January 1980

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Since You Asked

A fringe benefit of working at a Federal Reserve Bank is the frequent invitation to speak before various groups. And speeches inevitably generate questions. This is a brief response to the question asked most frequently following speeches during the past month.

Question: Are changes in the velocity of circulation of money affecting inflation?
Answer: They probably are, since their effects may not be completely offset by monetary policy.

We don't have a direct measure of the velocity of money, that is, the frequency with which money changes hands. Mostly, velocity is inferred from estimates of the total value of production and the amount of money. For example, last year the gross national product (GNP) probably totaled about $2,360 billion. Money averaged about $370 billion. Hence, there was about $6.38 of goods and services for each dollar of money. By this measure, therefore, it is said money had a velocity of 6.38.

Clearly, the actual velocity of money is much greater. Money is exchanged with each change in ownership of existing assets, not just for purchases of goods and services recently produced (GNP). For example, money changes hands in transfers of existing property—such as buildings, land, stocks, bonds, and the like—and when people move funds from one account to another in the same bank or different banks.

Another indicator of changes in velocity may be inferred from activity in checking accounts. About three-fourths of money is held in the form of demand deposits at banks; about one-fourth is currency and coin. We know virtually nothing about velocity of currency and coin. But we have data on the activity in checking accounts. In September 1979, bank customers drew on their checking accounts at an estimated annual rate of $54,233 billion. Checking account balances averaged $310 billion. Hence, demand deposit moneys had an annual velocity (turnover rate) of 175.

Whether one looks at the ratio of GNP to money or the demand deposit turnover rate, it is clear that velocity has been rising. In 1979 the ratio of GNP to money was about 6 percent higher than in 1978 and 41 percent higher than it was 10 years before. And the turnover rate of demand deposits increased about 24 percent during the past 12 months. Moreover, both of these measures vary substantially also in the short run, for reasons that are not well understood.

The longer-term rise in velocity is more explainable, however. There have been, of course, financial innovations that have made the payments mechanism more efficient; thus, a given volume of expenditures is made from lower average cash holdings today than in prior years. But, in part, the rise in velocity also results from inflation. With high levels of inflation and interest rates,
individuals and businesses give more attention to minimizing cash balances so as to maximize funds placed in interest-bearing accounts or securities.

But the relationship also runs the other way; that is, a rise in the rate of increase in velocity can contribute to inflation. Clearly, if the rate of growth of velocity picks up, the rate of growth of the money stock must be slowed or inflation will ensue. Rising deposit velocity indicates fewer deposit dollars are needed to accommodate the financial transactions associated with the production of goods and services at existing prices. So, the “excess” dollars must be offset through reduced money increases if inflationary pressures are to be avoided.

A number of years ago, it was widely believed that velocity had reached a post-World War II peak and that larger annual additions to money would be required to assure full employment and continued economic growth. However, the reverse turned out to be true: velocity has continued to increase, and no near-term ceiling on velocity is now foreseen.

—Ernest T. Baughman
President, Federal Reserve Bank of Dallas

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**New member bank**

Forestwood National Bank of Dallas, Dallas, Texas, a newly organized institution located in the territory served by the Head Office of the Federal Reserve Bank of Dallas, opened for business January 2, 1980, as a member of the Federal Reserve System. The new member bank opened with capital of $1,000,000 and surplus of $1,000,000. The officers are: Tom Jaeb, Chairman of the Board and President; Steve Melton, Executive Vice President and Cashier; and Sherell Bishop, Vice President.
Three amendments to Regulation Q have recently been adopted by the Board of Governors of the Federal Reserve System. The purpose of these amendments is to encourage the small saver and the flow of credit into residential mortgages. The changes authorize a new 2 1/2-year time deposit with no prescribed minimum size and with a ceiling rate linked to the average 2 1/2-year yield on U.S. Treasury securities. The ceiling rate for the time deposit will vary from month to month, but once a particular time deposit is purchased, the rate being paid on it will be fixed for the full maturity. To encourage the small saver, there is no federally required minimum denomination for the new deposit category, but the deposit must be issued in a nonnegotiable form. Interest on such deposits may be compounded and computed by member banks in accordance with any of the methods authorized by Regulation Q. Effective January 1, the new time deposit replaces the four-year or more time deposit with a ceiling rate tied to the average yield on four-year Treasury securities. However, individuals that have outstanding deposits of this type will not be affected by this action.

