SAVINGS AND LOAN ANNALS 1971

United States Savings and Loan League
111 East Wacker Drive
Chicago, Illinois 60601

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United States Savings and Loan League

PRESIDENT

FOREWORD

THE YEAR 1971 HAS BEEN VIEWED by many largely as a statistical triumph. Every commentator dwells upon the extraordinary numbers achieved by the savings and loan business; but, while the numbers are noteworthy and certainly favorable, they do not tell the whole story.

They do deserve attention. Net savings gains of $28 billion, mortgage loan volume of $38 billion and achievement of the $200 billion asset mark all represent accomplishments far beyond anything envisioned as recently as two years ago.

We can take genuine pride in the service to the savings and home buying publics which these numbers represent. Many of the speeches appearing in this volume of *Annals* reflect the exuberance which these savings and lending achievements have produced.

The annual convention in New York City was a happy convention because the savings and loan business was in a happy state of mind. The true cause of this happiness, however, lies much deeper than anything shown on the savings flow scorecard. At the root of the current mood is a new feeling of confidence that past problems are being overcome and that future problems can be dealt with.

That this should be a new feeling is easily understood by those who have lived with the savings and loan business during the past six years. War-caused inflation, a squeeze on earnings, tight money, rapid market changes on both the savings and investment sides have all contributed —and in very rapid succession—to a defensive feeling of being harassed and uncertain.

Many outside the business, including academic observers, economists and some public figures, have openly questioned whether the specialized financial institution still has a valid role in the American economy.

The year 1971 marked a turning point when the business once again demonstrated its resiliency and its capability of doing a job for the public that no other financial institution—or any other type of institution, for that matter—could begin to match.

While it is true that the dramatic drop in short-term money rates coupled with strong housing demand combined to create an optimum

savings and loan environment, the record-breaking performance figures tend to obscure the fact that underlying structural changes in the business are beginning to produce fruit.

A new liability mixing capability, for example, now enables savings associations to emphasize either passbook or certificate savings and thereby adjust the cost, maturity and volume of savings account holdings. The Federal Home Loan Bank System has improved its techniques not only for tapping the capital markets but also for feeding this money to the business as needed so as to maintain home financing capability. A leveling of the mortgage money supply roller coaster should, in turn, permit better planning and more efficient operations within the home building business.

Increased flexibility in mortgage lending and improved secondary market outlets have enabled associations to diversify portfolio holdings, improve asset liquidity and increase earnings, all of which strengthen the business competitively.

The point is not that 1971 represents a new norm, or that there will be no more tight money, earnings squeezes or housing market fluctuations; rather, the point is that the savings and loan business has become far more sophisticated in perceiving and adjusting to these challenges as they occur.

We still face problems in liability management, in stabilizing local housing demand and in meeting the shelter needs of those who cannot afford to purchase housing in the open market. Government subsidy operations not only are becoming overwhelmingly expensive, they are failing to achieve the goals set in spite of all the money provided.

We face challenges in finding the best way for this business to mesh with coming systems of electronic funds transfer in the banking business. We need to devise proper responses to such reports as that of the Presidential Commission on Financial Institutions.

PRESIDENTIAL COMMISSION ON FINANCIAL INSTITUTIONS

Within this volume, however, is a key to the way these challenges will be met. One of the basic questions facing the business has been the matter of federal chartering of capital stock associations. A reading of many of the topical forum speeches and committee deliberations reported in *Annals* will indicate clearly that this question has been and is continuing to be given widespread exposure within the business and full discussion by the United States League's committees and policy-making Board of Directors.

Such broad-based participation in decision making, drawing as it does on the collective experience and wisdom of the entire business, is part of the reason the savings and loan business has emerged from its recent trials in stronger condition than it entered.

This spirit and this effort on the part of all segments of the savings and loan business will, I am confident, continue to serve the business and the public well in the years ahead.

LEWIS S. EATON

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Year	Convention Site	President
1939	Atlantic City, N. J.	Clarence T. Rice, Kansas City, Mo.
1940	Chicago, Ill.	George W. West, Atlanta, Ga.
1941	Miami Beach, Fla.	Paul Endicott, Pomona, Calif.
1942	Chicago, Ill.	Fermor S. Cannon, Indianapolis, Ind.
1943	Chicago, Ill.	Ralph H. Cake, Portland, Ore.
1944	Chicago, Ill.	John F. Scott, St. Paul, Minn.
1945	Chicago, Ill.	W. M. Brock, Dayton, Ohio
1946	Milwakee, Wis.	Henry P. Irr, Baltimore, Md.
1947	San Francisco, Calif.	Walter W. McAllister, San Antonio, Tex.
1948	New York, N. Y.	Ralph M. Smith, West Somerville, Mass.
1949	Chicago, Ill.	M. K. M. Murphy, Rutherford, N. J.
1950	Washington, D. C.	Henry A. Bubb, Topeka, Kan.
1951	Miami Beach, Fla.	Walter J. L. Ray, Detroit, Mich.
1952	New York, N. Y.	Ben. H. Hazen, Portland, Ore.
1953	Chicago, Ill.	Charles L. Clements, Miami Beach, Fla.
1954	Los Angeles, Calif.	Ralph R. Crosby, Providence, R. I.
1955	Miami Beach, Fla.	J. Howard Edgerton, Los Angeles, Calif.
1956	Philadelphia, Pa.	Walter H. Dreier, Evansville, Ind.
1957	Chicago, Ill.	Roy M. Marr, Memphis, Tenn.
1958	San Francisco, Calif.	Joseph Holzka, Staten Island, N. Y.
1959	Dallas, Tex.	C. R. Mitchell, Kansas City, Mo.
1960	Miami Beach, Fla.	W. O. DuVall, Atlanta, Ga.
1961	Chicago, Ill.	C. Elwood Knapp, Pittsburgh, Pa.
1962	Washington, D. C.	M. L. Dye, Salt Lake City, Utah
1963	San Francisco, Calif.	F. B. Yeilding Jr., Birmingham, Ala.
1964	Miami Beach, Fla.	Eugene M. Mortlock, New York, N. Y.
1965	Dallas, Tex.	John W. Stadtler, Washington, D. C.
1966	New York, N. Y.	C. A. Duncan Jr., Nevada, Mo.
1967	San Francisco, Calif.	Otto L. Preisler, Chicago, Ill.
1968	Miami Beach, Fla.	Hans Gehrke Jr., Detroit, Mich.
1969	Chicago, Ill.	Tom B. Scott Jr., Jackson, Miss.
1970	San Francisco, Calif.	John H. Randolph Jr., Richmond, Va.
1971	New York, N. Y.	Lewis S. Eaton, Fresno, Calif.

GENERAL SESSIONS

PRESIDENT'S ADDRESS

by LEWIS S. EATON, *President*

United States Savings and Loan League

Fresno, Calif.

IT IS VERY PLEASANT to address this convention as we near the end of the greatest year of growth and progress in savings and loan history. Naturally, I'm proud to have been the president of the U. S. League to announce that the business has passed $200 billion in assets. The League staff and the Savings and Loan Foundation have put together excellent promotional material to assist you in the proper observance of this $200 billion milestone. The catch words in this promotion are: "We're doing a lot for America; we want to do more." I urge you to use the special material when planning your year end promotion.

The statistical record of the past year, impressive as it has been—a $28 billion gain in savings and a $38 billion dollar volume in mortgage loans—is far less important than the fact that 1971 marked the end of an era for us, and an end of a period of constant and incessant anxiety brought about by a war and a war-inspired inflation.

