrasion. Genuine coins, as well as die-struck counterfeit coins made of silver, will resist the acid test.

Aside from our primary interest in suppressing counterfeiting, we are making a determined effort to reduce the loss in genuine money sustained by banks, retailers and the general public through acceptance of counterfeit issues. In our endeavor to educate the business man to recognize the quality and character of our currency, we are coming down from our Sinai and, like Moses, we are spreading the truth so that the public may be better prepared to protect itself against fraudulent money. Heretofore we have hidden our light under a bushel, monopolizing, so to speak, certain information which should be available to anyone. Now that the bushel has been removed, the luster of this light extends to the highways and byways, the glare so strong that the counterfeiter finds his activity more hazardous with his proposed victims forewarned.

As a forerunner of this campaign under Chief Wilson's direction, an educational campaign was conducted in New York City early last year to familiarize the retail business man and his associates with the identifying characteristics of genuine money and the defects apparent in counterfeit money. Secret Service agents lectured before 2,160 meetings attended by 93,909 persons, including bank employees, police and postal officials, members of business clubs, small shopkeepers and others. Radio talks and short movie subjects were made in line with this educational activity. More than 100,000 store employees were instructed orally and approximately 900,000 warning notices describing counterfeit notes were distributed through the mail.

While the campaign was under way traffic in counterfeit money in the New York area began to decrease noticeably and marked reduction was also observed in other sections. One of the larger New York banks, with more than 60 branches, took a loss of $4,800 in counterfeit notes in 1934, and at the same time intercepted more than $40,000 in counterfeits in customer deposits. This bank last year lost $723 and detected $14,347 in counterfeit notes. We are convinced the reduction reported by this bank is due to the effects of our educational work in New York, which has been the operating base for many years of some of the most dangerous and persistent counterfeiters in the country.

Notwithstanding the skill of their tellers, banks in the United States last year accepted as genuine 7,094 counterfeit notes for a loss of $62,002. In New York State alone the loss aggregated $20,228, represented by 2,285 different counterfeit notes. This is a comparatively small amount considering the record of former years, and we attribute it to the splendid cooperation we received from the banks, coupled with the enlightening influence of our educational campaigns and intensive drives throughout the country against those who violate the counterfeiting laws.

Losses sustained by the public, and the banks as well, have decreased steadily during the past four years, the reduction last year amounting to $302,512 as against a figure in excess of $1,000,000 in 1935. The public loss in counterfeit coins was reduced from $69,745 in 1935 to $50,873 last year. Our agents last year arrested 448 persons for making and passing counterfeit notes, 557 for making and passing counterfeit coins and 2,980 for violating other laws which come under the investigative jurisdiction of the Secret Service. Arrests and convictions for the fiscal year ended June 30, 1939, exceeded any previous year in our history, convictions being secured in 97.03% of the cases going to trial.

It is well known that the successful banks in any community are those which establish a close public relationship with their customers. You gentlemen who attended the California bankers' convention earlier this year were doubtless impressed with the program which was built around the theme of public relations.

The public relations departments of some banks are overlooking an opportunity to render to their depositors a genuine service in which effective missionary work may be accomplished with little effort and little cost. When a bank detects a counterfeit, the teller making the discovery notifies the depositor. There may be in the teller's voice a tone of regret intended to register sympathy. Now if that depositor had been forewarned by the bank, there is a strong probability he would not have been deceived by the bogus note or coin.

In the public relations program of the banks you represent, can you think of a better public service than the sponsorship for the benefit of your depositors, and others who may not be your depositors, of a campaign having for its object the education of your retail merchants in the detection of counterfeit money? An occasional meeting arranged by your bank in any public auditorium, with a bank officer or Secret Service agent as lecturer, will interest your merchants, shop-keepers, service station employees, who may or may not be your depositors, and will attract large groups when properly advertised. The Secret Service believes it to be its duty to provide this education, and we shall be pleased to cooperate with your banks by supplying, at your convenience, experienced agents who will supplement their lectures with exhibits of large photographic reproductions of genuine and counterfeit notes, together with a collection of counterfeit note and coin specimens, plates and molds. We participated in approximately 2,000 such meetings last year, attended by more than 160,000 merchants and their employees. In a few months we shall have available a sound motion picture which will be featured in our educational talks furthering this program. We shall also be pleased to supply your banks with an agent qualified to give special instructions concerning counterfeits to your tellers. Incidentally, we feel that your tellers should know that counterfeits should be retained by the banks instead of being returned to unfortunate depositors, and also that the depositors should know what action to take whenever they are placed on the spot by a passer of counterfeit money. Your banks will render a fine degree of cooperation if you will notify our nearest office by telephone or telegraph, or communicate with local police authorities, whenever a counterfeit is detected in a customer's deposit.

The Government last year issued the tremendous number of 148,967,048 checks. Some of these checks naturally fell into unauthorized hands. Since it is our responsibility to investigate forgeries of Government checks, our agents last year conducted investigations in more than 20,000 such cases. We are now placing in effect preventive measures intended to reduce the number of forgeries and expedite investigations in such manner that banks may be relieved of part of the additional work incident to investigations of forged checks bearing their endorsements. In this connection, we are asking the banks to cooperate further with us. If a bank in which a forged check has been deposited is located at a point some distance from our nearest office, and it is impossible for agents to arrive on the scene within 24 or 48 hours, our office handling the case will then forward direct to the bank a photostatic copy of the check, with a questionnaire, and request the bank to interview the depositor and obtain as much information as possible concerning the circumstances under which the check was negotiated. The Secret Service adopted this procedure not only with the thought of locating the forger quickly, but as a means of assisting the bank, and also the payee, in obtaining restitution speedily.

A Government check is a worthless instrument unless it is endorsed by the payee and carries the last endorsement of a person known to the agency which negotiates it. Your depositors do not cash commercial checks for strangers unable to identify themselves satisfactorily. Why should they cash Government checks for persons who cannot satisfactorily establish their identity?

As a further means of assisting your depositors to protect themselves against forgery, we have caused to be printed on all Work Projects Administration checks the following warning in red ink on the front near the bottom: *"See identification procedure and instructions on reverse of check."* This admonition is also reproduced in red ink on the back of the check above the space provided for the signature: *"When cashing this check for the individual payee, you should require full identification and endorsement in your presence, as claims against endorsers may otherwise result."*

May I say in conclusion that alertness is of primary importance in any business in which money is the main commodity? We know there is little salvage value in mistakes. If your bank accepts a counterfeit note, there is the possibility it may be paid out again innocently. I know depositors who claimed in full sincerity that this or that counterfeit came from their banks. I also know of banks able to trace a counterfeit to a depositor's account after the customer left the bank. Unless he is present to witness the discovery, the depositor is rarely ever convinced of the bank's claim. When controversies arise, the bank is the ultimate loser, not only in the amount involved, but also in prestige, which is more important. Sometimes a good depositor is lost because the bank does not subscribe to the theory that "the customer is always right." Tellers may avoid these unpleasant experiences by learning to recognize the "unfriendly faces" on counterfeits, for, after all, by their faces ye shall know them.

The World Today

By Dr. Fred I. Kent, Director Bankers Trust Co., New York, N. Y., Chairman Commerce and Marine Commission, American Bankers Association

In introducing Dr. Kent, President Williams of the Division said, in part:

It may have surprised some of you who have known this gentleman for many years to see designated on the program the final speaker as "Doctor." While it may have been a surprise to a good many of you, it is no surprise to me. I can vouch for its authenticity because I was present when this doctorate was conferred upon him by the University of Southern California some years ago. Never was such an honor better deserved than in this particular case. Not only was this honor conferred upon Dr. Kent by a university, but he has been exceedingly active in university affairs, particularly New York University.

I know, as you do, that any introduction of the gentleman would be inadequate at best, but I just want to remind you of some of the things that he did during the World War. During the World War he was Financial Adviser to the United States Government, and on many occasions he has been called as an adviser by foreign countries and has had honors bestowed upon him for his work. Quite recently he was in Europe addressing the International Chamber of

Commerce, so that he is a man who comes to us with authority.

In spite of the fact that he is a banker by profession, he is also a scholar.

Dr. Kent presented his address as follows:

World psychology has developed in such manner that no statement of conditions can be comprehensive nor understandable without taking it into consideration.

The mental turmoil left by the World War, instead of calming down and enabling mankind to think and act constructively, has steadily grown worse. The reason seems to lie entirely in the fact that men did not return to work after the Armistice in sufficient proportion to solve the problems left by the war. Instead, many millions were provided with buying power for doing nothing, which increased their unrest and started the world upon a false recovery. Added power was given to those who were willing to promise the people prosperity through false methods. This was equally disruptive whether those ignorant of economics and safe procedure had their way or whether those who wished to utilize the multitude for their own power prevailed. As a matter of fact, these two groups worked together, as those striving for power—who understood the futility of the means to the end that they promised—were more clever than the first group, and were able, therefore, to obtain added force because of the good intentions of the first class, despite their ignorance.

The result was the development fo a "gimme" attitude on the part of millions of people, accompanied by the wishful thought, with which they hypnotized themselves, that they could have something for nothing and live off the efforts of others in complete happiness. As mankind is constituted, happiness is based on one's own efforts to do his part in the world, and any temporary satisfaction that may come otherwise is followed by discontent.

The development of such psychologies inevitably led to the formation of organized minorities whose purpose was not the general good, in important part, but to obtain favors for themselves directly or indirectly through the exercise of such power as they could bring to bear upon legislators and Government officials. Such procedure naturally followed into coercion and the great unorganized majorities have been led by the nose to approve, on the basis of misunderstanding, policies of government that could only work to their detriment.

In the United States we have been directly affected by this development, as has been true in practically all countries of the world. In addition to this unfortunate psychological movement, together with the resulting forces built up under it, Europe has also been obliged to struggle under the inequities and unwise provisions of the Treaties of Versailles, Trianon and St. Germain. It was only natural that under such a sequence of conditions the world should find itself in a new competition in armament that was outstripping any other similar activity in its history.

When I was asked by M. Poincare to go to Hungary to investigate that country to see whether he was justified in allowing the reparations to be postponed in order that Hungary might obtain a $30,000,000 loan, I had a chance to see what a terrible development was certain to follow those treaties. I found, for instance, 600,000 Hungarians north of the Danube were put into Czechoslovakia and taken away from Hungary, and the condition right straight through the country was most unfortunate. It made it difficult and impossible for them to live. When I made a recommendation to have certain parts of the line between Czechoslovakia and Hungary changed, parts that the Czechoslovakian people were willing to have changed in order to make it possible for Hungary to live, the League of Nations said: "No, that is not a good change, because it needs to be where it is in order to have military strategy able to prevail." That was one of the things that happened after those treaties went through.

No competition in armament between many nations has ever been stopped short of war. There are impelling reasons why this should be true. Competition in armaments of necessity lowers the standard of living of the peoples involved. This comes about because of the strain of expenditure upon governments, the utilization of the time of men and women in the production of goods that are useless for any economic purpose with the resultant fall in the building up of consumption and capital goods needed by the people for their better living and the diversion of raw materials from useful articles into those whose only purpose is to destroy men and the creations of men.

The breaking down of such a system once started has in the past proved to be impossible. It was the hope of the world that we might have progressed sufficiently in our understanding to stop the competition in armaments that had been going on short of war. There is some reason to believe that this might have been accomplished if the nation which started the armament development had not done so with the full intent of its government to utilize the force that it was creating to either bluff the other nations into giving up to them, in ways that humanity could not stand, or in going to war to obtain its purpose.

Even while the present war is being fought out, the peoples of the world must turn their minds so strongly toward the accomplishment of peaceful conditions afterward that it will relieve the strain of the aftermath of the war and allow the consummation of a peace based upon intelligence or humanity may find itself unfit for civilized living for generations. The governments involved, through the demands of their peoples, must realize that their continuation is dependent upon their ability to bring about peace. Sufficient pressure from peoples upon governments to accomplish any such outcome is inconceivable unless the men and women of the world are willing to sacrifice their hatreds, envy and greed and replace them with goodwill toward their fellow men, integrity in their thought and an active desire to do their part individually to make the world a better place in which to live. Such a change in the morale of the people of the world can only come about through a revival of spiritual faith which will restore the power of individuals to make the good that lies within them work for the benefit of all.

The economic problems that must be solved require such a change of heart upon the part of the people equally with every other character of difficulty that lies within the situation. Ways must be found to provide employment in constructive fields for those now engaged in war and the production of instrumentalities for war. A great resumption of trade between the nations is necessary if sufficient employment to meet the needs of such a transfer is to become available. Ways must be found, through the meeting of the minds of those in government in the nations, as to how best to correct the errors made in the past through treaties and pacts between the countries which will bring about fairness to all and the sense of overweaning power to none. Ways must be found to increase production and its distribution on a basis that properly rewards ability and integrity, furthers private initiative and makes possible the best use of the forces for good that lie within the hearts and minds of every individual.

The development of isms offers the greatest obstruction to the accomplishment of economic and political peace between the nations. They are also at the bottom of the dustruction of democracy that has been so progressive in the world since the Armistice. The political power of the isms is forstered through a development of so-called ideologies that presumably represent the final attainment in methods of living that are aimed to attract the people.

In general, the ideologies represent, in important part, conditions of life that all right thinking people would welcome. It is due to this fact that the ideologies have become a menace to mankind. Most of those who are attracted by certain phases of them are incompetent to see that the means suggested to the end make them impossible of accomplishment. They cannot see that regimentation of all the fine forces that make men men and within the control of self-picked dictators must prevail if the ways that are advocated to bring about better conditions in which the ideologies are to be lived are followed.

People do not seem to realize that those who deliberately arouse envy and hatreds within them cannot lead them without destroying their happiness—regardless of the pretensions of those would-be leaders. As history moves forward there are moments when strong men must take control in order to save disaster. Such strong men, however, who can justify their temporary control are not among those who see all of the rest of the world as being dishonest and living under improper motives.

Ideologies cannot be achieved, no matter how fine they may be, by ignoring historical experience and through processes of sapping and undermining the honest forces of other men who are themselves striving during their daily activities to bring about betterment in the world.

One reason why the churches of the world have lost so much ground since the war has been due to a turn from the preaching of the Gospel into the condemnation by ministers of their fellow men without proper knowledge as to the right or wrong of the acts of those whom they criticize. Sermons of condemnation on this basis, which are easier to prepare and are more spectacular, are just as destructive to sound community life as those individuals whom they may decry would be—if such persons were actually as bad as they are made to appear. It is as vitally important to the well-being of a people that their spiritual leaders keep themselves free from false criticism of other men and from inducing envy and hatreds as it is for their political leaders to do so.

The church, not having actual experience in business life but being able to see the errors of men here and there and, particularly, being subject to the statements of self-seekers who want to utilize the church for their own needs, should feel duty bound through its ministers to check and recheck every process in the economic and political world that critics claim are dishonest and detrimental. This should always be done before anything of the kind is carried to the pulpit. Only when there is a turn on the part of churches of all denominations in this direction and more attention is being given to the preaching of the Gospel than to the damnation of other men, will there be substantial progress toward greater happiness on the part of the people and economic and political progressions that will lead to a higher standard of living. After saying this, not in a spirit of criticism but for purposes of better understanding, we must give credit to those great churchmen of our time who have held themselves above the tearing down of other men and whose influence for good has been so farreaching. Such ministers are among us everywhere, and we must depend upon them, in large part, to help restore humanity to a sane way of thinking.

In order to allay the unreasonable and unnecessary turmoil existent in the world, which must come about before there can be better conditions of living on the part of all, approach must be made toward the creation of the true State—a State that is not subject to dictation and domination by organized cliques. For better understanding it might be well here to state briefly the elements of a true State by repeating the description of such a State made by this speaker at the meeting of the International Chamber of Commerce at Copenhagen.

I want you to think about this because a very different State has been advocated in Europe in some of the countries. In Italy the people are for the State and not the State for the people, and they have developed a very interesting series of works upon why that should be so, but let us think of the true State from the standpoint of reason:

"The true State is the protector of the people, economically and socially."

True protection of the people by the State requires:

1. That mankind be allowed to live in peace and comfort;

2. That there be the greatest possible individual freedom consistent with safety and proper satisfaction in living in order:

a. That individual ability may work for the benefit of the whole;

b. That the higher grades of intelligence may not be submerged by the lower grades of intelligence with a reduction in the standard of living of all; and

c. That the incentive to the accumulation of private property, not at the expense of the many nor the few, but for the general good, be furthered.

3. True protection requires that production needed by the people and its distribution be stimulated by encouraging private enterprise under sound governmental regulation because:

a. The mentality of all men develops to their own greater efficiency and capacity for happiness and in the public interest if they are allowed to exercise proper initiative in their undertakings whether they may be of major or minor importance;

b. The good of the people is better served when every man has the urge to earn his own living and something over that my help provide for protection, government and growing culture, and because

c. The wants and desires of individuals form the basis for supply and demand of goods and services that can only be measured from the currents of the contacts of men with each other and that are, therefore, not available to the consciousness of men in government who with the finest of intent can only regiment with a destruction of individual initiative which dulls intelligence, dissipates happiness and lowers national efficiency.

4. True protection requires that there should not be Government operation of business or industry in competition with the people—a condition certain to cause stagnation in production and retrogression in the national life because:

a. Government can hide its errors in taxation at the expense of all the people;

b. Changing regimes break continuity in the growth of efficiency through killing incentive of the workers;

c. Political forces destroy the exercise of individual ability that under private enterprise strives for results which, when successful, make for the public good, and because:

d. Even with the finest intent, governmental bureaucracies engaged in what should be private enterprise expand and grow until they become parasites that live upon the income of the people and prevent its use in furthering progress through developing a better means to live and in furnishing employment that is productive in character.

5. True protection requires that Government spending be confined to normal amounts required to operate the State on a sound basis and in cases of emergency involving hardship and suffering to any part or all of the people to methods of expenditure aimed to restore economic order and the individual financial independence of its people as quickly as may be.

The foregoing, in a great general way, represents the ultimate in the true State, as government on any other basis must lead to wars—both internal and external.

In time of war this character of government is exactly as essential in the interest of the people as in time of peace. This is true even though in time of war government must have greater freedom to meet emergencies in order that it may act promptly in case of necessity and consequently it must have greater power for such purposes.

Differences of opinion on the part of those in and out of government that have to do with theoretical matters must be set aside. War produces practical problems that must be solved in a practical manner. Under the functioning of a "true State" the intelligence and ability of the people can be made more effective in serving all of the people and their Government even though government temporarily has emergency powers that are essential in time of war. Such powers can exist and be effectively exercised without the necessity for government, by means of bureaucracy, to reach deep into the management of a country's business and industries. The problems of government, regardless of their difficulty, are complicated and multiplied when it tries to dip into the management of the enterprises of a nation through its various departments.

If, for instance, in the United States a million men should be absorbed by government in a war emergency and should be placed in positions where they had power to reach into the operations of business and industrial management, it is inevitable that the ability of experienced men to carry on in the interest of the Nation would be curtailed, that the speeding up of production where needed would be possible only after great and unnecessary waste and that the powers given to the million, who is tremendous proportion would work into positions where their previous experience had not provided them with understanding, would of necessity sabotage the smooth functioning of every character of enterprise.

The experience of the great World War proved this beyond any manner of doubt. Witness the millions and millions and millions of dollars that were spent by this country for airplanes and the fact that after all such expenditure, American airplanes never got into the battle areas.

This thought leads into another most important consideration which has to do with the receipt by Government of the money and credit of its citizens. It has been proved time and again that Government, because of the very nature of men themselves, cannot be put in possession of huge sums of money without developing enormous waste. What Government must have in the interest of its people is a steady income under which funds reach it each year as they are needed to enable payment for services and things that may be required. It is only over a period of time that production can be accomplished on a sound basis even for emergency purposes and Government does not require funds until its obligations become due. In case of war, where some funds are needed for plant expansion, they can better be obtained through borrowing than through excessive taxation.

The people are better able to take something from their income for government each year under an opportunity to earn an income through the years than if they are called upon to pay out large sums at one time which restricts their ability to live and to help others to live.

Taxation, whether it may be intended to prevent war profits or is levied for any other purposes, that dries up the businesses under which the people earn their living and develop production; increases the waste of Government and decreases the ability of a nation to give either its military forces or its civilians the greatest protection which lies within its power. Those who may be at the front in a great war have a much better chance of coming through if the finances of their country are handled without governmental waste and without disrupting industry. Again, their morale is infinitely better and their ability to protect themselves—because of a better morale—is much greater if they know that the finances of their country are being handled in such manner that there can be a constant flow of war materials to them while at the same time those for whom they care at home are able to earn what they require for their own protection and something over to help government.

No right-minded person wishes to further the creation of so-called war profits at the expense of a nation, or of those who may be among the military units, but when a government kills the earning power of its people and the ability of a nation to produce for war emergency by passing unwise laws just because of fear that somebody may make a profit, it is almost criminal.

Conscription of capital in time of war, because there is conscription of men, is suicidal. They have nothing to do with each other. Men are required to fight the nation's battles, and capital is required to protect them in doing so. Capital should, therefore, be so conserved and utilized that it will give Government the greatest economic power possible to its people in order that those at the front may have needed supplies of all kinds and that those at home may live. Such conservation of capital requires that it be left with the people in order that they may use it in natural ways to earn an income for their living and for their Government.

You gentlemen are going to be faced with all kinds of tax laws aimed to do things that can destroy the power of our Government to meet the emergency that it may be led into, and you must use your most careful thought in thinking about these things and not be led away by emotion into feeling that because men are conscripted it is fair to conscript capital. It isn't a question of fairness or right; it is a question of protecting the men. If you conscript capital you destroy the power of your Nation to meet its economic problems. It is something that you must not be ashamed to stand for. It will be put before you in such a way that you will be made to feel that though you want to have a sound governmental financial situation you want to do that at the evpense of the men at the front. It will not be at the expense of the men at the front; it will be for their protection.

Money demands by Government that result in forced sales of property by its citizens in depreciated markets reduces the national wealth, curtails industry, causes unemployment and increases the difficulty of Government in carrying on either in time of war or in time of peace.

This simple economic fact is either unknown or is temporarily forgotten when men clamor for Government to take over the wealth of its citizens in the belief that it will protect those who must fight its battles. It is not realized that the lives of its soldiers are put in jeopardy by such procedure and that the ability of Government to carry on its curtailed.

The condition that prevails in the United States today, under which nearly 10,000,000 persons are unemployed and the Federal budget is running huge deficits from year to year, must be corrected immediately or we will have to face a very real disaster. The great war that is now going on says to our Government and to our people in no uncertain terms that they must ge together and take such action as is necessary to restore industry in the United States or we will be unable to hold our own in this world turmoil. This requires the rescinding or correction and clarification of all laws that prevent the sound functioning of private enterprise that are in existence today.

Government must ascertain from industry what laws are involved and industry must cooperate and collaborate with Government in obtaining their amendment or elimination.

When this is accomplished and industry is functioning soundly, the unemployed in large proportion will be absorbed, thereby decreasing the expenditures of Government, greater profits will be available that will increase Government income on reduced taxation and the United States will be able to balance its budget and move into position to meet any emergency that may befall it.

We must realize that this is a very serious situation that is going on in the world, and that we are not as far from it as we may think. We must put our hours in order. We must be willing to do what is necessary to put our house in order, and it is simple to do it if we are willing to demand that laws that prevent the functioning of industry on a sound basis are corrected.

The intelligence of the whole Nation must be applied immediately to this great problem. Those in Government cannot do it alone. Neither can those out of Government do it alone. Government and the people must attack the problem together and in full accord as to purpose. Dictatorial methods by Government will not uncover intelligence which in this crisis is essential to success. Unruly opposition to Government by the people, if Government is willing to do its part, would be ruinous, and it is inconceivable that it can prevail.

It is the duty of Government and of the people to find the way to economic stability. They can only find it by working together faithfully and in confidence. This must be done. The solution of our problems will help the world. It will bring peace nearer, strange as it may seem.

When we have found the way to economic stability we will at the same time uncover the best means to prevent a false peace as the aftermath of the horrible war now in progress.

Our minds, our hearts and our souls must strive for understanding.

Our destiny will be as our faith determines.

COMMITTEE AND OFFICERS' REPORTS—SAVINGS DIVISION

Address of President P. R. Williams, Vice-President of the Bank of America N. T. & S. A., Los Angeles, Calif.

The Year's Work

If I should take literally the assignment as it appears on the program, it would take much more than the time allotted to me today. Also, it would make it desirable to call to the platform, Chairman of various committees of the Savings Division, who carried out our Savings Division program during the past year. That would not be practicable, and so I will endeavor in a very few minutes to bring to your attention some of the highlights of the accomplishments of the Association year that now ends. In a sense, it will be a report of our stewardship in a very condensed form.

The question has often been asked as to just what the purpose is of having several divisions in the American Bankers Association, and perhaps the same question is in the minds of many others, but has not been given expression. If in doing this; we succeed in whetting the appetite along any particular line, or if more facts are desired about any of these topics mentioned, please remember they are yours for the asking. The full reports of the committees to which I shall refer are lodged with our very able and genial Secretary, Deputy Manager W. Espey Albig. A line addressed to him at the New York office will elicit a prompt and full response. When I say they are lodged in the New York office, I do not mean that the reports are buried in the archives, labeled for identification with the year 1938-39, and then promptly forgotten. It has been in the minds of each Chairman that the cobwebs of disuse shall not be permitted to collect on this year's work. To this end certain constructive ideas have been developed, and it will be the business of this Division to provide the opportunity for bankers throughout the country to make full use of them.

In passing, let us remember that in speaking of the Savings Division we include savings banks and the savings departments of commercial banks. This represents approximately 45,000,000 savings depositors (44,738,752), and they represent approximately $25,000,000,000 of savings deposits, $10,000,000,000 of which are in mutual savings banks and $15,000,000,000 in savings banks and in savings departments. These savings deposits are about 51% of the individual deposits in all banks in the United States. Perhaps you will be interested in knowing how the saving depositors also are grouped. They are as follows:

Mutuals	14,132,000	State	8,881,000
National	15,934,000	Trust companies	5,761,000

Let us now quickly take a glance at what has been done.

Perhaps first, it would be appropriate to speak of the work of the Committee on Savings Development, for we must have the savings deposits before we can go ahead with the savings business. This Committee has been fortunate in having as its Chairman, Stuart C. Frazier, Vice-President, Washington Mutual Savings Bank, Seattle. A particular study of this committee this year has been that of Methods of Computing Interest on Savings Deposits. There has also been at work a sub-committee under Wendell Smoot of Salt Lake City. It has been endeavoring to find out just what is a bona fide thrift account.

In regard to methods of computing interest this study, as might have been expected, has shown so great a variance in practices, and therefore in the results obtained, that it is, to say the least, startling. The Committee has done a tremendous amount of research and the results should be placed in the hands of bank executives in the interest of uniformity and what is even more important, that as far as possible, the methods used should be fair to both the depositor and to the bank. To obtain the results, the questionnaire was sent to 3,500 banks, and these comprise every State in the Union. Replies were received from 53% of these, and the findings are therefore based on that number. It was found that 97½ of the bankers who responded feel that all banks in the same general locality should follow a uniform method of computing interest. So our objective among bankers is popular one. In a report as exhaustive as this one, it is not possible to give much more than a hint as to what it contains. There are a number of elaborate schedules and analyses that would require study to digest them. With respect to the use of actual methods of computing interest, the Committee found that 22 basic methods are in use, and 79 variations of these. Of these 22 basic methods in use, 10 of them were used by 90.39% of the reporting banks, and it therefore was these 10 basic methods that the Committee studied. It appears that in the preponderance of these cases, the interest on the accounts commences on the first of the month following the deposit. The great variance comes in the practices regarding withdrawals and the treatment of the interest in such cases. To determine the amount of interest that would be earned by the use of each one of these 10 methods, four actual savings accounts were taken to show various types of savings account activities. Variation from the least amount of interest earned to the highest, on identical accounts, was as high as 330%. In one case the earnings computed at a 2% rate was 15 cents by one method and exactly the same account by another method was computed at $7.70. Exactly the same account figured by the 10 different basic methods at the same 2% rate, produced 10 different results, varying from 15 cents to that of $7.70.

Surely the banks of the country should find some degree of uniformity in the computation of interest.

The results of the labor of the Committee, as I stated before, will be made available to member banks which desire it.

Another Committee job of great interest is that on time deposits, the Chairman being Roy R. Marquardt, Assistant Vice-President, First National Bank, Chicago. This Committee has pursued a study along original lines and in a field that apparently had been untouched or neglected up to the present time. The investigation seeks to determine the relative value of time deposits and demand deposits in different parts of the country, in cities of different sizes, and in various types of trade areas. Among other matters, it will ascertain, if possible, the extent to which time deposits are used, whether seasonally or continuously, to finance normal banking operations or banking operation of a seasonal nature. These studies have been made by Federal Reserve districts that are complete in a few Federal Reserve districts, and the study will continue until all 12 Federal Reserve districts have been surveyed.

You might be interested in learning something about the turnover of time deposits.

In mutual savings banks in 1938 the turnover was 24.6%, while the turnover of time deposits in all banks in certain Federal Reserve districts studied was 43.7%. A few years ago there seemed to be considerable favor for legislation which would make it compulsory to give notice upon withdrawals above a stated amount. If that sentiment ever existed among bankers, the questionnaire of our Committee indicates it is not in the majority at the present time, for only 29% reported favorably to such legislation, while 71% were opposed. Also, it is a matter of interest that 87% of replies indicated that no notice of withdrawal is required at present, while only 13% require notice.

Another fact which requires further study is that the replying banks indicated that 58% of them commingle their time and demand deposits, while 42% do not commingle them.

It seems to be quite impossible to do justice to the work of this Committee in a brief summary such as this is. I am satisfied that when the Committee has finished its work that the results will prove eminently worthwhile.

One of our standing committees is that on school savings, the present Chairman being Robert W. Sparks, Vice-President of Bowery Savings Bank, New York City. A notable incident in connection with this Committee's work is that of the annual regional conference, held in the spring in New York City. The attendance very largely comes from the New England States, where mutual savings banks are chiefly located. Latest school savings figures available are as follows:

Number of schools	8,448	Total deposits	$12,854,113
Number depositors	2,543,472		

Also under the same Chairmanship of Robert W. Sparks much work has been done by the Committee on personal money management. The Committee is preparing a manual of money management which will shortly be ready for distribution.

We have talked about the development of savings business and we will now consider what we are doing with the savings deposits after we get them. Under the chairmanship of Walter R. Bimson, President of Valley National Bank, Phoenix, Arizona, is the Committee on Investments. This Committee has made many new observations and some very constructive suggestions.

The Committee has pointed out that the change in the nature of the bank assets during the past few years has made the close study of the bond portfolio imperative. In the brief period of five years from June 30, 1933, deposits in all banks of the country increased over $17,000,000,000, while the loans in the same period have decreased $1,371,000,000. This huge deposit increase is now evidenced in our banks by increases of $8,153,000,000 in investments and $9,339,000,000 in cash. There has been a steady increase in the proportion of assets invested in bonds. Recent market changes brought about by the European war conditions have not lessened the problem. Mr. Bimson says:

"We are familiar with the conventional safeguards, the choices that confront us in attempting to minimize the risks. We know that a portfolio with regularly spaced maturities may safeguard us against the necessity of selling depreciated bonds at a loss. We know that the short maturities and the highest quality bonds are likely to fluctuate less than the long maturities and secondary grades. We know that our investment program should be carefully geared to the special conditions of our several institutions. We know the advantages of carrying bonds on our books at par, or if we haven't sufficient reserves to do that, of amortizing the premium. We know we should not speculate. We know we must distinguish between the credit risk and the money rate risk. We know we must analyze our investments carefully and make use of all the expert advice we can obtain from hired counselors, investment services, bond manuals and our banking associates. All these and many more of the rules of the game we know and have tried to follow.

"That the observance of these sound principles will not eliminate worry or difficulty is known to us all. That within the limits of these sound investment principles there is a wide scope for individual judgment and error is obvious. Otherwise how could we account or the fact that many banks have drastically changed their views of the market and their policies of investment, changing from a preponderance of short to long maturities, or vice versa, within the last five years. How else could we explain the fact of divergent policies at the same time by soundly managed institutions. For example, one important financial institution follows the practice of buying government issues the moment they go to or approach a no-yield basis. Another, equally important, sells these issues as they move to a no-yield basis. . . . .

"It is our unfortunate lot to be faced with a problem in this matter which cannot be evaded. We cannot, however difficult it may be, give up the problem as insolvable, nor can we turn it over to some magician, who can amaze us by a deft working of the puzzle. Increasing deposits pour into our vaults. Decreasing demand for funds from local borrowers leaves a constantly growing volume of cash to be invested. Increasing cost of bank operations press urgently upon us the need for earnings. And against this stands our never-to-be forgotten responsibility as custodians of the people's savings.

"Under these circumstances, what can this committee do, having in mind that a great many of our members are from small institutions in which the difficulties of the problem are somewhat intensified by the smallness of the investment portfolio and the unavailability of trained and experienced investment counsel?

"No dogmatic answers to these problems can be given. The general principles, so frequently stated, are of necessity, perhaps, too broad to be of much help."

The Committee recommends that in connection with bankers group meetings such as State bank conventions, that conferences be held to study the problems uncovered. Tentative conference plans have been prepared, along with programs, and such plans are available for your use. This, we think, is splendid and constructive work by Mr. Bimson's Committee, and we do hope that State Associations will immediately profit by it.

Another matter of very general interest is the work done by the Committee on Real Estate Mortgages under Chairman Russell M. Daane, Executive Vice-President of Plymouth United Savings Bank, Plymouth, Mich. The particular studies embraced uniform mortgage law and uniform mortgage foreclosure procedure. The statutes in some States are cumbersome and more or less obsolete. In many cases, the law is thought to directly hamper mortgage activity. A great burden in some instances is placed upon the borrower by making it necessary for lending institutions to charge a greater rate of interest or to lend a smaller percentage on security than would have been possible had the statutes been equitable. There is great variance in foreclosure costs and in the time necessary to foreclose. In New York State, where 3,500 cases were analyzed, the average cost of foreclosure approximated $490; the average time of foreclosure was four months. It has been estimated that $4 out of every $5 spent for foreclosure in New York State is a kind of legalized waste. Texas has the shortest foreclosure time; about 21 days is required for publication and the average cost of foreclosure is $5.18. Massachusetts has what has been termed the ideal foreclosure procedure. A $5,000 mortgage can be foreclosed for $30 and requires only 60 days to accomplish this. Our Committee is cooperating with such organizations as the American Bar Association, Federal Home Loan Banking Board, U. S. Building and Loan League and others. The goal they are seeking is uniform real estate mortgage procedure and foreclosure law. This is an ambitious program and one which will require years to accomplish just as did the uniform negotiable instruments law. There seems no good reason why it cannot meet with equal success. The work of this Committee is certainly to be most highly commended.

The Savings Division obviously is also interested in legislation. We have our Standing Committee on State Legislation. Chairman is Vice President of the Savings Division. A. George Gilman, President, Malden Savings Bank, Malden, Mass. This Committee is a sort of watch dog of State legislation which might affect savings banks. Regarding the legislation of the States as a whole during the past year, either proposed or enacted, there was no law of vital concern to the Savings Department, either beneficial or restrictive, enacted. This is an important Committee, but its duties are important in any one year only to the extent that banking legislation is enacted. This would seem to be an off-year in that respect.

The Committee on Federal Legislation has as Chairman, W. W. Miller, President of Bloomfield Savings Institution, Bloomfield, N. J. It is the purpose of this Committee to keep a watchful eye on Federal legislation affecting savings business and to cooperate with the American Bankers Association Committee on Federal Legislation. At the spring meeting of the Administrative Committee of the American Bankers Association and of the Executive Council there was a discussion of HR-5535, later superseded by HR-6971. This is a bill to amend the Federal Home Loan Bank Act, the Home Owners Loan Act of 1933, Title IV of the National Housing Act, and for other purposes. The American Bankers Association Committee on Federal Legislation was instructed to attend the hearings and to take whatever action the Committee felt was desirable. The bill was reported out of Committee, but was not considered by the House before adjournment intervened. The Savings Division cooperated closely by having representatives from various parts of the country attend the House hearing and present testimony. In general, our testimony was in opposition to the proposed legislation, just as we were opposed to the Bulkley Bill in the preceding Congress. We pointed out that there was a continuous effort to drift more and more away from the expressed intent of Congress and that this treatment is against public interest. It was our opinion that a very pronounced effort was being made to make of these Federal savings and loan institutions banks of deposit, thus projecting a third banking system upon the country. The chain of legislation leading up to this point clearly shows that Congress' purpose was to assist in home loans and home financing. With that program and with that objective the banks of the United States were in accord. The words, home loans and home mortgage were emphasized throughout all earlier related legislation. The hyphenated words home loan and home mortgage appeared in the Federal Home Loan Bank Act of 1932, and in the Home Owners Loan Act of 1933 when an amendment of that Act provided for the organization of Federal Savings and Loan Associations. The hyphenated word "home-loan" has been used thousands of times since, including the new House Bill 5535. This leaves no doubt that the original purpose and the continuing purpose of Congress has been that of providing home loans and home mortgages, and not some other kind. This new legislation flagrantly proposes to change all of that. In its very first section it proposed to change the words home mortgage and substitute the words first mortgage, so that the word home is completely eliminated. We believe it to be a dangerous procedure and one which tends to change completely the character of the institution. There are many other proposed changes which at this time are too lengthy to discuss, but those interested can obtain them in detail by procuring the copy of the hearings before the House Committee. If proof were needed of the correctness of our position in regard to the bill, it can be found in the letter of Marriner Eccles, Chairman of the Board of Governors, Federal Reserve System. The letter is addressed to Henry B. Steagall, Chairman, Banking and

Currency Committee, House of Representatives and dated June 7, 1939. Mr. Eccles says in part:

"The proposed bill contains a number of provisions leading to these ends and in my opinion its enactment would tend to establish a separate and complete banking system which would compete on favored terms with savings banks and the savings departments of commercial banks. I, therefore, do not favor its enactment."