The second amendment to Regulation Q increases the maximum rate of interest payable by member banks on time deposits with maturities of 90 days or more but less than one year. The interest rate was increased from 5 1/2 percent to 5 3/4 percent, and the change will affect certificates of deposit entered into or renewed on or after January 1, 1980.

The third amendment allows banks with IRA/Keogh Plan and governmental unit depositors to be more competitive with savings and loan associations and mutual savings banks. For these depositors, the amendment allows member banks to use the same ceiling rate that the thrift institutions use on 26-week money market certificates and the new 2 1/2-year certificate.
Petroleum Spot Market Plays Key Role in Pricing and Distribution

By Edward L. McClelland

Prices of crude oil and petroleum products doubled on the spot market last year following the disruption of crude oil production in Iran. Although price increases of such magnitude are uncommon, the spot market is known for its volatility. Relatively small changes in the quantity of products supplied or demanded result in sudden, sharp price movements.

The spot market provides the means for efficient allocation of product on the outer edge of the petroleum market. Its primary function is to balance surpluses and deficits that arise continuously in the production, processing, and distribution of products in the highly diversified petroleum market. But with supply restricted so that demand presses relentlessly upon available supply, rising spot market prices have become a key factor boosting contract prices, under which most crude oil moves to refiners. The Organization of Petroleum Exporting Countries (OPEC) has rationalized large price increases on the indicated willingness of importing nations to satisfy marginal demands at spot prices that are far above contracted prices. That pricing strategy holds little promise for a quick end to increases in petroleum prices without sharp cutbacks in demand, increases in domestic oil production, or development of economical alternative sources of energy.

Characteristics of the spot market...

The term market has many connotations. The American Marketing Association defines market in two ways. First, it is "the aggregate of forces or conditions within which buyers and sellers make decisions that result in the transfer of goods and services." Second, it is "the aggregate demand of the potential buyers of a commodity or service." Some other definitions are:

"A market is a distinct group of people and/or organizations that have resources which they want to exchange, or might conceivably exchange, for distinct benefits."

"A market is a group of buyers and sellers within a geographical area: (a) for a product or reasonable substitutes; (b) at a particular stage in the trade channel, such as manufacturers selling to retailers, or consumers buying from retailers; and (c) at a particular time."

The American Marketing Association's first definition best describes the spot, or cash, market for crude oil and petroleum products because it is not possible to delineate precisely who trades in the market and when or where trades take place. The spot market has no formal "structure," "rules" of operation, or central "place" of business. It is a "process"—an ongoing flow of communication between sellers, buyers, brokers, and traders operating in many locations on the fringe of the petroleum industry. Before the 1973 Arab oil embargo, the spot market was the dumping ground for excess supplies that could not be sold by contract through integrated marketing channels. Spot transactions accounted for no more than 5 percent of all sales and were consummated at salvage prices.

Since 1973 the spot market has changed dramatically. With world supplies of petroleum products lagging demand, spot prices have risen far above contract prices and, during the past year in particular, have heavily influenced contract prices. Estimates now suggest that spot transactions account for as much as 20 to 30 percent of all OPEC crude oil sales, although there is no solid evidence to indicate how much product is actually traded in the market.

Several hundred companies participate in the spot market, although only about 15 are considered major traders. The role of individual firms in the market can change readily from seller, buyer, or broker, depending on the position they want to take. However, sellers typically are crude oil producers, refiners, and other holders of undedicated stocks of unregulated crude oil and refined products. Buyers include refiners that require supplemental crude supplies and such petroleum product users as jobbers, distributors, and large industrial users. Brokers bring buyers and sellers together, while traders—who often act as brokers—deal for their own account. During periods of tight supply and sharp run-ups in price, such as oc-
curred last year, speculators are drawn to the market.