But the war now seems to be phasing out, the national administration is moving forcefully and effectively against inflation, and significant new initiatives have been undertaken in order to reduce internal tensions.

Admittedly, there is some progress yet to be made in restoring confidence among the American people about the new road along which we now are moving. But the savings and loan business, as a business, need suffer no misgivings. The bitter problems of 1965 to 1970—rising inflation and surprising rises in interest rates—are behind us.

I realize this optimism on my part about success in the inflation fight is not shared by all economists. Yet I think the record is clear: The United States has never had serious inflation except when directly related to a war. The American people will not tolerate serious peacetime inflation, and if you doubt my words, consider the Gallup Poll of recent weeks which shows 86% of the American people favor some controls over prices and wages until inflation is brought under control.

As for the savings and loan position toward Phase 2, I want to make it unequivocally clear that we support it, and that our institutions will do everything responsible to assure that it will be implemented suc-

cessfully. I have no doubt that all of you will do your part.

On the basic premise that the war is moving toward an end and that inflation is slowly but surely coming under control, I want to suggest to you that the savings and loan business has now begun playing in a brand new ballgame—one that is very different from the kind of defensive game we played from 1965 to 1970.

SAVINGS, LOAN BUSINESS ON SOLID FOOTING

At no time in recent memory has a president of the U. S. League appeared before the annual convention when the business was on such a solid footing as it is at the present time. To be sure, we have a few areas of concern to us, and I will review those with you in a moment. However, to help remind you of the great progress we have made in the past five years, permit me to reminisce with you and recount some of the pleadings of my predecessors on this podium.

In 1966, right here in New York, C. A. Duncan pointed to a need to develop flexibility in the liability side of our balance sheet with perhaps dual-rate savings plans. He also urged liberalization of the reserve regulation, and appointed a Blue Ribbon Committee to study and recommend ways of restructuring the business. In 1967 Otto Preisler in San Francisco pointed to the problem of declining earnings and urged more flexible investment powers for better profitability.

The year 1968 saw Hans Gehrke tell the convention in Miami we needed to press for implementation of the Housing Act to give the business more flexibility. He also stressed the need for new savings instruments, and a secondary market facility for conventional loans within the Federal Home Loan Bank System.

Tom Scott stepped to the podium in 1969 at the Chicago convention and told us inflation was our greatest problem to solve. A few of his "near term priorities" were to get the U. S. agencies out of such active competition for household savings, increase insurance of accounts, seek adequate rate differentials between banks and savings and loans on certificates, and obtain trustee powers for Keogh Act funds. Scott also said the business needed comprehensive legislation to restructure.

Last year, in San Francisco, Jack Randolph deplored the fact that no innovative thinking was in sight in the fight to curb inflation. "This means, once again," he said, "excessive reliance on Federal Reserve monetary policy and high interest rates to curb inflation."

Here we are in New York again, five years after C. A. Duncan stood here. I need only to remind you briefly and hurriedly that we have accomplished solutions to most of those concerns and trouble spots. As I have said, never has the savings and loan business been on a more solid road to the future than it is right now. But there are a few loose rocks on the road which we must keep our eyes upon.

The first concern which I think deserves our attention involves the demand for housing in local markets. As I have traveled around the country in the past year, I have been impressed with the strength of the recovery in virtually every market. I also have been impressed by the increasing flexibility of our lending operations in response to the changing housing demands of the American public and, in particular, financing the shift toward multifamily housing.

Some years ago it had been expected that following the great apartment boom in the 1960s we would face a resurgence of demand for single-family houses in the decade of the 1970s. This is one of the predictions which has not fully developed as yet, and it is clear that large-scale apartment building will continue to play a very significant role in the years just ahead. Apartment living, for a variety of reasons, including a surprising drop in the birth rate, is "in," and it is particularly "in" among younger people. Many young couples who discovered the apartment way of life apparently do not seem to be as interested in a house in the suburbs as was the prior generation. The attraction in housing of the young people today is having a sense of freedom without responsibility, and apartment living more nearly satisfies this feeling.

In moving toward a role of increasing importance in the apartment market, our business has been greatly assisted by the regulatory changes by the Federal Home Loan Bank Board which have liberalized the conditions under which we can make apartment loans. With the help of a task force headed by my fellow Californian, Bob Rand, the Board is continuing its efforts to supply the powers necessary to serve the multifamily market adequately. For our part, most of our institutions have developed the lending expertise required to make these loans on a financially sound basis.

It is true, of course, that the financing of apartments involves substantially greater risks, and it also is recognized that this is the type of housing where surpluses can be developed literally overnight.

We will build more than 2 million homes and apartments in the United States this year. Because of continued demand and the availability of mortgage funds supplied principally by savings and loan associations, there will be approximately the same number of new starts in 1972. But this huge volume for 1971 and 1972 excludes mobile home production, which in 1971 will approximate 450,000 units with a comparable number next year. Can the country smoothly absorb these?

MORE HOUSING MARKET RESEARCH NEEDED

In the early and mid-1960s some areas went through the problems of over-building and had a rather serious excess of housing. It was not a happy experience, as many of you will remember. For a business investing nearly $40 billion a year in mortgage loans, it appears to me we don't do enough research in measuring housing demand and supply factors. Right now there seems to be pretty good balance in most parts of the country. However, with bond interest rates falling, as they have, we might suddenly find new and vigorous competition from returning investors who temporarily left the mortgage market for the higher yields in the bond market. It is in times like these, of plentiful supplies of money and intense competition for loans, when market research is most necessary. I commend you to do more sophisticated planning in this area.

Another matter which bears watching by all of us is in the area of liability management. Obviously, closely related to our loan markets is the question of how much savings money we can prudently accumulate at our higher rates and put to work. I am not suggesting that we take any immediate action to slow our savings. I am raising the question of continuing the vigorous push for new 6% certificates when the Treasury is offering a 15-year bond to yield about 6%. Fortunately, we now have great flexibility with our savings certificates, and we deal appropriately with the current money situation by developing a mix of savings plans in keeping with market conditions. I believe the flow of funds bears rather close watching at the present time.

One reason I earlier suggested a cautious attitude toward the financing of apartments in the days ahead stems from a concern over the impact of government subsidy programs which, in effect, are "force feeding" the market in certain price categories.

With the winding down of the war in Vietnam and with the significantly increased ability of our institutions to finance the housing market, it seems pertinent to raise this question: Haven't we reached the time when the role of the federal government in supporting housing markets needs reexamination?

In recent years, we have seen a variety of new federal programs designed to bolster housing and home finance. While some of these were consistent with the long established and dominant practice of the federal government to strengthen the housing market through private channels, several have done violence to the performance and operation of the private market place.

The federal government has a long history of involvement in the housing field, and the most important of these programs have been essential to the improvement of American housing standards since the early 1930s.

Without federal insurance of savings accounts in our institutions, without the FHA and VA programs, without the Federal Home Loan Bank System and without the secondary mortgage corporations, it is very obvious that we would not have made the progress we have in improving housing standards or in setting in motion the great American homeownership movement.

Bear in mind that the normal operations of these insurance and secondary market programs are self-supporting, involve no tax funds and have the over-riding purpose of trying to help people to help themselves. They stand in substantial contrast to handout programs, which like most welfare programs stifle individual incentive and dignity.