So says Mr. Eccles. So says the Savings Division of the American Bankers Association.

Report of Committee on Nominations

President Williams: I should like to call for the report of the Nominating Committee. We have changed the order of procedure somewhat, in this respect—we thought that it was fair and a beneficial thing as far as the Association was concerned to give some time and thought to the nominations, and the Nominating Committee therefore was selected weeks ago, so that the names they bring in will be names that have been thoroughly considered. I should like to ask Charles Deppe of Cincinnati to present the report of the Nominating Committee.

Mr. Deppe: Your Nominating Committee proposes the following candidates for the various offices:

For President—A. George Gilman, President Malden Savings Bank, Malden, Mass.

For Vice-President—Roy R. Marquardt, Assistant Vice-President First National Bank, Chicago, Ill.

For the Executive Committee:

(One year)—W. W. Slocum, President United Savings Bank Detroit, Mich.

(Two-year term)—W. R. Bimson, President Valley National Bank, Phoenix, Ariz.

Charles F. Chubb, President Dollars Savings Bank, Pittsburgh, Pa.

(Three-year Term)—Henry M. Hart, Vice-President National Bank of Commerce, San Antonio, Texas.

Fred F. Lawrence, Treasurer Maine Savings Bank, Portland, Me.

Oliver W. Roosevelt, First Vice-President Dry Dock Savings Institution, New York City.

Respectfully submitted,

E. L. ROBINSON

F. J. COLWELL,

CHARLES H. DEPPE, Chairman,
Nominating Committee.

Mr. President, I move that the nominations be closed and that the Secretary be instructed to cast the ballots for the candidates named.

[The motion was seconded.]

President Williams: Are there any remarks? Any other nominations? If not, all in favor of the motion signify by saying "aye"; against. It seems to be unanimous, and, Mr. Secretary, you are instructed to cast the ballot.

Secretary Albig: The ballot is cast.

President Williams: The ballot is cast, and now we have some new officers. I might say some of these names that were mentioned were men who, for some reason or other, had just been given a one-year term. There will be no installation for them. They have just had two years added to their term to make it complete. Some of the other men who have been elected are not here. You know conditions that have kept a number away from this convention, and, as far as we were concerned, they were not notified that they were to receive this office because you never know, something might slip. So the only new member of the Executive Council to be installed is Mr. Lawrence.

TRUST DIVISION

AMERICAN BANKERS ASSOCIATION

Forty-Third Annual Meeting, Held at Seattle, Wash., Sept. 25, 1939

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Meeting for Elections Only

The Trust Division of the American Bankers Association convened at the Olympic Hotel, Seattle, Wash., at 1:00 p. m. Sept. 25, Samuel C. Waugh, President, presiding. There were no addresses, the business before the meeting being that of the nomination and election of officers.

Roland E. Clark, Vice-President of the National Bank of Commerce, Portland, Me., was elected President of the Division; Carl W. Fenninger, Vice-President of the Provident Trust Co., Philadelphia, Pa., was elected Vice-President of the Division.

The following seven men were elected to membership in the Executive Committee of the Trust Division:

Richard G. Stockton, Vice-President, Wachovia Bank & Trust Co., Winston-Salem, N. C.

Louis S. Headley, Vice-President, First Trust Co., St. Paul, Minn.

Preston B. Doty, President, First National Bank, Beaumont, Texas.

A. V. Godsave, Vice-President and Trust Officer, The Pacific National Bank, Seattle, Wash.

James C. Shelor, Trust Officer, Trust Co. of Georgia, Atlanta, Ga.

Henry A. Theis, Vice-President, Guaranty Trust Co., New York, N. Y.

Joseph W. White, Trust Officer, Mercantile-Commerce Bank & Trust Co., St. Louis, Mo.

STATE SECRETARIES SECTION

AMERICAN BANKERS ASSOCIATION

Annual Meeting, Held at Seattle, Wash., Sept. 25, 1939

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Advantages of Bank Research Program in Association Plans

By DON E. WARRICK, Secretary Indiana Bankers Association

In 1937 our President, Mr. Enlow, decided, with all the research going on in the country, it might be wise for us to undertake some research in Indiana, and he appointed a committee and outlined a program. Just told them he wanted to do some research. Bob Meyer was delegated by Mr. Enlow to undertake that as Chairman, and after some study the committee decided to make an investigation of what had happened in the last 20 years of banking in Indiana, and we secured the services of the School of Business of the Indiana University who did the fact-finding for us. It entailed some expense, some $300 or $400. They had to go to St. Louis and Chicago, and maybe a trip to Washington, and gather some factual information, and then they prepared the information and did the journalistic work, and our committee, in cooperation with them, edited it.

That was the first part of the report. The second part had to do with merchandising bank services. We recommend it as to the service charges and trying intelligently to sell the service departments of our banks to the Indiana public.

The next year the committee decided to make an examination of the assets structure of our Indiana banks because they had noted in the 1937 report such a transition in the asset structure of our Indiana banks which I guess was typical of the Nation, where back several years ago very few of the banks had what might be called investment portfolios. And then we all recall the days when bank examiners were advising the banks what they were needing was secondary reserves, so they made an examination of the earning assets of our Indiana banks, touching upon loans and discounts, and they dealt with the new personal loan departments and consumer credit picture that was coming to Indiana, the Bankers' Bond Act, analyzing the bonds, commenting upon the bond policies as to marketability, maturity, distribution, ratability and liquidity.

Of course, we have in Indiana a system whereby our bank examining department in our State take a bond account of the State bank and keys it, then they send it to the School of Business at the Indiana University, and they have a staff there, supervised by some members of the faculty of the School of Business, who analyze this bond account as to marketability, diversification, ratability, and then they send this analyzation with their comments back to the banking department, and the banking department, in turn, turns that over to the bank under examination. Indiana got the idea from Minneapolis. Some of the same people who do that for the Department of Financial Institutions in Indiana did our work in this research project on bonds.

Then the next year—all of you have seen these booklets, I think—we sent them to every State Association. The next year it was decided that we would undertake an examination of bank personnel, that is the last project we have completed. That was also done by the School of Business of the Indiana University, job analysis, specifications, salaries, financial incentives and non-financial incentives, working hours and conditions, and we bore quite a bit upon the hours for the working conditions of employees and hours by which the employees might work in the light of the current Wages and Hours Act and its application.

We have felt in Indiana, I believe, that the majority of banks have felt that the effort and money expended has been worth while. It is hard to prove that tangible but we have had a lot of comment on the service as fine educational medium to the banks in some of the elementary as well as the fundamental principles of banking, and we think, all in all, that we have been repaid.

I think the last project cost us something like $1,500, including what we donated to the School of Business to defray their expenses, clerical help, &c., in printing these books. This was more expensive (indicating) because it is thicker.

We ran into a very interesting situation in this last project. We had on the faculty from the School of Business some of those gentlemen who are sometimes referred to as "rather liberal in their thinking," and they wrote a chapter (this was quite an issue) upon "Labor Unions in Banks." I think there were four or five of them in on it. They took the attitude it was coming, couldn't be stopped, and the only wise and constructive and intelligent course for us to pursue was to recognize its coming and deal with it accordingly, and they were very much disappointed that our committee refused, after quite a bit of pressure, to incorporate that chapter in our book.

I believe that is all. That gives you a bird's eye picture of our work in Indiana.

All Year Program for State Secretaries

By HAYNES MCFADDEN, Secretary Georgia Bankers Association

At the risk of seeming to begin by wandering from my subject, there is one factor in Association work that promises to demand our most studious application. That is the multiplication of meetings. No man lives to himself alone, and State Secretaries, in particular, are finding their duties spread over constantly increasing areas. They do now, in fact, cover every unit or subdivision of the earth's surface from a county to a continent.

In the old days when a Secretary's domain stopped at the boundaries of his own State, he led the simple life. Since the advent of the thrilling '30's banking has become rapidly more and more complex. The interests of our members have led us into a variety of new fields of interest. Each of these segments or tangents of the banking circle requires the Secretary to possess an accurate working knowledge of its foundations, its operation, its overlapping and its dovetailing with every other segment it touches or concerns.

Typical of these segments and tangents of the banking circle that impose new duties, straight thinking and extracurricular activities, so to speak, on the part of the State Secretaries are such agencies as:

The Federal Deposit Insurance Corporation
The Federal Reserve System
The National Bank Examination Serivce
The National Association of State Bank Supervisors
The Reconstruction Finance Corporation
The Commodity Credit Corporation
The Federal Labor Relations Board
The Congress of Induscr'al Organizations
The Securities and Exchange Commission
The Federal Housing Administration
The Federal Savings and Loan Association
Social Security
Et cetera and ad infinitum

Your memory may supply others I cannot think to name, but certainly every name in the calalog I have listed is an extra string to your bow. No Secretary can keep up with a single one of these stories in our modern tower of Babel by merely reading something out of a book. You have not only got to read a whole library, you have got to master every facet of the banking mind, every interpretation and angle of thought, and then through the maze you have got to steer a straight course. You have got to be true not alone to your Association as a whole, you have got to be true to every single member; not minus one, but 100%.

To make a success of the job requires as delicate a balance as a high wire walker, and your only safe balancing-pole is your daily contact with the banking fraternity. This may be an interview with an individual, a conference with a committee, a hearing in the halls of Congress, a convention of bank examiners, or what have you.

Then right under our own umbrella we have national conventions, the nation-wide Graduate School of Banking, regional conventions, State bank study conferences, State and local A. I. B. activities, group and county meetings, the nation-wide mid-winter trust conference, regional trust conventions, State trust conventions, regional bank management conferences, and in the majority of grand subdivisions of the country an annual conference of the State Secretaries themselves.

We are literally meeting ourselves to death, yet every one of these meetings has a definite purpose and a logical and useful destination. There is a certain group that derives a positive advantage from each of these meetings. The Secretary says grace over them all. There is still a certain overlapping that has a tendency to defeat the purpose of more or less all of these meetings. By way of illustration, it is impossible for a small bank to attend all of the meetings in which it has a natural interest. The highly departmentized bank can solve the riddle by sending different men to different meetings.

That is the bone I am throwing in the ring. I don't pretend to know the answer. It demands our best thought, the simplification and systematization of the bank meeting schedule in its most general sense. Some day some new Daniel will rise up who is smart enough to work it out. It is a process of evolution, and the closer our application to its study the faster this process of evolution will be speeded up.

It is my very definite conviction that what the average Secretary needs is not an all-year program, but a year with about twice the usual number of months so that everything he has to do can be squeezed into it.

At the same time I want to avoid emphasizing the so-called extra-curricular activities to the injury of established routine. Each association must possess a variety of appeals to a diversified membership. Each association has a well-rounded committee organization. The sequence of its functions is not so important as it is to lay out a consecutive and systematic work program and to follow it, though the heavens fall. You have one year that begins with the calendar, another year that begins or ends with your annual convention, and a fiscal year that is marked by the collection of membership dues. There is no uniformity in the turn of the latter two annual periods, so in 49 different associations we will naturally follow 49 different or modified sequences.

You have one set of members who figure they get their money's worth if your farm program clicks; another set of members gauges your usefulness by the character and success of your efforts to enact beneficial laws and defeat injurious legislation; another set puts the loud pedal on the association's leadership for concert of action in service charge enforcement and the spread of correct bank management rules and principles; another set is chiefly concerned with the promotion of uniform practice among banks exercising trust powers; the younger generation is best served by a militant A. I. B. committee; the public relations program from the association viewpoint is enlisting an increasing number of disciples, and many members are wrapped up in the success of the annual convention, or the bank study conference, or of their respective group meeting.

The sky-line literally bristles with opportunities for useful service. The desired result can never be obtained by the blundering blows of a blind giant. The important thing is the system. Set up a definite schedule for the work program and synchronize your convention year, your fiscal year, and your calendar year, so that each will keep step with the other. Combine with the activities I have mentioned many others that I have omitted for the sake of brevity, and you will find yourself in possession of an all-year program, an every-month, every-week, every-day program combining the greatest usefulness to your members with the greatest satisfaction to yourselves—a good job well done.

Need of Co-Ordination of Bank Regulations

By CHARLES F. ZIMMERMAN, Secretary Pennsylvania Bankers Association

Mr. Chairman, perhaps I might refer to something that would be of use to some of the Secretaries here under the head of New Business, by offering a suggestion regarding a project we have taken on in Pennsylvania.

We happen to have as President of the Pennsylvania Bankers Association a very live, courageous country banker. He has made it his business to tour the State, visiting the small banks throughout Pennsylvania.

As the result of that visitation he has been sold on the idea that the greatest service that the other member banks can render is to . . . send in to a committee, information that has to do with the handicaps placed upon the conduct of the business, particularly of smaller banks, as the result of supervisory policies resulting from Federal regulations.

There has been a lot of legislation that has been imposed upon the business of banks, and much of it hasn't a thing to do with the solvency of a bank. . . . The result of all this is that as far as the President of our Association is concerned he wants to see the A. B. A. start out and render a service to the smaller banks in our State in their defense.

My observation doesn't refer to the Comptroller's office or to the Federal Deposit Insurance Corporation or to the Federal Reserve Board. My criticism is against the system as a whole which needs coordination and straightening out, and it can be done if the practical bankers of America will get in and help to do the job. . . .

Under a Senate resolution, for the first time in a decade the small banks of this Nation have an opportunity to be heard in their defense, because Senator Wagner has promised that he will permit the rights and privileges of banks to be recognized in the Senate hearings, and so we believe that is a real opportunity. If you men would talk to a lot of the small bankers in your State I think you would find you could do a very signal service in that respect also.

Please don't get the idea the Pennsylvania Bankers Association wants to find any place in the sun in respect to Federal legislation. We are starting a ball rolling, and we thought through the State Bank Division of the A. B. A. and through the Legislative Committee of the A. B. A. and through the executive officers of the A. B. A., perhaps the Research Council, we can put two and two together and help to do a job for the good of the independent unit banking system of this Nation.

COMMITTEE AND OFFICERS' REPORTS—STATE SECRETARIES SECTION

Remarks of James E. Baum, Secretary of A. B. A. Insurance Committee

Only a week before we left New York we had our annual conference with the National Bureau of Casualty Insurance Underwriters, regarding rate reductions, on bank burglary and robbery insurance. Briefly, if we use the same formula that the Underwriters' National Bureau has used for more than 20 years, the smaller banks of this country, at least five or six thousand of them, maybe ten, are entitled to another reduction in burglary and robbery rates, approximating 25%. The Bureau has come forward with the plea that the premium income has dropped so much in recent years as to make the total of 550 odd thousand dollars too small for rate adjustment purposes; that is, too small a base for clipping off a reduction here and there, but I submit our whole argument with them a few weeks ago was based on their own formula which, as I said, has been used for more than 20 years, namely, 25% loss ratio, mea ing 25% of each dollar going back to the banks in losses, based on five years' past experience, as a base. Using that formula, the banks of this country which use burglary and robbery, with payrolls as a primary, are entitled to 25% reduction as of now and last month.

I doubt, however, if we can get that, unless we can arouse the insurance departments of some 45 States into action, by your State associations' protests.

I am speaking about it now simply to emphasize the importance of it in this meeting, and I will follow it up with an explanatory letter with figures, premiums and losses and whatnot in a few weeks, and I do hope you will get busy with your insurance commissioner and let him know this is the Underwriters' own formula you are talking about.

The other item which has the same approach, that is the insurance departments in your States, namely to get your insurance commissioner (and there are about 20 of them that need some inspiration on this) to insist upon the new fire insurance policy, the new later 1939 form that was approved by their own National Association of Insurance Commissioners in San Francisco last June. I don't think it is possible to exaggerate the importance of this fire policy. We have some idea how important the insurance is on property. There are so many kinds the banks loan on, or own; in many cases the fire insurance contract is the last bulwark for collateral and I can stand here an hour and a half and not cover the weaknesses of the three forms used in this country the last 10, 15, 20, 25 years—fire insurance, only.

Briefly—there were two different New York forms in use in about 30 States, 35 States, and then in the other 13 States a so-called "Massachusetts" form has been used.

Now, this is of great importance not only to the banks but to their multitude of customers, who aren't borrowing on property. You can help them immeasurably by insisting upon the Insurance Department of your State forcing the adoption of that new 1939 form, which, briefly, does this:

It brings up to date the three forms which, as I said, are already antiquated. One of them, for example, the new New York form, so-called, was written in 1918, and the old New York form is about 35 years old, the Massachusetts form is about 40 years old, and each one of those forms, in order to make them conform with up-to-date conditions as nearly as they can, are plastered with all kinds of indorsements, any one of which might be adopted.

If they haven't all the indorsements on them, a loss might occur which is not covered but which would be covered if the indorsement had been there; but companies for the most part are against this new policy, and that accounts, perhaps, for the close vote which was tabulated here in San Francisco, when the commissioners voted 16 to 11 in favor of the new form.

There are very few States that have really come out openly against the form and I can't give you the names of the 11 States that voted against it, but when you get my letter in a few weeks, I do hope you will find time to study it carefully and see the differences between the new forms and the old forms, even though they have indorsements.

There are a lot of advantages on the new forms not on the old forms. They will be a great service not only to your bank but to the bank's customers throughout the country.

Report of Committee on Nominations—Newly Elected Officers

C. C. Wattam, Fargo, N. D., Secretary of the North Dakota Bankers Association, was elected President of the State Secretaries Section of the American Bankers Association at the Section's annual meeting, Sept. 25.

L. S. Scarboro, Denver, Colo., Secretary of the Colorado Bankers Association, was elected First Vice-President, and Armitt H. Coate, Moorestown, N. J., Secretary of the New Jersey Bankers Association, was elected Second Vice-President.

William Duncan Jr., Minneapolis, Minn., and Lauder Hodges, San Francisco, Calif., Secretaries of the Minnesota and California Bankers Associations, respectively, were elected to the Board of Control.

ROUND TABLE CONFERENCE

AMERICAN BANKERS ASSOCIATION

Meeting Held at Seattle, Wash., Sept. 27-28, 1939

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CONTROL OF INTERNAL OPERATIONS AND EARNINGS

Three talks were given under this head, by respectively, J. L. Dart, R. C. Tait and K. C. Bell

Expense Control for Better Earnings

By J. L. Dart, Vice-President Florida National Bank, Jacksonville, Fla.

There is an unqualified certainty in the meaning of the subject I have been asked to discuss today that is pleasant and quite refreshing. We need not concern ourselves with a variety of possible meanings, interpretations, or translations. The subject is unequivocal: "Expense Control for Better Earnings." It does not say or imply that possibly we could have better earnings if we controlled our expenses, or if we could control our expenses, but is a direct and positive statement, meaning but one thing and that one thing is simply this, we can improve and increase our earnings by controlling our expenses. I am sure every one of you has heard not once but many times that old saying, simple, yet filled with such sound philosophy and truth, which goes something like this—"It is not what you make but what you save that measures success." Underlying a considerable portion of my remarks will be the idea that controlled expenses positively prohibit the spending of money uselessly, foolishly, or unwisely. In other words, one approach, probably the most important one, will be upon the principal that for every dollar spent in operating costs we must secure 100 cents, or whatever a dollar is worth, in value.

I am tempted to assert—in fact I shall do so—that not a person present here today would object to learning how he might increase his bank's undivided profit account without augmenting its income by a single penny. I am quite sure I should not object to receiving such information, and I am not, please believe me, intimating for a moment that I know the absolute and undisputed answer to that problem.

I have the good fortune to be connected with a splendid bank, located quite some distance from Seattle, in Jacksonville, Fla., which has had during the past two years average deposits of $35,000,000 in round figures. Compared to many banks in the country the one with which I am connected is a small bank and this, together with the fact that my experience in that bank dates back to the time when its deposits were 2½ million dollars, probably makes it permissible for me to counsel with those from that great majority of banking institutions throughout the country, those that are in the final analysis the backbone of our American banking system, the small banks.

It is my sincere hope that some of the things pertinent to my subject that I shall discuss today, ideas that experience has taught me are well worth serious consideration, may strike a responsive chord in some of you gentlemen, with the result that after consideration and serious thought they will prove beneficial to you and your organization's profit account.

Obviously, or perhaps I should say theoretically, better earnings can be obtained by increasing income. I use the word theoretically mainly because increased income in this day and time, due to certain competitive agencies over which we have no control and to certain oppressive powers and policies of a regulatory nature, is largely, if not entirely, a matter beyond our dictation and in the realm of conjecture. Our subject, however, makes no mention of income and since it refers to earnings only as they are affected by controlled expenses, we shall eliminate that problem from our discussion.

I feel certain you will agree it is reasonable to assume that before we can control our expenses or costs of doing business we should be reasonably conversant with them. We should have at least a fairly good knowledge of them and know why they are what they are and what their dollar value means in point of service or usefulness to our operations.

The larger metropolitan banks of our country have made remarkable progress in the installation of cost finding procedures, and have, through their efforts and experiences along this line, contributed much to our general knowledge of operating and per item costs. I do not feel, however, that it is absolutely necessary, desirable as it may be, for us to install or provide an elaborate system of determining costs in order to benefit and to control our expenses. A simple workable system, easily adapted to even the smallest bank, is productive of much good, and if properly applied and used can save many, many dollars. Booklets numbers 5, 9, and 15, especially number 15, prepared under the supervision of our Association's Bank Management Commission, are valuable and informative contributions on this subject, and I commend them to your serious study and consideration.

I shall not dwell on the subject of per item costs as applied to service charges for, while I readily admit that earnings can be increased by their installation, that application of them appears aside from the subject we are discussing, namely Expense Control, being rather in the realm of Increased Income. For the purpose of our discussion, however, I believe you will find their determination most valuable, not only for comparison with similar figures from institutions comparable to yours in size and type of service rendered, but also because I am sure that in so doing you will find some things now overlooked in your operations that can be eliminated or changed, quite likely with a reduction in operating costs. However, for the purpose of expense control the mere determination of per item costs is of little value unless you make use of the information. Compare your figures with your neighbor, with other banks, with average figures from groups of banks in your section of the country or the nation as a whole. Find out why they differ, let your curiosity run rampant so to speak, and in the answers you get regarding the difference between your figures and the others you will have a valuable lead to reduce and controlled expenses, or you will have performed a service to our profession by giving the other fellow something to think about.

Suppose, for example, your item cost of "on us checks" were out of line with those of another bank comparable in size and type of service rendered, and you learned that the other bank obtained the more favorable cost figure because of a different method of posting its ledgers, permitting it to handle the same number of items with several less bookkeepers than you require. Would such information be useful to you? Would it result in a decrease in your operating cost? Similarly, comparisons of other costs may reveal ways in which you can reduce and perfect methods of controlling expenses. So I repeat, one suggestion for increasing your earnings through expense control is to compare your expenses with other banks and give serious and thoughtful consideration to the adopting of those procedures found profitable by them.

It has been my experience that no matter how careful you might be or think you have been, that at any time you go to the trouble to prepare a detailed and itemized list of expenses charged to a certain account such as stationery, advertising, subscriptions, memberships or donations, to mention a few, you will find many dollars spent for things and services the value of which is decidedly questionable. This, therefore, is another thought that I suggest you follow, venturing the assertion that if you do so, studying carefully and seriously the appropriateness of each expenditure in the light of usefulness and profit to your bank, many charges made during the period under review will not be recurring items in the future. Naturally each such unwise expenditure eliminated means that your net earnings have increased by that same amount.

In reference to control of expenses for stationery and printing let me suggest a few things that you might profitably consider, realizing full well that at first thought they might appear penny wise and pound foolish, but assuring you that many dollars can be and have been saved by banks willing to approach seriously this matter of reducing expenses. Do you have adequate facilities for housing your supplies of stationery and printed forms? Is there any attempt made to control their distribution to the various departments of the bank? If improperly housed considerable loss will result in a year's time by dust and injury and if no one attempts to control its distribution considerable waste is inevitable. What about the size of the various forms you use? Can they be redesigned so that by permitting the printer to use all of a certain size piece of paper their cost can be reduced? Can they be purchased in larger quantities at a cheaper price? Can they be printed on a cheaper grade of paper? Do you receive competitive bids on orders of any size? In other words, do you buy your supplies or does some one sell them to you? Are pads of deposit tickets placed on your customers' counters used by them as office or home memorandum pads? If so, the printing of certain rules or an ad on the back might cost less than the cost to you of supplying such convenient scratch pads. Maybe putting them up in smaller pads or having them unpadded would prove profitable to you. Have you considered the advisability of doing your own printing?

Membership, Subscription and Donations

A few hours thoughtfully spent in consideration of the items that appear on a list of such expenditures will no doubt show several opportunities for reducing this classification of expense. Are you getting face value from the various organizations you think you must join? How about the large number of periodicals that clutter up the post office box of the average bank? What value do you receive from them? I dare say you will find several duplications, if not in the periodicals then in the service or information that they are furnishing. If a certain official wants one magazine and another a different one, both furnishing the same information, maybe one subscription could be eliminated and both officers share the one periodical. Careful consideration ought to be given to expenditures of this character, many of which come from depositors particularly interested, especially when they can only be justified on the ground that a certain customer suggested them.

Another vexing problem, and an expense frequently hard to control, is donations. Here again many of us give all too much consideration to who is making the request and all too little to the good the granting of such request will do. Banks are considered legitimate prey for every organization, club, association, or group that think they need money for any purpose whatever, and I realize it is easier to talk about saying no than to actually say it.

Relief can be had, however, by cooperating with your neighbor bank or by clearing house agreement under which such expenditures are limited and controlled, or by setting up at the first of each year a budget figure for such expenditures. Frequently we are afraid to say no but I have seen the straightforward statement that no provision had been made in the budget for such a contribution or expenditure accepted without question and with no unfavorable reaction. This applies also to the many opportunities the average bank has for the purpose of schemes, systems, and new business ideas.

Budgetary Control

I had intended to talk of budgetary control a little later but since I brought up the subject a moment ago I will do so now. For a budget to provide the highest degree of control an accrual system of accounting is necessary although excellent results can be obtained and many dollars of expense saved by its use even when income and expenses are reflected by a cash basis of accounting. I purposely spoke a few moments ago of the desirability of making an itemized and detailed list of various expenses. My reason for doing that was two-fold: First, as I suggested, for the opportunities such action would give for consideration of the usefulness of such expenditures, and second, for the reason that you then have a figure to use in preparing your budget for that expenditure for next year. Follow through with all of your expenditures in like manner and set up, on a basis of previous experience, less the useless expenditures, the amount you should spend for that particular classification of expense next year. If you will then break down these figures into monthly amounts and compare them each month with the amounts actually expended, as well as with the figures for the previous month and the accumulated year to date, both cash and budget, you will have provided a most important procedure for the control of your expenses. Variations will occur of course—increased business, additional personnel, increased taxes, rising cost of supplies and many other things will be the cause—but the important thing is, you will have before you in black and white comparative figures that can't help but challenge your curiosity and demand an investigation as to why the difference. An increase for instance in your light and power bill over the budget or over last month's figures might show that some lights are not being turned off when not in use or that fans are left running after working hours. Again let me repeat, the opportunity afforded by such comparisons for reducing and controlling expenses is almost unlimited. A careful check of your long distance telephone calls and telegrams may show the unnecessary use of such services, with a letter answering the purpose just as well and at considerably less cost.

Efficiency of Operations

A matter that should be given the utmost consideration is the question of your routine operations. Does the work flow through your bank in an efficient and speedy manner or do you find bottle necks and traffic jams that impede its progress and movement? For the maintenance of proper safeguards and records an item in passing through the bank must be handled by several persons or departments and if its progress is impeded at any point operating efficiency is lacking and expenses begin to pyramid. It is, I know, frequently difficult to keep every one busy at all times, but the inauguration of systems that permit an even flow of transactions through the bank is an excellent way to reduce operating costs. This not only frequently results in reduced personnel but also allows a fuller utilization of your equipment.

If you will pardon another personal reference, I will cite two instances in my own bank where thinking along this line has resulted in improving efficiency and lowering operating costs. In the early hours of our banking day our transit department is concerned with the proving in and distribution of the incoming cash letters lent us by our correspondent accounts. This must be accomplished by 10:30 in order to make sure all local items thus received enter our clearings of that day. A very small volume of deposits are received over our counters until noon, and from that hour until closing time such transactions are quite numerous. A sizable crew is necessary to keep this work flowing to the bookkeepers and other departments, and after this is accomplished we are concerned with the dispatching of foreign items so received to our correspondents for credit or remittance. It has been found possible to coordinate these functions and to make full use of the personnel and equipment necessary by the following procedure: The entire transit and proof departments, during the first two hours of the day, concentrate on first proving in the cash letters received from our correspondent banks. A small crew then takes up the function of the proof department, proving and distributing the small volume of deposits that have been received by this time, while the remainder of this force prepares cash letters to our correspondents for credit and remittance, effecting a balance of them against the figures used in proving them in a short time previously. This means that by lunch time all cash letters have been proved in and all foreign items received therein written up on our outgoing cash letter forms and proved. Upon returning from lunch the entire force centers its efforts to the proving and distributing of customers deposits, and then, leaving a skeleton force to balance the proof department and prepare the local items on other banks for clearing the following day, the remainder of these clerks complete the outgoing cash letters with the foreign items received over the counter by either adding them to the letters prepared during the forenoon, made up of items received from our correspondent banks, or by writing up additional ones. This, as I said, enables us to make the fullest use of both personnel and equipment.

Another procedure that has resulted in saving considerable time, in addition to permitting us to reduce the personnel of one department, has to do with the analysis of our correspondent accounts. Formerly our analysis department obtained float figures and exchange costs, used in analyzing our bank accounts, the day following the receipt of the cash letters, not from the items but from the cash letters. This meant that on the day they were received a certain separation was made of them for distribution to the various racks and departments, and they were of course listed for proof purposes. Then the following day the analysis department employees took the cash letters and from the description thereon calculated the float and exchange cost on the non-par items. This virtually meant that in the entire process these checks were being handled twice. By separating these items in the transit department for proof purposes according to the outstanding time necessary to effect their collection and in conformity with our method of clearing them through our correspondents, we have obviated the necessity of our analysis department's calculating the float or exchange, since this information is now obtained as a by-product of the proof operation and the figures showing outstanding time and non-par items are noted on the back of the incoming letters when they are proved in.

I am quite aware that there is nothing unusual about these procedures and am also aware that many of your possibly are doing the same thing, but I mention them solely for the reason that they do represent definite ways in which expenses can be reduced and controlled and the efficiency of routine operations increased. I also mention them in the hope that they might cause you to think about some operation in your bank, with the result that some ideas may suggest themselves and your expense account benefit accordingly.

New and improved mechanical equipment is constantly being developed and perfected, and much of it is worthy of consideration. Its installation has in numerous instances improved routine operations and reduced operating costs. I am not advocating the purchase and installation of every new device or machine that is placed on the market, but am suggesting that in your attempt to control and reduce expenses you consider their possibilities to this end.

Salaries account for some 40% of your total expenses and it is only natural to suggest that they possibly might represent a fertile field for consideration in this question of expense control. Note I said consideration, and the idea I am trying to present is the taking of steps to see that you receive commensurate value for the amounts paid. I firmly believe the laborer is worthy of his hire and that we have a golden opportunity to benefit our organization and the men and women who perform the multitudinous daily tasks necessary in its operation by encouraging them to become better qualified to perform those tasks through education and training. No matter what the task is, an unskilled and untrained worker cannot perform it in the most effective or efficient way, nor in a manner that reflects credit to his institution. If this is true the dollar values we receive from employees who are paid small salaries, or more important, who are only qualified to earn small salaris, must of necessity be less than we receive from the larger amounts paid to trained and educated employees. Recognition of those employees who are seriously and honestly trying to improve themselves by pursuing the courses of study available through the American Institute of Banking or other educational institution is bound to benefit your organization, because the efforts and performance of those individuals who are improving their mental capabilities cannot help but give you a more efficiently operated organization, with increased business and profits the inevitable result.

I should like to refer to my earlier reference to the part comparisons play in expense control. My knowledge of the benefits to be derived and of the savings that can be made by such comparisons is the result of experience with an accrual accounting and control system successfully operated for over eight years in the bank with which I am connected. Through its operation a daily picture is presented showing the bank's daily income from every class of earning asset, predicated on calculations made for each note, security, mortgage, or item, as the case may be. This is tabulated on a form and compared with the same date of the preceding month, accumulated quarter to date compared with accumulated figures for previous quarter, and accumulated year to date compared with accumulated to date figures for the previous year. Expenses are similarly compared, and for purposes of control and comparison are broken down into some 20 accounts. The difference between these daily income and expense figures is naturally the bank's net profit from that day's operation. Since we also accrue for every known operation expense, also making daily provision for dividends and reserves for contingencies, this daily net profit figure is exactly that—that day's net profits. Obviously the management, by studying this sheet—and I assure you it is the first report the Executive Committee, which meets daily, looks at—is enabled to exercise a fine degree of control over the operations, of the bank, and through it also are immediately informed of the effect of any change in policy, in earning assets, or of unusual or unbudgeted expenditures. Any difference between the current day's figures and those for a previous comparable day or period become an oral question mark and some one has to explain. Since that is usually my job I can tell you the explanation has to be good.

The sale or purchase of a block of securities, the granting of a sizeable loan or the payment of one, increases or reduces, of course, the bank's income from the date such transaction is consummated, but the point is that under our operations such change is noted that day, not a month or several months later, and steps can be taken immediately, if any are desirable or necessary, to correct, improve, or change the situation or policy of the bank.

Accordingly, the answer to this question of expense control would appear to be irrevocably bound up in control of operating procedure. By that I mean efficiency of interior routine, a thorough knowledge of costs, the budgeting of expenditure, and serious and thoughtful consideration by the management of their improvement and application.

Discussion Following Remarks of Mr. Dart

Chairman Dean: I know Mr. Dart must have stimulated in your minds some questions you would like to ask him. To the best of his ability, he will be delighted to answer any of your questions. The rest of us will be glad to hear your suggestions.

B. N. Phillips (Port Angeles, Wash.): I would like to ask Mr. Dean if he has any suggestions for State associations or perhaps groups as to what they might do in order to compare notes on salaries, costs, charges and what not. There is a committee about to be appointed in this State to work on that matter and perhaps revise our charters, perhaps study our costs. I know down in central California there is a group of banks, all about the same size and within a radius of 50 or 100 miles, that get together and compare notes on various items, salaries for bookkeepers, salaries for tellers, and maybe even salaries for vice-presidents.

We are kind of groping around here. We realize we don't know as much as we should as to what salaries ought to be. We don't know as much as we should as to what it costs to do this or that. I would like to know whether he has any suggestions for our committee.

Mr. Dart: No, sir. I will admit I have no suggestions on your particular problem. Many of the States, as you of course know, through their State associations and through research committees, are obtaining data from the various banks throughout the State and developing some very good comparisons and some very good figures.

On your question as to what you should pay an officer, I don't see how any man can answer that. What a man might make in one place for a certain type of work or for performing a certain job, would not necessarily mean that in another location he should get the same thing.

I tried to bring out the point that in my opinion salaries should be based as far as we can figure them on the man's ability and not so much on the particular routine or detail operation he is performing. The comparative figures that are being worked up, as I just said, by your State associations will no doubt prove valuable to you in arriving at some reasonable basis for figuring costs and establishing service charges. As to how best to do that, I have no suggestions, except to obtain the figures through your State associations. They will no doubt be able to get the various figures and data from the various member banks, and they can be compiled in the form in which you wish them, or the form from which you can obtain the necessary data.

William O. Grauel (Indianapolis, Ind.): You had a question there on providing forms to be printed. Does your bank have a printing establishment to do that, or mimeograph?

Mr. Dart: We operate a small printing department which takes care of all our inside forms and the imprinting of customers' check books.

Mr. Grauel: Have you found that profitable?

Mr. Dart: Yes, sir.

Mr. Grauel: We have only one bank in Indiana that I know did that, and I understand there was considerable expense to putting that in. You have to have printers to do that work, and it is a matter of getting in conflict with another line of work. In Indiana, I don't think we would get very far on that basis. We feel in Indiana that banking is a profession, and that printing should be left for the printers and those who make their livelihood in that manner.

Mr. Dart: We have naturally had that suggested by some of the printing establishments in our locality. We solved our problem in this way: We have a printer and a young assistant, and they not only take care of our printing but the young fellow is also in charge of our stockroom and has supervision over the distribution of supplies and stationery, and it is proving quite practical and economical.

L. H. Lopes (Watsonville, Calif.): Referring back to the question this gentleman from Port Angeles asked a while ago, I might state in all modesty that I am father of the little group he mentions in central California. The group was organized in 1934 prior to which time I had kept rather accurate data on our own institution without any opportunity of comparing it with similar information from other institutions. At a meeting of our Committee on Banking Practice at one time, I suggested the idea that we organize a group of 10 or 12 banks all located in agricultural territories, as ours is, and for the purpose of carrying on uniform studies, starting in with our capital structure, our gross income, and right down to the net loss or net profit, with everything confidential according to code so that if the information got out it wouldn't be of value, and still we would have those comparisons. I have worked up schedules for that, and since 1934 I venture to say there is not a member of our group who would give up his membership and the securing of this information through getting together three, four or five days a year. We take each item of income and work it out in percentage and expense. By those comparisons we have saved ourselves considerable expense.

I think it would be a splendid idea if various organizations could organize, and then maybe have a comparison of one group with another. If I could be in position to furnish any information on our group, I would be glad to do so.