Major oil companies and many lesser firms buy and sell in the spot market to balance inventory positions. In addition, private trading companies—such as Coastal States Petroleum, Vitol Trading, Philipp Brothers, Tampinex Oil International, and Marc Rich and Company—are some of the large firms that account for much spot market activity.

Secrecy is a major characteristic of the market. Information is extremely valuable and, hence, is closely held. Participants are reluctant to discuss market conditions—product availability, who is buying, who is selling, and so on—for fear of jeopardizing transactions. If, for example, a buyer gets a hint as to a trader's source of available product, he could attempt to deal directly with the seller or otherwise undercut a competitor's position.

There is a significant barrier to entry that newcomers must overcome in order to gain the high degree of financial and performance credibility needed to deal with established buyers and sellers. While it is said that all one needs to begin is a telephone, it takes considerable time and effort to break into the inner circles of the market where trades actually take place. Participants have to have credibility because most transactions are consummated on a trader's word. Buyers demand prompt delivery, while sellers require assurance of prompt payment. Spot transactions are paid with cash, letters of credit, or bankers acceptances in the case of international trades. And sometimes payment is required in advance of delivery.

Several sources report on conditions in the spot market. One widely read publication is Platt's OILGRAM Price Report, an international daily oil and gas price and marketing letter published by McGraw-Hill. Platt's also offers a number of other periodicals, books, and services on spot market conditions, including Telex reports during the business day. Oil Daily, an oil industry newspaper, reports daily spot market quotations for petroleum products in U.S. markets. Foreign sources of information are also available. For example, Petroleum Argus publishes information from a European perspective.

Spot market reports fall short of the market information reported on the stock market and many other commodity markets. For example, the quantity of product exchanged is rarely revealed by buyers and sellers and is, therefore, normally not available to reporters. Moreover, spot prices are reported as representative quotations and offerings, obtained from market sources that are deemed reliable, and are not necessarily transactions prices. Price quotations for a given product in a given market do not change until sufficient evidence becomes available to indicate price changes have occurred.

Because of the volatile nature of the spot market, business does not rely heavily on published prices as being representative of actual buying and selling prices. But similar situations exist in other markets. For example, yesterday's spot prices may not be indicative of today's prices, and buyers and sellers must negotiate their own transactions as existing market conditions dictate.

The spot market has no geographic boundaries as transactions can span the globe. However, Rotterdam, the U.S. Gulf Coast, New York Harbor, and various pipeline and waterborne terminals scattered around the United States are recognized trading centers in the spot market. But transactions extend beyond those locations and overlap. For example, the Rotterdam market involves not only trades of refined products sold in Europe but also worldwide transactions in crude oil located as far away as the Far East, the Persian Gulf, or the United States. Even trades in the Gulf Coast or New York Harbor markets can engage buyers and sellers located elsewhere in this country or overseas.

Nearly half of all U.S. refinery capacity is located on the Gulf Coast. Most domestic crude oil production is processed there, and fully two-fifths of all foreign crude imports are landed in the region. As a result, it is a net buyer of crude oil and a net seller of refinery output since only about a quarter of all U.S. petroleum products are consumed in the region.

New York Harbor and the East Coast are major net consumers of petroleum products, together accounting for two-fifths of total U.S. consumption and only a tenth of total refinery capacity. Most of that region's needs are supplied by Gulf Coast refineries, but almost 25 percent of all foreign crude oil imports and about 85 percent of all foreign imports of petroleum products are landed at ports on the eastern seaboard.

Another major U.S. market is the West Coast. It accounts for a tenth of total domestic consumption of petroleum products and obtains more than...
OPEC Pricing

The OPEC cartel, with huge crude oil reserves and low production costs, can seemingly increase its total oil revenue at will by raising crude prices. The success of OPEC (the Organization of Petroleum Exporting Countries) in raising oil prices has a theoretical basis.

The demand schedule for crude oil slopes downward to the right; that is, more oil can be sold at lower prices than at higher prices, all other things being the same. But as prices decline and sales expand, total revenue increases to a maximum and declines thereafter.