For many years we have had the public housing programs for low-income families, but in more recent years federal subsidies have become available to middle-income families. Housing Secretary Romney has said that the existing 10-year subsidy program will cost $200 billion and still will assist only one-fourth of the families eligible for subsidies. If it takes $200 billion in housing subsidies in the present decade to aid only one-fourth of the eligible families, what do we do for the other eligible families, spend another $600 billion?

The newest subsidy program is the so-called "tandem plan" announced early in August by the Department of Housing and Urban Development. This program is aimed directly at holding mortgage yields on FHA and VA loans, and indirectly influencing the interest rates on conventional loans as well. It is difficult to know, at this time, just how much in subsidies will be required under the tandem plan; all we do know is that it seems to be an example of unnecessary tampering with the mortgage market.

All over the United States today there is a wave of unrest about excessive taxation at all levels. Sooner or later the outcry will begin against the housing subsidy programs which have the effect of hampering greater efficiency in building operations, producing over-building in some price categories, and ultimately pitting the nonsubsidized family against its subsidized neighbor.

NEED TO REEXAMINE HOUSING SUBSIDY RATIONALE

The idea of housing subsidies for middle-income families is a comparatively new one brought about by sky-rocketing inflation and housing costs, and unprecedented rises in interest rates. With abatement in inflation pressures, the rationale for these programs should disappear.

The fourth concern is the speed with which commercial banking is moving in implementing an electronic funds transfer system generally under a program known as "SCOPE." Under SCOPE, the banks plan to eliminate many of the payroll checks in this country, and then hope to put a great portion of the recurring monthly checks written by individuals on a pre-authorized payment basis.

Our basic concern is that we soon may be seeing the banks trying to switch many of our loan customers to a pre-authorized payment basis under terms dictated by the banks rather than under arrangements we would develop with our customers. Knowing the urgency of the banks in finding a solution to their paper burden, I don't think we should underestimate the momentum behind the efforts of the banking system to implement its SCOPE programs. I urge you to take an interest in this subject.

Despite these questions I have raised—the need to keep a vigilant eye on our local housing markets, the need to review our liability structure, the need to re-think the problems of housing subsidies, and the need to take an interest in the electronic funds transfer—I still feel the savings and loan business is sitting on an extremely solid base and in a position to continue to fill its primary role of serving the housing finance needs of this country. With considerable help from the Congress and the Federal Home Loan Bank Board—and with thoughtful and constructive industry leadership through the U. S. League—we have worked our way through some rocky times and have emerged a much stronger and more versatile business.

Only two years ago there were real questions in the minds of many over the future of savings and loan associations as specialized financial institutions. There was some concern that we inevitably would be absorbed into the commercial banking business. Yet as we meet here

today, $200 billion strong, there is every reason to believe that the future of specialized institutions is bright.

Let me quickly add that it will remain bright if we continue to press forward with a wave of innovative practices that began in the late 1960s, if we continue to respond to change with vigor and intelligence, and if we bear in mind that our institutions have more than their share of public interest responsibilities.

A $200 billion business has a responsibility for becoming more involved in the full spectrum of planning and financing activities which affect the environment in which we live. Few issues are more important to the American people than the environment, and public opinion of us will depend greatly on the kind of neighborhoods we help to create.

A $200 billion business has a responsibility of broadening its role in the residential housing market. We should expect to do more home improvement lending, including substantial rehabilitation lending in our urban centers, more lending for land acquisition and development, and more construction lending. In addition, we should play a much larger role in mobile home and park lending.

A $200 billion business has a responsibility to do more—much more—in trying to solve the crisis of deteriorating neighborhoods in our cities and towns. With a return to more normal conditions in the mortgage markets, we should now begin to work harder in redevelopment programs and in curbing the spread of blight.

Finally, a $200 billion business has a responsibility to join in programs to solve America's greatest internal problem—the racial crisis. It is not enough to help provide housing for blacks and other minority groups. We must also see that the way is open for the representation of minority groups in management. The Federal Home Loan Bank Board is to be commended, in my judgment, for its efforts in this direction through Operation Vanguard.

Yes, ours is a very promising and exciting future. It is the future of the "'full service real estate lenders." To help move us along the road, the Federal Home Loan Bank Board has submitted a package of imaginative legislative proposals to the Congress.

As you know, the Senate Banking Committee has held hearings on these proposals but has deferred action pending receipt of the report of the Presidential Commission on Financial Structure and Regulation. We have been fortunate to have two exceptional savings and loan men on this commission—Howard Edgerton, a past president of the U. S. League, and Richard Gilbert, our incoming vice president—and, because of their work, I think all of us can be confident that the commission report will include a forward-looking view of the business.

During 1972, the Congress will begin its consideration of the details of the various legislative recommendations of the Board and the Presidential commission. Not all of the ideas proposed will be enacted, but surely enough will be to maintain the forward thrust of our business.

We have closed out a problem-ridden old era and begun a good new era to which all of us look forward with optimism and confidence.

We're doing a lot for America; we want to do more.

THE LONG-TERM LENDER IN A TIME OF INFLATION

by DAVIDSON SOMMERS, *Chairman of the Board*
The Equitable Life Assurance Society of the United States
New York, N. Y.

SAVINGS AND LOAN ASSOCIATIONS and life insurance companies have much in common. Both deal face to face with individuals on matters of important family concern. They also share common problems, particularly those concerning the proper functional relationships among various groups of financial institutions competing for the savings dollar and for lending opportunities. We await with keen interest the report of the Presidential Commission on Financial Structure and Regulation.

Today I want to discuss another major question of common interest: What happens to long-term lending functions in a time of inflation? Have the long-term lenders been able to operate with reasonable effectiveness—to attract savings and make funds available for economic and social priorities—in such a period? We cannot avoid this question since inflationary expectations are deeply ingrained, and even optimistic forecasts are for continued inflation, though hopefully at ever-reducing rates.

One of the obstacles long-term lenders face in discussing this question is that the public does not know, or tends to ignore, the importance of the long-term lending function in our economy. To the public, the "market" is the stock market. That is what gets most of the space in the financial pages and most of the discussion in public forums. The total transactions in stocks and the amount of wealth held in the form of stocks are huge. But in terms of the amounts of new capital channeled into what the economists call "gross private domestic investment," that is, residential structures, business plant and equipment, additions to business inventories—the long-term private capital of the country, the contribution of the stock market is minuscule compared to that of the bond and mortgage markets. Even in the year 1970, a

recent record year for new equity issues, only $6 billion was raised in this way, compared with a tremendous $22 billion raised by business through long-term fixed debt obligations. When to this business investment is added the $25 billion provided for all types of mortgages and the $13 billion raised for state and municipal financing, the long-term lending market, even in a record new issue year for the stock market, is found to have provided 10 times as much new capital as the stock market.

LONG-TERM LENDING MARKET HAS GROWN

More remarkable than the absolute size of the long-term lending market is the fact that it has been growing during the period of inflation. The aggregate amount raised for gross private domestic investment from external sources through long-term debt financing doubled roughly from 1965 to 1970, the years of most intensive inflationary pressures. Including public financing, the net long-term bond and mortgage financing will probably reach $80 billion in 1971, again about double the pre-Vietnam escalation figure.

Thus in general we must say that the capital market for long-term debt financing has functioned well in the face of inflation, contrary to gloomy predictions that it could not perform. For many years our long-term capital market has been the envy of the world. That envy has been substantiated by its performance in a difficult period.