Chairman Dean: May I say this also: In the Kansas Association we made some rather elaborate studies for the last four or five years in which we broke down the classification of the banks by the size of deposits. Then we held a series of clinic meetings, 15 in all, and got the active managing officers of their banks to show their value compared with all other banks in that class.

Mr. Ereidenthal, of Kansas City, Kan., conceived the idea of calling in just this group of banks, from one to two million, from three to five million, and five million and over. Those officers came to Kansas City, or some central point, and sat around the table.

Assignment of Life Insurance Policies as Collateral Security

By Robert C. Tait, Assistant Trust Officer Genessee Valley Trust Co., Rochester, N, Y.

The big increase in the use of life insurance policies for credit purposes came with the depression. First, thousands of people found it necessary to pledge their life insurance to protect the shrinking collateral against already existing loans. Second, interest rates fell and the insured found he could borrow at his bank against the cash values of his life insurance at a lower rate of interest than charged by the companies. Third, it was convenient for the insured to deal with his own local banking institution, and his life insurance provided an easy and speedy means of credit. And finally, many people had come to believe that borrowing against life insurance reserves was essentially a banking and not an insurance company function.

This last point is a moot question about which there has been considerable argument. I will not take the time here to discuss the various arguments pro and con, for I think the whole question of whether borrowing against life insurance reserves is properly a banking or insurance function is more academic than practical. The fact is that at the present time banks all over the country have insurance policies in their collateral files already assigned to them. So the problem of proper assignment is with us in any case, and it seems to me it is likely to continue to be. The insured public, moreover, has been educated by the insurance companies and their agents to regard the emergency value of policy reserves for collateral or credit purposes as one of the most important values contained in the contracts. I think this is one of the most important values, and as long as policies are written on their present basis and sold with these representations, I believe every effort should be made by the insurance companies and the banks to perfect a means whereby the insured may realize on these credit values quickly and easily in any manner he chooses.

Most of the difficulty in dealing with life insurance as distinguished from other forms of property arises from the fact that it is a peculiar contract wherein a company contracts with an individual to pay money under certain conditions to a third party. And it is the rights of this third party, the beneficiary, which have been disputed throughout the law's development on the subject, and which cause us most of our trouble. The assignment of life insurance for collateral purposes, therefore, almost always involves three parties other than the assignee—the insured, the insurance company, and the beneficiary—and the bank is sometimes not only assignee but beneficiary, as trustee under an insurance trust.

Another distinguishing characteristic of life insurance as collateral is the fact that a policy has a definite and fixed cash value which increases in accordance with a definite pre-determined schedule, providing the insured continues his premium payments, but which may rapidly decrease to the vanishing point if the insured fails to pay his premiums. Also, this cash value may be relatively small on one day and many times greater the next, by reason of the immediate maturity of the policy on the death of the insured.

A further complication arises from the fact that the enforced surrender of a life insurance policy may deprive the insured of a considerably greater value than the actual reserve at the time of surrender, because if the insured is at that time uninsurable the policy is really worth more to him than the actual reserve, which is based on the company's tables for average insurable risks. The actual value to the insured may be anywhere between the reserve and the full face value of the policy, depending upon the indeterminate factor of the imminence of his death.

As to this matter of the beneficiary, it is almost universally conceded that where the insured has not reserved the right to change the beneficiary, he has a vested interest which cannot be divested without his consent. Where the insured has reserved the right to change the beneficiary, the case law of the various States seems to be hopelessly irreconcilable. Not only are there contradictions between States but frequently within the States themselves.

This confusion with respect to the rights of the beneficiary and the extent of the insured's actual ownership of his life insurance appears to stem from the old days when life insurance was really a contract between the beneficiary and the insurance company, not the insured and the company; when a policy was merely a contract on the part of the insurance company to pay a sum of money to the beneficiary on the death of the insured, provided only that the insured paid the premiums regularly until his death. That's about all there was to the early contracts; the insured had no rights except the privilege of granting a gratuity through payment of premiums; policies possessed no surrender values, and by their very nature there was nothing that the insured could enjoy in possession during his lifetime.

With the development of legal reserve life insurance, as it is known today, this earlier concept of the contract as between the insurance company and the beneficiary changed. It became apparent that the reserve that was being accumulated in a policy was really the property of the insured who paid the premiums. Surrender values and various rights began to appear, at first simply as company practices, and then by express provisions in the contracts, and later by statutes in many States. The policy underwent a complete change: It became a contract between the insurance company and the insured, not the beneficiary; and the insured became the real owner. It also acquired a cash value which could be withdrawn or pledged as collateral security by the owner, a loan provision whereby the insurance company would loan money against the reserve, non-forfeiture provisions whereby if the policy lapsed the reserve would be applied either to extended term of reduced paid-up insurance; and the insured was given the right to change the beneficiary and to assign his policy. The law has not kept pace with this fundmental change in the character of the life insurance policy; and the effect of this early legal concept is felt in many jurisdictions down to the present time.

The cases on this subject may be divided roughly into two general groups:

1. The first group of cases holds that the beneficiary has an interest in the policy at least sufficient to require that any act of the insured which would affect his interest be done in accordance with the provisions of the policy; and that even if the insured has the right to change the beneficiary he does not have the right to make an assignment of the policy without the consent of the beneficiary unless he first changes such beneficiary in accordance with the provisions of the policy.

2. The second group of cases holds in general that the beneficiary has no property right in the policy during the insured's lifetime, and that the provisions of the policy prescribing a procedure for changing the beneficiary are for the protection of the insurance company, not the beneficiary: that where the insured has reserved the right to change he is the owner of the policy and has the right to assign it without regard to the interest of the beneficiary. He has, in other words, a mere expectancy, or as the lawyers say, an inchoate right.

This second group is gradually increasing, and we hope and believe that it will ultimately be the prevailing law of the land. The number and standing of the courts, however, that continue to adhere to the first view are so impressive that we cannot feel safe in accepting an assignment without first being sure that the interest of the beneficiary has either been removed or definitely made subject to the assignment. We must also bear in mind the fact that, regardless of how the courts may interpret the beneficiary's interest during the lifetime of the insured, all courts appear to agree that the beneficiary's interest becomes a vested right immdiately upon the death of the insured.

A most important point and one frequently not given due consideration, in my opinion, is the fact that the legal relationship between the insured and the assignee is simply that of pledgor and pledgee. The pledge of a policy for collateral purposes does not transfer title or ownership to the assignee, regardless of form of assignment. Many banks, through the use of so-called absolute assignments, have attempted to put themselves in the position of owner; but it is universally held that regardless of form of assignment evidence may be submitted to show that it was the intent of the assignor (the insured) merely to assign the policy as collateral security, and that therefore, though absolute in form, the assignment is collateral in fact. The assignee holds a lien against the policy, not title to it; a mortgage, not a deed. In other words, there is no such thing as an absolute assignment for collateral purposes. Only the conditions and circumstances surrounding an assignment—a gift, or sale for value—can make a so-called absolute assignment actually absolute.

There are a number of other important points in this relationship of the insured, the insurance company, and the assignee. For example, the insurance company has a responsibility under its contract to fulfill the terms thereof and to see to the payment of the amounts due to the persons properly entitled thereto. The bank, as assignee, assumes a similar responsibility as to any surplus of insurance avails which it may receive either on surrender or maturity of the policy. New York State has an important case on this point which has been cited by the Supreme Court as the law of New York (Toplitz v. Bauer, 161 N. Y. 325), and which holds that a pledgee really becomes trustee of the pledged property. Thus, if the bank, let us say, holding an assignment absolute in form but merely for collateral purposes, surrenders or otherwise disposes of the policy without observing the legal requirements of foreclosure (unless expressly waived in the assignment), it may be held guilty of illegal conversion of the property to its own use and liable to the insured. And not only is the bank liable but many insurance companies fear that if they have anything that may be interpreted as constructive notice that an assignment is actually for collateral purposes, they may, by allowing the assignee to surrender without proper foreclosure of title, be equally liable with the bank for facilitating the conversion of the pledged property.

Another problem arises if we require the beneficiary to join with the insured in the assignment and note. He then becomes an accommodation party to the obligation with the same rights as a surety, and any change in the contract of indebtedness for the performance of which he is liable as surety, made without his consent, will either discharge the surety entirely or to the extent injured by such change. And, as you all know, there are any number of such changes that might be made in the contract of indebtedness over a period of time. This is why it is most important to banks that the assignment specifically permit the assignee to release security or co-obligators, and to grant extensions, renewals, indulgences, &c.

The modern life insurance policy confers upon the insured a number of rights, powers, and privileges which he can presumably assign. It is essential that certain of these rights and privileges definitely be assigned to a bank in any assignment for collateral purposes; other rights are neither necessary nor particularly important to a bank-assignee; and some rights are held by many companies to be peculiarly the insured's and really not assignable. In a simple assignment of "all right, title and interest" there is considerable difference in the points of view and practices of various life insurance companies. The assignment should therefore cover these points. We haven't time to discuss them all now, but you may wish to consider some of them in the discussion period.

I wrote my thesis on this subject for the Graduate School before the development of the new proposed standard form of assignment for banks' use by the joint committees of the American Bankers Association and the Association of Life Insurance Counsel. So my approach to the subject was to illustrate and discuss the various methods of assignment that had been and were being used by banks, pointing out what I considered the advantages and disadvantages of each. These included collateral and so-called absolute forms provided by the insurance companies; bank forms of so-called absolute assignments, alone and with separate agreements between the bank and the insured (not revealed to the insurance company except in case of dispute); other forms of separate agreement in which the bank purported to act as trustee for the insured in a sort of passive or dry trust of any surplus that might exist over the indebtedness; and several special bank forms of collateral assignment.

At the time, my bank was using a collateral form very similar to the new proposed form, originally developed by the First National Bank of Boston, largely through the efforts of their Henry K. White and Basil S. Collins, the former of whom became Chairman of the A. B. A. committee on this matter. In drawing conclusions from the various methods of assignment considered, I gave as my reasons for preferring this collateral type of assignment to any of the arrangements involving the so-called absolute form with separate agreement:

1. It reflected the actual collateral purpose of the transaction and did not purport to be anything other than an assignment of such of the insured's rights as were deemed necessary by the assignee for proper security for loans against his life insurance values.

2. It expressed clearly to the insurance company, the insured, the beneficiary, and the assignee, in one instrument, all the rights and powers conveyed to the assignee and the conditions of the contract of indebtedness.

3. By thus revealing the whole situation to the insurance company and recognizing the possibility of a surplus to which the assignee was not entitled, it permitted the naming of a beneficiary subject to the assignment, and did not relieve the insurance company of all responsibility for proper disposition of any such surplus; and I believe the banks would receive more payments of the exact amount of indebtedness and have to assume far less responsibility and liability for distribution of surpluses than under any of the former arrangements involving so-called absolute assignments.

The proposed standard form was included in my printed opus at the last minute just before going to press, after the committee of the Association of Life Insurance Counsel had submitted it to the semi-annual meeting of the Association in New York last December. It not only had all of these advantages I had mentioned for this type of assignment, but had the further advantage to banks—more important than any of these—that it had been recommended to the Association of Life Insurance Counsel by its own committee and that the Association had sent a copy to all member companies advising them that their committee recommended acceptance of this form and compliance with its provisions when submitted by assignee banks. Perhaps many of you saw it reproduced in an article entitled "A Form of Life Insurance Assignment" appearing in the August issue of "Banking." D. P. Cavanaugh, Associate Counsel of Aetna Life, who succeeded George Hoague of New England Mutual as Chairman of this committee, and H. K. White of First National Bank of Boston, Chairman of the A. B. A. committee, both expressed confidence that the insurance companies would now generally accept this form wtihout objection. And uncertainty as to different companies' interpretations of various rights under various circumstances has been the greatest disadvantage of all the forms of assignment heretofore used.

The Bank Management Commission of the American Bankers Association has now officially approved this form and is offering it to banks at $1.75 per 100. It has been designated "Form No. 10—Insurance Assignments," and bears the official certification, "Form Approved by Bank Management Commission, American Bankers Association"—so that insurance companies may quickly identify it. When an insurance company receives this form and notes the legend "Approved by," &c., it will not have to read and compare it word for word with the form which the Association of Life Insurance Counsel has approved—a great advantage to the insurance companies.

Now, I think it is up to the banks to carry the ball from here. By that I mean that the insurance companies have already gone father than most people who have followed this subject ever thought they would—including many members of the Association of Life Insurance Counsel itself. The thing that will consolidate this gain is for the banks throughout the country to adopt and use the proposed standard assignment form, in which case some of the insurance companies who at present may be reluctant to accept it and comply strictly with its terms will be forced to do so in order to stay in line with the other companies, we hope with the result that all of their dealings with banks will be simplified and become more nearly standardized.

An interesting point in connection with this subject, about which little appears to have been said or written, is the effect that policyholders' borrowing from the banks instead of the companies may have on what the insurance companies call conservation—that is, keeping existing insurance in force. I understand that the records of one of the large Eastern life insurance companies show that not over 26% of the loan interest regularly billed on their policy loans is paid, the remainder, or about 74% of the entire loan interest, being added to principal. This is probably fairly representative of the experience of the average life insurance company; and the lapsation of encumbered policies is extremely high. In the case of bank loans made against life insurance cash values, on the other hand, interest must always be paid or the loan is called; in only a very few cases is interest paid by increase in the loan, and in a few others increases in loans are known to be applied toward payment of premiums.

I have had a study of this situation made in my own bank and several other banks in Rochester, and although it is difficult if not impossible to obtain precise figures comparable to those of insurance companies (because some loans are straight insurance loans and some have mixed collateral, and we can't always be sure what increases in the loans are used for), the experience of the banks reporting is approximately as follows, on the average: both premiums and loan interest are paid without increase in loan in about 95% of the cases, and interest is paid without increase in loan in about 98% of the cases; also approximately 50% of such loans are being reduced regularly by repayments of principal. Lapsation of policies assigned to the banks is practically non-existent. So from the standpoint of conservation, at least, the insurance companies should be glad to see their policy loans go over to the banks—that is, the underwriting departments should; it may be a horse of a different color to the investment departments.

Perhaps I should mention, though again there isn't time to discuss it here, a chapter of my book that deals with procedure in making insurance loans, outlining first what must be determined from an analysis of the policies themselves, by someone in the bank who is thoroughly familiar with policy forms and provisions and their requirements for good collateral; next, what must be determined by inquiry from the insurance company; and finally, a discussion of procedure in regard to this confusing matter of the beneficiary and what to do in the most common situations that arise, including that of the bank as trustee-beneficiary under an insurance trust.

In conclusion I should like to express publicly my thanks to Hal Stonier and The Graduate School of Banking, without which I would probably never have made a very exhaustive study of this subject, and certainly would never have written anything on it.

Discussion Following Address of Mr. Tait

Chairman Dean: We want you to ask any questions you care to at this time.

J. M. B. Petrikin (Greeley, Colo.): I wonder if some of the other banks have had the experience I have had, and what the practice of the insurance companies is in this respect. Do these insurance companies, when they make loans on policies, require the surrender of the policy? Is that the general practice? I will tell you why. With a great insurance company in this country I had a lot of correspondence. A man came in and borrowed some money on a policy. He had it in his own possession, of course, and it was an urgent case. Figuring what the cash surrender value was, we made him a loan and sent him an assignment. We found that the company had made a loan, and they absolutely refused to recognize any preference and were quite cocky about the whole proposition. Since then we haven't made any loans on policies of that company.

There ought to be some protection. They ought not make a loan, in my opinion, except that they have the policy surrendered, because a whole lot of people, as you all know, make just temporary, urgent loans. We are not protected at all. Some think the companies would like the banks to carry the loans. I don't. I think they want to carry them themselves. I know there is a lot of hazard about making those loans.

Mr. Tait: The reason I said that was because I said the companies ought to be glad from the standpoint of conservation. That is our record. The record of lapse ratio on assigned policies to banks is infinitely better than with the companies, and the underwriting departments of these companies do worry about this situation of their loans, because the incumbered policies lapse so rapidly. The lapse ratio is very high. I did say I think the investment department feels the other way, of course.

As to this business of surrendering a policy, most companies, to my knowledge, no longer require it. You mean by surrendering, taking possession of the policy. Most companies no longer require that. Most of them let the insured keep their policies. A good many used to some years ago, and there are several still remaining who will require the policy.

It doesn't make any difference whether they have the policy or not. If they have a loan against the policy, they have the prior lien. We have a few loans where we have an assignment that is clearly subject to an original or former assignment running to the insurance company for the amount of indebtedness on them.

Generally, of course, a fellow comes in with his insurance loans and wants the company paid off with our loan, which is the purchase of the loan, but there are a few situations in which for one reason or another the insured has pledged his policy but doesn't want the bank to take over the original loan with the company. By their contract of first lien they are ahead of us, but it doesn't in any way impair our right under our assignment if the cash value is sufficient as collateral to cover us. Incidentally, the new proposed assignment form specifically gives that right to the insured, not to increase without consent but to recognize the prior lien that might exist.

Mr. Petrikin: The point I made was that when people want to borrow on their insurance policies, they need the money immediately, urgently. We understand the assignment isn't good until recognized by the company, but you are so far away from the home office you don't know they have already obtained the loan. It seems to me it wolud be a nice practice if the insurance companies would insist on having the policies surrendered when they make a loan. The insured would have to turn in his policy, so he wouldn't have it to come to you and make a loan.

Mr. Tait: I though that was what you complained about.

Mr. Petrikin: I complain about the man who makes a loan from the company and keeps the policy. Then he comes to the bank and there is no notice to the bank that there is a prior loan. Of course you say: "You should find out. You shouldn't advance the money until you know the assignment has been recognized," but that doesn't give the man his immediate relief.

Mr. Tait: Frequently, the policy shows that. In most of them, the existence of a prior loan is stamped right on them.

Alfred T. Gibbs (Montclair, N. J.): I would like to ask Mr. Tait if, when we get the form exactly right and satisfactory to the company, and when it is admitetd that a man has the right to pledge his cash value—it has been our procedure to send a questionnaire to the company and say, if an unfortunate chain of circumstances brought about the inability of the man to carry on with his note—we will assume he has disappeared, or something of that sort—"We want our money. Will you give us the check?" About two-thirds of our great companies will say yes, but there are still very prominent insurnace companies who demand further signatures. How can a bank do business on that basis?

I think our Association should continue its efforts that when all the proper assignments the companies want are in their possession and a bank makes a loan, such as on telephone stock or General Motors, and conditions arise that they must liquidate on their collateral and they go about it in the right way, we get our money without going through the whole business of getting the consent of the owner of the policy and beneficiary. There are still about one-third of our great companies that will not deliver a check direct to the bank, in spite of the fact that we have everything they demanded in the beginning. What can we do to pursue the fine work you have been doing to bring about some uniform practice, so as to make these loans safely?

Mr. Tait: That is one of the things they have done most of the arguing about. The reason you said about one-third—I think that is probably correct; at least one-third will not guarantee to pay to your sole order a check upon demand. They have a pretty good reason for it. Unless they have predetermined and agreed upon the assignment form, they may not know exactly what the assignment form covers in your particular instance, what the beneficiary's situation may be, what date the policy was issued, what the circumstances may be at the time the insured defaults, or whether he defaults. A lot of them never do anything until he has defaulted.

In a lot of cases the right to surrender the policy itself is a nonforfeiture provision, which technically means it can't be exercised unless there is default in premium payments, but it isn't their practice to insist upon that. They make a practice of giving the cash value on demand to the insured at any time, but in many cases that isn't a part of the contract.

Mr. Gibbs: I had an interesting experience in making an insurance loan to a man prominent in the utility field in Connecticut. His policy came in to us. We gave the company everything they demanded and still they refused to say in writing that they would give us a check upon demand. We passed the buck back to our customer and he took it up with his company. He said he had a perfect right to pledge the cash value and insisted that the company consent, and rather reluctantly they did consent in writing, but only after their policyholder put it up to them in pretty strong terms.

Mr. Tait: They have that evidence on his part, which is what he does in a normal assignment. He simply supplemented the assignment by a letter of direction, and they determined in his case that he was the owner. I won't attempt to read this now because it is a pretty long assignment, but there is a clause in here that takes care of this pretty clearly, providing the companies comply.

Mr. Gibbs: I know we don't want to get into detailed discussion, but I do feel our American Bankers Association, recognizing that the loans on insurance policies are vital to banks—and it can be argued that it can be handled by the local bank—should arrive at some basis of understanding with the insurance companies, so that in case of need, in case of our customer disappearing or becoming unhappy with the bank, we can liquidate our note just the same as on any other type of collateral.

Mr. Tait: I agree with you, sir.

Mr. Gibbs. I think we ought to pursue it, and I think it is important enough that our Association ought to recognize it and move steadily forth and arrive at some satisfactory conclusion.

Mr. Tait: Of course this committee of the A. B. A., headed by Mr. White, has done just that. That is the development of this assignment form, getting the Association of Life Insurance Counsel to approve the form. This assignment specifically provides that a check be paid on our order, directly to our sole order, and so on, and releases them from all liability, and so on. It covers that very clearly. No one can prove whether they are going to do it or not. I claim that the use of this from, plus the approval of the Association of Life Insurance Counsel—perhaps not officially, but the committee approval of that in conjunction with our committee—will force the companies who still may be standouts on that point to comply. In court, you have it anyway. The whole thing is to get compliance without having to go to court. With that assignment, you are perfectly good going into court, if you had to, and my hope is you won't have to.

Loss Prevention First—Indemnity Always

By K. C. Bell, Second Vice-President Chase National Bank, New York, N. Y.

In this last phase of our afternoon's discussion on "controls" we shall treat briefly of certain rarely stressed aspects of *insurance*—insurance, that is, against losses of physical assets or personal property. We shall not include in the discussion the prevention of, or indemnity for, any credit or investment losses. The particular theme of this paper is, as announced, "Loss Prevention First—Indemnity Always."

Loss prevention is by no means a new subject of discussion for this Association. Physical safeguards and accounting and auditing controls have been repeatedly stressed (as some of them were earlier this afternoon). But possibly it may be somewhat novel for you to consider *insurance* as a loss preventive. Yet it is principally of insurance in its loss prevention aspects that we shall speak during the few minutes at our disposal. Probably all too little thought has been given to that phase of insurance treatment. Loss avoidance through the proper use of insurance pays real dividends. In times of abundant bank earnings, as well as when earnings are meager, we should not overlook the advantages of loss prevention in every form. Also, if loss must occur, why not see to it that the loss, or the cost of it, so far as possible does not fall upon our banks?

Now, by that last remark I do not mean to imply that any bank should evade any liability which is properly its liability. Far from it! All too many banks fail to carry the insurance which they should carry, such as forgery insurance, and merely because they are self-insurers they resist all claims. But there frequently are cases where a customer transaction is involved when an insurance arrangement is both possible and proper whereby the burden of any loss will fall upon the customer's policy. If that is done, the bank's loss record is not made worse, and the bank's own initial insurance premiums will ultimately be lessened, and reinstatement premiums for the bank can be avoided, or at least, minimized.

Our domestic surety companies have put at our disposal excellent loss prevention devices in the form of their bankers' blanket bond and fidelity questionnaires. Bank interest in these questionnaires is steadily growing. Are you taking full advantage of them? There is scarcely a bank that cannot find in such questionnaires at least a few helpful ideas for loss prevention. Have you, yourselves, ever devised and applied a questionnaire for your own bank? If not, you might try it, as a novel experience. And as a further suggestion, why not consider loss exposure and general insurance matters among the problems which are discussed regularly in your bank staff conferences? Self-analysis along these lines may lead to very effective loss prevention as well as to the needed loss indemnity through proper insurance coverage.

The prevention of loss makes loss recovery unnecessary. A bank with a low loss record generally has little difficulty getting any desired insurance coverage. Careless banking increases insurance costs, as well as other costs of doing business. Insurance premium rates are the reflectors of loss experience. Even though merit or credit rating has so far generally been restricted to the compensation and public liability fields, there is a very definite trend toward the extension of that principle of insurance. Personally, I feel that that is as it should be. I trust that we shall see it soon applied in blanket bond underwriting. In that field, as in any other, we should not expect others to bear any sizable portion of the penalty for our own negligence or indifference.

Blanket bond coverage generally provides for the reinstatement of losses. These reinstatement premiums are costly. Speaking before this Association at Hot Springs in 1933 on this same subject, and referring only to crime losses of the previous year, your genial Insurance Secretary, Mr. James E. Baum, made this remark:

"Of this huge (premium) outlay (i.e. $17,000,000 in 1932), made for the purpose of securing indemnity of losses through crime only, I estimate that reinstatement charges or the amount of premiums duplicated totaled at least $2,000,000. Translated into preventive measures these reinstatement charges, which accomplished nothing more than to restore the banks' insurance to original amounts, would have defrayed the cost of installing adequate protective equipment or stronger auditing procedure within the banks."

Now, directing our attention more closely to our specific bank insurance coverages, may I ask how many of you have ever given any thought to the loss prevention aspects of even our commonly used bank fidelity and bankers' blanket bonds and of our bank burglary and robbery policies?

The mere requirement of a fidelity bond and the filing of an application for one probably constitute effective deterrents against any crook seeking employment with a bank, particularly if the bonding procedure be coupled with a minute checkup of the applicant's prior business career and school record, with a verification of his signature all along the line. Once employed, the realization that the bonding company would prosecute him even if the bank did not, may tend to keep a wavering employee on the straight and narrow path. Surely loss prevention at the outset is most desirable in the fidelity field, which absorbs 80% of all blanket bond losses.

In the burglary and robbery field, while such insurance primarily provides indemnity for actual losses, still the urge for more profitable and more voluminous underwriting by the insurance companies and the desire for lower rates on the part of the banks have resulted in amazing progress in the assault-resisting construction of bank vaults and bank buildings. The increasing severity of Federal and State statutes for crimes against banks, as well as the cooperation of Federal and local law enforcement agencies, has supplemented these bank and surety company activities in recent years in lessening bank losses of the burglary and robbery types, with the resultant effect of steadily lowering our insurance costs for indemnity against such hazards. With continued improvement in the construction of banking premises and with increased police protection, these losses—and therefore the cost of insuring against them—should continue to decline.

I am well aware that bankers' blanket bonds and also fidelity and burglary and robbery insurance to which we have just referred briefly may be commonplace coverages with many of you. Moreover, these coverages are dealt with at length in your Insurance Committee's report. For these reasons, and because these particular types of coverage have been the ones most stressed in previous insurance discussions and in the literature with which you have been made familiar in the past, we shall not delve further into them at this time. Suffice it for me to emphasize that coverage for those hazards is unquestionably the most essential insurance protection for any bank to carry. Blanket bond risks deserve our utmost consideration, both from the approach of loss prevention and for loss indemnity.

Having thus inadequately dealt with and disposed of our all-important blanket bond and related coverages, let us turn to consider briefly the loss prevention aspect of other types of insurance affecting our banks:

Safe deposit legal liability policies provide an excellent example of loss prevention through insurance. The older standard types of safe deposit insurance had very limited value in my opinion, particularly because they restricted recovery to 10% of the amount of the policy in regard to the contents of any one vault compartment. But the legal liability form which has been brought to the fore by our domestic underwriters in the last few years does have real merit. Except in the few cases where burglarization of vaults has actually taken place, the loss of contents of any safe deposit box has been extremely rare, especially when proper access controls have been exercised. Accordingly, probably the most threatening exposures to loss to which our safe deposit vaults are subject are (1) the deliberately false allegations of loss, and (2) the loss claims which are predicated on a misunderstanding or lapse of memory on the part of the box renter.

The insurance protection which banks and safe deposit companies vitally need includes adequate legal defense against assertions of loss where no loss has actually occurred. Even considered solely as a means of providing without further cost first-rate legal talent for the defense of claims against a bank, safe deposit legal liability coverage should prove attractive to us. What better example in a concrete policy form can we find of "loss prevention first—indemnity always"?

Very similar in nature is public liability coverage. Here too, in addition to the actual cases of imjury or death which are covered by and compensated under the policy, there are, as many of you are well aware, a much greater number of improper or exaggerated, if not fraudulent, claims for injury or damage advanced. Therefore, the legal defense feature of such a policy is of paramount importance to the insured bank, as well as to the underwriting company, in keeping policy losses at the minimum. As we have already said, experience rating is broadly used in this public liability field. The losses accumulated and charged against the record of the insured in the assessment of future premiums include the fraudulent claims which must be compromised, as well as the actual injury cases. Probably every bank in the country carries public liability coverage as a matter of course, but few of them may have given much thought as to how indispensable is the loss prevention feature of that form of insurance coverage.

Another example of defense insurance is the contingent liability automobile policy. A great many banks direct or permit members of their staffs to use their personal automobiles on bank business, occasionally if not regularly. Any bank which does so should certainly carry adequate limits of contingent liability insurance. It can also take advantage of both loss prevention and loss indemnity for the bank by having as a first line of defense the policies which such persons themselves carry maintained in such form as to protect the bank. As a matter of fact, this is generally now done, automatically. But it is important for the bank to see to it in connection with any such personal insurance arrangements that the policies indicate that the insured cars may be used for both business and pleasure.

In addition, there is a fourth form of liability coverage which is often important for banks, particularly in connection with premises leased for the bank's own occupancy, or in connection with properties leased to others by the bank as a part of its trust activities or as a part of a loan workout proposition. What I have in mind is insurance coverage, or indemnity, for so-called "contractual liabilities." Such liabilities usually arise out of lease agreements, wherein one party undertakes to hold harmless and fully to indemnify the other party under certain circumstances. These circumstances can be much more far-reaching than has been anticipated, particularly if the agreement be one inherited from some third party. All of a bank's leases should be thoroughly scrutinized to ascertain if there be any contractual liability or "hold harmless" agreements to which the bank has committed itself, intentionally or not, where the potential loss exposure is sufficient to warrant the obtaining of indemnity in the form of an insurance contract. Both loss prevention and loss indemnity are of great value in such cases. Policies providing protection against such risks are usually procurable.

Most of us look upon our fire policies as providing only indemnity for losses. Primarily that is the case. I mention fire insurance only as an example of the sort of coverage which, upon consideration, we may be amazed to find is susceptible of treatment for loss prevention and for reduced premium costs, as well as for reimbursement for actual losses sustained. As an example, a breakdown of the premium rate struture for any building, when coupled with a careful inspection of the premises by an insurance engineer or other competent person, may reveal not only opportunities for improvements which would result in lower premium rates, but the survey of the premises may also bring to light certain actual existing fire hazards which can be substantially reduced, if not eliminated. That is real loss prevention. We should give constant thought to possibilities of this sort in connection with all of our insurance coverages.

So far, each of the types of insurance we have mentioned has been a form of bank insurance only, with the excep ion of employees' automobile policies and of public liability coverage, which applies also to trust properties. Now, let us look at a few types of strictly customers' insurance in which as banks we have a real concern.

For the first example, let us take depositors' forgery insurance. While such insurance has certain limitations in its attractiveness for our depositors, it nevertheless has a real value for them and, so far as the bank is concerned, such policies provide very desirable coverage. As you doubtless know, the standard forms of depositors' forgery bonds undertake to protect the banks of deposit as well as the named insured. This coverage can therefore be looked upon as anti-litigation insurance. It is designed to eliminate any direct cause of action between the customer and his bank of deposit. That feature of the policy is often stresssd by the companies' agents.

Also, as many of you know, the use of mechanically signed checks is growing among our larger business organizations because of the internal economy which such device affords. For the paying bank, these mechanically signed checks are exceedingly dangerous because there is no possibility of their detecting a forgery or a wrongfully issued check. Therefore, as a very important and effective means of loss prevention for our banks, I suggest that we should require depositors' forgery insurance from all depositors who use mechanical signature checks, in addition to our requiring from them indemnity agreements in the fo m of resolutions adopted by their boards of directors which will relieve the bank of all liability for the payment of forged checks bearing facsimile signatures resembling the authorized specimens on file with the bank. These indemnifying resolutions are already being required by the banks in several metropolitan centers. Such resolutions are indispensable. But depositors' forgery insurance is also important, if the banks are not to assume an entirely unfair burden in honoring facsimile signature checks. I can see no objection to a bank's even paying the reinstatement premiums on losses under these customers' policies, since the bank also is indemnified, if the depositors are otherwise unwilling to file claims under their own forgery policies. And, as one of the most effective measures for preventing protracted forgery schemes, where facsimile checks are used, may I suggest the very frequent return of canceled vouchers, even a daily return, if possible? The oftener, the better.

Then there are instances occurring occasionally at the larger city banks at least, where special transportation of securities in large blocks must be handled, particularly for big corporations or estates and under unusual circumstances. Often it may be possible to arrange for specific transit policies to absorb the risk for the customer's account and at the customer's expense. Such an arrangement exempts the bank's own blanket bonds or transit policies from loss and saves the bank reinstatement premiums if losses should occur. It is exceedingly difficult and probably impolitic to collect from a customer the cost of reinstating a loss under a bank's own policy. But frequently a customer is willing to pay at the outset the premium cost of specific insurance arranged by the bank for his particular benefit.

In the trust field, banks have for some time been accustomed to the use of the standard mortgagee clause in fire policies, to protect their interests as mortgagee. These standard clauses are also used in the case of individual mortgagees. Probably all of you gentlemen are familiar with these standard clauses to some degree. Therefore, we shall not discuss them at length but shall merely emphasize that by the use of the clause, particularly the mortgagee clause without contribution, the mortgagee is protected against acts of the insured which are beyond the mortgagee's control and which might serve to suspend the insurance or render it void, were it not for the existence of the protecting clause. Under certain circumstances this phase of the insurance protection can be as important to the mortgagee as is the control of loss payments, for which provision is also made under the standard form. The mortgagee clause is an outstanding example of protection afforded the bank at some one else's expense. But even here, the cooperation of the bank is necessary to assure compliance by the insured with the coinsurance conditions of the policy, if the insured property be located in a State which requires or permits coinsurance provisions in the fire policy Otherwise, the bank as mortgagee may have to absorb a portion of an uninsured loss.

In connection with customers' commodity policies, there has recently been developed an adaptation of the principles of the mortgagee clause, so long used in building and contents policies. A number of the larger New York banks have, during the past year or so, been requesting of their customers to whom they make loans against the pledge of commodities copies of such endorsements executed for attachment to policies covering commodity shipments, warehousing, or processing. By this means the bank (1) controls loss payments, (2) has due notice of intended policy cancellation for any cause, and (3) also has protection against the voidance or suspension of the policy through acts of the insured beyond the control of the bank. These bank commodty endorsements are extremely valuable. When appropriate, they can be applied to inland or ocean marine insurance just as well as to fire policies. Little, if any, company or cutomer opposition will be made to the issuance of such special endorsements, but probably they must be prepared by the bank, and certainly they must be requested by it. The loaning bank has a real insurable interest in such commodities which deserve protection. Like the mortgagee clause, these commodity endorsements constitute an excellent adaptation of a customer's insurance to meet his banking needs while at the same time providing proper indemnity for the loaning bank.

Another example common these days of the practical combination of loss prevention and loss indemnity through customers' insurance lies in the group life insurance arrangements of banks which have small personal loan divisions. The device of insuring the lives of all such borrowers in decreasing amounts which will at all times reflect the outstanding indebtedness of the borrowers is an excellent safeguard for the bank and for the debtors' estates. Here also, loss prevention and loss indemnity are provided without premium cost to the bank.

By a comparable arrangement, banks require from their customers, at their expense, insurance against loss of, or damage to, automobiles in sales financing loans.

Previously, when discussing bank coverages, we mentioned public liability insurance and the loss prevention aspects of that form of defense policy, as well as the indemnity provisions of such protection. Similar comment can be made with respect to the protection of the real estate holdings of our bank customers. But there is a further point which should be stressed for the protection of our banks in their operation of trust properties. That is, that in any repair, or alteration, or decoration jobs we should do business only with actual contractors and only on a contract basis. Moreover, we should restrict our relationship to such contractors as carry and will furnish the banks with evidence of proper workmen's compensation and public liability insurance.

In a surprisingly large percentage or our States the courts have held the owners of the property—in the case of trust properties, the banks—liable for injuries or death inflicted on the public by or through the operations of the contractors or sub-contractors, or have held them liable for injuries or death sustained even by employees of those contractors, where the contractors themselves did not carry proper and adequate insurance to indemnify the injured persons. It would be wise for each of us to check up on the practice of our own bank in this regard. Contractor's insurance in adequate amoutts, which protects both the bank and the contractor, is a very vital loss prevention requirement for a bank. And for further indemnity, contingent liab lity coverage should be carried by the bank itself. The rates for such insurance are not excessive.

From even these few examples it would seem that, because of our own direct interest in such insurance, we may have to pay considerably more attention to our customers' coverages in the future than we have done in the past, possibly to the point of analyzing and commenting upon specific policies in some cases. However, that service must not be overdone. Our banks must avoid setting themselves up as insurance counsel and they should not in that regard invade the field of company representatives, agents and brokers. Nor should we invite the responsibility of persuading our customers as to their insurance arrangements unless we have a direct insurable interest in their coverage. But a frank discussion between the customer and his bank of the purposes to be served by the customer's insurance cannot help but be enlightening and beneficial to both parties.

As a possible starting point, advantage might be taken of an insurance survey, or a statement of insurance, such as was recently released by the National Association of Credit Men for bank use. Of course, no mere listing of coverages has a great deal of significance unless there be coupled with it a knowledge of the policy terms and of the amounts of insurance, and, furthermore, an understanding of the insurable hazards and exposures of the customer. Yet even a recital of the coverages carried, or contemplated, may serve to indicate gaps in the insurance arrangements. In such discussions the bank can be sincerely helping its customers safeguard their own interests. Any ensuing benefit to the bank through the avoidance or minimization of losses for the bank, while important from its standpoint, can be really incidental.