The price that maximizes total revenue is unknown because the demand schedule for crude oil is not known with a high degree of certainty. Therefore, OPEC is currently "testing" the market, by increasing prices and threatening to cut back production, to determine the price and quantity of output that will maximize total revenue.

If the price of OPEC oil is currently in the inelastic portion of the demand curve, price increases will not result in much of a reduction in the quantity of oil sold, and total revenue will rise. Such is the case when the price of oil is raised from \( P_1 \) to \( P_2 \), resulting in a fall in oil sold from \( Q_1 \) to \( Q_2 \) yet an increase in total revenue from \( TR_1 \) to \( TR_2 \). If the price of OPEC oil is in the elastic portion of the demand curve, the rise in price will be more than offset by a drop in oil sold, and total revenue will fall. Most analysts think the demand for oil is fairly inelastic in the short run but becomes more elastic with the passage of time as people conserve oil and use substitutes in response to higher oil prices.
enough crude oil locally and from Indonesia and Alaska to satisfy refinery and user demands. Moreover, that area is far enough removed from the central and eastern distribution systems that few shipments of petroleum products move across the Rocky Mountains.

... and why it operates

There are two sides to the spot market. Imbalances in supply and demand create the need for a spot market. A surplus of crude oil production over contractual obligations makes the product available for cash sales, while disruptions in production and transportation increase demands for crude oil on an interim basis.

Sharp differences in the number and types of plants in the refinery industry create surpluses and deficits of refined products. There are nearly 300 refineries in the United States, ranging in capacity from 1,000 barrels a day to more than 500,000 barrels a day. Each is geared to process crude oil into predetermined numbers and grades of products, with greater economies of scale, manufacture more products than small refineries. All told, the industry makes more than 2,300 specific products. However, nearly half of all refinery output is gasoline, about a quarter is middle distillates, and a tenth is residual oils. It is these products and crude oil that make up almost all spot market transactions.

Imbalances in supply and demand create the need for a spot market.

Matching refinery output to market demands, however, is a difficult task. Imbalances are created because refinery runs generally do not match the quantity of product under contract. Surplus output is inventoried or sold outright, while deficits are made up from inventories or by spot purchases. Also, mechanical breakdowns and fires disrupt refinery runs, and affected refiners may have to arrange immediate purchases or trades to make up the deficit supply positions.

Refining yields joint products, that is, more than one commodity from a single raw material. For example, the manufacture of gasoline also yields quantities of middle distillates and residual oils. Therefore, while the quantity of gasoline produced may satisfy demand, quantity imbalances often are created for other products. That problem is compounded by differences in product quality stemming from differences in feedstock characteristics and refinery operations. An increase in refinery runs to obtain one product results in additional output of other products, and all have to be sold or incur inventory carrying costs until more favorable market conditions arise.

Geographic mismatches in quantities of products supplied and demanded give rise to spot market transactions. For example, firms selling in a large region might find it unprofitable to transport their own refined output to distant outlets, and building additional refinery capacity might be too expensive. In these circumstances, a firm may minimize costs by closing distant outlets or by supplying them with purchases from the spot market.

Regulation of prices in a market as far flung and loosely organized as the spot market for petroleum products—one dealing in such a variety of products—is a herculean task. It is not surprising, therefore, that accusations of profiteering, supply manipulation, and "daisy-chain" conspiracies have surfaced during periods of tight supply. Traders suggest that the patchwork of government regulations that has evolved since August 1973 has helped create a segmented market where deals are made by moving a product from one market category to another. Some moves are legal while others are not, depending on judicial interpretation.

Government regulations categorize crude oil supplies as regulated and unregulated. Gasoline and propane are the only refined products whose prices are regulated. In addition, consumers are divided into classes of trade. Differentiation of prices provides opportunity to "free up" for sale at unregulated prices a product whose price is regulated, and if "new" classes of trade are established, sales are not geared to a prior base price. Gray areas of the law abound, and opportunities for willful or accidental violations are numerous, all the more so because products quickly lose their identities in the marketing channel.