Several principal factors have contributed to this record. First, the sharp and often-criticized upward shift in long-term rates over the past five years, though now somewhat attenuated, has been sufficient to keep the long-term investor in the market. Second, the flexibility afforded by recourse to convertible bond offerings and debentures accompanied by warrants has attracted considerable investment which could not be reached through higher fixed interest alone. Similar flexibilities have been introduced in the commercial mortgage market and have been significant factors in maintaining the flow of capital. The switch by corporations from debt financing to stock issues has taken some pressure off the bond market.

The residential mortgage market, as we all know, presents a special case. During the recent period of persistent inflation and occasional sharp monetary restraint, it has been subjected to serious pressures that handicapped and at times threatened to cripple its effective functioning. At present, things are more comfortable, with record cash flows in all types of mortgage-financing institutions, combined with housing starts running at a 2 million-plus annual rate; but 1966 and 1969-70 are too recent to forget and the underlying causes have not all been eliminated.

RESIDENTIAL MORTGAGE LENDERS SUBJECT TO RIGIDITIES

In major part, the special difficulties of the residential mortgage market arose precisely because the inflation-adaptation mechanisms that have worked elsewhere in the capital markets are not fully applicable to residential mortgages. For a combination of reasons, partly

economic, partly social, partly political, the residential mortgage institutions are subject to rigidities that exposed them to disintermediation and made them less adaptable than other lenders. These are familiar to all of us: usury laws and FHA-VA ceilings; interest rate ceilings on deposits; inability to turn to the bond market when disintermediation dried up the normal source of funds. The freedom of other lenders to turn to other investment fields increased the pressure on the depositary institutions.

Progress has been made in this area. In practically all states, although the process was too gradual and has not removed all potential difficulties in this area, usury laws have been gradually liberalized and in most are at levels where home mortgages are more nearly competitive with other capital market instruments. Some gradual relaxation of deposit interest ceilings has taken place. Of more importance, perhaps, has been the "new federal system" of mortgage support activities and regulations, accounting for a significant part of the encouraging recent growth in residential mortgage debt and housing starts. Accordingly, if we exclude the depressing and terribly difficult question of providing for the nation's under-housed needy (which I do not purport to cover but which should not be forgotten), I do not feel too pessimistic about the performance of the residential mortgage mechanism. Housing financing has stood the credit restraint period of 1969-70 better than it did the crunch of 1966. Credit is now flowing at fine levels, and housing construction is fulfilling the important role of a lead sector pointing towards recovery.

FEDERAL ROLE MUST BE CONTAINED

However, we should not feel too complacent. Given the circumstances, federal intervention through back-up credit packaging and subsidization has so far been most helpful, perhaps even a lifesaver; but continued vigilance is needed if we are not to drift into an ever-increasing federal role which would continually reduce the area of private activity in this field, a result which no one wishes.

Many argue the need of further adaptation of the private residential mortgage market to inflationary stress. I agree that all potential methods for allowing the private market to cope with inflation and disintermediation should be explored; but I find no panacea. Each proffered solution—variable mortgage rates, flexible deposit interest ceilings, liberalizing portfolio restrictions, and the like, may offer some advantages in protecting deposit institutions and bringing the small depositor more nearly into a position of equality with possessors of large funds in guarding against inflation; but there are also difficulties with each suggestion, and some of them, though affording more flexibility, merely point to less private contribution in the long run and increasing federal activity in the field.

Therefore, although I recognize the need and justification in present circumstances for an active federal role in the residential mortgage market, and though I favor exploration of ways of making that market ever more adaptable, I am convinced that the best way of keeping the

residential mortgage market healthy is by avoiding the inflationary excesses of the past few years. National policy on inflation, though not all we could have hoped for, has had a significant impact.

If we succeed in returning to anything like the relative stability of the early '60s, I see no reason for the private residential mortgage market, with appropriate federal subsidies for the needy, to do otherwise than function adequately and responsibly. In my view, anyone who is interested in a sound residential mortgage market must be a strong supporter of anti-inflationary policies.

Long-term lenders have no exclusive stake in stability. The adverse effects of inflation on our lending markets have, after all, been kept within bounds. In the light of the more widely damaging effects of inflation—the problems for retired people, the revenue plight of our cities, the obstacles in the path of achieving social gains—our special problems fall into perspective.

Our country has been approaching dangerously close to the brink. Restoring an atmosphere of substantial price stability is a major national objective.

HOUSING AND FINANCIAL INSTITUTION LEGISLATION IN 1972

by the HON. JOHN J. SPARKMAN

United States Senator

Huntsville, Ala.

IN THE LAST FEW MONTHS, we have seen developments on both the domestic and international fronts of such significant proportions that their outcome could affect the future of our nation and the well-being of each of us in the years ahead.

On the domestic front, the President's economic package, announced on August 15, is the most drastic measure to control the economy and the pocketbooks of each of us that has ever been proposed by our government in peacetime.

Some have referred to it as being "revolutionary."

Surely it is, when one considers that it was sponsored by a Republican President who had previously spurned even the "jaw-boning" technique of the previous administration as an undue interference by government with the free enterprise system.

Circumstances often determine one's political or economic philosophy, and I suppose that with both unemployment and inflation at the inordinately high rate of 6%, the President had little choice but to take this drastic action if he hoped to stabilize the economy by next year.

The Congress gave the President authority to issue economic controls two years ago only after it saw that the President's original economic game plan was not working.

Many members of Congress, including me, had urged the President to follow the so-called "incomes" policy advocated by Federal Reserve Board Chairman Arthur Burns, as an effective tool to overcome the twin economic scourges of unemployment and inflation. If such a policy had been initiated two years ago when it was first proposed, I am confident that we would have been able to avoid the current cathartic treatment of compulsory wage and price controls which are so repugnant to believers in our free enterprise system.

Nevertheless, this is water over the dam, and I believe it is up to all of us to do our part and support the President in his efforts to re-

establish a stable economy as soon as possible. Whether we agree or disagree with the President's plan, we are all party to it.

The months ahead will be a great test and challenge to the ability of the American people to forego some personal benefit and act together for the common good of all. If we succeed, it will be the best medicine we could find to heal the deep wounds to our pride as a nation which the Vietnamese experience has incurred. It will be an equal challenge to our political leaders who will be under great pressure from special interest groups and who, by ineptness, favoritism or indifferent administration, could fumble this unusual opportunity.

PRESIDENT'S AUTHORITY EXTENDED FOR ONE YEAR

The Senate Committee on Banking, Housing and Urban Affairs has just completed hearings and is ready to report a bill to the Senate to extend the President's authority over wages, prices and credit beyond the present expiration date of April 30, 1972. We finished work yesterday afternoon and agreed to an amendment relating to retroactivity—an amendment "good and proper and favorable to the administration." The authority has been extended for a full year.

The big issue during the hearings was basically a concern about the administration's capability of administering a fair and equitable wage and price control program without getting our whole economy bogged down in a frustrating mass of red tape.

It is quite clear that the success of the stabilization program is dependent upon the voluntary cooperation of all segments of the economy.

There is no doubt about the cooperation of the American people provided they are convinced that the program is being administered in a fair and just manner.

Organized labor has made its position clear that it will only cooperate if the government carries out a strict surveillance over profits and interest rates to keep them in line with controlled wages.

The 5.5% standard set last week by the Pay Board has upset organized labor because it would appear to rule out retroactive higher settlement awards already agreed to between labor and management.

It would be inconceivable to attempt a comprehensive wage and price stabilization program without the support of organized labor, so I feel confident that the President will do all in his power to work things out with labor.