Whether dealing with its own insurance, or with its customers' insurance, a bank should first of all assure itself of the sufficiency and the appropriateness, for the purpose of providing loss indemnity, of any insurance coverages which it purchases for itself, or which it accepts from customers. But it should go further. There are many ways in addition to the few hinted at in this fragmentary discussion of the subject in which insurance policies, surveys of hazards or risk exposures, and analyses of rates and forms can be utilized, directly or indirectly, for loss prevention as well as for loss indemnity. From either approach, undesirable policy limitations or omission of coverage can frequently be removed for the asking—well, maybe a persistent asking! But improvements in coverage are seldom offered to us except upon our own demand.

It seems scarcely necessary for me to mention here that no insurance or indemnity policy is wisely purchased if the standing of the underwriting company and its loss paying record are not of the highest type. Probably a check-up on the standing of the company should be the first step in arranging any indemnity coverage for our banks.

And as a final point—although it is important enough to have been stressed at the outset—let me urge upon you the centralization of insurance supervision, if your bank does not already have it. The insurance problems of our banks are multiplying daily. Even with centralized supervision proper protection, economy and uniformity are not easy to achieve; without centralization the problem must be still more difficult.

So, in conclusion, let me suggest that, whatever the particular situation to be covered may be and whether it be bank or customer risks that are involved, you may find in future considerations of insurance problems by your respective banks that it will be of some value, however slight, to recall the theme of our brief discussion here this afternoon, namely, "Loss Prevention First—Indemnity Always."

Remarks of W. Laird Dean, Presiding as Chairman

W. Laird Dean, President of the Merchants National Bank, Topeka, Kan., spoke as follows in opening the session:

In the last five or six years thinking men all over our country have worried about the force of social reform, that in the judgment of many has been striking at the very fundamentals of our American economy. All of those worries have been immensely multiplied in the last few weeks, since across the water the nations of Europe are again at war to try to find out just what "ism" is going to control that continent for the next century, or quarter of a century. All of those worries about social reform: all of the worries about this titanic struggle that has just begun, make every one of us worry about just what kind of a system we are going to live under when this is all over, what kind of an economic system, and then, because we are bankers, what kind of a banking system.

We have differences of opinion as to just what kind of a system is best for America today. Some say it should be a regimented system controlled completely by our Federal Government. Some men tell us that in a few men's hands, men if possible endowed with unusual wisdom, should lie the ultimate control and the policy-making part of our entire financial system. Others of us believe that out of the individual unit banks can come some contribution at least to the best financial thought, and in those unit banks are found some bankers, some men who are destined to lead that unit system to its glorious conclusion, and following with the sort of an economy that has made America great and, we hope, can be continued here.

All of those things are worries; all of those things are something we have been wondering about and we have wondered what we could do about it. Regardless of all that, it doesn't make any difference if we are to have a Federalized system, if we are to have a closely controlled system or if we are to have the broad unit system, the success of any one of them must in the last analysis depend on the kind of operations inside each one of those banks. Whether it is the operation controlled by one or the operation conducted by many, the operating problems, the operation of our business is the most important thing to which we can devote ourselves. If those operations are sound, then we have time to do some clear thinking about general problems.

I think it is very wise that the officers of this Association have decided in their major meetings to give some attention informally to the operating problems of banks, to bring to the bankers of the country the men best qualified to discuss particular problems, and then to ask you to raise any questions you wish. Let the discussion run free from the floor, and let's get at the problems in the fashion that all such problems can be ultimately and properly settled by free discussion, by free expression of opinion.

I am going to introduce these speakers to you, all of them men who, in the judgment of the officers of your Association from their broad knowledge of men studying the problems of banks throughout our country, are best qualified to lead the discussion. They all will be disappointed if their talks don't stimulate you to ask some questions and to get out of each one of these subjects the very most we can possibly get out of them.

The first subject on our program, as you have read in the bulletin, is a discussion called, "Expense Control for Better Earnings." This subject is to be discussed by J. LeRoy Dart.

INVESTMENTS AND MORTGAGES

Three talks were given under this head, by respectively, O. Paul Decker, Edward A. Wayne and Frederick M. Babcock

Investment Problems Confronting Trust and Savings Departments Today

By O. Paul Decker, Vice-President American National Bank & Trust Co., Chicago, Ill.

In the period allocated to this address, it is possible only to suggest the wide variety of investment problems confronting trust and savings departments today. They are, to be sure, only variations of the age-old problems that have always confronted both departments. In the case of the trust department the problem is one of providing income for the life beneficiary of a trust at the same time that proper security is provided for the assets of the trust in order that the trustee may deliver to the remainderman the sum the testator originally provided. In the case of the savings department the problem is one of earning a sufficient sum to pay expenses and to pay an adequate interest return to depositors, while at the same time maintaining the necessary liquidity of assets to provide for withdrawals and the necessary quality of assets to provide proper solvency. In each case the technical selection of the investments has become increasingly difficult as the legal safeguards or controls surrounding management have increased, as the political, business and monetary background of investment has become more confused, and as there has been, in some cases, a lack of agreement by management as to what its true function should be. It will therefore be the purpose of this paper to suggest a few of these difficulties and a few of the methods that have been used to solve them.

Specific Investment Problems Facing Trust Departments Today

Probably the foremost investment problem—in reality the major problem of investment policy that has had to be faced by a trustee in recent years—has been the problem of whether it was the duty of the trustee to seek for the income beneficiary only as many dollars of income each year as the corpus of the trust would produce from its investment in legally qualified trust securities and whether it was the trustee's duty to deliver to the remainderman at the maturity of the trust the same number of dollars as the original trustor contemplated, or whether it was its duty as trustee to protect, in so far as its human judgment would permit, the purchasing power of both the income and the corpus of the trust estate for the benefit of both the income beneficiary and the remainderman. Particularly has this problem face the trustee charged with the entire responsibility for investment—a trustee operating under an agreement that grants it full discretion and does not in any manner confine its investment operation to the usual group of securities known as "legals for trust investments."

Surveys have disclosed many methods being used to solve this problem. These methods range from the methods of the distinct minority who, in all honesty, deny that this duty is part of the trustee's obligation—who deny this duty from the firm conviction that it is a trustee's sole duty to protect the number of dollars of principal intrusted to its care—to those who suggest that protection of purchasing power is a trustee's duty and advance as a method of protection the suggestion that a given portion (in some cases as much as 30%) of the corpus of a trust be invested in common stocks. On the one point, however, that a trustee is not fulfilling its duty if it seeks to obtain a riskless rate of return—a rate of return equivalent only to pure interest on capital—does there seem to be an agreement. On how far beyond the point of obtaining a riskless rate of return a trustee's duty requires it to go there appears to be no agreement or to have developed even a common ground of agreement. The problem is too new as yet for standards of what constitutes good trust investment management to have developed.

Historical precedents seem to be of little value in solving this problem. Only in recent years, certainly in the last decade, have the main commercial countries of the world decided or been forced to free their currency from gold and hence free their economic systems from a relatively stable price level; and to turn universally to the use of a managed currency, a currency managed in some cases for the express purpose of reducing the burden of debt or increasing a country's internal price level or improving its position in foreign markets. It may well be that a new concept of the trustee's duty will have to be developed as a result of these new concepts of money and its relationship to prices, and a new theory of what is proper investment for trust funds will appear in the law as a result of this new economics. Trustees appear forced to recognize that, while the last part of the 19th centuary was not a period of stable prices even though currencies were tied to gold, the fact that they are no longer tied to gold makes the possibilities of instability in the future much greater.

It is interesting to anyone reading recent literature on trust investments to find that common stocks have generally been assumed to be the proper investment for a trustee to use if he wishes to obtain a hedge against changes in the purchasing power of the income and corpus of a trust. Only very occasionally are other hedges, such as investments in commodities or real estate, discussed. This is unfortunate, for it must be recognized by every trustee that, in times of political as well as economic upheaval such as the present, common stocks, representing the final, ultimate equities in a business, are themselves subject to the greatest upheavals. Hence, any policy of purchasing common stock becomes a matter of timing and of good judgment as to what stocks should be included in a trust investment portfolio. Even this is not all there is to the problem, for every trustee may well raise the question with himself as to whether every account irrespective of its size should at such times have common stocks as hedges and whether as trustee it is actually obtaining a purchasing power hedge for its account when a purchase is made of a stable, depression-proff dividend-paying common stock. If the common stock it purchases is not a stock of that type, it may well then raise with itself the question as to whether its purchase is an investment or whether it is a speculation.

The desire by a trustee to protect beneficiaries from the vagaries of the price level is evidence of its desire to exercise the discretion for which it was appointed, but if it makes investments in high-grade, depression-proof, dividend-paying common stocks, it should recognize that it may not have solved its problem. Such purchases create problems for the trustee of increased operating expense, of difficulties of distribution—particularly in those cases where distribution in kind is impossible—and lay the trustee open to possible charges of mismanagement. It is hot unusual for even the best of stocks to fluctuate in price in a single day more than the amount of their dividend for a year, and in a given year to fluctuate in value more than 50% of their value at any one time during that year. The success or failure of a perfectly sound business may depend upon the action and activitiels of politicians, governments, investors and the general public. These risks certainly such a purchase assumes. Should increased public expenditure, inflationary price movements, war or social upheaval eventuate in this country, heavily increased taxation and circumstription of the operation of corporate enterprises, with all their impact upon earnings and the price of equities, would become the order of the day.

Certainly on the point of what inflation hedges should be used by trustees, if the assumption is made that it is a trustee's duty to hedge those estates with whose management it is charged against price level changes much additional thinking needs to be done. Any policy now adopted must be pursued with great care, particularly if the laws of the State in which the trustee operates do not recognize this feature of its responsibility.

A second problem that has faced trustees in the last few years, in an aggravated form, has been the problem of obtaining an adequate interest return on funds due to the unprecedentedly low rates of interest which high-grade securities have been yielding and the ever-growing income and personal property tax burdens such securities have been forced to bear. Cases exist where tax rates have forced changes in investment policy and have made necessary the inclusion in accounts of tax-exempt securities in order to obtain relief. Beneficiaries have suffered reduced standards of living due to reduced income. Particularly have trustees been faced with these difficulties where their investment powers were limited to a legal list of securities or were limited by statutory requirements.

A number of methods have been adopted to solve this problem of declining income. They range from the somewhat ingenious ones of dodging the problem in part by having a portion of the fees of the trustees charged against the corpus of the trust rather than its income, or by arranging to revise amortization practices so as to reduce premiums paid on securities more slowly, or to charge such premiums against the corpus of the trust if the instrument permits. In very rare cases where the instrument specifically permits such discretion, principal has been invaded or profits on securities have been construed as income. By far, however, the most usual methods have been to vary the percentage of the different classes of securities contained in the corpus of the trust or to extend the maturity of such securities so as to obtain the higher rate of return borne by bonds of long maturity. In some cases one other method, namely, the use of preferred stocks as investments, has been adopted.

The changes in accounting practices that have been adopted have proven to be relatively unimportant methods of solution, for although they have made the results look better, actually they have not improved the results. The next two methods, the methods of varying the percentage of classification of the different investments and of buying long-time securities, contain definite elements of danger. If the percentage of the holdings of any one class of securities has recently been increased because its rate of return was greater than that obtainable from other classes of securities, a trustee can be certain that if the general level of interest rates changes the rate of return on such a class or group of securities will also change. It is axiomatic that the securities which bear the highest rate of return at the present time bear such return because they embody features of weakness because of which a borrower must pay a high rate of return and that, unless something happens to change these features of weakness, he will still have to pay a higher than usual return in the future. Within relatively narrow limits it seems perfectly proper to vary the percentage of government bonds, municipal bonds, corporation bonds and mortgages contained in the investments of a particular trust, but it does not seem proper to reduce diversification beyond a point of reasonableness by eliminating particular classes of items of investment. The cry that trust fund mortgages can not be obtained is frequently heard, but actually they are being obtained and their advantages of short maturity and amortization still remain as real as ever.

Trustees must recognize that the recent low level of interest rates has been an aritifical condition created by an intesne desire for national self-sufficiency over the entire world. This has prevented the free flow of trade and capital. In addition the cheap money policy of the Federal Government of this country has aided in forcing interest rates to the low levels seen in July this year and produced in part the tremendous supply of excess reserves under which all banks labor.

While one might think that this plethora of funds would make it impossible for rates to rise even under present unsettled conditions, we must all recognize that the bond market has substantially declined since the first of August, that rates have risen and that the increased rates which are now available and which would have looked extremely attractive two months ago have failed to attract any substantial amount of the available funds into the bond market. This failure of funds to flow into the bond market seems to be due largely to the fact that long time, permanent investment funds have never sought use except in countries and at times when political and social peace have existed and where the sanctity of the lender's contract could be enforced. War, in spite of whatever action governments may take short of the actual conscription of capital to prevent a rise in interest rates, has always caused capital to become more valuable and interest rates to go up if for no other reason than the fear that they would go up. A question may well be raised as to what justification a trustee charged with the duty of preserving income and principal can have if it now buys long time securities when political and social conditions are in such a state of flux and assumes the risk of a substantial market decline and an inadequate income for several decades to come.

Some trustees have assumed that the way to obtain a satisfactory rate of income was to purchase high grade preferred stocks which yield a rate more compatable to the normal rate on high grade bonds than any other class of securities. The general assumption seems to have been that such stocks, while they do not offer a security equivalent to that of a high grade bond, nevertheless offer a certainty of income that is comparable. Such reasoning would seem to be fallacious, for though it is true that preferred stocks have sold in recent times to yield a rate of return comparable to that normally obtainable from the highest grade bonds, their divergence in return from that obtainable on a bond of the highest grade has not materially lessened. At the best they offer the trustee the rate of return at which they are puchased in perpetuity. Irrespective of their quality they still contain some amount of the risk inherent in the ownership of an equity and they do not afford a protection against the potential rise in the interest rate on maney.

The solution to this problem probably has been the acquisition of a group of securities of diversified maturity in order to minimize the risk of obtaining an inadequat income over a long period of time. Obviously such a policy has been somewhat hard on the income beneficiary, but it appears to be the only one that, over a period of years, affords his income the maximum protection.

A third problem of investment facing trustees at the present time, in an aggravted form, is the old problem of retaining non-legal securities which come into a trust as original investments. The two general rules regarding such items are well known, but their application has been subject to much confusion and at the present time is subject to even greater confusion. These two rules theoretically are widely divergent, but as a practical matter they have operated in much the same manner in the past. The first rule, namely, that a trustee holding an investment not sanctioned by the trustor, by the statute of the State in which the trustee operates, or by court decisions has a duty to sell such investment as soon as he reasonably can and to re-invest the proceeds in accordance with the terms of the trust, the statute or the court decisions, has been subject to the confusion of what was "a reasonable time." The courts seem to have generally, but no means universally, construed a reasonable time to be one year. The second rule, which imposes on the trustee a duty to convert non-legals within a reasonable time into cash and to re-invest the proceeds in legals, makes the exception that in extraordinary cases the securities may be retained where the trustee's decision to retain is made after it has used good faith, reasonable diligence and prudence in reaching the decision. Both rules, of course, give freedom to the court, the first rule permitting retention if the trustee uses reasonable judgment in deciding that the proper time for conversion has not yet arrived, and under the second rule the court can free the trustee from responsibility for retained non-legal investments either on the theory that ordinary care was used in deciding that the time to convert had not arrived or on the assumption that the special circumstances surrounding the particular investment were such that good judgment justified the retention of the security indefinitely. As a result, therefore, under the first rule the burden is theoretically upon the trustee to prove that it did dispose of the unauthorized, or original, security within a reasonable time, and under the second rule the burden is upon the beneficiary to prove that the trustee retained the unauthorized, or original, investment after it had ceased to be prudent longer to do so. As a practical matter neither rule is extremely helpful at the present time to a trustee who must make a decision on a particular security, especially if that security is a piece of real estate or a stock or a bond selling at a substantially depreciated value, which depreciation in value could be quickly restored if general business in the country should improve, if the price level should rise or an inflation psychology should become dominant in the people Nor is either rule helpful if the security has been or still is without a market, or if it is one of those cases where, though an illegal investment, it pays a high rate of return which appears necessary for the maintenance of the necessary income of the beneficiary, or if it is the stock of the trustee's own bank, concerning whole value it has special knowledge but which value is not now reflected in the stock's market price.

The problem is not solved from the point of view of proper trust administration of investments if the trustee simply takes such action as is necessary to protect its own position, irrespective of the effect of that a tion on the protection of the income or corpus of the trust. The proper solution to this problem probably lies in the trutee using the best judgment of which it is capable within the limitations of the rules governing in its particular jurisdiction. While each trustee may regret the rigidness of the particular rules governing in its jurisdiction, the possibilities of error in judgment at the present time due to present conditions make it imperative that the trustee does not assume to render an investment service which the courts or the Legislature have previously decided it should not render.

The last investment problem confronting the trust department that I want to mention today is the problem arising out of the decline in the amount of securities available for the investment of trust funds required to be invested in "legals." The magazine "Trusts and Estates" in its July issue points out that the latest change in the legal list of New York State, dated July 1, 1939, removed from the list of eligible investments an addition $940,861,000 par value of railroad securities and left only approximately $2,580,000,000 of the same eligible, compared to $7,600,000,000 in 1931.

Actually, there has been an increase in the par value of the eligible securities in New York State due to the tremendous increase in the Federal debt since 1930, the larger list of eligible utility bonds and the inclusion of other items, particularly municipals, which were not included prior to recent years. The possibility, however, of diversifying the investments as between issues and as between types of securities has definitely been lessened.

A number of States have sought to solve this problem for themselves by the passage of laws increasing the list of eligible items or by giving, as in New York State, some authority to a Banking Board or Commission upon application to add items not otherwise eligible. Tennessee and Minnesota, for example, have recently passed statutes permitting investment in single premium, life, endowment or annuity contracts. Arkansas and Missouri permit investment in building and loan association certificates; Illinois in Federal savings and loan association certificates. Florida, Michigan, Nebraska and Ohio now permit investment in building and loan and also in savings and loan or national mortgage association obligations. Housing authority obligations are permitted in California, Colorado, Rhode Island, Maryland and a number of other States.

The theory of the "legal list" itself is subject to grave question. Prof. George W. Edwards of the College of the City of New York has made a study of the effectiveness of the provisions of the statutes of those States having legal lists that pretty definitely proves that either the provisions of the statute were not satisfactory in their inception or conditions have so changed that they can no longer be used as proper standards for separating satisfactory from unsatisfactory trust investments. Undoubtedly, too, these attempts at enlarging the list of eligible securities by the inclusion of new types of securities are only palliativse in solving the problem of the trustee who must invest funds in legals. Undoubtedly they are helpful, but upon the trustee still rests the obligation of selecting items which will protect the corpus of the trust from within that whole group of items that meet the qualifications of the statute. A reasonable question can be raised as to whether a number of these new items, even if they are approved by the statute, should be used by a trustee attempting to do a satisfactory rather than a purely legal job. More than ever is judgment required in the making of such investments.

In summary, therefore, it may be said that the problems of investment facing the trustee today are no different than they have ever been, but their solution is far from easy to see. The economic system of this country is itself in a state of migration and the economic system of the world is influenced by war which is based as much on the use of econmoic forces as it is based upon the use of military forces. While the temptation to take advantage of the new forms of investment is undoubtedly great to every trustee on whom the pressure to obtain income for life beneficiaries has not decreased but has actuallly increased, the need for using good, sound judgment is still greater than ever. A decision to follow the old and tried patterns of trust investment at the present time may not be popular, but certainly it involves a substantially smaller degree of risk for both the beneficiary and the remainderman than a policy whose main justification, irrespective of the word in which it may be couched, is expediency.

The investment problem confronting the savings department today is generally not recognized because it is the practice of most commercial banks not to segrgate their savings deposits from their commercial deposits, but to co-mingle them and invest the entire sum of co-mingled deposits according to the general investment program of the institution. Frequently, only when the quality of mortgages becomes a matter of concern is the segregation of deposits considered.

If the scientific investment program is to be followed by a commercial bank with a savings department, it may well consider what proportion of its deposits come from its savings department and it may well develop a specific investment program for such deposits. The basic reason for this split investment program is that savings deposits, in all but rare instances, do not have the liqidity of commercial deposits, do not require the same operating staff to provide service to customers, and yet do have a very definite cost to an institution because of the interest rate they bear.

In the preparation of an investment program for savings departments a bank is far less hampered by statutes than it is in the preparation of an investment program for trust accounts. The sole controls over its actions are the regulations governing the percentage of mortgages that an institution may own, governing the quality of investments that it may buy, and the amount of an individual investment in relationship to capital. The problem is one of making the investments earn a sufficient income to pay the expenses of the operation of the department, which normally run about ½ of 1% of deposits, the interest rate guaranteed to the depositors, a proportion of the general overhead, and a profit.

Such a program may recognize that while the commercial department of a bank may not at the present time be justified in placing more than 75% of its entire deposits in loans and investments, the savings department is justified in placing 80 to 85% of its deposits in these types of assets. Mortgages, unquestionably, should constitute the backlog of the investments for a savings department. The experience of the mutual savings banks throughout the country, as well as the experience of the insurance companies, leads very definitely to the conclusion that a good mortgage, properly amortized, offers security, steady income, and reasonable maturity in better proportion than any other asset. The experience of banks with mortgages during the deflation of the last decade, difficult as it has been, cannot contradict this fact, for it was measurably better than the experience with corporation bonds. Moreover, the ability of a bank to acquire mortgages guaranteed by the Federal Housing Administration has greatly enlarged the mortgage lending field available to banking institutions and provided a liquidity for mortgage investments because it has created a similarity of them such as they have never previously enjoyed. The experience of the FHA to date bears out the frequently made assumption that if a backlog of insured mortgages is used to provide investment for savings funds only a small reserve need be provided for items that default.

Although the last war did not produce a substantial reduction in the quantity of savings deposits in the country, even though the drives were put on to sell bonds to the public, the increasing familiarity of the public with bonds, and the better rates of interest they bear, may lead in the future to increased investments by the public in Government bonds, particularly of the baby bond variety. Therefore, it is probably desirable that the balance of the investments of the savings department be concentrated in obligations of the United States Government, for while it is impossible to predict the course of the market of United States Government obligations, it is well to recognize their price stability compared to all other forms of obligations. The present war in Europe can well produce a world-wide increasing trend in interest rates and may well cause a further unabalancing of the United States Government budget, but, nevertheless, we must all recognize that the ultimate payment of United States Government securities, irrespective of what may happen to the price level, will be in the form of a monetary unit that can be passed out to the customers through the teller's window. While the holder of a security may be taxed substantially on his income, it is obviously impossible for the Government to tax itself so that it will destroy its only ability to pay.

In setting up this Government account, it is now particularly necessary to stagger maturities over a reasonable period to protect against substantial changes in the market prices of securities that might affect solvency. We can only estimate the possible effect on prices and bankers' psychology of a falling bond market but the great gold imports of recent years certainly have increased the lending power of the Federal Reserve banks to a point where they probably can continue as long as it is considered desirable to cushion the Government market. The impact resulting from the lack of a cushion we have all seen, in the last few weeks, when we watched the precipitous price decline of the railroad, utility company, and industrial corporation securities. Mortgages may fluctuate and the trend of bond prices may turn downwadr, but if the investments of the savings department are concentrated in mortgages and United States Government obligations of not more than medium-term maturity, earnings should always be sufficient to pay present rates of interest, liquidity should always be sufficient to meet requirements, and the operation of the department should always be profitable.

Basis for Analysis of Municipal Securities for Bank Investment

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The topic which has been assigned to me to discuss with you this afternoon is "A Basis for Analysis of Municipal Securities for Bank Investment." I am particularly glad that the small "A" in included, for that makes it clear in the beginning that I am simply presenting to you one approach to this problem. It correctly infers the existence of more than one approach. In relation to some bases currently advanced, some of my views may appear unorthodox.

Before we can intelligently consider together this topic, certain definitions seem in order. "Basis" is defined as "that which supports or sustains; a foundation; the groundwork; the first or fundamental principle"—something upon which we may rest with confidence. "Analysis" is "an examination of anything to distinguish its component parts, separately, or in their relation to the whole." For the purpose of this discussion this afternoon no reference is made to obligations of any State government, and the term "municipal securities" is being used to include obligations of counties, cities, towns, villages, townships, school districts, parishes, and such like civil divisions of these United States.

It seems appropriate to define one other term in the topic assigned to me, that is, "for bank investment." This assumes, and I think correctly so, that there can, and does, exist a different problem in considering an obligation as to its appropriations for bank investment as against its desirability for purchase by an individual or institution, such as an endowment fund or insurance company. An individual has, undoubtedly, the right to speculate with his own funds, but I hold that no bank has that right with its depositors' funds. Therefore, speculative obligations should be excluded from consideration by banks, and only obligations which are "money certain" should be considered eligible. The funds which a bank has for investment differ from institutional funds in that they are subject to unpredictable fluctuations in volume, and a bank, therefore, must endeavor to so plan its whole investment program as to include only obligations which can be more or less rapidly converted into cash either through maturity or shiftability, without any appreciable discount of the principal. One further theory of bank investment which I hold is that securities purchased should be bought always in anticipation of being carried to maturity, with payment of principal at maturity the first consideration, marketability definitely secondary, and yield the last consideration. Therefore, under my theory securities (whether municipal or otherwise) eligible for bank investment will be confined to the medium and short maturity obligations, with maturities so arrange, or "staggered" as to provide a steady flow of funds, through payment at maturity; will include only prime obligations, of obligors of recognized reputation, and will avoid speculative investments as a wise man shuns a contagious malady.

We seek then a fundamental principle for examining the various factors—both as component parts, separately, and in their relation to the whole—affecting the obligations of minor civil divisions so as to determine the suitability of such securities for the employment of bank deposits. We are endeavoring to answer two questions, and these questions are the same questions we endeavor to answer in connection with an application for a commercial loan, namely: "Can the borrower meet the obligation in accordance with its terms?" and, second, "Will he do so?" Stated another way: "What will be, at maturity, the ability and the willingness of the issuing unit to pay?"

First, of necessity, we must know the whole truth about any unit under consideration—and the unvarnished truth is not always easily uncovered. . . .

Let us give at this point a little consideration to the historical record of municipal debt in the United States.

In "The Debt Problem of American Cities," published in August, 1933, **Philip H. Cornick says:**

"None of us here can remember what happened a hundred years ago. That is one reason why progress in municipal finance is so difficult. Our cities go on for century after century, but the citizens who have to administer them, and the other citizens who buy their bonds, change from generation to generation. . . . Consequently the cities themselves and the successive generations of bondholders are prone to go on doing the same old thing over again once or twice in every century."

One of the most comprehensive and valuable studies in this field which has come to my attention is a book entitled "Municipal Bonds—A Century of Experience," by A. M. Millhouse, J. D., then Director of Research, Municipal Finance Officers' Association, published in 1936 by Prentice-Hall, Inc., New York City. I want to quote briefly from the first chapter of that book:

"Until the present depression it was generally believed that municipal defaults belonged irrevocably to the past. Defaults and railroad subsidies somehow had become inseparably connected, and were assigned together to the realm of forgotten limbos. The present generation of municipal bond men and investors grew up with a genuinely honest and implicit faith in the Gibraltar-like character of 'municipals.' Pre-depression bond literature of the present century was replete with evidences of such faith; likewise, local officials knew little of past default troubles. A long period of rising prices, increasing public revenues and general business prosperity had taken the sting from debt payment, so that a borrower's day of reckoning conjured up no unpleasant thoughts. The depression era 1929-1936, with an almost unprecedented crop of municipal defaults, has taught municipal officials, bond men and investors alike a new lesson. The downward swing of the business cycle has made them debt-conscious; and for the majority of the present generation this is a new experience.

"The 13-year period 1918-1931, which preceded present default difficulties, must be re-examined, since the causes thereof can largely be found in over-expansion of credit during those years. Prior to 1918 the yearly totals of State and municipal bonds issued combined had not exceeded 500 million dollars. Municipal issues for several years had averaged close to 400 millions. . . . The years 1919 and 1920, however, witnessed a marked increase, and by 1921 the era of over-borrowing was 'hitting a heavy stride.' From the vantage point of what is known today, the rapid pyramiding of municipal bond sales during the decade 1921-1930 can be surveyed. . . . The annual average of municipal bond sales for the decade 1921-1930 stood at the unprecedented height of $1,147,618,500—more than the total amount of municipal debt outstanding in 1890. . . . More significant than sales, however, were the net additions to total municipal debt, which averaged approximately $845,500,000 annually from 1923 to 1931, inclusive. Thus, within a short space of years financial ills were crowded into our history in such number as to keep municipal finance in a turmoil for two decades or more."

What we are now endeavoring to do is to arrive at an acceptable basis whereby we may profit from the experience of the past; whereby, at least this generation of bankers may distinguish between the "sheep" and the "goats" in the field of municipal borrowers. My studies in the field have convinced me that the majority of our municipal units are in satisfactory financial shape and their obligations sound. The bankers of the United States are evidently convinced of the same thing. The last annual report of the Federal Deposit Insurance Corporation shows that during the calendar year 1938 the total investment of insured commercial banks in such obligations (including in this instance State obligations also) increased 16.3%, the largest rate of increase of any general asset head used in that report.

In our search for a sound basis of analysis we are sometimes like a child seeking the pot of gold which is said to repose at the end of the rainbow. He seeks and he never finds the end of the rainbow, and therefore never finds the pot of gold. We seek some simple rule of thumb which will always separate the good from the bad, the sound from the unsound, and we never find it for the simple reason that it does not exist.

Alexander Hamilton said: "The basis for public credit is good faith." True, but who can foretell "good faith" a generation hence, and are there not other considerations? In the "Financial and Investment Review" of July, 1935, Dr. Laurence R. Lunden observes:

"Willingness to pay and ability to pay are not coordinate factors in the case of county bonds. Neither governments nor, as a rule, individuals, are likely to show unwillingness to pay until their ability to pay has been reduced from what it was at the time the debt was contracted. . . . In general it may be said that the criteria of ability to pay forecast willingness to pay."

If that be true, and the record of the past seems to support it, we seek, then, "the criteria of ability to pay."

Here let us glance for a moment at some criteria of ability to pay most frequently emphasized as they appear in the light of the record of the past 10 years. Someone advances the thought that the ratio of debt to assessed valuations or to estimated true value of taxable real property will distinguish between sound and unsound, that a debt above a given ratio is unsound, and by inference, that a debt below that ratio is sound. Well, "the test of the pudding is in the eating thereof," and to my mind the most satisfactory way to test any theory is to apply it to some case or cases where the facts are known and thus prove its truth or fallacy. That I have attempted to do in this instance, and I am sorry that the record simply does not support a standard so easy of application as that. In one State I have been able to secure a record of the debt, both direct and overlapping, of 100 counties as it existed in 1928. Also available are assessed valuations for those same units, which valuations are reliably estimated to have approximated true values. Let us assume that in 1928 you decided to purchase securities of any of these counties whose ratio of net direct debt to assessed valuations (which as I have noted in this case approximated true values also) did not exceed 8%. You would have purchased obligations of 68 of the 100 counties included in the study, and the average would have been in your favor, for of the 32 counties whose obligations would have been excluded, 31 defaulted within six years. But the sad part is that of the 68 whose obligations you did purchase, 33 defaulted within the same period. You would have been 48½% wrong, and that is entirely too heavy a percentage of error for bank investments.

Let us look then at the ratio of net overlapping debt to assessed valuations and see if that is any more reliable. Let us assume that your maximum acceptable ratio here is 10%. You would have purchased the obligations of only 36 of the 100 counties, and again the average is in your favor. For of the 64 units excluded, 50 defaulted within six years. But what of the favored 36? Sad but true, 13 of them defaulted in the same period, a percentage of error of 36%, which is too high.

I have had opportunity during recent months to study over 100 cases of actual defaults which have occurred during the past eight years, the units studied being scattered over a dozen States in the Union, and I have found units with a high ratio of debt to assessed valuations side by side in default with other units having relatively low ratios. True assessed valuations of taxable property is one base upon which the debt rests, and properly used in relation to other factors, the ratio of debt to assessed values is valuable and indicative, but not infallible.

Another criterion sometimes advanced is per capita debt. Here there are wide differences of opinion both as to the reliability of such a measure, and, if relied upon at all, the acceptable figure to be adopted. Let us assume that in the cases under consideration you adopted as your maximum acceptable figure the median per capita debt of the 100 counties. Your maximum figure would have been $64.00 per capita, which figure incidentally is well below most such standards which I have seen advanced. Using that figure as your standard, the obligations of 29 counties would have been excluded and you would have purchased obligations of 71 counties. Again the averages would have been in your favor, for of the 29 excluded counties, 27 defaulted within six years. But that would have been little consolation to you, for of the 71 eligible counties, 37 defaulted within the same period.

But you say, "A study of what happened in one State is not enough." Admitted; so let us look at another State. In this second State 44 county units were studied. Let us apply the same criteria and see what happens. Of the 44 units here included not a single county has a ratio of net direct debt to estimated true value of taxable property in excess of 6½%, yet since 1930 nine of the 44 have defaulted. In this second States the basis of assessment differs sharply from the other, so perhaps you prefer to rely on the ratio of direct debt to assessed valuations. If so, you would have fared better, but you would not have escaped altogether. Thirty of these 44 counties have a ratio of 8% or below, and 14, being above that figure, would have been excluded. Of the 14 above the 8% ratio, six defaulted, while three of the 30 below that figure experienced default. Turning then to the ratio of overlapping debt to estimated true value, and using the same maximum acceptable ratio of 10%, only one county is excluded, and it did not default. Forty-three of the 44 would have been included and nine of the 43 defaulted.

And what of per capita debt in this second State? And here a striking difference is noted. In the State first mentioned we found the median per capita debt figure of the 100 units studied to be $64.00, whereas here we find the median to be only $13.00 per capita. Again using the median as our maximum acceptable figure, we include in our portfolio the obligations of 26 counties and exclude 18. Of the 18 excluded, five defaulted; of the 26 included, four defaulted. But bear in mind that in both of these States the median per capita debt figure which we used as our maximum acceptable figure is far below the acceptable figures usually advanced.

The further illustrate the fallibility of the criteria heretofore mentioned, let me point out the following interesting facts: In the State first mentioned the ratio of direct debt to assessed valuation (which in that case, as previously noted, also approximated estimated true value) in the defaulting counties varied between a low of 2½% and a high of 24½%; the ratio of overlapping debt to assessed valuations between a low of 5% and a high of 38%; the per capita from a low of $15 to a high of $205. In the counties which did not default the ratio of direct debt to assessed valuations varied between a low of 1% to a high of 9%; the overlapping ratio from a low of 3% to a high of 15%; the per capita debt from a low of $15 to a high of $80. In the second State mentioned we found the following variations in the defaulting counties: Ratio of direct debt to assessed valuations from a low of 6% to a high of 25½%; ratio of direct debt to estimated true value from a low of 1¼% to a high of 6½%; ratio of overlapping debt to estimated true value from a low of 2¾% to a high of 9¾%; per capita debt from a low of $8 to a high of $31. In the 35 counties in the second State which did not default we find the following: Ratio of direct debt to assessed valuations varied between a low of ½% and a high of 26% (higher than the highest defaulting county); ratio of direct debt to estimated true values from a low of ¼% to a high of 5¾%; ratio of overlapping debt to estimated true value from a low of ¼% to a high of 12½%; per capita debt from a low of $1 to a high of $42 (with three non-defaulting counties having a higher per capita figure than the highest defaulting county).

It would appear, therefore, that with the wide variation in methods of assessment in the various States (and for that matter within States), with different controlling statutes, powers and limitations it is impractical, nay impossible, to develop any acceptable ratios of "measuring rods" of nation-wide application.

I submit that the only practical approach is on a State-wide, State-by-State basis. Here is apparent an unusual opportunity for the respective State bankers' associations to render a most useful service, both to their members and to government. Within each State a study should be made county-by-county, by some banker in the county, and within each county each individual unit. The county studies should pay special attention to the economic foundation and trends. The studies should then become available to all through a central file, probably in the office of the State association. In such a plan you will receive hearty support of all supervisory agencies and especially your State banking departments.

If then it be true, as I have suggested, that no standard of nation-wide application appears possible, what then? Well, for one thing, far too little attention has been directed to the indices of approaching trouble which may be detected in a careful analysis of the economic foundation of units. And so as a first step in the development of a basis for analysis of municipal securities for bank investment I suggest that the following facts be developed:

1. What is the trend in the population? Static, or up or down? and why?
2. What is the composition of the population? What racial groups predominate?
3. Into what principal groups do the gainfully employed fall? What is the relative importance of the main sources of employment, such as agriculture, textiles, mining, &c. And what is the long-time trend in employment?
4. If the unit depends to any extent on agriculture, what is its record? What crops are produced and how stable are they? What is the trend in crop production and money value? Are the crops of a nature which exhausts the land and leaves it valueless?
5. What industry is present? What is the trend in that industry as shown by a comparison of the following indices over a period of years: (a) Invested capital; (b) Raw material consumed; (c) Annual value and volume of manufactured product; (d) Average employment, net profits, &c.
6. If mining of any character is of any importance, how near is depletion of known supply?
7. How serious is the problem of public assistance? And what trend is evident?

And here we have a growing problem which, if not carefully handled, may in some cases disrupt municipal economies.

You have probably noticed that in every item mentioned in the suggested "economic analysis" stress has been laid on trends. I submit that trends, the road which the unit is apparently traveling, and not the position in which it appears at any given moment, is the answer to our whole problem.

Now let us consider the second step in our basis—Financial Analysis.