The tail that wags the dog

The role played by the spot market in determination of petroleum prices has changed dramatically. Little more than six years ago it was a...
dumping ground where products were sold at salvage prices, but now spot prices have a strong influence on pricing of long-term contracts. OPEC members maintain that the spot market provides a key barometer of the prices petroleum markets will bear and have used such prices to rationalize sharp increases in contract prices.

Economic theory suggests cartels can maintain their power as long as individual members do not cheat on each other by lowering or discounting prices and expanding supply. After the 1973 embargo, many petroleum market analysts predicted that OPEC could not maintain its monopolistic position for any length of time. It was contended that individual member countries would spend their oil revenues on overly ambitious economic development programs that would require increasingly greater sums of money. As the demand for funds of individual nations grew, they would begin to discount oil prices, and the market power of the cartel would quickly diminish.

In the long run, OPEC may still break up if individual members have to reduce prices to maintain or increase oil revenues. At the present time, however, just the opposite is occurring. Demand for crude oil is highly price-inelastic—a large percentage increase in crude prices results in a disproportionately small percentage decline in the quantity of oil demanded—and world consumption of petroleum products shows few signs of weakening. Therefore, OPEC has found that oil revenues can be increased by further price hikes. The price and rate of production that would maximize total oil revenues are uncertain, but the current high level of spot prices indicates to OPEC members that contract prices could go higher and revenues would continue to grow.

New nonmember bank

Short-term interest rates jumped sharply in late 1979 as the Federal Reserve System initiated changes in the discount rate, reserve requirements, and operating procedures designed to slow the rapid growth of money and credit, which in turn would help slow inflation and strengthen the dollar abroad. Long-term interest rates also moved up but at a slower pace.
Apparently, the high interest rates had an impact on the demand for bank credit in the Eleventh District in October and November. Loans and investments rose sharply in the District through the first three quarters of 1979. In October and November, however, all member banks, on balance, experienced only minimal growth in total credit, and large banks experienced contraseasonal declines.

Although overall loan demand at District commercial banks slowed in October and November 1979, loan demand was mixed. Loans to businesses and nonbank financial institutions tapered in October, and these groups made net repayments in November as the cost of borrowing reached record highs. Real estate loans and consumer loans, however, continued to grow appreciably. The continued strength in real estate loans appeared to reflect the taking down of commitments made prior to the sharpest increases in interest rates.
New Restrictions Proposed for Foreign Banking in U.S.

Proposed amendments to Regulation K are before the Board of Governors of the Federal Reserve System that would set limitations on the interstate banking activities of foreign banks in the United States. The proposed amendments, if adopted, would implement the provisions of the International Banking Act of 1978 (IBA) that restrict foreign banks from establishing branches and subsidiary banks in this country in any state other than their "home state."

Before the International Banking Act was passed, foreign banks could establish branches or agencies in one or more states, under state license. The IBA placed foreign banking in the United States under Federal regulation and imposed restrictions on the interstate operation of branches, agencies, commercial lending companies, and subsidiary banks of foreign banks.

Without the legislative constraints of the IBA, foreign banks in the United States had a competitive advantage over domestic banks with respect to receipt of domestic deposits at interstate offices. As a result, one of the primary functions of the IBA emerged: to limit the interstate domestic deposit-taking capabilities of foreign banks.

The Board's proposals outline procedures by which a foreign bank could choose a "home state" for its offices in the United States; establish rules limiting interstate expansion of domestic deposit taking by foreign banks; and provide Federal standards for distinguishing deposits from "credit balances."

The Board is requesting comments on these proposals and has extended the date for acceptance of comments to February 4. An extension was granted because of the impact the proposed amendments would have on the operations of foreign organizations and because of the necessity for branches and subsidiaries of foreign organizations in the United States to coordinate with their home offices.
The Board of Governors of the Federal Reserve System has published amendments to Regulation O that implement the reporting requirements of Titles VIII and IX of the Financial Institutions Regulatory and Interest Rate Control Act of 1978 (FIRA). The revised regulation, effective December 31, 1979, applies to both state-chartered member banks and national banks.