No standard has been set for interest rate reductions, but Dr. Arthur Burns, chairman of the Federal Reserve Board, and also chairman of the President's Committee on Interest and Dividends, sees no problem in interest rate reductions for highly competitive market issues but implies that some nudging may be necessary to speed the adjustment of sluggish interest rates such as those on mortgages.

Interest rates, particularly for long-term loans, are a unique economic factor. There is a lot of mystique in how the rates are set, the most important consideration being competition and what the market will bear rather than an intellectual computation of a fair return over the life of the loan.

Temporary inflation, such as we have had over the last few years, has been used as a reason for raising interest rates, but rates are always sticky on the way down, and I doubt whether temporary disinflation will be enough reason for lowering the rates to what they were six years ago.

If disinflation succeeds, the savings and loan business is going to be deluged with requests to refinance the many high-interest rate mortgages placed in the last few years. Some policy will have to be worked out to meet this issue at a minimum cost to the home buyer and all concerned.

The current situation illustrates the need for some such technique as the variable interest rate plan which your business has been discussing for some time. As I understand it, rates on existing loans would be tied to the cost of living index or some other national cost of money indicator, and rates would change annually, consistent with the index.

In the volatile economy which we have had over the past several years, some new devices are needed to level out both the debit and credit fluctuations in your business. This plan might be the answer, and I believe that you should continue to explore it and be prepared to make a formal presentation as soon as it may be convenient.

TAX RELIEF PROVIDED FOR CONSUMERS, INDUSTRY

The second part of the President's new economic plan involving tax reductions is also of great significance.

After the plan was announced, conflict arose immediately on the issue of lower personal taxes which would help the economy by increasing purchasing power, or lower business taxes which would help the economy by encouraging investment and by improving productivity.

After extensive hearings and debate, the two Houses of Congress came through with separate packages providing tax relief for consumers as well as for industry. The two bills are alike in their emphasis on tax relief to encourage production which is badly needed to increase employment and to stabilize the economy.

However, the Senate bill contains a number of very favorable provisions reducing taxes for lower income families and consumers in general. This, of course, would increase purchasing power because these families are likely to spend the tax reductions and not put them into savings.

The large number of amendments by the Senate surprised everyone but, on balance, I believe that our economy will benefit greatly by this new injection of spendable funds.

SURTAX OF 10% LEVIED

The third part of the President's plan, that of levying a 10% surtax on imports and "floating" the dollar, seems like a relatively minor action but, when viewed in relation to other recent international developments, it may turn out to be the most significant of all three as far as the long-range peace and security of our nation is concerned.

It is impossible to separate cause and effect, but it would be interest-

ing to know the result of this drastic unilateral action on such significant events as the United Nations-China affair, the strengthening of the European Common Market by the addition of three more nations, including the United Kingdom, and Russia's recent apparent political successes in visiting and strengthening its position with nations traditionally friendly to the United States.

Secretary of the Treasury John Connally said earlier that the special import tax would last only three or four months, but I understand that its elimination depends upon how soon the United States can work out new arrangements with other world powers to correct imbalances in international trade and in its balance of payments.

It may not be due to this action alone, but many developed countries are beginning to have serious unemployment problems because of sluggish economies and a slowdown in international trade. The fear is that retaliations against the U. S. surtax may kick off a ruinous international trade war. This would be a tragedy, and I hope that an equitable solution to both our monetary and our trade problems will soon be worked out.

The recent action of the Senate in voting an end to foreign aid is symptomatic of the upheaval taking place in U. S. international relations. The position of the United States as the absolute leader of the free world economies has been badly eroded as a result of Vietnam and the rising strength of Japan, West Germany and other European powers. In many respects, this is good because it may relieve us of some of the awesome responsibilty of maintaining a stable and peaceful world. It will more clearly demonstrate the need of the other more affluent nations bearing a larger share of the world's economic needs.

TREND TOWARD ISOLATIONISM WOULD BE TRAGIC

What I fear, however, is that the U. N.-China reversal and other recent international adversities may cause a new trend toward isolationism.

This would indeed be a tragedy and would do no good to anyone except our enemies who would be pleased to move into the vacuum of leadership created by our moving out and thus be in a position to dominate the world for their own selfish purpose.

We have too much at stake and have invested too much blood, sweat and tears to maintain a stable and peaceful world for us now to become a "drop-out" nation because of a few reversals in our international dealings.

The Congress has been so tied up with international matters and the President's new economic plan, that no action has been taken, or is likely to be taken, this year on highly significant pending proposals on housing, urban development and mortgage credit.

The Senate Subcommittee on Housing and Urban Affairs has had hearings on four comprehensive subjects this year, all of which involve matters of deep substance.

The first hearing was on the subject of operating subsidies for mass transit systems. The issue brought out here the extent to which federal funds should be used to meet operating losses in existing bus and rail mass transit systems.

We were told that unless the federal government comes to the assistance of the local systems, many of them will be forced out of business. Fares have been raised to the breaking point, and cities have no funds of their own to subsidize the systems.

Because of the extreme difficulty of developing a just and workable formula for such a subsidy, the Congress requested the Department of Transportation to make a study of this and to submit a report. We are now awaiting the report and will probably work out legislation on which action can be taken next year.

The second hearing was on land use, planning and management, involving proposals for federal assistance to states, municipalities and regional bodies for the development of land-use policies and improvement of local management capability.

PLANNING FOR LAND USE RAISES BASIC ISSUES

The most significant issue raised in these hearings involved the subject of land use, and its relation to concerns about the environment. Ech of these—land use and environment—raises basic issues cutting across many jurisdictional and philosophic grounds.

The Senate has a number of bills pending before three different committees which, in one way or another, would involve the federal government in assisting the states and local governments in the development of national land-use policies. Land and its use is a very sensitive issue which mankind has been struggling over since the beginning of time. The issue before us is to develop a proper balance between the rights of private ownership in the use of land and the rights of governments representing all of the people. Furthermore none of these rights can be exercised without regard to the environment which affects broad areas and overlaps political jurisdictions.

The one clear-cut decision from the hearings is that land use is primarily a state concern with federal back-up financial support to help the states develop and carry out a national land-use program.

As for the jurisdictional issue, efforts are being made to develop a comprehensive land-use program which the states would carry out with federal support to take into account the needs and concerns involving coastal zones, waterways, natural resources, air, water and other environmental matters, as well as community development. In other words, there would be one program for land-use planning, not four.

The difficulty is agreeing on what body of government should develop the policy and administer such a comprehensive approach to this complex land-use problem.

Four committees of the Senate have had hearings but are unable to agree at this time on the final resolution of the different jurisdictional concerns.

The third hearing this year was on the President's special community development revenue-sharing proposal and related housing and

urban development bills. One basic issue brought up in these hearings is how to save the nation's cities.

The biggest and most challenging problem brought out in the hearings was the deterioration and housing abandonment taking place in shocking proportions in the cities of this nation. Outside of the waste and loss of tremendous physical assets, our country faces the prospect of a demise of many of our proudest centers of industry, commerce and culture.

HOUSING ABANDONMENT IN CITIES IS GREAT LOSS

Here in New York City alone, it is estimated that 40,000 units have been abandoned in each of the last few years. This means that landlords just give up and walk away from the once valuable property and abandon it to the vandals and almost sure destruction. New units in New York cannot be built for under $30,000, so you can see what a great loss this is. The Congress approved a study of property abandonment last year, but so far no results have been reported.

Housing abandonment is only a symptom of the deep sickness of the nation's cities. The reduction in income from real estate taxes and the movement of middle class whites out of the cities have created a nearly insurmountable financial problem for the cities. They must get federal funds for survival.