What trends should be developed here? I suggest:

1. Assessed valuations and estimated true values on a comparative basis—the current year, the first, second, fifth and tenth previous years.
2. The tax rate on the same plan—this year, last year, year before last, five years ago and ten years ago. An understanding of the treatment of delinquencies is also valuable.
3. The tax collection record. You should know the actual levy in dollars for the past ten years, with the amount and percent of levy delinquent for each of these years, as of the date of the statement, and with additional year columns to show the amounts delinquent as of the five preceding years. Thus the trend in year-end and accumulated delinquency is revealed.
4. Data on total receipts and disbursements. Probably no more important index of ability to pay exists than the trend in income as related to debt and other requirements. Here again the ideal statement would cover the current year, the two preceding years, the fifth and tenth preceding years. The date should reveal the principal sources of income so that you may determine their stability, and in the main items under disbursements so that dispensible and indispensible expenditures may be segregated.
5. A summary of debt over the preceding ten years so that the trend is apparent. Here let me call attention to something which a study of a number of default cases has shown. Units with rapidly developed debt have shown marked susceptibility to default.
6. A complete break-down of the debt existing at the date of the statement, showing (a) full-faith and credit obligations, (b) special obligations, not full-faith and credit, and (c) floating debt. Here let me call your attention to another thing which a study of default cases has emphasized: Heavy and continued reliance on floating debt financing is a fairly reliable symptom of impending difficulties. The schedule of debt should be complete enough to make possible preparation of a chart showing the maturity schedule of the then existing debt. Poorly arranged maturity schedules have contributed in no small degree to municipal default in the past.
7. What sinking funds are on hand and how are they invested? I need hardly remind you that the temptation to "raid the sinking funds" by borrowing therefrom for current purposes is hard to resist.
8. What is the amount of and trend of overlapping debt, so that you may determine its effect, if any, on the fiscal policies of the unit under consideration.

In the "financial analysis" as in the "economic analysis" trends are basic.

The third great factor which we must consider is management. Hard to evaluate, too often expressed opinions influenced heavily by personal likes and dislikes, and yet—no other answer can be found to many cases in the "crazy quilt" of municipal defaults of the past eight years, except management. Why has one unit, with a high debt by any standard, been able to avoid the troubles which have involved some other life unit with equal or even lesser debt to cope with and equivalent economic resources? The answer seems obviously to be sagacious management. Why have units with comparatively low debt, with more than sufficient economic resources, experienced debt default? And the answer seems clearly to be incompetent management. More and more attention must be paid to the management factor in our municipal units, as their problems become more and more complex through public demand for increased municipal services.

Our studies covered two small cities in one State, about 40 miles apart. The population of each is in the neighborhood of 15,000. City "A" has most of its streets paved, has good schools, has a well-operated municipal water and light plant; its citizens enjoy an excellent police department, fire department, health and sanitation department, and its economic resources are not above the average for like cities. It has a low tax rate, a very small general obligation debt, no floating debt, a sizable cash surplus on hand, an only nominal outstanding special debt in the form of special assessment obligations for paving and water and sewerage extension. It has never experienced any debt trouble of any kind. City "B," in so far as services rendered are concerned, is almost an exact duplicate of City "A." Streets are paved, it has good schools, a municipal hospital; it has a fair police department, fire department, health and sanitation department, and yet it has very heavy debt. Its economic resources are, of anything, slightly greater than City "A," and yet, in the past eight years, it has been in default as to principal and interest; it has had judgments recorded against it, and on two or three occasions has been unable to pay city employees for short periods. Management alone is the answer to the difference in these two units. City "A," for the past 15 years, has had outstanding business administrations; City "B," on the other hand, until four years ago had a series of incompetent administrations. Four years ago the citizens of City "B" rebelled, and elected new officials from top to bottom. In four years City "B," with efficient management, has completely corrected the debt defaults, has practically restored the credit of the city, has reduced its debt by nearly 25%, and has been able to ease the tax burden on the citizens. Case after case might be cited, "Where every prospect pleases and only man is vile." We must pay more attention to management.

I have paid scant attention here to special districts, organized usually for the sole purpose of issuing obligations. The principles outlined, however, are believed applicable. No comment has been made on so-called single-industry towns. The default records for the past eight years clearly show that such units are, on the average, hazardous credit risks; their economic foundation is unsound, and where the foundation is unsound, the superstructure must be constructed and observed with extreme care. And, in so far as investors are concerned, obligations of such units must be carefully watched and limited to very short maturity.

About a year and a half ago the President of the National Association of Supervisors of State Banks appointed a committee to study municipal obligations. I have had the pleasure of serving on the committee to date. That committee has evolved a credit file which, while not advanced as ideal or all-inclusive, is nevertheless recommended in the belief that, properly used and understood, it presents a basis for analysis of municipal securities for bank investment.

In these remarks I have wandered inexcusably, but it is a big field and if I be permitted to attempt to sum up my remarks into any simple statement, it would be this—that in municipal finance as in private finance, "it isn't the strength of the wind which blows but the set of the sails which counts."

Discussion Incident to Address of Mr. Wayne

Chairman Frazier: As these facts and figures have been shot at you very rapidly, it seems to me you will probably have questions you would like to ask the last speaker. You may ask such questions now.

Dr. Preston: I should like to ask if a local political situation does not often enter into the ability to pay?

Mr. Wayne: Very, very definitely. I felt I was pressed for time and did not include an illustration of that kind in my talk to you. As an illustration of two situations which illustrate that very forcefully, take two small cities just a few miles apart, operating under the same conditions, same size, same economic background. One had for 15 years an excellent business administration; the other had an accursed one. The one in excellent condition has a very good ability to pay; the other, God help them! The character of the management enters into that problem to a very high degree. Where a city or a county has had bad management and has suffered difficulties and the people rebel, as they sometimes do, and elect a new administration that gives competent management, in our own department we wait until the next election before giving credit. If the people support the new idea or administration in the next election and continue with a good business administration, then they are entitled to credit.

W. A. Hale (Martinez, Calif.): Do you know something about the political ability of the counties right around where we are? Suppose we want to buy securities of a town or city two or three hundred miles away, how could you find out about the efficiency of the management of that city?

Mr. Wayne: In my State there has been prepared a staff in every county in the State. For every city, every school district, every taxing unit—we have only 710 of them in the State of South Carolina—we have endeavored on a county-to-county basis to have some reliable banker in the county study the units in his county, and that is available in my own department. That is available, however, without the endorsement of the department. However, I hold that my department has no right to tell the bank what to buy. I submit that that is the only practical plan. Some States, like in Michigan, have a municipal advisory council which is very capably managed, but we must develop some medium for gathering that information.

Modern Mortgage Standards

By Frederick M. Babcock, Assistant Administrator and Director of Underwriting, Federal Housing Administration, Washington, D. C.

Currently all topics are discussed in terms of the world situation. How will the war affect housing, the mortgage business, and real estate? How will our modern mortgage standards hold up under the impact and shock of conditions created by the opening of war? What will those conditions be in the near future and what policies may we adopt to direct our operations?

The Federal Housing Administration insures lenders against losses resulting from the investment of private funds in mortgages secured by dwelling properties. The wisdom of the use of the insurance device as a mean of introducing an element of control into the mortgage market has been generously discussed during the five years that this governmental agency has been in operation. In general, the justification has been found in the results obtained. Construction has revived; reemployment has resulted; confidence in the quality of the risks and in the insurance protection itself has made investment funds available; and numerous by-products of the system, such as better construction standards, better control of neighborhood development, better selection of credit risks, and better facilities for the flow of investment funds earmarked for mortgage investment have indicated that this insurance device is a means by which the Federal Government may safely and effectively cooperate with business.

The system does present one element of danger—one which has not, to my knowledge, been brought out sufficiently in meetings of this character. I refer to the tendency which such an insurance system has to cause lenders to feel less responsible in the selection of risks for investment. There are an increasing number of lenders who rely more and more on the examinations of the FHA's underwriting organization and look to the insurance rather than to the credit status of the borrower and the quality of the real estate security. Admittedly, this is most flattering to the FHA underwriting organization. But, in so far as it does represent a shifting of the responsibility properly imposed on lenders by their stockholders, depositors, or policy-holders, it is to be deplored as a bad tendency.

It is only fair to point out, however, that the tendency appears only in a portion of the lending institutions with whom we do business and I suspect that these lenders would be a bad element in the competitive mortgage market anyhow and that, by reverse reasoning, the FHA underwriting operations are essential and beneficial safeguards which would be utterly lacking if they were not provided by a governmental agency.

The presence of the Government in this relationship with private enterprise has a number of good aspects. The facilities which the Government offers to provide market guidance to mortgage lenders are superior to the facilities now available or likely to be provided outside of the Government. Statistical surveys to secure information on housing and real estate can be made by the Government on a scale which would not be possible if such activities were attempted solely by mortgage lending institutions.

Congress has authorized the inclusion of real estate and mortgage data in the 1940 Census. While there has been no specific appropriation for this work as yet, it is confidently expected that there will be. What items of information will be included in the enumerations is not yet known, but it is reasonable to suppose that data covering rent trends, costs of home acquisition, vacancy statistics, types of financing, and numerous other significant fields will be adequately covered.

The mechanics of operation of the FHA system of underwriting has long since gained a general acceptance. It is based on the concept that each proffered mortgage loan has a degree of risk attached to it and that the risk is subject to measurement—at least predictable by groups of risks in te ms of probability. We use what we call the risk-rating system which embraces a number of direct analy es of the relationships which various factors have one with another. The system does not assume that risk is directly measured by the ratio which the amount of the loan bears to the estimate of the value of the property. Rather it looks directly to the varying qualities of the many elements of relative strength and relative weakness in arriving at a final conclusion or mortgage pattern rating which determines whether or not the proffered loan is eligible for insurance.

The syetm works. At least we may say it works if we are allowed to express a preliminary judgment based on the record of the last five years. We have insured more than 416,000 mortgages to date. We have acquired only 856 properties as a result of foreclosure by lending institutions. We have sold about half of these with an average loss of about $575 and a total net charge against the mutual mortgage insurance fund of about $237,000,000 or less than 1% of the assets of the fund.

At the same time, we have, after five years of operations, achieved a self-sustaining basis. In the fiscal year ending June 30, 1941, we will have expenses of $13,800,000, as now contemplated, against an expected income of $20,000,000 or more. This will enable us to pay all our expenses without having to ask Congress or the Reconstruction Finance Corporation for any funds whatsoever and to add during the year more than $8,000,000 to our reserves.

During the first and second years of our operations, the cases which we rejected were deemed unacceptable for a great variety of reasons. The causes for rejection were divided almost equally between factors related to the characteristics of (1) the physical security, (2) the locations, and (3) the borrowers. Since those earlier periods we have seen a shift so that currently something like 37% of all cases rejected are refused because of the characteristics of the first two, namely the physical security or locations and over 60% are refused because of low ratings of the borrowers. Of course, this means primarily that the builders and developers are now better aware of our standards and less disposed to try to foist inferior housing on the public. At the same time it also indicates a lack of awareness or carelessness on the part of some lending institutions with respect to the characteristics which eligible borrowers should have. It would seem that the picking of credit risks would be easier for most institutions than the selection of real estate risks. Perhaps, however, the traditional bad habit of relying solely on real estate security still persists and that the more modern shift to a recognition of the fact that good mortgages combine both good security and good borrowers has not yet gained the acceptance it should have.

But here again our data shows that lenders may not be classed in a single category and that a surprisingly large percentage of institutions send us few cases requiring rejection.

There is always a great temptation to offer a plan like FHA as though it were a panacea to cure all the problems in the construction, housing, mortgage and real estate world. Few of the officials of the FHA are prepared to do this. We feel considerable pride in the achievements which this particular agency of Government has made but we are constantly seeking formulas for improvement and refinement of the system. The part to be played by bankers in making FHA a more effective instrumentality is, or should be, obvious. I am sure that, from the Administrator himself on down through the ranks, you will find few persons who are not open-minded and hungry for suggestions. By and large, we are the types who cannot only take advice but really know we need it.

For example, we have set up the FHA and are operating it under a number of policies which were geared to the probability that real estate was in for a gradual improvement in early years but certain, at future periods, to have to meet depressions of serious proportions. During the five years we have had no really violent changes in the price levels of real estate, rents, or building costs. Now this European war breaks out. What does it do to the mortgage business? What does it do to our mortgage insurance business? Should FHA start to close down on its volume and take only the exceptionally safe loans? Are some radical changes needed in our regulations? Let us look for a minute at the probable effects of the war on the mortgage business.

In the secondary market for mortgages the purchasers of mortgages, especially the commercial banks, switched back to the purchasing of bonds upon the opening of the war. This has had the effect of removing, to some degree, competition which savings banks, mortgage companies, life insurance companies, building and loan associations, and other sources of mortgage money have had to meet.

Some people say, quite wrongly, I think, that a pickup in the demand for commercial loans will cause many banks to abandon their activity in the mortgage loan business and to devote their excess funds and energies exclusively to the commercial field. It is commonly agreed that banks as a whole have more than enough excess funds to take care of almost any given amount of increase in the demand for commercial money, and that there will still be plenty of room in their portfolios for mortgage loans, especially those insured by the Government and returning a substantial yield over a long period of years, with less risk and greater investment return than most commercial loans can possibly offer. And further than that, of course, most lending institutions which have participated heavily in the FHA program will continue to do so if only because they have large amounts of long-term deposits which quite naturally must be segregated against long-term assets. And there is, in all probability, no long-term asset more liquid and more suitable as investment for these deposits than FHA insured mortgages.

The making of mortgages at rates under 4½% seemed to disappear almost immediately upon the opening of the conflict. 4% and 4¼% money appears to be no longer available. 4½% money for insured mortgages is available. This has also helped the traditional mortgage lenders to compete for business. Upon the breaking out of war a few institutions shut down on all mortgage lending temporarily. It is supposed that this means nothing except sufficent uncertainty to wish to observe trends before changing or adhering to present lending policies.

Prior to the opening of the war, insured mortgages in many instances, were selling at a premium, typical prices being 104½-105. The price has now declined to 102-102½. Because of this decline, there has been a decided tendency to reverse the placing of origination costs. Instead of virtually buying business by appealing to builders with low initial costs mortgagees are now tending to place this expense on the builder and, of course, on the borrower.

The purchasing of houses is continuing at the same peace. During the first week of the war new purchasers were defiitely scared and sales contracts were cancelled in some instances. However, the market revived ptomptly and there is no evidence to indicate that fear is a depressing factor in the market.

It is perhaps unfortunate that the pent-up demand for houses should reach its flood just at this juncture in world affairs when a sudden change in outlook may make it impossible for us to satisfy the demand. I say this only because all of us want more than anything else to maintain America in its peaceful ways and to continue our efforts to rebuild and revive the American economy. I do not think, on the other hand, that an even greater industrial pick-up than anything we now anticipate will greatly reduce the willingness of lending institutions to participate in the FHA's home-building program.

Builders, capitalizing on the war situation, have commenced to complain bitterly about the advancing of prices of building materials. They are, in some instances, using this as a sales argument saying in their advertisements that "the price of this house is $5,995 until Oct. 1—thereafter $6,495."

Building costs shows a tendency to increase somewhat, principally steel. It is too early to attempt to be precise with respect to building costs. We hope (possibly against hope) that no pronounced advance occurs. The Department of Commerce says that costs are up 1% only since Sept. 1. The character of our neutrality or, Heaven forbid, participation in the war, will control. Costs could remain well in line. Or they could advance to high levels.

Some people feel that rising building costs may accompany greater industrial activity and will check building, and that the uncertainties of the present crisis will deter people who would otherwise do so from undertaking home ownership. Thus far we have been able to see no appreciable reaction in our business to the war crisis.

It is generally agreed that there is a strong probability of booms in industrial areas, especially ship-building and steel-mill towns, that such booms will come somewhat later due to oders for arms and other items of war trade both for foreign markets and the United States Government. The extent to which such booms gather headway is presumed to depend heavily upon the revision of neutrality laws and, ultimately, of course, upon actual participation in the war by this country.

The ultimate effects of the war on real estate and mortgage investments will probably depend on its duration. It is probable that the early effects will be more stimulating than retarding.

The FHA will carry on at its present tasks. First problem will be the relation between valuations and higher costs of construction. Other problems will arise inevitably. We can, at this immediate juncture, do no more than suggest that we know of no reasons as yet to abandon the confidence which we had a month ago.

Discussion Incident to Mr. Babcock's Address

Chairman Frazier: Do any of you have any questions you would like to ask of Mr. Babcock, any questions that you may have had previously or any that have come to your mind during his talk?

Mr. Chaffee: I would like to know whether he can say anything concerning the possibility of an increase in the FHA rates from 4½% to 5% in view of the circumstances existing today?

Mr. Babcock: The reduction to 4½% last summer, followed a series of conditions with which you are all familiar. That was before the opening of the war. There has been no discussion except the corridor discussion of a change upward from 4½% to 5%.

Mr. Baker (San Francisco, Calif.): Under Title I, Section 3, I should like to ask whether it is contemplated that the amount of recovery of the FHA will be credited against the 10% insurance after foreclosure?

Mr. Babcock: Under the existing regulations, as I understand it, claims paid are scored for what they are worth. Where the Government has acquired a property through foreclosure after the Government sells that property, the proceeds will be recredited to him.

Mr. Baker: One further question. Can you now give us any idea as to the approximate average amount of the FHA loan and he average term, with its present reference to what it may have been a year or two years ago, in other words, whether the average loan is smaller or not, and the term shortened?

Mr. Babcock: There has been a decided tendency for the amount of the loan to be smaller. I do not have exact figures to give you, I am sorry, but the trend has been to lower loans.

C. H. Olswang (Seattle, Wash.): Foreclosure costs are naturally different in different districts. Do you have any data as to whether foreclosures are concentrated in certain districts in relation to the costs of foreclosure?

Mr. Babcock: Our foreclosures have definitely been localized in five districts. Our experience to date is the great majority of foreclosures we have had have been in five districts, and greatly less in the other districts. It is just in my mind in giving you this information that they did not seem to relate to the costs of foreclosure being greater or less.

Chairman Frazier: Have you any further questions you would like to ask of Mr. Babcock, gentlemen? I am sure you feel as I do, that the round table discussion is something that ought to be encouraged. I did not expect the number of members that we have had here today. In fact, there are two and a half times the number we thought would be present. There seems to be nothing further so we will close this round table meeting at this time.

Remarks of W. P. Albig and Raymond R. Frazier, Presiding Officer

The procedure incident to bringing under way the Round Table Confrerence on Investments and Mortgages in connection with the convention of A. B. A. follows:

W. Espey Albig (Deputy Manager, A. B. A.): The meeting will be in order. The bringing of a round table conference to the annual meeting of the American Bankers Association is a new adventure. It represents something of real value to the assnual meeting, and because of that it is our hope that meetings of this type will be introduced at every annual convention. You might call them "grass root" meetings.

I am exceedingly gratified that I was called upon to introduce the presiding officer of this meeting. He came as a pioneer into this country at a time when the savings institutions and banks had not developed in this part of the Western country. His record bears testimony to the principles he developed since he settled in this State a good many years ago. He is a banker and a gentleman, and it gives me great pleasure to introduce to this meeting Raymond R. Frazier, Chairman of the Board of the Washington Mutual Savings Bank of Seattle.

[Mr. Frazier assumed the Chair]

Chairman Frazier: We are all familiar in a general way with the basic principles which should govern the management of trust funds. We have several experts on our program today who will address themselves directly to the technical details involved in this problem. It is not my intention in any way to anticipate their contributions to these discussions.

It is safe to presume that most bank failures are caused by bad management,—and oftentimes we may lay the entire blame for the bad management to one thing—*Inexperience*. Someone has said that a man is not equipped to take over the responsibilities of bank management until he has gone through at least two major depressions. Even so, life is very short and we have had to do something to make up for lack of individual experience. As a result, Congress and Legislatures of many States have undertaken to set up rules and regulations based on the experience of our forefathers down through the generations.

There can be no doubt of the wisdom and value of legislation governing the pooling and the investment of the surplus earnings of thrifty workers, because savings are the base of all prosperity and seconomic advancement everywhere.

They tell us if a bank fails in China, the State corrals all the officers and directors of the bank and decapitates them. The fear of having one's head chopped off should prove an effective deterrent to looseness in bank management. We cannot well hope for the adoption of such a short-cut remedy here in the Occident.

Of course you cannot endow a man with intelligence or character by legislation. It is possible, however, to provide better and better investment laws which, among other things, undertake to insure that only men of recognized high character may be permitted to manage savings funds of banks.

The laws of New York State and Washington State, for example, are calculated to insure the high character of savings bank trustees. In New York and Washington State no man is permitted to serve as a director of a savings bank who has had his debts, his individual debts, I mean, forgiven by the bankruptcy courts. That's a good law. You do not want a man who has been a failure to the extent of bankruptcy, to manage your savings funds. Neither do I.

Also the laws of the two States mentioned provide that a savings bank director forfeits his office if he fails to pay a personal judgment lodged against him within three months after such judgment,—unless he appeals the case and files a bond in form and amount sufficient to protect the judgment creditor.—That kind of law helps. Moreover, the laws of the two States mentioned—I mention New York and Washington State because of greater familiarity with those laws (other States may have as good or better)—prohibit the lending of savings deposits of a bank to a director—or "trustee" as a director in a mutual savings bank is called. That would be a good law for banks of all kinds.

Of course banks of discount have a lot of deposits on which they are not required to pay interest, and they can afford to take bigger chances than can a trust company or a trustee savings bank which must pay interest on all deposits.

I think behind desire for volume lurks the greatest individual danger that besets the management of savings institutions.

The desire to be big leads to the acceptance of deposits to the legal limit, and oftentimes of accounts which do not classify as genuine savings accounts. When you get too big for the community there is an overwhelming temptation to reach out and make improper investments.

In connection with our mortgage investments, we should bear in mind this fact: There will not in your generation be another HOLC to bale you out.

May I ask you to listen attentively to the words of wisdom which these distinguished gentlemen will utter here. You all know the subject of this afternoon's round table conference is "Investments and Morgages." Our first speaker [O. Paul Decker] is a former lecturer in Northwestern University, and at present he is the Vice-President in charge of investments of the American National Bank & Trust Co. of Chicago, Illinois.

ADDITIONAL BANK SERVICES

Three talks were given under this head by, respectively, Bert H. White, H. V. Prochnow and W. B. Harrison

Industrial Research as an Aid to Bank Customers

By Bert H. White, Vice-President Liberty Bank, Buffalo, N. Y.

The Scientific Research Committee of the National Association of Manufacturers held a most important meeting last spring. Present were representatives of American industry, both large and small, who had been invited to sit in to help solve a common problem. Statistics were introduced which emphasized the fact that notwithstanding a generally accepted belief that industrial research goes hand in hand with good management, only one company in a hundred has research facilities worthy of the name. This joint committee was endeavoring to develop ways and means of making at least a few of the remaining 99 more conscious of the benefits of industrial research.

It was an informal meeting. Dr. Karl T. Compton, who, you will recall, addressed one of the general sessions at last year's convention, made the first suggestion:

"Let's tell them more about the new products being developed as a result of research. We all like a winner. Let's whet their appetites by showing them some of the plums their competitors have plucked."

That seemed logical enough and was well received.

Then another very able gentleman, Dr. W. B. Bell, President of the American Cyanamid Co., arose and said:

"Isn't there too much of this going on already? We can't tell these boys that all they need do is go in for research and from then on everything will be milk and honey. That's going to develop repercussions. Let's tell them about the difficulties in carrying through on a research project so that this movement doesn't turn out to be a boomerang."

Bradley Dewey, President of Dewey & Almy, one of New England's good old companies, was the next speaker. "What good," said Mr. Dewey, "is it going to do to whet a man's appetite for something if he cannot get its benefits? And, what good it is going to do to tell the manufacturer about the failures of something he doesn't know how to use? I think the way for us to begin is to show this fellow who has no research laboratory how to use research facilities already available. Let's get a central office started where a manufacturer can find out where to go for help if he isn't big enough to maintain a laboratory of his own."

I was the next person called upon, and both Mr. Dewey and I were surprised—I because he had given me such a good opening, and he because my whole talk told of exactly such a service already in existence. It is the Research Advisory Service and was started after years of preparation by the Liberty Bank of Buffalo for the benefit of manufacturers on the Niagara Frontier.

Since then the service has been extended to other institutions, among them the Wachovia Bank & Trust Co. of North Carolina, The National Commercial of Albany, The Merchants National of Boston, Equitable Trust of Wilmington, Harris Trust of Chicago, The Syracuse Trust Co., The Hartford-Connecticut Trust Co., and Rhode Island Hospital National of Providence. These banks now offer it, without charge or obligation, as their contribution toward the growth and development of industry in their respective communities.

The Research Advisory Service was designed to help industry, thereby strengthening customer relationships and increasing goodwill toward the cooperating bank. It consists of taking technical problems of manufacturers and submitting them to a number of laboratories selected in accordance with their specialized experience in the field represented by the inquiry. As the laboratories respond, a report is formulated and presented to the inquirer by the bank.

The problems vary; for instance, here was a manufacturer of brass valves. In the process generally in vogue it is the custom to sand-blow brass castings and later tumble them to give them a bright finish. This manufacturer had heard that some foundries were beginning to dip the castings instead of sand-blowing them, and he wanted to know the best dip for the purpose. We not only directed him to a dip that enabled him to obtain a bright golden color, but one that was non-fuming so as to decrease the danger to employees working with the process. Another company wanted to check on the procedure to be used in manufacturing and distributing fresh orange juice. A third wanted to know whether it would be advisable to change from coal to oil for fuel under a tannery boiler. Problems running the whole gamut from "How should I do it?" to "Where can I get it?" and "Who does it best?" have been solved by the hundred.

It was to cope with problems such as these that the service was originated, but, frankly, we didn't begin to realize at the outset how great the need was.

We began to study the industrial research situation early in the '30s, and, after visiting laboratories both here and abroad and witnessing the type of work these research men were doing, the thought would come up again and again—why couldn't the banker take the hand of the manufacturer, who in part at least is his bread and butter, and lead him, not to sales departments, but to the research laboratories of industrial companies, technical schools, universities and associations for assistance in finding the solution to problems? Simple enough; nothing remarkable or complicated about that. The idea grew, and today the service is backed by the enthusiastic cooperation of over 800 laboratories in every conceivable field of activity here and abroad.

We maintain that the purpose behind the service is simply one which most good banks have had in mind for many years. Some banks, like National Shawmut in Boston, go to considerable length to help customers or prospective customers exploit certain markets to best advantage. Others, like the National City of Cleveland, employ a full-time industrial engineer to assist in reorganizing and modernizing industries. Others, like the Marine Trust of Buffalo, advise business men in connection with methods of operation. The basic purpose in each case—to help business men make more money—is identical with ours. At that point our plan begins to diverge from theirs. Under the Research Advisory Service the Liberty Bank itself does not advise on any problems; neither does anyone in its employ. We do not have chemists or engineers on the bank payroll, nor do our officers even pretend to understand the complexities of industrial research. All the information we obtain for our customers is from specialists, sources well qualified to know the answers. We have no intention of engaging in research work ourselves. Banking seems to have quite enough problems of its own. We tell our customers that, as Mr. Kettering of General Motors says, "We are exponents of intelligent ignorance." We know nothing about the answers to their problems, which may, for instance, have to do with materials, processes, machinery, or packaging, but we believe we do know definitely who should have that answer, if there is an answer.

What surprises some people is that such a service should have been originate by a bank. After all, we have been given some rather uncomplimentary nicknames during the past few years, but when the record is written I am sure it will show that the banker has played his part in harnessing the test tubes of laboratory research to the needs of the manufacturer, and to the facts and figures of banking. And why shouldn't it be so? Research has proved itself to be one of the best safeguards for capital invested in industry. The research appropriation of an industrial company is nothing more than the insurance premium that capital must pay so that industry will not die.

The bank that takes tangible steps to help its customers keep ahead in the competitive struggle, to develop new products, save money and improve its methods—that bank will benefit generously in the long run. A company which is getting the benefits of modern research is more likely to borrow to expand and will be a stronger credit risk. On the contrary, if the industry which furnishes employment for the people of a given community were to hit the toboggan, the banks of that community wouldn't do so well. Every bank, in a sense, owes its existence to the community it serves. Therefore, banks, more and more, are beginning to recognize not only the desirability, but the necessity of industrial research, and are doing their part in carrying the ball.

I have been asked some pointed questions about this Research Advisory Service. One banker said: "What are you trying to do—get the banks back into the 1920's when they were performing a million free services? Why will the laboratories help out on the program without charge? Suppose you get a wrong answer, what will the customer think of the bank?"

I told him that what I was interested in, as a banker, was to bring about as many calls on customers as I could, at as small a cost as possible, and with the largest possible results. I didn't care whether the medium which brought this about was a free service so long as it accomplished something we hadn't been able to do before in any other way without unreasonable expense.

The average senior officer of a bank feels that he has more important things to do with his time than just go around and swap aimless chit-chat with customers or prospects. But when he knows from a few test calls that he can depend on an interested hearing and an appreciative reception, he finds reasons for going out to make such calls instead of finding reasons to stay at his desk. After a while he finds that he knows customers and their operations better than he ever did before in his life, and their feeling toward him is entirely different. They aren't afraid of him. They know that he's on their team, hoping they will be successful whether or not be can always say yes to every request of theirs.

A natural question is, why should the laboratories extend such assistance? This is a tough, dollar and cents world. Scientists' babies have to have shoes. Besides, many of these laboratories are simply the research departments of companies like United States Steel, Goodrich Rubber, International Paper, or one of the oil or motor companies. They aren't charitable foundations. Why no fee? And suppose they do help out, gratis, once or twice—aren't they going to get a bellyful when the problems start accumulating in volume?

The answer comes in half a dozen parts, depending on the particular situation. For one thing, scientific men, in their search for knowledge, are genuinely cooperative by nature. For another, there's a considerable group of problems—the largest, in fact—in which a manufacturer wants to find a machine or a material that will do something better or cheaper. He's willing to pay for it, and he sees plenty of salesmen, but none of them have offered what he wants. So we make a general survey of the field, and finally narrow the matter down to three or four companies who make something like the desired article. Their technical men give us the exact story—and you'd be surprised, I think, to see how frank they are in exposing the limitations of their products, as well as the advantages. They don't talk like salesmen. They realize that the service, already functioning through 11 banks, is likely to grow into an important channel for directing would-be buyers to new or little-known products, and they are on their mettle not to claim too much, for that would discredit them as sources of dependable, impartial information in the future.

So, many sales have resulted. A rubber laboratory developed a large synthetic gasket for a manufacturer of electric refrigerators and got at least one new customer on the spot. A candy manufacturer found a chocolate coating that would not melt when shipped in hot weather. A button manufacturer was looking for a mechanical means of attaching buttons to cards. We put him in touch with a company that had just perfected a new machine to do this very job. A company that had to pump acid solutions in its manufacturing operations had a lot of trouble because the packing was eaten away by the acids, and leakings resulted. We found them a pump that knew better.

Now you can see that if we increased the number of such problems a thousand-fold, it would be pretty hard to get those companies angry. Suppose that they only get a new customer one time in 10, and that the other nine times they have to write us a rather careful, technical letter—it's still good business for them. Some of the leading companies have technical men traveling around the country for the sole purpose of telling people about their new products. That's fine, and necessary. But they can't cover the ground that this service can, or strike just at the time when a particular product is most needed. So, they are welcoming the supplementary assistance which we offer.

Other reasons for their cooperation are that in this work we often are able to make reciprocal assistance available when it is needed by laboratories which are cooperating with us, giving the research men and their employing companies an opportunity to widen their circle of friendships in industry, giving universities and technical schools actual living problems of industry which they would rather work on than do shadow boxing.

Probably the question that most of us would put first (and you can ask other questions later if you care to) is this: Of what benefit is the Research Advisory Service to my bank?

One way to answer that question is to tell you what has happened in our case and in other cities where the service has been adopted. After we determined our plan of operation we made test calls on both customers and prospects. Let me again revert to case histories. I made an appointment with one manufacturer who had a reputation for courtesy, but shortwindedness. Not being a new-business man myself, I discussed the call with one of our new-business men, who predicted that the reception would be cordial, but that I would be out of the office in 15 minutes, feeling fine but back where we started. Our conference began at 2 p. m., and I left this company's Treasurer at quarter to five. In the meantime I had explained the service and gone through his plant. Two months later this company went on our books with a substantial five-figure account.

Another institution that had been in business for over 75 years, but had never done any business with our bank, heard about the service. They sent in one of their Vice-Presidents, who spent a day with me looking into it very carefully. We have repeatedly stated that the service was installed as a community gesture for customer and non-customer alike, and at no time did I even intimate that we would like to have this company's account on our books. I told him to go right ahead and use the service. The following week, entirely unsolicited, they opened a $50,000 account. That was two years ago, and they must be satisfied, because the account is still with us.

Uses for the service are as broad as one cares to make them, but if I were asked to name any single group of manufacturers who need this service more urgently than any other, I should pick concerns which are now receiving what industry calls "educational orders" from the War Department—companies fitting themselves to undertake new products as part of our national defense program. These people are going out of their accustomed fields and therefore can use the technical experience of other companies to especial advantage, since it enables their own technical men to concentrate on new development work instead of losing valuable time in repeating each trial and error of others. Is it far-fetched to suggest that such voluntary cooperation as this among technical men in a free democracy, financed by banks which will benefit, may compete effectively with the totalitarian method of regimenting the technical men on a national scale? I think not.

Many of you undoubtedly recall that about five years ago the Bank Management Commission of the A. B. A. made a survey to determine the most productive means for a bank to use in building up deposits and goodwill. Their conclusion was "Personal solicitation has no rival as a means for obtaining new business." We agreed, but concluded that the method of approach should be improved and modernized. So now we no longer go in as we did, with just the old glad hand, the cheerful smile, chat a bit, and leave with the threadbare "Now don't forget, anything we have is yours for the asking." Instead, we try to give the manufacturer something that will help him. We start talking about research and tell him what the service is doing for others—what it can do for him. What happens from then on varies. Sometimes it is a trip through the plant, in which case, if it is a present customer, the officer in charge learns things about the manufacturer's business without snooping. Sometimes we get leads for our trust or travel departments. In one week one of the smaller banks in our group, as a result of research calls, received good loan inquiries aggregating $300,000.

Sometimes we carry a message telling of new products that might affect the manufacturer's business, things constantly coming to our attention as a result of our contacts with research laboratories. For instance, when we heard of du Pont's new revolutionary synthetic bristle, we gave this information to our new-business men, who carried it to the brush manufacturers in Buffalo, and they were interested. You may say, "These manufacturers should and will already know about these products." They should, but our experience has been that they don't, and you are a welcome caller because you are actually giving the manufacturer something in return for the time he is giving you.

The service is a gesture toward the community which brings the bank columns of continued free publicity. Our Chamber of Commerce recently published a series of booklets, each for a specific industry, showing advantages of locating in Buffalo. It used the service in every case as a drawing card.

In the case of prospective customers, and especially new industries coming to town, instead of simply scrambling with other banks for the business, you are immediately set apart as a bank which has special usefulness to the prospect.

From a broad gauge public relations standpoint, it is unfortunately true that various surveys of public opinion indicate that bankers are looked upon as having little interest in their customers and the community. Many think the banking system should be Government-owned. One of the best ways for persuading the average man that bankers are people, and rather decent people at that, is to offer practical cooperation where it counts and where it will be appreciated and discussed. This service, offered modestly and unpretentiously, cannot help creating goodwill for the individual bank and for banking as a whole.

The Credit Facilities of Banks

By HERBERT V. PROCHNOW, Vice-President of the First National Bank of Chicago, Chicago, Ill.

No one who has examined even superficially the development of the banking system of this country will contend that the methods of extending credit over the years have remained unchanged. The facts are that the swift whirl of economic and political affairs through the decades has left an indelible but changing impress upon the bank credit structure. And the present period is no exception.

We are grappling today with a great many new forces, for the world is economically disheveled. It threatens to ride to its distiny in a powder cart. There are some who believe that the world's economic machine is running down, that its soundest business and financial traditions have been repudiated in various parts of the world, and that unless somehow there be a release again of the great fountains of private and free enterprise, the progress of decades may be lost.

No one can mistake the fact that in recent years an older order of affairs seems to have been shaken down about our ears, in part due to the economic hangover of the last war. However, it is not necessary to accept these facts wholly in a spirit of defeat or resignation. But it is imperative not only that we understand the important forces today affecting the extension of credit, but also that we be familiar with the development of bank credit facilities over the years. For the banking system, with the granting of credit, is in many respects the corner stone of the economic structure.

Forces Affecting Bank Credit

As a background for this discussion, let us, therefore, sketch briefly some of those major forces that have had so great an influence in the extension of bank credit. In a period of approximately five years the monetary gold stock of this country has increased by about $12,000,000,000, with the result that the excess reserves of the Federal Reserve System have risen to more than $4,000,000,000. The pressure of these unprecedented idle reserves resulted in a sharp reduction in interest rates which was promptly felt in commercial banks. Short term assets rapidly reflect such changes.

In recent months we have witnessed commercial paper at ½ to ⅝ of 1%, prime bankers' acceptances at 7-16 of 1%, the best grade 10-year municipals at 1½ to 2% call loans at 1%, long-term Governments a little over 2%, Treasuries due in 1941, with a yield so low that it took $75,000 par value to earn enough just to buy a morning paper every day, and interest rates on loans at the lowest level in years. The effect on bank earnings obviously has been unfavorable. As the "Monthly Review" of the Federal Reserve Bank of New York for August pointed out, the average yield on new Treasury bills sold during July at no time reached a level sufficiently high so that an investment of $10,000 in the bills for three months would produce income of as much as 50 cents. The yield on the highest grade corporation securities has been at the lowest level for years. It is too early to determine the ultimate effects of the European war upon bank credit and interest rates, but this crisis may provide a turning point in recent trends.