In general, Regulation O pertains to loans to executive officers, directors, and principal shareholders of member banks. Title VIII of FIRA prohibits banks that maintain correspondent account relationships with other banks from providing preferential lending to one another's executive officers, directors, and principal shareholders.

To implement the reporting requirements of Title VIII, the revised regulation requires that an annual report be filed with a member bank's board of directors that declares the individual indebtedness of the executive officers and principal shareholders of the bank, as well as that of their "related interests," to each of the bank's correspondent banks.

This title also requires that an annual report be sent to the appropriate bank supervisory agency listing the name of each executive officer or principal shareholder who files a report of indebtedness with the bank's board of directors, together with the aggregate amount of indebtedness of these persons and their related interests to the bank's correspondent banks.

To implement Title IX of FIRA, the revised regulation requires that each member bank file with its appropriate regulator an annual report listing the names of the bank's principal shareholders at year-end, the names of the executive officers and principal shareholders of the bank who were indebted, or whose related interests were indebted, to the bank during the reporting year, and the aggregate amount of such debt to the bank.

The first such annual report will cover the period from July 1, 1979, to December 31, 1979. Executive officers and principal shareholders filing reports of indebtedness under Title VIII will file before January 31, 1980, and the member banks will file reports with their appropriate regulators, based on these reports, by March 31.
"There was in early October no conflict or meaningful 'trade-off' between the domestic and international objectives of economic policy. Nor was there any real trade-off between inflation and unemployment. The clear and present danger was that failure to deal with inflation and inflationary expectations would in time produce more—not less—economic instability, ultimately with higher prices and greater unemployment.

"In that setting, the priority for policy was decisive action to deal with inflationary pressures and to defuse the dangerous expectational forces that were jeopardizing the orderly functioning of financial and commodity markets. The Federal Reserve clearly had a key role to play in this situation. Although the solution to the problem of inflation should not reside with monetary policy alone, control over money and credit is an essential part of the overall policy framework. In the long run, inflation can continue only if it is nourished by excessive monetary expansion; in the short run, it was clear by early fall that the growth in money and credit was threatening to exceed our own targets for the year, and was nourishing inflationary expectations."

"The October 6 actions involved a change in instruments and tactics to reinforce, and underscore, our intention to achieve moderation in the growth of money and bank credit.

"The new steps taken did not reflect any change in our basic targets for the various monetary aggregates for 1979; they did provide added assurance that those objectives will be achieved. In doing so, the new measures should make abundantly clear our unwillingness to finance an accelerating inflationary process and our desire to 'wind down' inflationary pressures.

"One component of the October 6 package was a change in our operating procedures. In recent years, with the support of this Committee and others, explicit targets for the growth of money have been a central feature of our approach toward monetary policy. However, the operational guide from day to day in conducting open market operations has typically been the so-called federal funds rate—the rate established in interbank trading of reserve balances. Translation of money stock objectives into day-to-day management of the federal funds rate is effective if the relationship between the public's demand for cash balances and short-term market interest rates is relatively stable and predictable. But in an environment of high and relatively volatile inflation rates, the relationship between interest rates and money (or for that matter, between interest rates and economic activity) is more difficult to appraise. Moreover, the operating techniques over time may have contributed to excessive supplies of credit by encouraging a view by banks or others that they could count on access to liquidity at interest rates reasonably close to whatever levels were currently prevailing.

"Consequently, we are now placing more emphasis on controlling the provision of reserves to the banking system—which ultimately governs the supply of deposits and money—to keep monetary growth within our established targets. In changing that emphasis, we necessarily must be less concerned with day-to-day or week-to-week fluctuations in interest rates, because those interest rates will respond to shifts in demand for money and reserves. I would emphasize that, in an important sense, our objective has remained the same: to achieve the growth of money that we believe
suitable to the nation's economic goals. What is involved is a tactical change in the approach to control of the money stock. We did not before, as we do not now, attempt to maintain a fixed or predetermined pattern of interest rates over time. But changes in interest rates will necessarily be observed and evaluated over time, along with the entire array of economic and financial variables, in reaching policy judgments."