The President's community development special revenue-sharing plan would have federal funds allocated by formula to the large cities of the nation for use for developmental purposes without strings attached.

Because I believed that the Congress would never agree to a federal grant program to communities for unrestricted use of the funds as a city saw fit, I introduced an alternative community development bill which would assure continuity of funding but which would require certain specific performances on the part of the cities as a prerequisite for federal funds.

By insisting on annual performance, I believe we will overcome one of the basic weaknesses of the urban renewal program which spreads redevelopment over periods of 10 to 15 years.

Another subject of the hearings was the proposed consolidation of practically all existing housing laws, including the FHA law which has been on the books since 1934. This entails many substantive decisions but would not make any basic changes in the general format of existing federal housing programs.

DISPOSITION OF RESERVES CONTROVERSIAL

The fourth hearing by the subcommittee was on the Housing Institutions Modernization Act of 1971—S. 1671. As you all know, the principal issue in this bill is the authority to convert federal mutual savings and loan associations to stock associations. We heard a spirited discussion at the hearings from various points of view supporting and opposing the proposal. Most of the discussion involving conversions centered around the proper disposition of existing reserves built up

over the years by shareholders of the mutual association. The unanswered question is to whom do these reserves belong?

The disposition formula presented to the committee by Preston Martin, chairman of the Federal Home Loan Bank Board, makes the assumption that the reserves belong to the shareholders of record as of a specific point in time. The specific date suggested was April 19, 1971, but this date would have flexibility for associations newly created since that date, or as time made the date impractical.

Others claimed that the reserves belonged to all shareholders of record over the years the association has been operating and even to borrowers who helped build up the reserves. No conclusion was reached at the hearing, but there seemed to be strong support for those who stated that the reserves belonged to the association itself and not to any group of shareholders or management.

Other issues were discussed, but I believe the overall question facing the savings and loan business is the outlook for the future and the place of associations in the restructuring of financial institutions, now being studied by the President's Commission on Financial Structure and Regulation.

The report from the commission is due in December, so we will soon have its recommendations. I don't know what's in it. I am sure the Congress will study the report and take appropriate action to implement it if statutory changes are called for.

SUPPORT OF HOME FINANCING STILL NEEDED

In any event, however, I see the need for continued support of the specialized business for home finance, and I am sure Congress will want to see that your business is strengthened to improve its performance in serving the nation's home finance needs.

As you probably know, our committee reported to the Senate last week a joint resolution which, among other things, would reduce the reserve requirements for the FSLIC from 1.75% to 1.6% of insured savings. This provision had already passed the Senate once in a previous bill, but no further action had been taken so, by adding it to other items of an emergency nature, we hope to get final action on it this year. If passed, it will release approximately $400 million of additional funds for home lending purposes.

In that same resolution is a provision to extend for another six months the authority of the Secretary of the Department of Housing and Urban Development to set the FHA mortgage interest rate at a level above the statutory 6%. This would also apply to the VA rate which is tied to the FHA rate.

The housing consolidation bill before us would establish a dual interest rate procedure under which a lender is given a choice of setting the interest rate without regard to a ceiling but would be barred from charging discount points, or he could accept the administratively established interest rate with authority to charge points. I hope that within the six months extension period action will be taken to write the dual interest rate procedure into law.

The resolution also would amend the GNMA law to permit the purchase of mortgages above the existing $22,000 and $24,500 ceiling under its tandem plan. The committee was told that FHA mortgages in only about one-half of the states qualified for the existing ceiling. In view of the purpose of the program to retain the 7% interest ceiling, the committee believed it should apply to all FHA and VA mortgages. As you realize, the GNMA tandem is another federal government subsidy program made necessary because of high interest rates. Our committee does not favor government subsidies except for needy lower income families but in this case we supported Secretary Romney in the program because we wanted to see interest rates kept down. We believed that this large infusion of federal funds would tip the scale and establish a more competitive interest rate level which would help set a standard for the whole business. I believe that it has worked.

I understand that GNMA has made commitments to purchase nearly $2 billion of mortgages under the tandem plan, costing the government $16 million. According to the GNMA auction held this week, the prices of mortgages have risen once more and I believe they are now at a point where this special use of the tandem plan may not be needed much longer.

SAVINGS, LOAN BUSINESS HAS FLOURISHED

I am pleased that your business has done so well. You in the business are due most of the credit, but I like to think that during the more than two decades I have been chairman of the subcommittee in the Senate which initially handles all of your legislation, I have contributed toward making possible your outstanding achievements.

Many, though, in addition to your friends in Congress, have played a part in the legislative programs which have benefited your business so tremendously. Spokesmen for your League, your League staff and congressional committee staffs are among those that come to mind.

I believe that every housing bill since 1960 has contained some provisions broadening the lending and borrowing authority of your associations. These were written into law to make your associations more competitive and effective in carrying out your home lending responsibilities. It took a little time for the administration to put into effect many of these laws, but I believe by now almost all of them have cleared and you are reaping the benefits.

There are many others who have played a key role in updating the savings and loan laws by working closely with the Congress. We need to keep this working team intact and pushing forward for further improvement. Your business is facing many new challenges in the highly competitive environment of financial institutions, and you will need all the help you can get legislatively and administratively to accomplish your goals.

You can be assured of my continued support and, I believe, the support of the majority of the Congress who recognize your worth in promoting the principals of thrift and home ownership so basic to the future well-being of our American people.

THE SAVINGS AND LOAN BUSINESS UNDER THE NEW ECONOMIC GAME PLAN

by DR. ARTHUR M. WEIMER, *Asst. to the President*
Indiana University
Bloomington, Ind.

THE SAVINGS AND LOAN BUSINESS has been enjoying a favorable period in recent months. Savings have been flowing in, loan demand has been brisk, competition has not been too intense. Although the situation has varied from place to place, things generally have been going well. Savings and loans have been doing about 75% of the home financing business. Such conditions may persist for a while longer, but we should recognize that our recent experience can hardly be characterized as normal.

As we move into 1972, it may not be as easy to get the spreads between savings and lending rates that have prevailed recently. Housing markets may be less buoyant.

The money markets seem to be saying that the new economic game plan will be successful in the short run but that over the longer term some inflation will persist. This would help to explain the spread between short- and long-term rates currently. Hopefully, the longer term rates of inflation may be held to ranges that do not greatly exceed productivity gains, but at present the markets seem to be expecting something more.

Both for the short term and the longer term, the savings and loan business has a big stake in holding down inflationary pressures. Thus, we have a major interest in the success of Phase 2. Although it is early to make a careful judgment, the chances for success now appear to be good—if by this we mean that Phase 2 will moderate inflationary pressures but not eliminate them. The 5.5% guideline on incomes has an inflationary bias. It should, however, help to check the big upward adjustments that were growing all too common. We must recognize the problems facing the Pay Board. Too restrictive a position would have cost the support of the labor leaders and jeopardized the success of the effort. This has been the history of several of the efforts abroad to make use of an incomes policy. It now appears that Phase 2 will have the support of the labor movement, and this will greatly increase its

chances to moderate inflationary trends.

So far, popular support has continued to be strong, and this is most important for the success of the program. The billions of economic transactions that take place each day could not be monitored very closely by even the most extensive kind of control system that might be designed. Phase 2 contemplates no such detailed controls. To work, this plan must be largely self-enforcing. To be self-enforcing, it must be popular.