If it had not been for recoveries and profits on securities, the member banks of the Federal Reserve System in 1937 (year ended Dec. 31) would have been able to pay less than half of the dividends declared, and in 1938 (year ended Dec. 31) would actually have operated at a loss, in other words, without any return to the common stockholders. If it had not been for recoveries and profits on securities, the National banks as a whole in 1937 (year ended June 30) would not have been able to pay half the dividends on their preferred stock and would have failed to earn any return for their common stockholders. In 1938 (year ended June 30), using the same comparison, they could have paid their preferred dividends, but would have earned only about one-fourth of their common stock dividend and 1½% on their common capital and surplus.

Paralleling the decline in interest rates, there was a comparative lack of demand for bank loans. In spite of abnormally low interest rates and billions of excess reserves, industry did not find it profitable in the past few years to use bank credit in large volume. For the 14 years from 1919 to 1932, inclusive, approximately 54% of all active manufacturing companies reporting income showed a profit and 46% a loss. An examination of the corporation income tax returns now reveals that the probability of earning a profit greatly decreased since then, with only a little over three out of every 10 corporation filing an income tax return reporting a profit in recent years. The odds have been almost two to one against the possibility of a corporation earning a profit. The hazards of business are never small, even in the best of times, and in recent years they have been little short of insurmountable.

Of the 2,101,000 active commercial and industrial business enterprises of the country, approximately 20% go out of existence each year, and about the same number hopefully start in again. Business is not invested with perpetuity. It must fight to live. For every retail store that lasts 14 years, one lasts only one year, the average life of all retailers being about seven years. The difficulty obviously, in the great majority of cases, rests with the management. Confronted with such facts, the banker must have a basic understanding of the fundamentals of good management. A western banker, located in a city of 12,000 population, has recently measured the mortality rate in his community. He found that as a general rule 100% of the retail merchants are eliminated every seven years, 100%

of the automobile dealers every four years, and 100% of the farmers every 10 years.

These are some of the significant factors which require sustained consideration in a discussion of bank credit, and in no small measure dictate the direction of our thought. With this background, let us then examine four major aspects of bank credit—as expressed in four questions.

What Can the Individual Banker Do to Facilitate the Sound Extension of Credit?

In the first place, what can the individual banker do to facilitate the sound extension of credit?

There is at the outset a need for a still better understanding of the principles of granting bank credit, in view of the hazards under which business and industry operate, and in order to reduce the losses on loans. One cannot dismiss casually the fact that the losses on loans and discounts for National banks for the years 1927 to 1935, inclusive, were about 24% of the total interest and discount earned, and all losses, excluding depreciation, were 76% of the total net earnings. Exclusive of recoveries and profits on securities, total losses and depreciation of the member banks in 1937 were over 80% of the net earnings, and in 1938 actually exceeded the net earnings. It is a reasonable presumption that a better knowledge of our loan operations would reduce these loss ratios and increase profits.

We need a thorough knowledge of the five kinds of financial statements:

1. Balance sheets.
2. Profit and loss statements.
3. Reconciliation of surplus in the case of a corporation or reconciliation of the net worth in the case of a proprietorship or a partnership.
4. Budgets.
5. Trial balances.

Although some bankers may assume that the subject of financial statement analysis has been thoroughly explored, the probabilities are that we are only on the threshold of an understanding of this important subject. As late as 1883, when Edwin Guthrie came from England to evaluate certain assets in this country, he was unable to find a single accounting firm here. There was no such thing as accounting practice. Later with John W. Barrow he formed the first accounting firm in this country. It was not until about 1900 that loaning money on single-name, unsecured paper backed by a financial statement became accepted American banking practice.

We shall examine only three phases of the subject of statement analysis. Consider the single item of inventory. When sales increase, prices rise and business conditions improve, the natural tendency is to add to inventory. Consequently, the turnover of the inventory, even with rising sales, may not improve. Finally, public resistance sets in to rising prices, and sales decline. The inventory is large in volume and high in price. The sales turnover falls. The business takes inventory losses and may even become frozen. This is a simple but often-repeated experience of business. As recently as 1937, bankers and business men might have profited greatly and reduced their losses substantially if there had been a better understanding of the item of inventory on the financial statement.

When a manufacturer, jobber, or wholesaler has a tangible net worth between $50,000 and $250,000, extreme care should be exercised, even though the inventory turnover is satisfactory, if the inventory is larger than two-thirds of the net working capital. When the tangible net worth is in excess of $250,000, the inventory ordinarily should be no greater than three-fourths of the net working capital. In a retail business with a tangible net worth in excess of $50,000, the inventory generally should be no greater than the net working capital. An excessive inventory often cripples a business seriously, due to unexpected losses from depreciation, changes in style, perishability and price fluctuations.

Closely connected with the item of inventory is the wholesale price level of commodities. Of the 2,101,000 active businesses in this country, to which we referred earlier, probably 20 to 22% are marginal businesses, with insufficient capital, heavy liabilities, inflated receivables, or other weaknesses. A slight decline in business wipes out thousands of them. A slight improvement helps them to survive, just as oxygen helps ill patients. If oxygen is administered long enough, some recover. No other single factor affects marginal businesses more than the commodity price level. If the price level goes up, selling prices rise and an unexpected profit results, particularly if the inventory is large. If the present world hostilities develop an increasing demand for commodities, a rise in prices may enable many businesses to earn profits on inventories. To a marginal business, on the brink of uncertainty, that means a longer lease on life. On the other hand, when prices decline, goods must be sold at a loss and the marginal concern dies. Consequently, the level of commodity prices is perhaps the greatest single factor in the life and death of businesses.

It is worth emphasizing that a business with a tangible net worth between $50,000 and $250,000 should be carefully analyzed if the depreciated value of its fixed assets is greater than two-thirds of the tangible net worth, or if the current debt is greater than two-thirds of the tangible net worth. If the tangible net worth is over $250,000, the respective figures are three-fourths instead of two-thirds. In no event should the funded debt exceed the net working capital. These comparisons are important tests of financial strength in businesses.

No financial statement is pehaps less understood by the banker than the trial balance. When it may be somewhat of an imposition to ask a borrower to prepare a balance sheet, there need be no compunction, as a rule, about asking for a late trial balance. Briefly, the trial balance discloses five important facts subsequent to the issuance of a balance sheet:

1. A closing of the books on an irregular date, or the possible inaccuracy of the last balance sheet.
2. The amount of inventory required to maintain the same amount of capital as that shown on the last balance sheet.
3. The approximate inventory on the date of the trial balance.
4. The approximate overhead expenses of the business.
5. Unusual transactions not apparent from a condensed balance sheet or income statement.

The foregoing comments, indicating the necessity for a better understanding of financial statements, apply in all banks which loan to businesses. But there is an exactly parallel situation in the smaller banks of agricultural communities where loans are made to farmers. There is a need for more comprehensive and adequate farm credit files, and a great many far-sighted country bankers are pioneering in the development of such files. A Colorado banker has prepared on a large card a special finacial statement form for farmers, the card also having a place for photographs of the property made by the bank's farm inspector. A Middle Western banker in a city of 10,000 population began the development of credit files on farmers nearly 20 years ago, and his files now cover the almost incredible number of over 6,000 farmers in his trade area. He began this work in the horse-and-buggy days. He now has a young man who devotes his time to gathering current farm credit data and increasing the lists into a little broader territory. All those who borrow in excess of $500 furnish statements. Farmers are encouraged to build up their credit to the point where they can borrow on their own names without chattel mortgages. His losses on chattel mortgages have been greater than on personal notes. An endorser is not required if the reputation and statement of the farm justify credit on plain note.

This bank employs a man who has had several years of experience as a land appraiser, farm manager and salesman of farms. He studies about new ventures into diversified agriculture, which may involve the reasonable extension of credit. At the close of the day this banker believes it pays to take his car and drive into the country to visit the farmers of his community.

In 1937, this banker made over 10,000 loans; in 1938, 11,000; and in 1939 he will make more than 12,000 loans. The number of loans is more than twice as great as it was five years ago. The final test of his success is the earnings of his bank. The bank has $100,000 capital and $100,000 surplus, plus a substantial undivided profits account. It pays 16% annually. This has been the rate since 1933. Prior to that date for 10 years or more the rate was 25% yearly. During the life of the bank since 1865, the shareholders have received a return which averages 16% a year. For about 20 years, one-half of the earnings above $20,000 per year has been paid into a fund distributed to employees. This distribution has aggregated an average of about 6% annually on the capital stock of the bank. The earning record of that bank, its development of comprehensive farm credit files, and its loans to farmers constitute a commendable achievemnet.

We may digress to include as a part of this program of improving our knowledge of loaning operations a new development—bank investment credit files. Many banks do not have separate bond, statistical or collateral departments to provide credit information on investments. But with the large amount which banks have invested in bonds, the importance of thorough investment credit files becomes obvious. If every bond in the portfolio represents a loan of the bank's funds, the information on that type of loan should surely be no less complete than the credit files on regular commercial loans. The same investigation and the same persistent follow-up are required.

What Have Bankers Done to Meet Changing Credit Needs?

We come, then, to the second principal question in this discussion—what have bankers done to meet changing credit needs? Bankers have faced new credit problems and new banking situations with an open mind and with an earnest desire to contribute their full share to business and industry. We have already discussed what aggressive bankers in farm communities have accomplished. There have been several developments in the past few years in credit facilities, of which we shall briefly comment on four: Term or intermediate loans; personal loans; insurance loans; and loans on assigned accounts receivable.

Banks in the larger cities have made a rather substantial volume of so-called term or intermediate loans, with maturities running ordinarily from one-and a-half to five or six years, with an average of two-and-a-half to three years. Under present regulations for the examination of banks, loans whose ultimate payments are reasonably certain, regardless of maturity, are not included in a separate classification by examiners. The question of ultimate ability to pay is determined by earnings, by the nature and value of assets, or by pledged collateral. These loans are made for many different purposes, such as the refunding of debt to reduce fixed charges, the expansion of plants, and an increase in working capital. The average interest rate is probably 1% or more above the short term rate for similar loans to the same borrower. The major portion of such loans are secured by mortgages on property, warehouse receipts and chattels on machinery. There is naturally a wide variation in the size of the loans and in the arrangements for repayment, which are made to suit each individual situation. It is important that unwise competition for these loans should not result in the excessive lengthening of maturities, the fixing of interest rates at extremely low levels, and a laxness in applying sound loan standards.

There are some bankers who feel that for various reasons it is unwise for their institutions to enter the field of personal loans, and they have made little effort to encourage this development in bank credit facilities. However, our purpose today is not to enter this phase of the discussion, but to report objectively on what has taken place. The greatest impetus to the personal loan movement, other than the small volume of local loans and low interest rates, was probably the Modernization Loan program initiated in 1934. It has been estimated that prior to that time perhaps not more than 150 banks were prepared to make personal loans on character and income of the type contemplated under this program. By 1937 almost 6,000 banks, in addition to many industrial banks and savings banks, were making such loans in almost every county in the United States. The potential field for personal loans is of vast proportions. A recent study on financing the consumer reports the following credit agencies in 1936:

	Credit Extended	*Credit Outstanding*
Personal finance companies	$423,000,000	$285,000,000
Industrial banks	350,000,000	234,000,000
Personal loan departments of banks	195,000,000	129,000,000
Unlawful lenders	160,000,000	119,000,000
Pawnbrokers	165,000,000	110,000,000
Credit unions	80,000,000	55,000,000
Remedial loan societies	54,000,000	34,000,000
Total loans	$1,427,000,000	$966,000,000
Retail instalment sales	4,500,000,000	2,600,000,000
Retail open accounts	8,100,000,000	1,500,000,000
Total merchandise credit	$12,600,000,000	$4,100,000,000
Total consumer credit	$14,027,000,000	$5,066,000,000

Out of total personal loans estimated at $1,427,000,000 and made by the seven principal consumer credit agencies, the personal loan departments of banks had loaned only $195,000,000 in 1936.

An examination of the practical experience of two banks with this type of loan reveals some interesting facts. A bank in a city of 65,000 population established a small loan department in 1928. From August, 1928 to Dec. 31, 1937 this bank made 57,460 loans. In 1938 they made 8,435 loans. At present they have 10,000 notes in their portfolio with loans outstanding of more than $1,000,000. Their losses are close to ½ of 1%. Without disclosing the actual earnings, the banker reports this department "has been and is a lucrative earning department, and the management is very pleased about its successful operation."

There is a western bank with resources of about $2,500,000 which established its personal loan department in October, 1935. The outstanding loans at various times in the succeeding years follow:

Dec. 31, 1935	$15,500
Dec. 31, 1936	54,000
Dec. 31, 1937	96,000
Dec. 31, 1938	138,000
May 15, 1939	175,000

It will be noted that each year the total increased about $40,000, and by the middle of 1939 this bank had $175,000 in personal loans. The approximate interest collected for the respective years follows:

2½ months of 1935	$700
1936	5,000
1937	10,000
1938	17,000
To May 15, 1939	7,200

The approximate net losses charged off were:

1936	$201
1937	217
1938	78

This particular banker summarized the reasons why he believes the establishment of a personal loan department is desirable as follows:

1. It brings great numbers of people into friendly relationship with the bank, many of whom may look upon banks as lending institutions serving only those who have relatively large financial interests.
2. It holds these loans in the banks.
3. It opens a new and desirable field of income.
4. It greatly increases the number of borrowers.
5. It may be of assistance in teaching people to save because of the systematic method of making payments at a bank.

It is suggested that bankers read carefully the splendid material on this whole subject prepared by the American Bankers Association.

There also has been an increasing volume of loans secured by the assignment of the cash surrender value of life insurance. There is still a difference of opinion regarding the desirability of making loans of this type in substantial volume. But the increase in insurance loans simply reflects again the endeavor to increase bank income from all types of desirable loans, and to satisfy the need of bank customers. During the depression many individuals borrowed against the cash surrender value of their insurance policies. The financial statements of some insurance companies showed as much as 28% of their investments in policy loans. Most of these loans were made at 6%. With declining interest rates, many borrowers naturally repaid their loans at the insurance companies by borrowing from banks at lower rates.

When banks make loans of this character, it is necessary to look beyond the mere fact that an earning asset is being acquired. Consideration should be given to the purpose for which the proceeds are or have been used and also to a definite program of liquidation. If there is no income available for the eventual retirement of the loan, the banker may find himself with a credit which can only be liquidated by cashing the value of the life insurance. There should also be some assurance that the borrower can meet his insurance premiums without further borrowing.

In many cities today banks are making an intensive study of loans on assigned accounts to determine the possibilities of adding to their profits. Loans against assigned accounts require a more complicated technique than is necessary with the more customary type of secured loans.

As early as 1905 the first specialized finance company began making advances against accounts receivable. Today there are 1,500 such specialized finance companies. In making loans against receivables, the finance companies cite such advantages to business as the following:

1. Businesses obtain additional working capital without taking in partners or selling more capital stock.
2. If the volume of sales is increased by this financing, overhead expense may be proportionately reduced.
3. Larger cash balances may be maintained at banks.

The most important advantage to business in "cashing its sales" or, in other words, borrowing on receivables, is the possibility of earning a definite profit by discounting all invoices.

There are three types of borrowers to which loans against receivables are generally made:

1. Concerns which have lost working capital, but appear to have sound prospects for profits.
2. Concerns which appeared to be good at one time and in which a bank already is frozen.
3. Concerns which are in such poor financial condition that accommodation against assigned accounts is the only way in which the bank can protect itself.

Loans on assigned accounts yield a better than average return and the experience so far with such loans, properly and carefully made, has been satisfactory.

What Are the Facts Regarding the Adequacy of Bank Credit Facilities?

We come then to the third principal question in this discussion—What are the facts regarding the adequacy of bank credit facilities? The answer to that question may be concisely stated. First, we have more lending agencies today than this country had even in 1929 at the peak of that period of credit expansion. Second, we have $16,500,000,000 in gold reserves—the largest gold reserves possessed by any nation at any time. These gold reserves are four times as great as those upon which the tremendous credit expansion of the 1920's was built. Third, we have had for some time the largest excess reserves in the history of the Federal Reserve System. Our commercial banking facilities are thoroughly adequate for the legitimate credit requirements of business.

What Is the Banker's Responsibility Regarding General Credit Problems of the Banking System?

In the fourth place, it may be fairly asked, What is the banker's responsibility regarding general credit problems of the banking system?

It is imperative that bankers also understand the more general credit problems of the banking system and the suggestions for their solution. We cannot too often challenge our loaning methods by a critical self-examination, although the banker cannot chase down the street after every Pied Piper who has a new theory relating to bank credit. It is our responsibility to think through each credit problem constructively and fairly, and to understand specifically what is wrong or right about it. Let us simply outline four of these problems.

First, it is said there is a bank credit problem relating to gold holdings and large excess reserves. The substantial excess reserves today do not represent savings primarily. They have arisen largely from the purchase of Government bonds by the Federal Reserve banks beginning early in the depression; the issuance of approximately 1 1-3 billions of silver certificates as the result of the purchase of about two billion ounces of silver by the Government; and finally, by gold devaluation, combined with the import of billions of dollars of gold.

It was hoped that the monetary policies of recent years would lead to borrowing by business, help the security markets, revive the heavy goods industries and raise commodity prices. But it became apparent that men would not borrow solely because interest rates were low, nor would they risk capital unless they had reasonable confidence that they might earn a fair return.

However, large expenditures of governments over the world have inherent in them significant problems relating to bank credit. If the large expenditures which are made by nations to prosecute war, to prepare for war, or for other purposes, should lead to a heavy demand for goods, a marked rise in commodity prices and a widespread expansion of bank credit might follow. It is the development of such conditions which requires a thorough understanding of sound bank lending principles.

Secondly, in a recent issue of the "Harvard Business Review," a Middle Western professor states that the country banker "has been losing ground" and "is today fighting for survival." He reminds ι that "local loans and discounts are a smaller portion of total assets and that earnings are low." He suggests "the abandonment of the liquidity and marketability theories of bank assets; the acquisition of local long-term paper; and the provision of rediscount facilities for farm mortgages." It is his viewpoint that country banks in recent years have shunned farm paper because of its lack of liquidity. The liquidity feature has raised the value of marketable bonds over that of equally safe local farm paper, which difference is not a premium for safety but liquidity. He holds that the answer is to establish a rediscount agency to permit the Federal Farm Mortgage Corporation to rediscount for commercial banks mortgages having a maturity not to exceed 10 years, with a five-year renewal privilege. This agency would only be used by banks in an emergency and banks should not permanently borrow from it. It should not be the agency whereby a bank would rid itself of poor paper.

The local bank would still conduct its business so that in the ordinary course of events it could depend on collecting its loans and selling real estate in the market to meet its demands. The writer who made the proposal believes the rediscount institution would prevent sales being made at a sacrifice. And he concludes that unless the country banker enters the farm mortgage market again, his future role in the community will be a small one.

In considering the wisdom of this proposal one might ask whether banks would wish to rediscount long-term paper and be liable on bills payable possibly for years. If prices of farm products should rise sharply with a corresponding rise in farm land values followed later by a marked decline, such, for example, as the decline of farm land values after the last war, who would take the loss—the bank or the rediscounting agency? Does the transfer by banks to a rediscounting institution of slow assets which have declined in value really improve the banking situation in a crisis, or does it merely move the frozen assets from one part of the banking system to another? These are only some of the pertinent inquiries which must be made of this credit proposal. The suggestion has been presented in one form or another for years.

There is a third credit problem involving the consideration of the exact character of the loanable funds of a bank. We know that the capital funds are with the bank permanently and that determines in part how they may be used. But how carefully, for example, have we analyzed our savings deposits, to determine how they may be loaned or invested? Are they reasonably stable and permanent, or are some of them demand deposits on an interest basis? It is suggested in this connection that the survey on the general subject of the behavior of deposits reported in the March, April, and June, 1939, issues of the "Federal Reserve Bulletin" might be studied.

Recently a banker in a city of 60,000 made an analysis of his savings department with its approximately $6,000,000 in deposits. The following figures give a concise picture of that department:

Balance Range	*No. of Accts.*	*Per Cent*	*Amount*	*Per Cent*	*Aver. Bal.*
Inactive accounts	2,860	21.3	$20,374	.3	$7
$ .01 to $ 10.00	2,221	16.5	6,840	.1	3
10.01 to 50.00	1,579	11.8	41,636	.7	27
50.01 to 100.00	1,045	7.8	72,874	1.2	69
100.01 to 500.00	2,950	22.3	701,003	11.3	236
500.01 to 1000.00	1,081	7.8	752,606	12.1	699
1000.01 to 2500.00	1,105	8.3	1,753,008	28.1	1,586
2500.00 and over	577	4.2	2,880,168	46.2	4,991
Totals	13,418	100.0	$6,228,589	100.0	$464

Of equal importance with these figures is the fact that 28% of all the savings accounts opened in this bank close within one year and 52% within two years. Although the savings department was designed to assist in the accumulation of savings, the ratio of deposits to withdrawals was only 1.3 to 1. Over 42% of the activity in this savings department was in accounts having individual balances less than $100, the total balances of which aggregated approximately 2% of all the deposits. The results of this analysis are not wholly unusual. They are probably typical. A careful study of savings deposits might indicate with some degree of accuracy to what extent they are actually similar to demand deposits and to what extent, as now carried in banks, they could be invested for longer periods than the typical short-term earning asset provides.

What methods might be developed to encourage steady saving and more permanent, less active, savings deposits, which might be used more freely in the extension of various types of credit, possibly longer term credit?

Every banker ought also to have some appreciation of the problem of bank loans or assets which are liquid in contrast to those which must be shifted to obtain cash. In other words, there must be a clear understanding of the difference between what has been called liquidity as contrasted to shiftability.

To illustrate, a manufacturer makes a seasonal loan from a bank to buy raw materials which he fabricates, and out of the sale of the finished product he retires the loan within perhaps six or nine months. This is the normal procedure by which the great majority of bank loans to industry are liquidated annually. They are liquidated when the commercial transactions of which they are a part are finally completed. But a portion of a bank's funds are ordinarily also placed in assets which must be sold or shifted in case the funds are needed in order to meet the demands of depositors. To what extent, then, may a banking system place its funds in earning assets which more or less automatically liquidate themselves through ordinary commercial processes, and to what degree may it properly place its funds in assets that must be shifted or marketed to be liquidated?

Some bankers would contend that it is the fact that large blocks of assets are shifted which greatly aggravates conditions in a depression. They would further contend that the business cycle can never be reasonably stable until the danger of such whoesale shifting of assets is eliminated. Some of those who hold this viewpoint believe that assets which must be shifted should be bought largely with savings deposits or capital funds. And they suggest more permanence in savings accounts to permit the acquisition of shiftable assets.

These are only a few of the general credit problems, which as bankers we might profitably study after the close of regular banking hours, and regarding which it is not too much to ask that all of us have an informed opinion.

In conclusion, it is important that bankers give every encouragement to sound requests for credit and be helpful in every way in safeguarding the American economy in the period of world stress which confronts us. Let us steadily increase our understanding of the hazards and financial problems of all types of business enterprises, so that we may continue to contribute our full share to the advancement of business. For the cooperation of business and banking through the years has played a significant part in the progress of this Nation.

Meeting the Public Need for Personal Credit

By W. B. Harrison, President Union National Bank, Wichita, Kan.

Banking is, and should be, a service. This service is an intelligent effort to meet a human need in business. In the particular branch of service I am to speak about, that need is personal credit. Is there such a need? Emphatically, yes! Hundreds of millions of dollars borrowed through scores of institutions that are not banks testify clearly to the need. Most of these institutions have grown up in the past two decades. If the banker had been meeting the need, fewer of them would be competing with him today. In a majority of banking communities in the United States there are enough existing loans originating in a demand for personal credit, including instalment credit, to give the banks a much nearer normal volume of loans than they now enjoy if the bankers had been sufficiently alert to keep those loans in their banks instead of permitting them to slip away to finance companies. Not all of such loans are suitable bank paper, but the bulk of them are. And the interesting part is that nine-tenths of the borrowers would prefer to borrow from the bank rather than from a finance company. Why, then, did they not go to the bank first? Because the banker waited for them to come in while the finance company was soliciting the business; and because the banker had an old fogey idea that a note made for 90 days and renewed every 90 days for two years was a better piece of paper than a note made for 18 months, payable in 18 monthly instalments.

A Surprise to Bankers

The first awakening our bank had to the merit of instalment credit was when we very reluctantly made some Title I loans. That was in 1934. We were the only bank in our territory for a time that made any of these loans. It just wasn't good banking, our friends said, because it never had been done before. A multitude of objections were made by astute bankers who always followed precedent. Title I loans couldn't be good because they never had been good. That proved it. But within 90 days our banks were all making these loans, and they all had the same experience—practically no losses. The surprise was that the loans were paid instead of being renewed. In our own case, and I know the same was true in many other banks, we did not have a dollar loss and did not call on Uncle Sam for one dollar insurance. To our surprise, the instalments were met as agreed with a very small portion delinquent a few days after payment date, but never as much as 30 days, and not one failing to pay in full.

From that experience we learned a lesson—and so did the bank examiners who, prior to the Title I era, were insistent on short-time paper. The examiners ceased citicizing notes just because they had more than 90 days' maturity. In fact, they fell into the habit of telling us that the experiences of other banks with instalment notes were about the same as ours, and so we were encouraged to expand our personal credit and instalment payment notes.

We do not have a personal loan department separate from our regular note case. We know many banks that do have and find them highly satisfactory as to payments and profits. We aim to give service to our customers who desire from six months to two years to pay for something that is needed when there is not cash in the bank with which to pay for it in full. If we lend an individual on the instalment plan, we expect and require him to carry whatever bank account he may have, be it ever so small, with us. We do not want loans to customers of other banks.

Character and Credit

As to taking collateral, this is advisable on auto loans and in many other cases, but it is also true that personal credit extensions can safely be made without collateral if the credit files are carefully built up and only those are given credit who have a good reputation, a record of paying current bills, living within their income, and who are not inclined to overbuy. Resistance to high-powered salesmanship and full realization that each individual is a law unto himself and not a competitor of the Joneses in high or fast living is essential. The banker must be able to accurately judge the moral risk as well as the ability to pay. Two-name paper is not only twice but several times as strong as single-name paper, even though the endorser has no more financial resources than the borrower. The wife's signature on her husband's note also adds much to the payment probabilities. If wife and husband do not cooperate, the note is a very poor risk with the husband on it alone. Always have her sign with him and agree to the plan of payment. It helps.

Personal credit notes are character notes. Many little remarks are made in the course of a banker's interview with a husband and wife that throw light on their character, their earnestness or lack of it in debt payment, their willingness to sacrifice to meet obligations promptly, and their ability to cooperate whole-heartedly in the family program and problem. All of these little things have a direct bearing on the character back of the note and, if the information obtained is not clear cut, frank, and convincing as to merit and purpose, it is best to withhold credit.

When a witness in the Pujo investigation in Washington, in 1906, J. P. Morgan Sr. was asked by a member of the committee, who was not accustomed to handling large finances, how much he would lend a man unsecured, said the great J. P., "I might lend him a million dollars." The committee was flabbergasted. Mr. Morgan calmly explained that if he knew his man well enough and approved the purpose of the loan, he would not hesitate to advance one million dollars without security. Few bankers in history have been as successful as he—not only in making money but in accomplishing things worth while. He was a good judge of character and ability. The banker who extends personal credit must rely largely on his judgment of character backed up with credit files which help form his judgment.

Courage and Judgment

Considering all of these factors, what should be the banker's attitude toward personal credit extension? How can he best serve his patrons, his community, and his stockholders? By exercising courageous but sane judgment in passing on such applications. He can have a personal loan department if he wants one and if the volume warrants it, but he may not need it. What he does need is courage to meet changing conditions. Instalment credit and small personal note credit are here in a big way. We have one bank in Kansas with around six million deposits that is carrying in its note case today $400,000 in small instalment notes. That bank is making money and it is also giving service to its community.

Instalment notes should carry a larger net rate than single payment notes because of the extra work entailed. Our bank's program, in the main, is 12 equal monthly instalments with 6% discount. When the extra work involved is made clear to the borrower, we have no complaints as to rate. And to avoid delinquencies in payments, we require the borrower to authorize us to charge his account each month at payment date. This saves his coming to the bank, makes sure of prompt payment, and keeps down past due paper. Only a verbal agreement is required because the right to charge the account is really given when the note is signed; but it is highly advisable to have the charge intention clearly understood. This done, the payments click off with surprising satisfaction to both the borrower and the bank.

Banking Reconstruction

The American banking system, unique in world affairs, is the outgrowth of experience. It has been necessary to reconstruct this system about every 20 years since our Nation was founded. Each reconstruction has been a step forward which has given added security and service to patrons of these banks. In this generation of bankers we are seeing many of the banking practices and regulations which were orthodox before 1932 thrown out of the window and new regulations and practices take their place. Practically every political objection to banking made before 1932 was eliminated in the 1935 statutes, yet there is still demand for further revision. There has been as great a change in the character of the average bank's note case and investment portfolio in the last 10 years as there has been in the amount and purpose of the national debt. Commercial paper, which was the backbone of thousands of banks a few years ago, is as much out of the picture today as the plug hat and Prince Albert coat that characterized the garb of our well-dressed fathers.

Prior to our time the changes that took place in the banking structure and regulations were confined to improvements in technique and methods of operation. Gradually through the years many excellent restrictions were imposed, more and more with each recurring cycle of financial stress, that strengthened the system and gave it better opportunity for service. But since 1932 we have seen something entirely new. The regulations and practices recently imposed on and surrounding banking deal largely with the so-called "social functions" of banks and with the public interest as affected by banking practices. In other words, we have drifted far from the old idea of banking as a private business, and have come pretty close to the time when it is regarded as a business in which the public has a predominant interest and in which the social duties of the banker and the social obligations of the business are paramount to private interests. I do not say that this should be so, but I do say that that is the situation today as reflected in a preponderant amount of the practices and regulations now governing our business.

Banking Must Change

It is apparent that banking, as a private business, is steadily moving toward banking as a department of government and an instrument of society rather than a private enterprise. It is useless to protest against this movement unless something is done to offset it, and this something can only be found in the field of better service to the patrons of our banks and to the communities in which we live. We must take care of the banking needs of our patrons, or banking as a private enterprise will fade out. These needs are changing and varying with the rapid evolution in our own industrial civilization. One of the most striking characteristics of this evolution is the growth of instalment loans and personal credit, first in finance companies and later in banks. Probably close to one-third of the banks in the United States today are increasing as rapidly as they can their volume of instalment paper. This movement is likely to continue. It is an integral part of our industrial civilization.

Like many other bankers, when the demand for instalment credit came in I was opposed to it and felt that it would be much better to encourage people to withhold their purchases until they could buy for cash. Experience, observation, and study have changed my mind. I still believe that it is best for the individual citizen to keep out of debt, to buy for cash, and to put away a part of his earnings for a rainy day. I still believe that it doesn't matter so much how much one accumulates as it does for him to know that what he has is his without lien or encumbrance; and that a man or a family with small assets and no indebtedness will generally be happier, and in the true sense more successful, than the man or family with large assets, large liabilities, and a high scale of living. But we must take into consideration that America, as a Nation, is entirely new in its industrial development. More and more our people become wage earners, factory hands, clerks, stenographers and skilled artisans. As our civilization develops the proportion of people engaged in farming and other private enterprises on their own account decreases and the proportion of those on the payrolls increases. That is the very nature of the American democracy. Our social and political system develops intelligence and uses that intelligence to increase the wealth of the country by giving employment in new avenues, for new purposes, new projects, and new products that had before not existed at all or existed only in less degree. We call it "mass production," but it is also intelligent management. This intelligent management has made us the richest country in the world, where the masses of our people have by far the highest income of any workers on earth. We produce and distribute our production among these masses. We produce more and make further distribution. At every step, when we increase production, we must increase distribution and consumption. If we fail to do that, the machine becomes clogged and we have depression, despair, and decay. If we keep on producing more and distributing more, we have peace, prosperity and patriotism.

Our Industrial Civilization

Our civilization is utterly different in its form of progress and in its essentials for what we call prosperity from anything in history. Throughout the ages, until the last century in America, the market for goods was confined to the 10% or 15% of the population in every civilized country that constituted the "upper" or wealthy classes. The masses bought almost nothing. They existed on what they could do for themselves, with their own hands. Today in the United States of America the masses constitute the market sought by every big industry from foods, clothing, housing, machinery and automobiles to silks and diamonds. Our giant industries are absolutely dependent on a high standard of living for the masses to sustain their market. This new feature of our civilization must be taken into account in any sound financial analysis.

Now, it is also true that the wage earner will spend his money in some way. The great bulk of them do not save and never will save regularly. If they do not buy something useful, they will squander a good share of their income. They cannot buy for cash, desirable as that would be, because a majority of them do not have the cash and will not lay up the cash by the hard road of sacrifice and persistent savings. They will purchase articles for their comfort and use and pay for them on the instalment plan. If the banker encourages them to do this, he is not only adding to his profit and usefulness in his own institution, but he is actually contributing a substantial share to the prosperity and soundness of our industrial civilization. It would simply be impossible for our great automobile plants, refrigerator plants, radio factories, washing machine factories, travel bureaus, household appliances establishments and other lines which turn out hundreds of millions of dollars in goods and services each year to operate on anything like the scale on which they are now operating without instalment selling; and unless they operate, unemployment will increase, business troubles will pile up, and bank income will decline. To these industrial institutions we can add the services of dentists, doctors, and other professional lines which add to the comfort, health, and happiness of the people, which services would not be utilized unless the one using them could pay for these services in instalments.

Living Standards Must Advance

It may be said that this is a weakness of our people which should not be encouraged, but to me it seems a weakness that should be recognized and taken into account in our business structure. There is only one way that democracy can move, and that is continuously upward, with continuously increasing wealth measured in goods and services, and wider distribution of that wealth. As men are thrown out of employment in one industry by labor-saving devices which reduce production costs, they must obtain employment in some other line which produces an article or a service not heretofore available or not generally used; and prices to the consumer must decline with production costs for consumption to keep pace with production. This means a continuously rising standard of living. It means not only more automobiles, refrigerators, radios, washing machines, and other common American family conveniences, but it means more and better clothing, food, housing, educational and cultural opportunities—a steady march upward in the living conditions of the masses of the people. It means the development and bringing into general use of an utterly incalculable number and variety of instruments of convenience, comfort, and happiness, the nature and composition of which we have not yet even dreamed.

Who could have predicted in 1890 that 30,000,000 autos would be crowding our roads in 1939? Not even the wildest dreamer! Who would have dared even 25 years ago to have prophesied that millions of radios would be enjoyed in American homes today? Such a prophet would have been declared insane. And who can predict the next quarter century? Not you, or I, or anyone else. But this we do know, that as the natural fruits of free enterprise of our democratic form of government and society, our tremendous streams of enlightenment, uplifting our people through our system of free education for all—we will continue to progress in the future as we have in the past—even at an accelerated speed. And this progress will be manifested in the constant unfodling of ideas expressed in new products of factory and farm, new uses of known products, multiplication of desired goods and services, lowering costs of commodities, ascending wage scales measured in terms of such commodities, which is the only true measure, and the diffusion of all this added wealth among the wage earners of America. That is the only way our democracy can live. If it fails to follow that path, it is doomed. If it fulfills its mission—the constant uplifting of the masses and the constant raising of their standard of living—it will survive any crisis, internal or external.

Banker's Duty as Citizen

Now that fact, that destiny of our country, is directly connected in some degree with the problem of instalment credit and personal loans. Each of us, as an American citizen, has his duty to perform, his niche to fill, in the building and maintenance of our society. If the banker shirks his part, he is no better—even worse because of his intelligence—than the humblest citizen who fails to do his bit. If the banker says, "I am not interested in instalment credit because it is too much work and requires too much of my time and effort," he is ignoring his part in our industrial program, which depends so much on instalment credit for its success. About 90% of us bankers weren't interested very deeply in any of these subjects a decade ago. If we had been, we could have saved ourselves many burdens carried by the banking business today. No, we just wanted to be let alone, and let George take care of the public interest. The Georges did it, and we are paying through the nose. We must broaden our interests and activities. We must be willing to do all we can as bankers for the society and government which gives us the wonderful opportunities we enjoy. If we do not, we may wake up some sad day and wonder why we were so stupid when we had abundant opportunity in our own hands.

A few weeks ago the Congress of the United States adjourned after rejecting a vast program of increased appropriations and taking a positive stand for saner economy in government. We all applauded. But more than applause is necessary to win a cause. If Uncle Sam quits spending so much, private business must spend more. Somebody must spend or consumption will decline, unemployment will multiply, and chaos will threaten. We bankers can help private enterprise spend wisely, carefully, fruitfully. Without transgressing the bounds of sound credit extension, we can let those worthy of credit know that we are willing to advance funds, repayable in instalments, to purchase useful household appliances, educate children, replenish depleted wardrobes, take a needed vacation, obtain hospital, medical, or dental treatment, or to procure any other goods or services, the purchase of which will create added labor and uplift the living condition of the borrower.

That does not mean irrational lending or spending. Instalment loans constitute a form of credit inflation, and such credit must be carefully supervised lest it grow into dangerous volume. If it is kept within the limits of the borrower's known ability to pay in a period of six to 18 months, the danger is small, but if it is extended in large volume beyond that time, such extension is inviting a recurrence of a disastrous reverse cycle of credit such as bankers in this day know full well can come most unexpectedly and ruinously. Beyond his known ability to repay in six to 18 months, he should not be permitted to borrow. Neither should the banker take any undue risk or be influenced by propaganda to extend unwise credit. Unwise credit helps no one.