Paul A. Volcker, Chairman, Board of Governors of the Federal Reserve System (Before the Subcommittee on Domestic Monetary Policy and the Subcommittee on International Trade, Investment and Monetary Policy, U.S. House of Representatives, November 13, 1979)

"The magnitude of federal credit activities has become quite large in recent years and further rapid growth is in prospect. Gross loans and loan guarantees outstanding are estimated to have totalled over $350 billion in the fiscal year just ended. This is more than double the $157 billion level reached just 10 years ago. In addition, loans held by government sponsored agencies are projected to have been $142 billion in fiscal year 1979, up $15 billion from the year before and by over $100 billion from the level 10 years earlier. Moreover, these credit activities are projected to grow rapidly in the years ahead. In January, for example, the Administration forecast that net credit advanced under federal auspices—direct, guaranteed and sponsored—would increase by almost $60 billion in fiscal year 1980. If total credit flows in the coming year turn out to be roughly the same as in the past year, then funds raised under credit assistance will account for about one-sixth of the total net funds raised in financial markets.

"As noted earlier, only a small portion of this credit activity is ever considered by Congress in its deliberations on the budget's expenditure targets. Loan guarantees, in particular, do not involve an expenditure of funds and are thus not reflected in the unified budget, except in those instances where appropriations are required to cover the cost of defaulted loans."

"The picture of federal credit activities also is clouded by the operation of the Federal Financing Bank. . . . In fulfilling its function, however, the FFB has reduced the accountability of federal credit programs, because lending activities are attributed to the FFB rather than to the agency originating the transaction.

"These problems of accountability are matched by imperfections in the Congressional review process. All federal credit programs, of course, have been authorized by law and are subject to oversight by the Congress. In the case of some loans made by 'on budget' agencies, this oversight is conducted annually."

"In general, these accountability problems—especially as regards resource allocation and stabilization policy—could be improved by establishing a federal credit control budget along the lines suggested by the Administration. Under this approach, annual limits would be placed on gross loan activity for both direct and guaranteed loans. These legally binding limitations would be established annually and would be included in the Presidential and Congressional budget process. When faced with a credit limit, Congress would be forced to consider how each program affects the ceiling, and how it integrates with other credit and noncredit programs to achieve specific budget objectives."

Nancy H. Teeters, Member, Board of Governors of the Federal Reserve System (Before the Budget Committee's Task Force on the Budget Process, U.S. House of Representatives, November 13, 1979)
"The condition of the mutual savings bank industry today reflects imbalances in our economy and our society that go far beyond the short-term aspects of the business cycle. We have the problem of low interest rates on old mortgages that the debtors are making every effort to keep in effect. This contrasts with the high rates that must be paid by savings banks on new money and also on money that would otherwise be withdrawn. We have the unfair treatment of the small saver who by law is prevented from receiving a market-oriented return on his savings, juxtaposed to the problem of the thrift institutions whose survival might be threatened if they had to pay the small saver a competitive rate. More fundamentally, we have in our society the conflict between homeowners who are obtaining large capital gains on their homes as a result of inflation, vis-a-vis the plight of the saver who is being expropriated by the same inflation, and vis-a-vis also the would-be buyer of a home who is forced out of the market by inflationary home prices and interest rates. Inflation is dragging this country into a kind of economic civil war.

"Basically, there is only one answer. We must bring the inflation to a halt. The Federal Reserve has taken strong measures. Consistently applied they will do the job over a number of years. But more is needed. Government spending must be brought under better control. Government policies raising prices must be turned around. Energy must be better conserved and its production encouraged if we are to avoid a constant menace to our price level as well as our national security from the side of OPEC. Expectations of real wage gains must be reduced so that they more nearly approximate average gains in productivity. None of these actions is easy; all will take time to become fully effective."

Henry C. Wallich, Member, Board of Governors of the Federal Reserve System (Before the National Association of Mutual Savings Banks, New York, New York, December 3, 1979)