Much will depend on the willingness of the American people to accept the immediate sacrifices that are required by wage and price controls. We have already seen some evidence of discontent, and there undoubtedly will be more. Obviously wage and salary increases have to be limited if we are to fight inflation successfully. Hopefully, we can limit price increases enough to make modest income gains worth more than bigger advances that are neutralized by big gains in prices.

LONGER RANGE ECONOMIC VIEW NEEDED

Savings and loan executives as well as leaders in other sectors of our society must help people to understand these relationships. We need to encourage people to take a longer range view of their economic situations—and we must encourage other business leaders and labor leaders and leaders in other fields to generate confidence in the prospects for noninflationary income and price changes.

Fair and impartial administration of the Phase 2 programs, of course, will be essential if widespread support is to be maintained for them.

At the present time the economic outlook for 1972 seems to be favorable. The current year will record good advances—not as big as some had projected a year ago—but still far from disappointing. GNP advanced at an annual rate of $16 billion in the third quarter and the fourth quarter appears to be registering further gains. Totals for the year may reach $1,050 billion, up from $974 billion last year. A fair share of this, of course, represents price inflation but prospects for slower rates of price increases have improved under the new economic game plan.

My reasons for optimism for 1972 are based in part on the performance of the automobile and housing industries. Our past experience indicates that the American economy prospers whenever these two industries are expanding. And expanding they have been in recent months. In October for the first time in history new car sales topped a million—over 930,000 of which were produced in the U. S. Sales continue to be good and prospects remain favorable because of the price restraints plus the probability of a refund of excise taxes, along with the ready availability and improving cost of money to finance car loans.

Housing also has responded to favorable financing conditions—to the improved availability and cost of mortgage money. Private housing starts on a seasonally adjusted basis have run ahead of the 2 million annual rate throughout the summer months. Mobile homes have been selling well. There are favorable prospects for continuation of good

housing markets despite some problems. Here and there we are beginning to see preliminary evidence of overbuilding, and there may be more as the year moves on. There are also problems related to rent controls. If rents on new structures are exempted from controls, the apartment market will reach anticipated goals. If not, since real estate taxes are not controlled, I would expect a substantial decline in this sector.

CONSUMERS SHOW OPTIMISM IN HOUSING, AUTO MARKETS

Strong housing and automobile markets reflect optimistic consumers, in my judgment. The demands for housing and automobiles are both postponable; people don't have to buy them right now. The fact that they are buying suggests to me that they have a good deal of confidence in the economic outlook, although continued high savings rates prevent me from being as sure as I would like to be in reaching this conclusion.

Although estimates at present are hazardous, I am inclined to think that 1972 will be a reasonably good year both for the savings and loan business and the American economy. An optimistic outlook for the economy is shared by a number of economists. For example, the National Association of Business Economists recently developed a forecast based on the opinions of 198 of their members. To quote from their summary, this forecast "looks for strong, steady economic growth in 1972 with lessened rates of inflation and unemployment."

The business economists look for unemployment to decline from around 6% to 5%. They expect consumer prices to go up by only 3% in contrast to 4.1% in 1971 and 5.9% in 1970. They also anticipate relatively stable long-term interest rates, better equity prices, a favorable profits picture, improved capital spending, rising industrial production and continued strength in housing.

Some estimates for the year ahead are more optimistic and some more pessimistic than those projected by the business economists. Dr. R. J. Saulnier projects GNP for 1972 at $1,140 billion "with reductions in both unemployment and inflation plus an increase (about 12%) in pre-tax corporate profits."

A part of the anticipated expansion, of course, will result from the continuation of a fairly heavy federal budgetary deficit. This is now estimated at around $27 billion for the fiscal year 1972 which ends June 30. If one uses the "full employment" budget, this is reduced to about $6 billion but I have never been too certain about the use of this concept. The estimate for the fiscal year 1973 is in the same general range.

These expectations are certainly encouraging. Of course, they may not be realized, as we all know. Phase 2 may bring a period of "profitless prosperity," for example. The programs of the Pay Board and the Price Commission may not develop as hoped. The politics of an election year may hold back developments in the economic sector. Weaknesses in economic systems abroad may affect our domestic economy adversely. And other things could go wrong.

Much depends on the behavior of the consumer as we look ahead to

1972. I believe he will not continue to save at recent high levels, but I do not expect him to turn into a spendthrift, either. Thus I would expect savings rates in general as well as inflows into savings and loan associations to remain good but not at current levels. The savings and loan business is enjoying a $28 billion savings year. The year ahead will probably not see that volume of savings, but they should still be at good levels.

You can, of course, adjust your savings programs to your own situations. If your cash flow estimates indicate you will be getting more money than you can use effectively, your certificate program can be adjusted. For example, some of you may wish to lock in some long-term money by extending the term of your certificates to five years. Of if you want to increase current earnings, you may plan to reduce rates.

I think you will continue to enjoy a good spread between the savings and lending rates, but, of course, you will want to watch this as the year goes on. It is always difficult to predict changes in the money market, so you will want to watch them with care. At some point there are possibilities that other lenders will come back into the residential mortgage market.

With near-term prospects as favorable as I consider them to be, what have you got to worry about? I am afraid there are several things. First, I could be wrong. I hate to think of that possibility but feel that I should mention it at least. Maybe you should be retaining your own economist if you have not already done so. Second, I have already indicated the possibilities for some increased competition in the mortgage market. Not the least of this will be competition among associations. Third, you have to worry about the longer term outlook. At present, I am optimistic for the short run, less so for the longer run. I am especially concerned about the dangers of long-term inflation.

LONG-TERM INFLATION IS POSSIBLE DANGER

Extending mortgage credit for a quarter to a third of a century or longer into the future require consideration of many uncertainties including long-term inflationary dangers. These dangers must not be underestimated. In adjusting to them you should consider the use of variable rate mortgages—even if you have to give fairly low starting rates to get them accepted. One of the worst futures I could project for you would be mortgage portfolios carrying interest rates that are too low for future markets. The variable rate mortgage can help you adjust to such risks. You have to learn how to use it. Another approach to this problem has been suggested by Professor Ed Edwards; this is the development of a system of insurance against interest rate risk.

If we can contain inflationary pressures we have a better chance to assure reasonable stability in our financial markets. Current relatively high long-term rates in the money markets may be saying that short-term rates will also be high later on. Reducing inflationary expectations will help us to keep rate relationships on a more desirable basis from our standpoint, that is, with longer term higher than short-term rates.

As the November issue of the First National City Bank's monthly

economic letter says: "An analysis of interest rates over 50 years concludes that efforts by government to regulate the price of credit through expansionary monetary policy fail, and that lower rates can be achieved only by damping inflation." Hopefully, we are in the process of accomplishing this.

In summary, the short-term business outlook under the new economic game plan now appears to be good; the outlook for the savings and loan business is somewhat better than for the economy as a whole. The housing market should continue strong, especially if rents are made flexible for new buildings. Interest rates should be favorable to borrowers; the rate structure should favor savings and loan associations with short-term rates below those of longer term.

Over the longer run, however, the outlook is less encouraging. Inflationary pressures may persist. This may mean a return to high interest rates several years hence. Another credit crunch remains a future danger. Make use of variable rate mortgages and similar arrangements. Watch the money markets with great care.

This business and indeed the entire financial community has a tremendous stake in assuring the success of current efforts to bring inflation under control and to take us in the not too distant future to a reasonably balanced set of financial expectations as to both short- and long-term risks and returns. I hope that when we meet a year from now we will be able to take an optimistic view not only of the short-term future but the longer run as well.