Must Shake Off Lethargy

Members of this Association, scattered all over the United States, reaching into every city and town, holding the purse strings of credit, can influence in great measure the extent to which private industry takes the place of pubic activity in the next few months and after. Either private industry will shake off its lethargy and pull us out of this 10-year depression, or we will fall back into the bottomless slough of increasing Government control, perilous public debt, political management, and general decay. Which road shall we as bankers choose, and lead others to follow? Let each answer that question candidly and truly, and measure his worth as a banker and a citizen not by words but by deeds. America is calling for that kind of leadership today. And America must have it if private enterprise is to survive.

PERSONNEL AND OPERATION PROBLEMS

Three talks were given under this head by, respectively, Ray A. Ilg, J. J. Gard and Claude L. Stout

Selecting and Developing Personnel

By Ray A. Ilg, Vice-President National Shawmut Bank, Boston, Mass.

Selecting and developing personnel covers a multitude of activities. I hope that we can delve into many of them in our open discussion, because it is impossible in the 20 minutes allotted to me to cover such subjects as the Personnel Department, the detailed procedure of selection and placement, job classification, salary standardization, working conditions, health, charting employment course and training, employee records, methods of promotion and employee relations, all of which might be said to come under my subject.

I am not here as an expert on personnel, unless you use that definition of "expert" which always serves as a definite check on dogmatic statements—namely, "An expert is one who is just beginning to understand how little he knows about a given subject."

In my preparation for this talk a world of new information was opened up to me. May I take the liberty of referring you to two works on these subjects, which probably have not had wide distribution, but which I found most enlightening and filled with information which cannot possibly be covered in our discussion. The first is the report of the Research Committee for 1939 of the Indiana Bankers Association. This report is on personnel management in banks and contains a survey of personnel in Indiana banks. It is most worthwhile reading. The second work may or may not be available, I do not know; but it is a thesis submitted to the Graduate School of Banking of the American Institute of Banking on the subject, "The Value of a Personnel Program for Banking Institutions." This is a very thorough job, produced by Leslie K. Currie, Assistant Cashier of the Mercantile-Commerce Bank & Trust Co. of St. Louis, Mo.

It seems to me that my contribution to our discussion today should be on a subject or subjects general enough to apply to large and small banks and specific enough so that I can hope to give you something worth thinking about.

After reading various works on the subject and discussing it with friends outside the banking business, and, naturally, with my associates, I wrote to 75 banks throughout the country representing what seemed to me a fair cross-section. I asked the officer addressed to answer eight questions regarding their personnel work. These questions were framed with the idea of receiving specific information, and, in addition, to get the "feel" of their attitude toward personnel problems and the progress they had made in the solving of them. The questions which I asked were:

(1) Who in your institution hires help?
(2) What type of young man do you look for, what are your requirements as to age, education, &c.?
(3) The third question was the same as the second, only it applied to young women.
(4) What do you do to train young people in your bank?
(5) Do you require A. I. B. courses?
(6) Do you have a regular plan for advancement and compensation?
(7) Do you have a definite "build from within" policy?
(8) Do you have public relations classes, and, if not do you have any other way of stressing the public relations side in your business?

The response which I received was most cooperative and enlightening. I shall not trouble you with details, but I would like to give you a little resume of the answers to each question:

(1) A personnel director or a junior officer hires the help in banks, depending upon the size of the institution. He is usually backed by a committee of two or three of the senior officers. The senior officers' contact with this hiring procedure is usually by application blanks.
(2) and (3) All banks look for young men with at least high school education, between the ages of 18 and 20, with a good, clean business appearance. They look for young ladies, single, about 18 years old, who have had a high school education or have taken a typing and shorthand course in some other type of school.
(4) The average bank puts the young man on the bench as page boy and shifts him from there to the transit department and from there to whatever job is open. The young ladies do not get that much attention but are put into a department and in most cases stay there until marriage or old age interferes.
(5) Banks, as a general rule, do not require A. I. B. courses, but do encourage them to the extent of refunding the whole or part of the fee if the course is passed.
(6) It is a rare bank that has a regular plan for advancement or compensation. Most compensation is taken care of on anniversaries by a review on the part of department heads and those in charge of personnel. There is in most institutions no charted course of advancement which takes into consideration the individual talents.
(7) The majority of banks have a "build from within" policy always hedged by the statement "except when experienced help is needed."
(8) The last few years have seen great stress placed upon public relations training in banks. For the most part it has not developed into a practical procedure. Here and there banks have evolved a system which apparently is getting results. But by and large it is a spasmodic or hit-and-miss type of education.

When banks plan public relations programs I think that there is a tendency to make, what seems to me, two fatal errors. There is one step that comes ahead of Public Relations, and that is Employee Relations, and we all have a tendency to forget it. We can give all the courses, conduct all the meetings, prepare all sorts of material to be used to Public Relations work, but if the employees of your institution are not interested in the welfare of the bank and do not consider themselves a real working unit within the organization then you have wasted your time and money on your Public Relations work. Therefore, it follows that Public Relations, through its most important part, Employee Relations, really starts right back at the employment officer's desk. He is the first contact with the employee, and his is the responsibility of seeing that the people he hires become satisfied, enthusiastic workers.

The other fault which comes to view in studying the various types of Public Relations programs is that banks bite off more than they can chew. Public Relations plans, both direct-to-the-public and through-the-employee, are all too often top-heavy. They are so complicated they fall by their own weight at the first lapse of enthusiasm. The few banks which have permanent and effective Public Relations plans have started gradually—

mastered and assimilated one step at a time. They have built their program modestly and soundly.

In studying the replies to my questionnaire it struck me that, large and small, banks generally follow the same procedure, and for the most part it is a procedure which has developed by evolution rather than revolution. Consequently, in the medium size and small banks, the responsibility of hiring help is usually considered a task rather than a mission. It is a routine job, borne of necessity rather than one inspired by a long-range appreciation of the value of man-power. The executive interest in the original hiring of help, which, after all, is the actual pumping of fresh blood into that often-termed "corpulent body," the banking business, is sadly neglected. It is one department of banking in which the new executive spirit—that spirit of keeping a sensitive finger on the pulse—has not yet really touched.

All in all, it seems selfishly logical to concentrate on two important parts of this personnel problem. I say "selfishly" because my institution is no different from any other, and we are trying to learn.

The two subjects which I selected are "The Planned Hiring of Help On a Long-Range Basis," and "The Studied Development of Man-Power."

First, I would like to make a general statement about the personnel of banks which perhaps is generally known, but which had never before struck me as being such a potent factor and one which, if overlooked, is bound in time to bring upon a banking institution a serious personnel problem.

It is only natural that throughout the years, with the banking business placed upon the pedestal of marble and stone—although, perhaps, in the last few years we have been inclined to think there may have been a little sand at the base—that the general conception of the public and one which is bound to permeate into the subconscious thinking of banking executives is that everyone who works in a bank must be the executive type; but actually a bank is no different from any other business organization or manufacturing concern. There are certain jobs which are routine or mechanical and which always will be routine and mechanical. For these jobs it is necessary, in order to produce efficient, smooth and accurate service, that you do not have a continual turnover of employees on this type of work. That means that the man or woman picked for one of these jobs should be picked with the idea that he or she will stay there. In normal cases, the longer they are on the job, the better they do it, and the highly educated, ambitious executive type of employee has no permanent place in this work except for preliminary training. If you plan your employment schedule without taking this into consideration, either one of two things happens: You will have, if you expect the ambitious person to handle such a job, either a continual turnover due to rapid promotion, a dissatisfied worker who feels he is due for better things, or you will have spent your good money training somebody for some other person, company or bank to reap the benefits from your labors.

It seems to me that you must definitely plan your hiring of employees so that the people you select fall into two definite classes: The mechanical or routine worker and the executive type. The fact that you earmark someone as a routine worker whom you expect to be satisfied with steady employment but low salary for the rest of his life does not mean that you are stifling ambition. The best example of this that I can think of is the Army. An army cannot be all officers. Therefore, the Government has a West Point where they produce Second Lieutenants. These men are earmarked as executives. If they live up to regulations and do their work they will some day be Colonels or Generals. They are the selected group on whom the money is spent to produce executives. They are paid higher salaries, they are given more advantages, they are continually schooled as a favored or selected group. This has to be done; otherwise, we would not have efficient army officers. At the same time, the man in the ranks is not completely shut out. If he is exceptional, willing to work hard, and is ambitious he can fight his way to the top. He has the odds against him, but when he does fight his way to the top he is, perhaps, a better man than those who were favored at the start. Whether or not this seems fair, it is true and is not only true but is absolutely essential in the formation of an efficient, progressive and staple force, whether it be an army, a commercial or a bank force.

You must not get the idea that such a division in hiring policy makes the man hired for mechanical work a "forgotten man." That group, too, must be carefully developed so that each year a number of young men can enter the executive training group from the ranks. When a young man of 18 years, taken into the bank after graduating from high school, has had five or six years of experience he may well develop into fine executive material. He will then be at the age level of college or business school graduates.

"The proof of the pudding is in the eating." In our particular institution, and taking the strictly banking business as a basis, we find that 86.73% of the jobs in our bank are mechanical jobs, or what you might call routine work, not requiring executive ability. This figure does not include officers. If we include officers in this figure, the percentage of mechanical or routine jobs is 81%.

Of the mechanical jobs, 6% at least are continually filled by executive material. This is the training and testing ground.

Every institution varies as to its needs. In each case, however, a careful review of past experience will show what is the normal need for mechanical and for executive material.

If these figures are not kept in an approximately correct ratio, you will have either a dearth of executive material or a too rapid turnover of mechanical material, which will naturally impair service and run up overhead.

Whether the bank be large or small, the officer entrusted with the job of hiring employees must clearly chart his requirements. When he goes into the market for man-power he must know what he is looking for. If his ratio is such that he needs 10 mechanical help and three executive help, me must avoid the tendency to overhire executive help. Of course, the people that have the executive ability generally make a better showing. They have better personalities and background. The employment officer takes greater pride in adding them to the payroll, but if he cannot provide jobs for them in the future, he will have a turnover in his executive material which will be most costly, because these are the people who will not sit still. He must either provide reasonable promotion and continually increased remuneration or they will leave him for better jobs. Therefore, it is better to hire only the executive material that you can properly take care of. This will insure you a long average employment of exeeptives, which is most valuable to any organization. It will also provide these executives with a chance to expand and grow. This feeds ambition and makes possible the highest grade of work.

In the selection of those to fill mechanical jobs it is the duty (and by "duty" I mean the employment officer's duty to the individual and to his organization) to pick those people who are in his mind truly mechanical or routine workers. By this I do not mean dullards, but you will all admit that there are certain people who are more efficient and more happy with routine employment. They do not want nor would they accept great responsibility. As I pointed out before, these men may develop into executive material, but if the officer who picks them is capable, you will agree that the percentage of those whom he picks originally as executives and who go to the top should be a great deal higher than the percentage of those who are picked primarily for a certain type of routine or mechanical work. After all, this is a free country and our business is free, and the man who has the goods can get to the top. They say that a free country is one where you can do what you please without considering anyone except your wife, the police, your boss, the life insurance company, the State, the Federal and city authorities, and your neighbors.

Let us assume that the man hiring the help, whether he hires three a year or 300 a year, does so with an eye to the future. He takes a vital interest in finding out what he will need in the future, and in this way he gives a fair deal to the men and women he hires. He does not send them up any blind alleys, and he does not hire people for whom the job will either be too much or will prove stifling. In the vernacular, "He gives them a fair break."

I have heard the comment made that to do too much research on this employment business and figure out on paper exactly the type of man that you have to hire and the kind you have to reject, has a tendency to become mechanical and that, after all, human relations should remain human and hiring people is a part of human relations. I agree that this is all true, but I wish to point out that the human side does not enter into the preparatory work or the determining of what type of man or woman you need for a job. The human side is in hiring the right type, so that the person will not prove unfitted for the work. To hire one who has not executive qualities and expect him to prepare for an executive job will prove disappointing to the bank and extremely harmful to the individual, and vice versa, to hire an executive type and put him into a mechanical job, remembering all the time that unless one is earmarked to start with executive work, it is a long, uphill struggle to reach the top. Every time an individual gets a job which is not suited to him and for which he does not have the necessary qualifications to make his way in the world, it is a fault on the part of the person who hires him. Therefore, I say that to me the human side of this employment business comes in hiring people who will have a fair chance to succeed on the job which you have for them.

There are certain jobs in a banking institution which must be filled by future executive material in order to provide a method of training. These jobs, of course, are not to be considered in what I have just said. As mentioned before in this talk, most banks use the bench, the transit, and sometimes the bookkeeping department to train employees, but we will touch on that later when we talk about the proper training for employees.

First, let us consider those who are hired for mechanical or routine work. What has proved to be the best way to handle this situation?

The banks which have had the most success seem to follow this procedure regarding the boys hired. Most of the young men of this type are around the ages of 18 to 20, with high school education. They serve about six months on the bench and are then put into the transit department as outside messengers. They do nothing but messenger work at first. Some time ago it was possible for those training in the transit department to help in all phases of the department. Now, the proof machine has changed things so that it is necessary that the first step is strictly messenger work. After this, they are given a job in this department as the transit clerk or settlement clerk, and from there they are placed in another department where they are expected, under normal circumstances, to stick to one job for a period of years and take their normal advancements.

In the case of girls, they are usually trained for a specific job, such as a machine job, and they do not get even as broad a training as the young men. In the case of stenographers, this is still more true, because they work in the stenographic department, if the bank is large enough to have one, and from there take a secretary's job or a job as a secretary-clerk in some department. All in all, this does not present a particular problem in any bank. It is simply a case of having enough people coming along to make replacements, which, in this particular type of work, can be gauged pretty accurately through past experience.

The type of employment which provides us with the greatest problem is that of executive training. Here we must be sure not to hire more than we can take care of because we will lose our investment through turnover. On the other hand, we must have a sufficient force coming along so that we can build our personnel through our own people, and can avoid going outside, which is always disturbing and usually expensive.

This type of young man is generally older, because he has had a college education, in most cases, and is about 22 to 23 years of age. He starts off on the bench but cannot be expected to stay there as long as the young man four or five years his junior. He has been picked because he apparently has executive possibility. You expect that some day he will be a Vice-President of the bank or perhaps President. At least, his chances, in your mind, are much better than those of any one of the young men hired for a mechanical job. Otherwise, you would not have hired him. In most banks, after a session on the bench, this young man is placed in the transit department as an outside messenger. If it is a large department, he does straight messenger work, and eventually is given a job as transit clerk or sorting clerk, or perhaps some job in the bookkeeping department, bearing in mind all the time that this man is being trained. The ideal method used by a few banks is to have a scheduled course which takes him into all departments, tellers, bookkeeping, credit, auditing, analysis, trust, foreign, &c. You are trying to give him a fundamental knowledge of the banking business as far as procedure goes, so that he may be better equipped to handle the job for which you are preparing him. This is all simple enough, but there is one part which I think we miss. I know we do in our bank, and I expect that many of you do in yours. As a matter of fact, I know that you do. The department heads and the officers of the bank do not know this young man. He has been in training for four or five years, yet the first time they meet him is when they have a position to fill. They should have had an opportunity to know something about him, to have become acquainted with him, to have followed his progress, to have decided ahead whether or not he is someone they want to use. Therefore, in my opinion, it is the job of the personnel manager to see that these young men in this selected group, these "second lieutenants" as we might call them, have an opportunity to meet and talk with the officers and heads of the various departments. If the department heads get to know the young man in training, they will be able to select for minor positions in their departments a candidate in whom they have confidence and feel that some day will become an executive for them, that he can take more and more responsibility as the years go on. It is only a human trait that an executive will take more interest in a young man if he has something to say about his training, and has taken a personal interest in following his progress.

There is no rule of thumb which can be used in mapping the training course of those young executives. To start with, you have a considerable investment in them, not only an investment of money but you have invested the future of your business in those young men. You cannot afford to lose them all or even a sizable percentage. If you lose one crop of young men that you are bringing up for executive positions, it will make a hole in your organization at a later date. All of us have been through this, and as a matter of fact, the very bad years of the depression stopped a good many banks and companies from bringing in their usual quota of young men to be trained as executives, and the time may not be far distant when they will feel the effects of this gap in the flow of man-power. I think it is safe to say that there is now a shortage of young executives who have had the necessary seven or eight years' training to make them effective.

The man in charge of personnel, whether he is handling one of 30 such young men, must make each one an individual case. This type of man does not catalogue as easily as the mechanical type. You must study him, keep pace with him, and see that his interest in his job never lags. It won't lag if he has enough to do, if the work is interesting, and if he can see that just efforts are rewarded by promotion and more responsibility. Remember that this type of man, if he is good and if he is one you are going to keep, is hungry for authority and hungry for responsibility. You cannot give him the authority early, but you can feed him a little bit of responsibility from time to time, which is in most cases regarded as the highest prize of all. A proper job of tailor-fitting this man to his work can only be done by frequent interviews both with him and with the department heads for whom he works. You have a long-range investment in this man and you can afford to spend time on him.

I do not feel that it is right to take time to go into more detail on this now. Perhaps it will come up again in the discussion.

Before I close there is one point I want to make which I think all of us can take home and find it very nourishing food for thought.

If this statement does not apply to your bank, in other words, if the cap does not fit, please do not put in on. If your institution is to start a new advertising campaign all the senior officers will show an active interest in it, they will spend time and help in the preparation of it, and, all in all, the result will be a composite effort of the leaders of your institution.

If you are to invest in new machines for one purpose or the other, and the investment runs into $25,000 or $30,000, the senior officers of your bank will take an active interest and will devote a good deal of their time to the consideration of the proposition and in deciding whether or not to accept or reject it. If you are going to put in air conditioning, install new heating or ventilating equipment in your bank building, build a new type of cage or counter, put in a new service such as personal loans, or decide to handle no minimum checking accounts, you will find that the senior officers of your bank will devote plenty of time to it, because they feel the bank is making an investment, because they feel it is their duty as officers and perhaps as directors, to pass judgment upon the action.

I believe also I am correct in saying that the biggest single item of expense, or shall we call it investment, although it is an investment from which the principal can never be withdrawn, on any bank's statement is salaries and wages. The total bill for all expense, including interest, in running the National banks of the United States for the year which ended June 30, 1938, was $585,882,000; of this, $239,643,000, or over 40%, consisted of salaries and wages, and yet by comparison, how little time is spent on these expenses, on these investments in man-power, on these investments in the future of your institution, on these investments in people who will represent the bank to the public, and on whom depends the public's goodwill. I dare say that in 99 out of 100 cases the senior officers' first interest in a man is after he has been with a bank eight or 10 years, and after the young man has been made or broken. The time to have known him was when he was first in the bank. I know it is impossible for senior officers to interview applicants for jobs, but once the experts in the bank on this particular type of work have selected a man and have placed him in their category of second lieutenants or executive training for future Vice-Presidents, then he should have the attention of the senior officers. They should meet him, they should follow him. He is one of the selected group in which you have a big investment, not only a yearly investment of dollars and cents, but you are counting on him to be in the bank when you need someone in an executive position. He is your stop-gap of the future. It may be years ahead, but you have got to keep his interest and hold him or you will have a shortage of executives. That is why I say that we pay too little attention to our biggest investment, to our biggest expense—man-power. Banks are known as a training ground for executives for other businesses, just as they are known in most cities as a fine training ground for stenographers and secretaries. That is because the bank provides excellent training but loses the guiding touch which holds those who are worthy of a chance for promotion.

If we do not get another thought out of this discussion today and from the questions which I know are going to arise in this meeting, let us review our own institutions and see whether or not we are properly guiding those young men, picked for future executive position. See if we are protecting our investment in them. See if they are the type of young men who are eager to learn, ambitious to advance, and loyal to those who place confidence in them.

Let us also make sure that we are doing everything in our power to help and guide those who are serving in routine jobs so that they may make of themselves executive material. There is so much that can be done to help the latter group, who are usually without advance educational advantages, to lift themselves to higher earning levels.

The young men that you have picked as the future executives and the young men that you will develop so that they can become executive material are the life blood of your bank. You cannot afford to ignore them. You must realize that these young men require special training, more personalized attention, if your "second lieutenants" are going to become generals.

Work Simplification and Organization for Efficient Operation

By J. J. Gard, Vice-President United States National Bank, Portland, Ore.

My topic is one to which I believe every banker is giving more and more attention and thought. It has been my observation that banks throughout the country are today operating with greater efficiency, which is in reality the improved handling of our customers' business whether in the commercial, savings, exchange or any other department. With today's interest rates, with present working hour restrictions, and ever-increasing volume of business, bankers must recognize that conservative operation of their banks must include this important part—a good organization with economical yet efficient and practical operation.

One of the first steps to consider in developing a smooth organization is the division of responsibility between the Board of Directors and the management. The technical definition of executive is "to carry through so as to affect, put in force, or accomplish." The Board of Directors formulates or approves policies and the management in the form of one or a group of officers puts them into execution. While there must necessarily be committees acting as liaison bodies between the Board and the executives, I am in favor of a strong centralized form of control in the way of management, where important problems are considered and decisions rendered. There must be evidence of finality and matters laid before them must be dispatched with promptness and regularity. The management must have a clear understanding of the authority granted by the Board and, in passing judgment, every effort must be made to gain full knowledge of the facts in each case. Too many times our judgment is only as good as our information.

Next to consider is the division of duties among individuals in key points and certainty that their responsibilities are well defined. This will offer these men new fields to explore and latitude in thinking and working out improvements within the authority granted to them. Consider the advantage an officer or employee has who understands what is expected of him, in contrast to the confusion that can exist when he does not know with reasonable certainty the extent or limits of his responsibility. Under the latter system it can be expected that advancements and needed changes will fall by the wayside for the lack of someone to concentrate on proposals and see them through. There is no better method to develop subordinates than to give them responsibilities. On the other hand, if the management is to guide the destiny of the bank it must have the proper control over all functions and be fully apprised of the operations in each division. Important matters must be referred for consideration and time is required for these conferences and reviews. Officers and subordinates must be instructed how to differentiate between the essential and the non-essential, thus enabling the management to keep in touch with the operation without resorting to the analysis of countless details.

I feel that the foregoing principles apply to every organization, large or small, and if practiced will clearly disclose the objectives and will filter down through the ranks and instill confidence and understanding.

A large city bank should give thought to the chart system of operation, which discloses, along engineering lines, the divisions and major departments, such as loans, investments, commercial, savings, internal operations, audit, &c., and the executive head or heads of each. There would be departments within these divisions; for example, under loans there might appear commercial loans, real estate mortgages, instalment and finance paper, credit department and controls. Under internal operations there would be the multitude of departments functioning for the entire bank, the number of such divisions and departments necessarily depending upon the size of the bank. A department should not be created unless it is required and the work cannot be performed by one individual or assumed by another department. It is just as inefficient and costly to create too many departments as it is to under-departmentalize the bank. In creating an organization it makes no difference if the duties assigned are performed by one individual or by a group or a department. The theory is just the same, and it can be carried out in most any size bank. In some cases the functions in the main might be restricted to loans, investments, and operations. Nevertheless, the management must decide upon assignments in the same way as a large city bank.

During my experience in examining banks I frequently made the observation, and it was apparent, that the officers, or officer, were directing their energies far too much toward details and the more important matters were neglected. In others the details were lost sight of because no one was delegated to look after them. There were still others where the officer tried to cover the executive duties and a large share of the clerical activities, such as tending the note cage, resulting usually in loose operation. All this is needless if the organization as a whole is set up to produce the best results for the bank. Teamwork is the desirable feature, and the goal we should strive for is the maximum service as is practical from the entire staff.

For example, someone in your bank might be delegated to keep the credit files in current condition and to see that proper analyses are made of new statements. Often one officer or employee is assigned to oversee the daily operations and systems; he performs much the same as the operating head of a very large bank. One may be interested in auditing and could be utilized in making periodical checks for the management, provided his other duties did not conflict. You may have a bright and energetic employee who is qualified to call on your customers in the interest of business development. A part of his time might be devoted to this enterprise. There are numerous other ways to distribute the various functions and duties so that all have the attention that is essential if the bank is to be termed "well managed."

In a recent article which appeared in a well-known financial publication, H. N. Stronck, a technical adviser to banks, in summarizing arguments in favor of the development of an organization with proper controls, said, among other things, that it proved an "aid in the determination of sound policies and detecting and eliminating unsound ones," and tended to "foster the development of a well coordinated, energetic, cooperative, loyal and self-perpetuating organization." That the foregoing system will prove of the greatest benefit to the Board and the executive head in skilfully carrying out established policies and practices to the finest degree, there can be no question. Our bank for a number of years has adhered to the chart system, and we have found this method to be of distinct advantage in distributing duties to the various desks.

As it will not be possible in a few minutes to follow through each component part of a typical organization, let us take for example the operating angle, and bend our energies toward the personnel, operating, and comptroller departments. Some banks combine the control with personnel or operating with control, and in certain cases these combinations have been demonstrated to be entirely satisfactory, although it is my belief that better results may be realized if each is separate and apart in positive form. For example, the Cashier may supervise both operations and personnel yet have assistants in each division working independently and without influence from the other. In your bank the three different functions may be performed by only one individual, and, though this is a fact, for the purpose of this analysis each will be dealt with separately.

The personnel department acts as the contact between the management and the employees, and is interested primarily in their welfare, fitness, and development. The officer in charge does not give particular attention to operations or systems and is more concerned whether an employee measures up to the right standard and can turn out an appropriate volume of work. From his angle he constantly keeps the question of training before him and, while this paper stresses efficient systems, I do not believe we should permit our mechanics to reach such a point that incentive vanishes. In other words, there should be a happy medium between the force of mechanism and the construction of an intelligent body of employees.

If the organization is to be successful in every respect we must not overlook the atmosphere that should prevail. In nearly every instance the responsibility for the right condition rests with the management. The spirit of cooperation must emanate from the top and, if given the proper encouragement, will soon permeate throughout the entire staff.

Working conditions play a prominent part in the efficiency and well-being of your staff. Experts have proved that faulty equipment and poor lighting and air have their adverse effect and in judging the qualifications of employees these fundamentals must not be overlooked.

Every bank has a large investment in its officers and employees, and to that extent is vitally interested in their welfare. It is our duty to encourage thrift and conservative management of their own affairs, as employees whose finances are impaired cannot always do justice to their work. As an outgrowth of this interest on the part of the bank, there has been a development of group accident and health insurance which is of untold value in assisting those who become involved in financial difficulties because of a misfortune over which they have no control. Group life insurance and pension plans have their part in the upbuilding of morale, and tend to strengthen the ties between the employer and the employees.

We must not forget the problems of the employees, and in dealing with them there must be firmness, no favoritism, and above all a spirit of fairness. Decisions reached must be based on facts and sound reasoning if the officer is to retain the employees' goodwill and confidence. In counseling with them good judgment must be exercised, and in many cases this requires a sympathetic and understanding heart as well as an intelligent head.

The operating head and his assistants must give the organization, large or small, supervision to the end that practices and routine are always adhered to or followed. Peak loads and valleys are prominent in the banking business, which requires this officer to arrange his employees from day to day as needed. The staff must be sufficiently flexible to accommodate full demands. Lacking a clear understanding of the activities, the bank will flounder in inefficiency, service is impaired and expenses may increase rapidly. Lieutenants in the form of department heads, and employees in key position as needed, make a large organization possible and will add to the efficiency of almost any bank.

An important duty of the operating head is keeping activities correctly divided so that overlapping, duplication and lost motion is avoided. This is no small chore in itself, and in our bank requires continued planning and thought. Some banks have developed committees to decide upon methods and systems, and others have established planning divisions. Still others have a capable operating head. Outside experts are sometimes employed. Each of these plans has its merits.

In cooperation with the personnel manager and department managers, employees must be developed for advancement and new help must be trained to fill vacancies caused by promotions and resignations. The operating head must have a hand in this if the organization is to run smoothly. A department crippled because employees are not trained up to a responsibility needed is an unsatisfactory situation, and errors resulting may bring criticism against the bank. I recall once that an applicant for a position in the bank stated that he preferred a job as a desk where little or no responsibility was required. He was, of course, informed that there were mighty few such places and that we have standards requiring a certain amount of training before assignments are made. An error by an employee can sometimes be as important as a mistake in judgment by a loan officer.

A new problem is the limitation on working hours. We have found that in general this also is a matter of planning and supervision, and in many cases overtime can be corrected by changing working hours, time of starting, and giving time off. Adjustments may be made so that the work can be concentrated in a few hours instead of spread over a greater number or by giving the department in need experienced help at certain times of the day. This latter plan has been very helpful in our bank and goes back to the shifting crew principle which has been advocated by well-informed bank men for many years. The result is more flexibility and much less expense than would result from the addition of more employees, whose time would be wasted during slack periods.

The inclusion of banks under the Social Security Act will create additional taxes for both old age benefits and unemployment. These assessments will be based on the payroll and increase with the number of employees and, to a certain extent, with salaries. It is needless for me to say that all these new assessments and burdens act as a syphon from our life line, net profits, and that, like a manufacturing or other commercial enterprise, we must look at operating costs without the use of rose-colored glasses. Tradition, if it is tradition, must be put in the background. By this I do not intend to convey the thought that we should change our methods for the sake of changing but, on the other hand, when something new has demonstrated its merits, we should not decide against it without careful analysis and application to our own organization.

Many banks have coped with the peak load problem, and while in some cases it is not practical to eliminate the causes, there are ways open to counteract some of these excess demands on the staff. For example, a number of banks are following the plan of staggering customers' statements throughout the month, or rendering them on a date other than the last working day, which is usually heavy. We have followed the latter system and have selected the 25th in a number of our offices. All statements, with a few exceptions, are prepared between the 25th and 31st for delivery on the first day of the succeeding month. We have been doing this for about a year, and it has been of real value to us. Furthermore, this change has been accepted by our customers with satisfaction. In looking at time cards of employees who are working under this plan, practically no increase in hours can be detected in the week the statements are completed. I have observed that some banks are delivering statements on the second and third of the month, although preparing them on the last working day. This should help in reducing hours.

The growth of consumer or retail credit has increased in the note department, and many banks have found it necessary to install a special system for this work. There is a certain volume which seems to make such a change advisable and more economical, which must be detected and the situation corrected. This is likely to occur in any part of the bank and the question is: has someone in your organization been charged with the responsibility of following trends, making tests and observations to determine what should be done to keep systems abreast of ever-changing conditions?

Many banks are utilizing single posting in bookkeeping, and by using the photographic method have streamlined their transit departments. More and more banks are coming to photographic records to avoid duplication and to highly developed electrically operated machines capable of absorbing a large volume of items. This use of new equipment applies to most of the operating departments. Whenever a person sponsors a change in equipment or in a system and considers the problem solved for a long period, if not forever, right there he makes a serious mistake. Your organization is not complete unless someone is making studies of the advantages and capacities of machines that are today offered in the market. The large bank equipment companies have laboratories where tests are consistently made to give us better and more productive machines.

There are too many current topics dealing with the mechanics and operations to discuss here, and my purpose is to urge you to have some individual or individuals in your bank designated to keep the foregoing objectives in mind, make reviews periodically, remain alert, and eliminate unnecessary activities and lost motion. How many times have we heard the following paraphrase: "This system is not altogether necessary, but is nice to have." We have in the past said that some things were impossible or, without going that far, completely disregarded new theories that were advanced. Now some of these proposals are an accepted part of our routine and are fully seasoned. Not long ago a banker wrote to me that he felt that banks returned too many checks because of minor irregularities, especially when endorsed by responsible firms and corporations. Considering the expense of handling return items, this may be a good point for consideration. Remember this, that every unproductive motion removed from operations today will save for tomorrow. Do we fully recognize that a reduction of $1,000 in expense is equivalent to the income on $25,000 loaned at 4% for one year; that each dollar of additional expense subtracts a dollar from our net profit?

To fulfill properly his function, the comptroller must be well informed of policies established by the bank's board and management, and must have the ability to sense and understand that which is desired. He must interpret instructions with practical and intelligent application. From the angle of bookkeeping, almost any trained accountant could act as comptroller, but actually to perform for the bank he must be able to view with perspicacity everything that he sees, for regularity, accuracy, and propriety. His examination of activities that come within his scope of authority must be minute and thorough, yet broad enough to prevent the defeat of the very purpose of his office.

For smooth operation and good results the accounting system in his department must be carefully planned and adapted to the bank's requirements. The control over assets and liabilities, income and expense accounts must be made possible by adequate records, and he must be satisfied that the system in effect in the bank provide him with needed information and offer proper safeguards. Volume of items handled should be gathered from the entire bank and translated into analyses showing trends, efficiency of operation, and costs. These statistics would include output of items per employee and the salary and total cost per item handled. Some banks have weighted certain relative transactions and arrived at a work unit which can be used to establish the efficiency of a department. Those employing the use of this principle indicate that it is very helpful in making comparisons.

In conjunction with the personnel officer and the operating head, the comptroller should analyze the output of an average good clerk to measure against one who may not be doing his part. The comptroller must know with reasonable accuracy the cause of an increase or decrease in the number of personnel in any department. In other words, the comptroller carries on research work and measures production by the various formulas of his department. The studies made and measurements taken are just as important to the management of a bank as the dimensions of a building are to a contractor who plans to build it. The comptroller's duties are to me the most important in the bank, and even a small bank can apply tests to its own organization, and keep detailed records at little cost and without the expense of a separate department.

As a word of caution, it is very easy to create one department to check another, and in deciding upon a proper balance the management should guard against a top-heavy number of employees in any non-operating department. Too much staff in the comptroller's department will produce too many studies that are of no particular importance. Sometimes we may find efficient operation but an overload in the supervision which can be even more expensive.

It is realized that every bank cannot have a comptroller or a personnel department, but I do believe it is the duty of the management of every bank to reap some of the advantages and share in the results. Consistent study of staff methods, routine, and systems is bound to bring forth improvements, which is the tonic needed to keep employees interested and thinking. They who share in these improvements take pride in their part and can be observed seeking new ways to expedite the day's work. The thought is not to burden employees, but to maintain a happier and more competent personnel, increase enthusiasm, and prevent rust. Such a course is necessary not only to show the capacity and capabilities of an organization but to insure its very foundation and perpetual existence. Let us remember that it takes a well-organized bank to bring about good performance by its officers and staff, and that they cannot serve a twentieth century business world with horse and buggy methods.

Account Analysis as a Guide to Charges

By CLAUDE L. STOUT, Executive Vice-President and Cashier of the Poudre Valley National Bank, Fort Collins, Colo.

To lay a foundation for some of the things I wish to emphasize, permit me to direct your attention to certain underlying facts which may appear unrelated to our topic, but which have a direct bearing upon the future progress of banking.

Speaking before the Wisconsin Bankers Association, Leo T. Crowley, Chairman of the Federal Deposit Insurance Corporation, said a few weeks ago:

"In pursuing his search for profits, I believe the banker would do well to apply to his problems the standards and the ingenuity he expects from his customers in other lines of business."

In other words, Mr. Crowley said: "Be what you expect your customer to be."

Apparently we bankers have studied everybody's business save our own. We have insisted that the general merchant close out his unprofitable shoe department, that the dairyman convert his boarder cows into producers, that the farmer abandon fallow soil, and that the manufacturer curtail production costs. Yet we have deliberately ignored our own merchandising problems.

The source of a bank's net income appears to be immaterial on first thought, whether from bonds, loans and other investments, or from adequate service charges. But this question, reviewed in the broader light, takes on a more profound aspect. With bank overhead constantly increasing in the form of Federal Deposit Insurance Corporation costs, rising taxation, social security, wage and hour regulations, and other uncontrollable expenditures, it resolves itself into a question of whether or not we shall seek this margin of net income from additional investments of a permanent, fixed capital nature, or purchase a sufficient volume of bonds at their present extreme prices to insure tempararily profitable operations. Either course involves relaxation of our vigilance as to the quality of these loans and investments.

Your depositors are not in position to evaluate your note case or bond portfolio. The mere showing of satisfactory earnings is not necessarily indicative of satisfactory investments. On the other hand, a note case of solvent loans, a bond portfolio composed of investments which will be liquidated from income rather than by refunding, combined with an adequate system of service charges, is uncontestable proof of solvency—you have a sound institution.

Certainly there can be no greater obstacle to progress than a breakdown of our financial system, a breakdown of our present banking system, because it is in fact not the cornerstone but the broad foundation upon which rests our present great democratic form of government. This statement is not far-fetched, erroneous or theoretical in any wise. It is substantiated by the very teachings of that eminent Socialist, Karl Marx, whose word is scripture to his followers. Karl Marx said, in substance:

"First, let us secure control of all banks and financial arteries. Second, let us secure control of all transportation and communication facilities. Finally, let us obtained control of the army and navy. The revolution is won."

In other words, the capitalistic system has now been completely obliterated.

Hence that is the reason banking is subjected to such vicious attacks by those who seek political power to regulate the rights of citizens. If banking were not such an important adjunct to government it would be ignored. Democracy is the only form of government which permits privately-own banking. Every other form of government, either socialistic or totalitarian, dominates its banking structure, eliminating all semblance of credit discretion on the part of the individual.

Please bear in mind that any reference to privately-owned or independent banking includes all institutions operating under our present system, whether branch or unit banks. It is intended to differentiate only between privately-owned banks and those under complete Government domination.

In an address at Colorado Springs, Colo., in June, 1934, I made a statement which then appeared to be radical indeed—a prophecy which appeared far from actual fulfillment. But today I submit to you that statement made in 1934, and leave to your determination the question of whether or not it is much nearer fulfillment today than it was five years ago. That statement was, in substance, as follows: "Independent banking is on trial for its life, and probably will not survive." This statement becomes more significant in the light of recent developments, and if the trend towards centralized or Government-owned banking is not checked within the next five years, if the people of this Nation are not willing and ready to work shoulder to shoulder with privately-owned banking, this prophecy made five years ago will have become an actual fact. If the barometer of human success is to rise according to a demonstrated ability to lead the people over highways of impractical, unworkable financial theories, into castles of unsound, destructive business principles, then banking—individually-owned banking—is in fact rapidly on its way out.

We are squarely faced with a problem of psychology—of counteracting the influence and leadership of these false prophets, these men who in too many instances have acquired high places in Government apparently because of their notable record of failure in the actual management of a business or profession of their own.

An understanding public is the one means by which bankers can expect favorable treatment from lawmakers, for the men who make the laws are still dominated by the people who elect them to office. Our business conduct must convince the man on the street that the presence of a community bank has a constructive influence upon the volume of business transacted in that community. He must be made to realize that a privately-owned community bank favorably affects the wage scale, the jobs available to labor, and the value of homes and real estate, whether actual cash value or assessed value. These home banks directly affect the amount of taxes which may be levied and collected for any particular phase of government, including educational institutions. I question whether the average person ever realizes the extent to which locally-owned banking is vital to the preservation of industry and to the preservation of a democratic form of government. So it is important that we keep constantly in mind that privately-owned banking will survive or perish in the future according to the understandings or the misunderstandings, the likes and dislikes of the man on the street—that group of citizens who today hold the balance of power.

If we bankers of America have faith in our free and independently-owned banking system, let's demonstrate our ability to stand on our own feet, without any more governmental aid or subsidy of capital structure. We do not for a moment doubt your sincerity of purpose, your determination to do your utmost to further the cause of privately-owned banking. But we do question whether or not the average banker realizes the immediate seriousness of this situation. For that reason we wish to emphasize in this brief address a factor which has a direct bearing upon the success or failure of this banking structure we have so carefully built in the course three-quarters of a century.

There is one thing that we have in common with all business and professional men, whether large or small, whether farmers, merchants, doctors, dentists, or manufacturers. If successful, we must deal in facts—we must know costs. Sooner or later we must turn our minds to this fact, because capital deteriorates, wears out, and must be replaced just the same as any other tool of industry.

The subject of cost analysis has too frequently been ignored or lightly touched upon by the majority of bankers. It is imperative that bankers cooperate to the extent of adopting a uniform method of arriving at banking costs and charges. Bank customers whose interests necessitate the transaction of banking business in various sections of the country are justifiably skeptical of the soundness of any service charge plan when they find such a wide divergence of opinion and such wide discrepancies in price schedules. Every banker should industriously seek to eliminate as many of these differences as possible, because, obviously, not all of the different plans can be correct, and so all stand convicted as incorrect.

Naturally, costs and charges will not be identical in all sections of the country, but certainly the method of arriving at these costs should be as nearly uniform as possible. Too many bankers install service charges in a hit-or-miss fashion, with no better reason for their installation than that their institution must have a certain amount of money with which to operate and meet overhead. They have no logical defense to offer when the customer asks: "Why do you charge my account this amount?"

The merchant is always prepared to answer such a question, because he knows his costs. When he places a price mark on a suit of clothes, he knows that this price includes not only the wholesale cost of the garment, together with its proportionate share of all fixed overhead, such as light, heat, rent, taxes, &c., but that merchant knows that this price contains a reasonable and necessary margin of profit as well.

Surely the banker should be foremost in scientifically appraising and pricing his merchandise. You cannot adequately sell fair charges to the public until you yourself are convinced that you do have a valuable and indispensable service which is being offered to your consumers, one that is essential to the well-being of this Nation and its people.

All the free service that banks have ever given away, individually or collectively, in the last 25 years, never produced a single cent of undivided profits, never strengthened the capital structure of any institution, never contributed one thin dime to the assimilation of a loss. I feel justified in saying it has contributed very little to the well-being and friendship of our customers.

We endeavor to convince the public we are operating a sound, conservative institution, that their deposits are safe in our care. And yet 35% of the depositor's dollar, in many instances, is invested in a concern which is running behind every year, invested in bonds of an institution whose budget is not balanced. As I ponder this situation I wonder what the results would be if we were to submit a questionnaire or inquiry to every depositor in our institutions asking permission to invest 35% of his funds in Government bonds, particularly if we explained that this Government bond represents a violation of every fundamental known to solvency?

We conscientiously explain to the public that our institution is solvent, that our banking structure was never in better condition. We make such statements even though we do not know our costs and therefore are unable to place an intelligent price mark on our merchandise. How can we reconcile this policy with the position that a sound banker must take in dealing with borrowers, when he tells the merchant that his loan will not be approved because his budget is not balanced—because overhead exceeds income—because he does not know his costs—that there is not a reasonable profit load in his selling price? The day is not far distant when you and I will be called upon to face this public and explain to them why we bankers, men who are trained presumably for a lifetime in the fundamentals of sound finance, have allowed the public to believe that the investment of their funds in deficit bonds could preserve our institutions upon a sound basis.

If the public were allowed to view this scene of banking in the proper light I am sure they would not only approve but would demand that all banks recover their costs through a system of adequate charges rather than invest the public's funds in high-yielding, questionable investments. An accurate and fair uniform schedule of charges is impossible of accomplishment without an accurate, careful cost survey of your own individual institution. Not only salaries of employees should be recovered, but fixed expenses, such as taxes, depreciation of building and equipment, protective insurance, Federal Deposit Insurance Corporation costs, social security, wage and hour requirements, and other actual overhead, should be allocated through an accurate cost survey and passed on by account analysis to the person who directly benefits therefrom. If these expenses are theoretical, if the expenses of serving the individual on our ledgers is a myth, then that portion of the expense voucher issued in payment of such theoretical or mythical expenses should never have been issued, because it is a misapplication of funds. It is a fraud on the stockholders.

Placing your institution on a cost-plus basis will, to a great extent, remove the incentive to invest in high-yielding, questionable bonds. Such loans and bonds are invariably acquired for the express purpose of obtaining income to offset dissipated earnings. In their anxiety to seek earnings, or in their search for earnings with which to meet an ever-growing volume of overhead, many of our institutions have already placed themselves in an illiquid position. Government bonds represent approximately 35% of earning assets, carrying interest coupons which are the equivalent of investment starvation. An approximate additional 10% is invested in obligations collateralized by the full and unconditional guarantee as to principal and interest by the Federal Government. Still another 15% to 20% is invested in more or less illiquid industrial, railroad, or municipal bonds, very few of which will be paid other than by substitution of similar obligations.

In 1933 our own institution paid the approximate sum of $2,000 for a cost survey, which amount was completely recovered in the first 45 days after the installation of the system recommended by the cost accountant. Today, 50% of our institution's annual net income is composed of recoveries for services rendered. This was one of the most profitable expenditures our institution ever made. In order to obtain this amount of income from loans, it would be necessary for us to increase our present note case 33 1/3%, or in lieu thereof, expand our bond investments 200%. Certainly there is not the risk in service charges that there might be in investments in these types of securities, particularly in the volume stated. We have never lost a dollar in service charges, but we lost our shirts in loans. That's why I have so little sympathy with the pressure that is being brought upon us today to supplement our incomes by the acquisition of illiquid long-term capital banking investments.

It is not my intention to bring the subject of average balance into controversial discussion, but merely to state that banks of northern Colorado universally use minimum balance in all account analyses. Minimum balance recovers approximately 25% more than average balance, so the question resolves itself into whether or not your institution wishes to make 75% recoveries or 100% recoveries for services rendered.

The subject of cost analysis as a guide to charges is one that certain men of national reputation and prominence in the field of banking have deemed of sufficient importance to justify a thorough study on their part. The results of their study are set forth in "Commercial Management Booklet No. 23," recently released by the Bank Management Commission of the American Bankers Association. This booklet is commended for your careful consideration.

Let's stop priming that old, worn-out pump of free service, using clear water from the wells of sound investments. For 25 years we primed this pump and have received not so much as a trickle from the spout. Ever since the public turned to the usage of checks and checking accounts as the major portion of our circulating medium, priming of the "free service" pump has consumed 20% of the income derived from our note case and bond portfolio, of the income from our sound investments. We yet have the privilege and opportunity of cleaning our own back yard. Let's get the job done in a respectable manner.

Our newly-elected President, Bob Hanes, recently said to the bankers of his own State at their annual convention:

"The banker who does not know his costs is simply working in the dark. Operating at a profit today offers a very real challenge to management with no promise of improvement in interest rates or bond yields in the near future. Yet there are banks today which have not made any effort to analyze their costs and lack of sufficient courage to ask for adequate compensation from those they serve."

An article in the September issue of Burroughs Clearing House, entitled "New York Sponsors Uniform Analysis," is certainly enlightening concerning the appalling lack of informity in the methods employed to analyze checking accounts by the banks of that State. A hypothetical account was submitted, for analysis, to a group of 16 banks in one of the counties, resulting in a variation from no charge up to $15.00.

The investigations of this committee revealed that bankers in New York State were inclined to agree that service charges should be based on actual costs. However, there was a tendency for the bankers to feel that they could not individually afford the expense of the services of a competent cost analyst, and they realized their own personnel was not competent to arrive at accurate cost figures. To meet this situation it was suggested that these bankers join together in obtaining a consultant for group study and that the result of such survey would establish sufficiently accurate cost data for each institution that the cost analyst would be in position to recommend satisfactory and workable service charge schedules.

It is the unanimous opinion of those who have availed themselves of expert guidance in the matter of cost analysis that the expenditure has been one of the most profitable investments ever made.

This is an inopportune time to pinch pennies. It is the duty of every banker critically to examine his own operations and to base the conduct of his bank's affairs upon an accurate knowledge of costs combined with the most efficient operation.

If we are satisfactorily fulfilling the position of trust occupied as an executive, our time is unquestionably far too valuable in discharging supervisory duties for us to attempt to enter the field of cost analysis. The expense of hiring an expert to peform this service for our institution is, after all, only a small fraction of our bank's annual earnings.

So I repeat, if we have faith in our free and independently-owned banking system, let's demonstrate our ability to stand on our own feet. Let's be independent of Government aid or subsidy through capital stock. Let's fulfill our true function of community service. And let's do that by knowing our costs and making our services pay their way, deriving our income from its proper source, which is service to the public. If we do this in the proper manner and in the proper spirit the public will understand. Then we shall not have to worry about the future of independent chartered banking.

Those of us who stake our time and effort in this enterprise should carry with us the knowledge that we have served our community and our country to the best of our ability.

So I leave you with this motto:

"Let us, then, be what we are, speak what we think, and in all things keep ourselves loyal to truth and the scared profession of friendship."

EDUCATION AND PUBLIC RELATIONS

There were two talks under this head by, respectively, H. R. Smith and S. N. Pickard

Meeting Held at Seattle, Wash., Sept. 27, 1939

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The Front Line—A Goodwill Focal Point

By Harry R. Smith, Assistant Vice-President Bank of America National Trust & Savings Association, San Francisco, Calif., and President American Institute of Banking Section

In introducing Mr. Smith, Chairman Hecht said:

Our first speaker originally came from the East, where he entered the banking business as a messenger. He gravitated to the West, where he entered the employ of what is now the Bank of America National Trust & Savings Association. He is a graduate of the Graduate School of Banking and is President of the American Institute of Banking Section of the American Bankers Association at this time.

The address of Mr. Smith follows:

Mr. Hecht, Ladies and Gentlemen—It is a privilege indeed to stand before you in this session devoted to two very important subjects, closely related, "Education and Public Relations."

Anyone who studies the history of banking in this country cannot help but be impressed by the fact that it is marked by an almost continual series of swings of public confidence in banking. There are periods in which everyone is full of confidence, a period of expansion both in banking and in the number of banks, and public confidence runs high; no one questions the banking structure, the banking practices nor the individual institutions. These periods of time in history are followed by other periods in which confidence seems suddenly to dissolve as quickly as the fogs dissolve in San Francisco, or as quickly as we wish they would. That confidence ssems to disappear overnight and people who the day before were perfectly calm, dispassionate about their consideration of individual banks and the whole banking structure, suddenly become seized with hysteria and lose all confidence in banks. Then, after a period of time in which those experiences seem to face from memory, business picks up again and confidence goes on again.

It seems that in years gone by, at least, bankers appear to have done nothing toward the resotration of confidence following a period of distress except to rely upon America's tremendous capacity to forget its economic lessons. America forgets very easily. That explains why after those periods of distress confidence gradually came back until we had the same story over again.

In the early thirties we had another period in which banking confidence subsided, culminating in the Bank Holiday of 1933 in which banking in this country took time out long enough to adjust some of the effects of the post-war deflation and to adjust the evil effects of an over-liberal policy of bank chartering.

But this time the bankers of this country are convinced that it is not enough to rely for restoration of confidence on the fact that the public has a short memory. We realize now that confidence of that sort is not really confidence at all, but is rather indifference, and the bankers of this country have therefore resolved that this time they shall do something actively, not only to restore confidence but to give it a sound foundation. Therefore we have this program in the American Bankers Association.

In addition to our desire to see confidence founded on a sound basis so it will be permanent and not disappear quickly, there is another reason for engaging in public education and public relations at this time. If you look again at banking history you will observe that all the major pieces of banking legislation have been enacted immediately following periods of great banking distress. They were enacted, therefore, at a time when public confidence in banking was not particularly strong and when, therefore, the bankers who should normally guide banking legislation were on the defensive. Thus it was made more difficult for banking to promote sound and constructive banking legislation. This, then, is another reason why public education in times when confidence is high, so that confidence may be made more sure and more sound, is a forward-looking step.

We stop for a moment and say, "How did it happen that the public obtained such a poor opinion of banking in past periods of distress?" Two things stick out very prominently. The first is this: The public has not understood banking and what we do not understand we tend to distrust, especially when it behaves in a manner which we do not understand.

Our public education program is an endeavor to educate the public concerning banking. The activities of the Association during this past year, in cooperation with the various State Associations and the local chapters of the American Institute of Banking, are a record of a remarkable piece of work, engaged in by thousands throughout the country; literally hundreds of thousands have comprised the audiences who have heard talks on banking and kindred subjects, talks for which the outlines were supplied by the American Bankers Association. This is doing a great work.

Unfortunately, however, we reach but a small fraction of the population, and this is partly due to the fact that the public does not wish to be educated. It is difficult for the public to understand such a complex set of economic phenomena as banking. It is difficult for them to find the time out of their busy lives to be willing to investigate and study. They are too busy, and therefore they resist, not consciously but they nevertheless resist, efforts to educate them in the principles and foundation practices, the legal restrictions which characterize banking. Therefore it seems impossible that we shall ever reach the vast majority of the people with a program purely of public education on the outside of banking. Nevertheless, we should continue our efforts to reach them through the schools, parent-teachers' associations, civic clubs, over the radio, and we should continue to grasp every opportunity that is afforded u to tell the story of banking in language that is clear and plain and which is not technical.

Too often we are apt to explain a banking process in language which itself is as difficult to understand as the process. So we must guard against the use of language which to us is plain but to the layman is not.

If we cannot hope to fully educate the public regarding this very complex and abstract business of banking, what then is our hope of building confidence in banking? Can we build confidence in something which the public does not understand? If we can achieve that, we have achieved our end. Can we give the public confidence in bankers even though they do not understand banking? Just which psychological factors determine confidence or lack of confidence is something which is exceedingly difficult to understand. If we examine some of our reactions to people, individuals, services, functions, organizations, and say "We have confidence in this particular individual," why is it? You have confidence in a great many people who do things for you which you do not understand.

I well recall an incident a number of years ago when my brother and I were driving in his car from Bakersfield to Los Angeles over what was then called the Ridge Road, a particularly long, arduous stretch of road. Suddenly, and to our dismay, his car began to falter. Fortunately for us we were not far from the garage. We stopped there and explained as best we could the situation to the grease mechanic. He lifted up the hood and sort of looked around inside, scratched his head, looked around for a screw driver and a wrench, and so on. He puttered around there for 15 or 20 minutes, and he "allowed as how he'd fixed it," and sure enough the car started up again. But we handn't gone very many miles before it began to falter, and we realized the man hadn't known anything about it. We stopped at another garage. He was about the same as the first. He didn't seem to know his business. We had no confidence in him.

Later we got to the third garage, and this was quite different in appearance. The mechanic was quite businesslike and asked us all about the symptoms of the car. He proceeded to check over the motor with apparatus which was very impressive to us at least. Then he checked off, one by one, the various possibilities, and finally, by a process of elimination, determined what it was that had caused the car to fail, and in very short order he fixed it.

The way he went at that business inspired us with confidence. Neither my brother nor I knew anything about the intricacies of automobiles, motors, machines, ignition. We didn't understand garage mechanics or garage machinery, but we had confidence in that mechanic because he gave us convincing evidence that he knew his business. We had confidence in him, in the man, even though we didn't understand the business.

Take another example. I am thinking now of two insurance agents in San Francisco, one who used to write my insurance and one who now does. The first was an ordertaker. If I asked him for a certain type of insurance, I got it, but that was all. This other agent is quite different. He has made quite a study of what he thinks I need, and, surprisingly enough, I pay less for my insurance now and get more coverage than I did before. In fact, he has given me sufficient evidence that he knows this business so that I am willing to entrust my insurance affairs to him now practically without question at all. I have confidence in him because I feel he knows his business.

If that is the type of impression which will create confidence, that seems like a pretty safe course for us to follow. If we can give the impression, and the correct impression, we can convince the public that we know our business, then the public will have confidence in us even though it may not understand our business.

At what points do we contact the public? How can we impress them, convince them, that we know our business? It is not enough for the executive officers of the banks to say, "I know my business, and therefore whenever the customer contacts me he is inspired with confidence because I talk with him intelligently, I explain things adequately, and he goes away feeling that I know my business." The real point of contact for many of your customers is not your own desk but the desks of your junior officers, your note clerks, head of the collection department, your commercial tellers, and it goes beyond that, too, to the bookkeepers, your messengers, and your telephone operator. As they have contact with the public either in the bank or outside the bank, the public is gradually but very definitely forming its opinion of your bank. Therefore, it is not enough that your President and the Chairman of your Board and your Executive Vice-Present and Cashier know their business. It is essential also that the man or the woman on the front line knows his or her business also.

Consider the frequency of contact. Take one of these instalment loans —the borrower meets the loaning officer once and he meets the note clerk 52 times—that is, he is supposed to. Fifty-two times as compared to one contact! It is essential therefore that our note teller know his business.

It won't surprise you at all if at this juncture I mention that the Association, through its Educational Section, the American Institute of Banking, is equipped to educate the young men, the young women, if you please the older men and the older women on your front line, and your front line extends from your officers down through the most humble of your employees. The Institute is equipped to provide for each one in your front line the basic training and education so that he or she will actually know the business to be performed and will give that impression in contacts with the customers. Does your front line work like automatons? Do they work mechanically or do they have a grasp of the significance of the things they are doing? How can we best assure that they know their business?

We in the Institute are very proud indeed of the growth of this Educational Section. It is now 40 years old. It has grown up considerably. In the last 10 years, under the guidance of our Educational Director, Dr. Harold Stonier, it has made perhaps its most startling progress. It is no longer really a training school for juniors. The Institute has become the Educational Section of the Association in fact as well as in name, and its program, now including 20 formalized courses leading to pre-standard, standard and graduate certificates, is wide enough to include subject matter of interest to every one in banking.

We are proud of the fact that there are at present 65,000 members, or more, of the Institute throughout the United States; that of this number—last year at least—40,000 were students, and that 25,000 have earned standard certificates. So I repeat we are proud of the 65,000 who are active in the Institute. But we are alarmed at the fact that there is another 170,000 bank officers and employees in this country who are not yet touched by the Institute program—170,000! Many of those are situated right in cities which are now served by our Chapters of the Institute. Many of them are situated in areas which are not now served by the Institute.

Would it be out of place if I were to suggest here that when you return to your own institution you inquire which among your employees and junior officers have taken sufficient interest in the business in which they earn their living and look for their future to improve themselves by pursuing the educational work of the Institute and which have not?

Would it be suggesting too much that you discuss with your personnel officer the wisdom of including as a part of his personnel and trainnig policy the participation of your staff in the educational work of the Institute, to the end that they might know their business better?

In addition to the formal educational work of the Institute, there is another type of educational experience which is not in the curriculum, which is not in the catalog. I refer to that experience which comes to young men and young women who participate in the administration of the local institute units, the Chapters and the study groups. The experience which these young men and women derive by that activity is something which oftentimes is of as much value and sometimes greater value than that which they may derive from their actual study courses.

Those of us who are active in the administration of the Institute naturally would suggest that upon your return home you investigate or become reacquainted with the type of administration in your local Chapter and encourage the junior officers of your own institutions to become active in this phase of the work, not only because of the benefit which will come to them, but because their participation and your continued interest will assure that each of our local Institute units will be held up to the same high standards for which the Institute has always stood.

It is not enough that our front line know banking. It is also essential that our front line know its own bank. Here again the American Bankers Association has taken a very progressive step in its program of constructive customer relations.

The family gathering within the bank, where officer and employee can sit down and discuss their common problems, their common aims, their common ambitions, can be a potent factor in developing an excellent morale within the bank, and also enable them to know their own bank in a way which will enable them to interpret it to their own customers. The Association does not propose that you discuss the details of every banking matter with every one of the staff, but there are undoubtedly a great many questions, a great many matters related to the history, the policies and the experiences of the bank which to the officers are common knowledge, but which the staff frequently has little opportunity to become acquainted with, unless it is by some such means as the constructive customer relations meeting suggested by the Association.

We have then these two things by which we can utilize the front line: the contact people of your bank as a potent factor in developing good will for your own bank, and the proper public attitude toward all banking.

If we will utilize the American Institute of Banking and The Graduate School of Banking as a means of training our staff so that they will know banking, and if we will utilize the family gathering within the bank under the program of constructive customer relations, so that the front line will know its own bank, then the public in its contacts with your front line will come away saying, "I have confidence in banking and in that bank because they know their business.'

Our Experience with Public Meetings

By S. N. Pickard, President The National Manufacturers Bank, Neenah, Wis.

It would be a great pleasure to me if I could claim that the idea of holding public meetings for bank customers originated in Wisconsin but, as you all know, the A. B. A. blazed the trail for such functions during the administration of Orval Adams, who conceived the plan and enthusiastically promoted and developed it in several of the principal cities of the country. It is interesting to note that the idea was continued by President Phil Benson with equal success this year.

The great record established by the A. B. A. in these efforts inspired us to try the experiment in Wisconsin with results which have been most gratifying to both the bankers and many thousands of citizens of our State.

In the few minutes allotted to me, I propose to relate to you our experiences in handling a total of nine such meetings in as many Wisconsin cities within the past year. I would like to tell you something about the objectives and the plans of these public meetings and then mention briefly some of the reactions and benefits we believe we derived from them.

Would it not be desirable and worthwhile for the customers of your bank and the other citizens of your community to know the undeniable facts as to the ultimate result of uncontrolled Government spending and what it means to the individual citizens as compared with a National budget that is at least approaching a balance; to know the effect on all people, and particularly those of modest means, of what is commonly known as a planned economy, wherein a centralized authority is able to exercise control over money and monetary policy to such an extent that free enterprise is strangled and the rights of the individual are almost entirely lost; to know the truth about interest rates; what causes them to be low and the effect of so-called cheap money on general business, employment and the savings of our people; to know the real story of heroic service rendered by the banks of America to its people in times of both war and peace, during depressions as well as prosperity periods; to know the actual record of the Nation's banks in meeting the credit needs of business, both large and small, and including farmers, working men, and all people having a legitimate need?

Upon reflection I believe you will conclude, as we did in Wisconsin, that it is highly important that these basic principles and facts be told our people in an open, public meeting. As a matter of fact, is any group better qualified to present these matters than bankers—who should be, and in the majority of cases are, the real leaders in their respective communities? If this be so, the customers of banks, as well as our citizens in general, naturally look to this leadership for direction and guidance in the problems of modern day finance and economics.

In my remarks up to this point, I have attempted to show you the reasoning back of our approach to this project, which we were soon to discover was a most outstanding and fascinating piece of public relations work.

In the introduction of the public meeting idea in Wisconsin a year ago this month we concluded to start by using our groups as the unit around which to build the sponsorship, and the annual meetings of these sectional groups as the occasion. Appleton, LaCrosse, Marshfield, Madison, and Waukesha were the five cities selected, four of which being college and and university towns made it easier to obtain large auditoriums and good sized audiences interested in the program and entertainment to be offered.

Two very important factors entered into our consideration of this venture from the outset. In order to achieve our objectives we had to have a speaker well qualified to put our story across to people of all ages and in all walks of life. At the same time we recognized the necessity of engaging entertainment for the program that would have sufficient popular appeal and drawing power to bring out a large and representative crowd. The combination of John Carter, young radio star and tenor of the Metropolitan Opera Association of New York and our own William A. Irwin, Associate Educational Director of the A. I. B., was a happy one and they both clicked 100% on each appearance.

As President of the Wisconsin Bankers Association at the time, I visited each of the five key cities to sell group officers and local bankers on the possibilities. There followed a rapid succession of advertising and publicity plans of the association's public relations department. Special news stories were prepared for Wisconsin newspapers and banking publications. Attractive printed folders, local newspaper advertisements, special advertisements in banking publications circulating in Wisconsin, lobby posters and tickets for banker delegates, customers and public were prepared—all localized for the benefit of the five host cities. In the meantime, Association group officers and local banker committees worked conscientiously to complete local arrangements. About 10,000 people in the five cities previously mentioned heard Mr. Carter and Mr. Irwin. The meetings were planned to move along with dispatch in special consideration of those who found it necessary to stand through the entire program after all available seats were taken. In some of the key cities more people could have been reached if larger auditoriums had been available. In Madison, for example, the University Stock Pavilion seating 3,600 was filled to capacity, with over 500 on the outside of the building and in nearby automobiles listening to the program over a public address system. Some of our bankers who may have been a bit skeptical when the plan was outlined were pleased with the public response.

After the first five meetings to which I have referred had been completed, there was an immediate demand for a similar function to be held at our State convention in Milwaukee in June. In response to this appeal we staged a public meeting at the Municipal Auditorium in Milwaukee on the evening preceding the opening of the annual convention of the Wisconsin Bankers Association. Conflicting dates of the artist and speaker who starred on our fall series kept them from appearing at the June meeting but we had excellent talent in their place. The 2,000 people who came out on a very hot night were enthusiastic in their praise of the program but the size of the audience was below our expectations and looked smaller because of the 7,000 seating capacity of the Milwaukee Auditorium. Let me tell you quickly where the mistake was made. Some of the larger banks in Milwaukee were concerned that if a big name artist was engaged to draw a crowd they would be embarrassed in the tremendous rush for tickets they would have from their large numbers of customers. Consequently, we deferred to their judgment but we found that it is a mistake to expect a large audience in a metropolitan city with its many competing attractions without a "drawing card" entertainment feature.

If we had followed our original idea and engaged one of America's outstanding artists we would have had an audience of 7,000 no matter what kind of weather prevailed. I pass this experience along to you to show some of the pitfalls and to give you the benefit of it in the event any of you decide to hold public meetings. However, we were not discouraged with the results, but we resolved not to make the same error again.

Just three weeks ago we had three more public meetings such as we sponsored last year. These were held at Janesville, Stevens Point and Eau Claire, respectively. We were fortunate to again have John Carter and Willaim A. Irwin, who teamed up in their inimitable fashion to entertain and inspire 4,000 more of our Wisconsin bank customers. These meetings were every bit as successful as those of last year and our new State President has every reason to be gratified with the showing made. I will not discuss this year's meetings further because the preparations for them and all other details were carried out in the same manner as a year ago.

The banks in the sponsoring city must be completely sold on the plan in advance, and committed to giving it their wholehearted support. No definite start on the project should be made until an enthusiastic local interest is shown.

So far as holding a public meeting in a large city is concerned, it is absolutely necessary to engage a top grade artist or some other attraction that will not detract from the dignity of the occasion and yet will have that all important quality of drawing power.

Inasmuch as tickets are given out by the banks in the city where the meeting is held, it is highly important that all officers and employees be thoroughly sold on the idea and not just pass out the tickets as though they were peddling hand bills. In other words, the psychology of the affair is to make each person receiving a ticket feel that he is fortunate to have one and that there is a large demand for them, as there actually should be, if the program has been arranged properly.

Do not hesitate to give out tickets in the proportion of about twice the capacity of the auditorium to be used. Many holders of tickets will be unable to come, and even if some people are turned away, it is better than to have empty seats. A house jammed to the rafters is always the very best background for a meeting of this type. It inspires the speaker and entertainer and it is much more thrilling and exciting to be in an audience that is large and enthusiastic.

With the exception of very brief introductory remarks, the program should definitely be confined to the appearance of the artist who is to entertain and the speaker who brings the message the bankers want to put accross to the citizens of the community who have assembled. The maximum time of the affair should not exceed one and a half hours, thus sending everyone home wishing it had been longer, rather than to have them weary and tired from too many long and boring speeches.

It is well to tie up a public meeting with an annual gathering of bankers —whether it be a State association, sectional organization, county association or local clearing house group, for the reason that it gives official color and sponsorship to the affair which strengthens the background for the event very substantially. In this way an invitation can be extended to customers of the local banks in the city where the meeting is being held to attend an "open" session of the convention. Thus, instead of giving impression of disseminating propaganda, it very definitely leaves the thought with the bank customers that they are being favored with an invitation to hear the inside story of how banks function.

Some very interesting reactions have come out of our public meetings which have convinced us of their value.

First, many of our bankers were amazed to learn that the public is really very receptive and sympathetic on the average to the problem of the banker after being given an opportunity to understand them.

Second, another result that had not been anticipated to any extent in the preliminary plans was the almost miraculous effect it had on the bankers themselves. They came to the meeting, saw, and heard hundreds of their customers and friends applaud the program and tell them afterwards what a splendid contribution the bankers had made towards the education of the community on the importance and value of banking in everyday life.

Third, we found a surprising degree of interest in the meetings on the part of students and young people. Each audience included a good percentage of boys and girls who appeared eager to learn more about banking and its problems, as well as to try to get the economic importance. This, we considered one of the happiest results of our efforts in sponsoring these meetings. If we can put out story across to young people our future is certainly secure.

Here are some comments from a survey of public opinion made by the Wisconsin Bankers Association. A school teacher said, "I learned more at this meeting about the problems bankers face than I would in a month of study." A housewife commented, "Our young people should hear this address by Mr. Irwin." Another said, "One of the finest things the bankers have done to acquaint people with the problems of banking."

The Wisconsin press, seeing news in the event, spread the message to thousands of Wisconsin newspaper readers. In Marshfield, where the second of the first series of meetings was held at the Purdy High School Auditorium, the "News-Herald" said editorially:

"Marshfield and the surrounding area are indebted to the bankers of Group 6, Wisconsin Bankers Association, who opened their meeting to the public Tuesday night. An audience of approximately 1,200 persons thoroughly enjoyed the songs of John Carter, brilliant young Metropolitan Opera tenor, and the address, 'The American Way,' by William A. Irwin of the American Bankers Association. The response from both singer and speaker should delight the hearts of the bankers who arranged the meeting. Both scored heavily with the audience. Speeches usually are dry, but not when homely truths are pointed out in a commonplace and understandable way. Marshfield will be glad to play host to similar bank meetings at any time we are given the opportunity."

When this same newspaper heard of our public meetings scheduled three weeks ago it said on its editorial page:

"The program given here last year was outstanding. Mr. Carter has an unusually pleasing personality and one of the finest voices to opera today. Irwin's speech enthralled the big audience which heard him. All we can say is that we regret Marshfield could not be chosen for this year's meeting but perhaps we should be thankful for past favors."

The nine public meetings sponsored by the Wisconsin Bankers Association thus far have made a favorable contact with 16,000 to 17,000 Wisconsin citizens. The constructive newspaper publicity resulting from these meetings carried the message of the speaker to many additional thousands who have had some banking and economic truths brought home to them in simple language. These meetings have shown a willingness on the part of bankers to discuss problems of mutual interest which has won for them public support and understanding.

We believe there is a need for public meetings to be held in smaller cities, possibly sponsored by local clearing houses or county bankers associations. Such meetings would naturally be conducted on a somewhat smaller scale, but if high-grade musical and speaking talent were furnished, they could be most effective in carrying our message out into the highways and byways. We hope to develop this idea further in Wisconsin.

Public meetings help to overcome the notion long held that bankers are distant and aloof. Meeting in public with your customers and friends to enjoy the music of a fine artist and to absorb the ideas of an outstanding educator creates a kindly feeling towards banking in general and your bank in particular. At these public gatherings the public learns that the interest of the banker and the community are the same and that not all the criticisms leveled at banks and bankers are true. The public learns the a, b, c, of banking and gains a new impression of the value of banking service. Public meetings create an atmosphere conducive to a discussion of mutual problems and a regard for the value of community banking institutions and the part they play in our American way of living.

Before closing, may I say that I do not claim that the public meeting idea solves all our public relations problems. There are many other mediums for work in this field which are both effective and necessary. In Wisconsin we have been endeavoring for the past several years to follow, under the leadership of a full time director of public relations, and our State secretary, a well rounded program with which to develop a better and more constructive relationship with our bank customers and the general public. This includes the preparation of conference material for use by bank staffs throughout the State who are in their third year of activity along this line; our new motion picture, "Your Money and Mine," which is being shown to thousands of our citizens throughout Wisconsin; a speakers' bureau organized to send our bankers to fill speaking engagements before civic clubs and meetings of various other types of organizations and close cooperation with with the press through preparation of news releases and special articles on banking subjects of interest to newspaper and magazine readers. Our program includes informative advertisements and other services too numerous to mention. So you can see that public meetings are just one part of what we need to do in this vital and important field of public relations but these public meetings proved in our case to be a fascinating and thrilling experience and inasmuch as they brought direct and worthwhile results, I am pleased to have had an opportunity to speak to you about them.

I have brought with me pictures of our public meetings to show to anyone who may be interested and they will be available for examination at the Public Relations Booth in Parlor D until Thursday night.

In conclusion, I would remind you that much has been made of the claim that the bankers of America cannot agree on the basic principles of their own business and thus cannot qualify as counsellors and leaders in the affairs of the Nation. I believe this is a statement which is entirely unjustified because the bankers of America can and do agree on many fundamental aspects of our economy which should provide a common meeting ground. However, we cannot sit by and think these things in a self-satisfied manner but we must do something about them. In other words, there must be action immediately and of the most virile type.

Do you know that the American people are again turning and looking to their bankers for counsel and leadership in the Nation's affairs? We need to be seen and heard in public: we need to be aggressive and the senior executives of our large banks must be willing to appear in person on occasions where banking problems are being discussed and allow themselves to be quoted on important subjects of the day in order to help win back for the banking profession the leadership it once enjoyed. This applied to the presidents and executives of smaller banks, too, but our large city friends must lead the way.

Fortunately an excellent example has been set for us by our own A. B. A. leaders and a certain few of the metropolitan bankers, but the field is wide open for action by thousands of bankers who have given no thought to public relations effort, to say nothing of doing any real work.

War is horrible, terrifying and useless in the judgment of most of us. However, with all its evils, perhaps we can say that the present situation offers the banking profession an opportunity to unite its forces for service to our country and our people whether we ultimately become involved in the war or are able to maintain our neutrality, and God knows we all hope and pray it will be the latter.

It seems to me that we need a little of the patriotic spirit that comes with a time like the present so that we can close our ranks and move ahead to a better and more complete understanding of banking both on our own part as well as by the splendid people of this great country.

As I close, I therefore call upon you, the bankers of America, the finest men I know, to fall in line and *Forward March* ! !

Remarks of Rudolf S. Hecht, Chairman, Public Education Commission—Comment on Congress on Education for Democracy

Chairman Hecht: *Ladies and Gentlemen*—If you will please come to order, we will start this meeting on Education and Public Relations which for the past several years has made up an interesting and worth-while part of the convention program of these several sessions.

The building up of public good will toward banking is, of course, the main object of your Education and Public Relations Committees, and you will hear from several excellent speakers tonight who will tell you both of past performance in that respect and take you far into the future, telling you what is ahead of us in the banking world.

Dr. Stonier has asked me, however, to take just a moment to tell you something of a somewhat different development in our educational work which we experienced recently and which I was particuarly asked to look after in attending in New York last month the Congress on Education for Democracy.

Dr. Stonier has for some years done some vary remarkable work with the teachers of this country, and particularly with Teachers' College in New York.

This Congress on Education for Democracy was held under the auspices of Teachers' College of Columbia University. It was a world-wide congress, attended by very eminent people, including Earl Baldwin of London, who came over especially to deliver an address, and it was one of the finest addresses it has ever been my privilege to listen to.

The purpose of this Congress on Education for Democracy was to bring together laymen and educators representative of all phases of American life to discuss the question, "What is the responsibility of education for the defense and advance of democracy?" The Congress was held just exactly two weeks before the war clouds in Europe finally broke, and it was a most unusual experience to sit down with these people, representing all phases of American life, and also there was the international atmosphere which the important representatives from England, France, and some of the other democracies brought, including one which has since disappeared temporarily at least, Poland. One of the main speakers of this Congress was a very eminent Polish official.

In any event, it was a new experience for us, and we felt that the American Bankers Association and the individuals representing your Association at that Congress got a great deal out of it, and we believe the closer contacts which have been developed in this manner with Teachers' College will be of great benefit to us in the future.

As I said at the outset, it is not my purpose as Chairman of this meeting to take your time, because we have a very excellent program ahead of us. In considering this subject of "Education and Public Relations," it is but fitting that we should begin this program with a representative of our Educational Section, the American Institute of Banking.