MAY I HELP YOU?

by PEGGY R. DRAHEIM, *Winner*

Institute's 42nd Annual Speech Contest

State Savings, Salt Lake City, Utah

MAY I HELP YOU? Allow me to introduce myself. I am a savings and loan association, and you people of the audience and people everywhere are the most important asset in my life.

Did you know that your savings are actually a very important part of our economic system? Savings and loan associations like me rely on your deposits for the formation of capital. Progress, therefore, in an economy like ours, depends upon the constant use and reuse of your savings in order that business may continue to grow and expand.

Because of your great importance to me, I continually strive to make savings for you safe, convenient and attractive.

First off, let me assure you that your money is very safe within my walls. No one has ever lost a cent in insured savings accounts. You are protected by the Federal Savings and Loan Insurance Corporation to a maximum of $20,000. The Federal Savings and Loan Insurance Corporation is a governmental agency established in Congress. I am continuously supervised and peridically examined by governmental authorities, and I come with a built-in alarm system and a giant vault.

Now to the matter of convenience. You name it and I have it. Besides the necessitities of savings accounts, savings certificates, loan departments and insurance departments, I provide for you travelers' checks, money orders, safe deposit boxes and funds that are readily available.

A strong reserve system composed of 12 regional Federal Home Loan Banks provides ready cash for member associations. Advances are made available when required to meet unusual or heavy withdrawal demands, and also for seasonal mortgage lending.

I also have a variety of accounts, at least one to meet the needs of each of you. Just to name a few, I have single and joint accounts, partnership and trustee accounts and Christmas Club accounts. Then I try to arrange my business hours so that they are convenient for all of you. Evening hours are good for you working people so that you can stop in on the way home. I also have a 24-hour mail depository, or a free bank-by-mail service, if that is more convenient for you.

So that you may enjoy the very best service available, I make it possible for my employees to keep themselves informed and up to date about their jobs. I pay fees to enroll the employees in classes sponsored by the American Savings and Loan Institute. These give them the opportunity to learn the newest methods, which means better service for you.

Besides all of these many things that I do for you, I also offer one more item—attractive premium promotions. If you save anywhere from $100 to $5,000 or more, I will at certain times during the year offer free gifts to you. These gifts range from wigs to trading stamps, and from punch bowls to appliances.

Really, when you sit down and consider all the possibilities, why would you put your hard-earned money in any place but me—the safe, convenient, dependable, friendly, savings and loan association?

CHAIRMAN'S REPORT: 1971 AND PLANS FOR 1972

by the HON. PRESTON MARTIN, *Chairman*
Federal Home Loan Bank Board
Washington, D. C.

I APPRECIATE THE OPPORTUNITY to share with the delegates to the U. S. League Annual Convention the rationale for decisions made in 1971 and plans for 1972 of the Federal Home Loan Bank Board. Members of the Board have a certain responsibility to render an accounting of their stewardship at these enormous conclaves. When we make decisions, we are aware that we must consider their multiple impact. No doctrine of infallibility is accepted in the Board room on Indiana Avenue, N. W.

This has been a great year for the business. What objectives did we spend our time and energy in reaching in 1971? The Board's emphasis was on the lending and investing side of operations. Heavy attention was paid to the mortgage corporation in its first months of infancy. A very substantial effort on the part of the Board and nearly every key staff member was placed on the first phase of a "management auditing" approach to examination and to developing the necessary information system and rating matrix.

Recruiting and training and the development of the examination manual were all staggering tasks during which the management information center staff filmed approximately a million and a half feet of training footage.

In 1971 the Bank System handled net repayments of $3,459 million through June 9 and then turned around to provide funds in 11 of the Districts of $1,231 million while accepting net repayments in the Eleventh District of $757 million, all by the end of October. It appears likely that the Bank System will be able to meet 1972 needs of the savings and loan business, although the rates which will have to be charged may be a bar to borrowing.

For two years I have been arguing that the FHLBank System cannot afford to price itself out of its market for advances when that help is really needed. Housing and mortgage finance cannot undergo as much "stop-go" as it did before 1969. Many of you apparently share this

belief because you have used our Bank System to borrow and to pay back, while maintaining and even increasing your loan volume. I believe that your use of the Bank System represents the most important development in mortgage finance in the past few years. The cynics said you would not borrow from us. After you did borrow, the cynics said you would pay back all your advances as soon as you had some savings. Instead, you decided to serve your communities at record levels.

What should we do about 1972 when the cost of borrowing is already high—more than 7%? I propose that we use the congressional appropriation both to maintain a reasonable volume of HOAP loans and as a standby fund to subsidize advances if the need arises in 1972. If you need the money, and there is housing to be financed in 1972, I think we should price our advances to fill the mortgage credit gap. However, pricing below cost should not always be done at the expense of the FHLBanks. They need to build up their capital, and they need to pay dividends to the stockholders. The standby arrangement I am talking about is what we are thinking of calling the "Home Development Advances Program."

HIGH LOAN VOLUME FORESEEN FOR 1972

The President's new economic policies and their impact in bringing down interest rates are most conducive for maintaining a high loan volume in 1972. Good management results were achieved this year within our agency in staffing, management development, financial control and improving the capability to serve the Bank System and the business. Finally, 1971 was the year in which substantial progress was made in the delicate areas of lending and employment for minority Americans. This progress has been made in the highest traditions of voluntary and cooperative approaches to problem solving. To the many executives among you who have counseled with us and participated in these efforts, my thanks.

In my book, 1971 will go down as a notable year of deregulation. This process has to be carried on with constant attention to the public interest. However, the Board must also facilitate and develop. The Bank System was set up to provide economical financing and home ownership for the greatest number of qualified Americans possible.

Some of 1971's regulatory changes are potentially massive in market impact—such as the 95% conventional loan. I believe the savings and loan business will move into whole lending areas hitherto dominated by FHA—areas of middle and moderate income family lending. I believe, also, that FHA will shift into lower income areas with greater emphasis upon subsidized housing. I hope you will not write off the 90% or 95% loan as unsound. The markets of today are very different from those of the 1950s. There is a stability of income in American families that persists even in the face of great shifts in employment such as we are presently going through.

I commend you for your remarkable record in 1971 of whole loan and participation purchases and sales—twice the volume achieved in

1970 and most of it in transactions that did not involve FNMA or FHLMC. The regulatory changes and the IRS rulings on whole loan and participation activities have greatly expanded the previously narrow powers available to you. I think the participation loan program has probably channeled more funds from capital-surplus to capital-short areas than perhaps any other of the 1971 programs.

If you are not originating and selling, or if you are not participating, take another look. You can now participate in mortgage loans secured by any kind of real estate which you can legally accept as security.

RISKY ASSETS MUST BE OFFSET

Our commitment to deregulation has a corollary requirement. The deregulator has to try to figure out ways of preventing trouble by giving management alternatives to risky assets. Overlending and overbuilding are one kind of problem. Nationwide lending is a useful alternative to members who feel that their normal lending areas are approaching the saturation point. Other alternatives are available via statewide origination of insured loans.

Two significant moves were made in the mobile home financing field. I am aware that it is difficult in most parts of the United States to develop a sufficient volume of mobile home paper to make it worthwhile in terms of administrative costs. On a national basis, however, an industry that is producing 400,000 or 500,000 housing units per year cannot be ignored. Regulations were issued permitting certain federal associations to purchase participations in mobile home chattel paper if (1) the seller is the servicer of such paper and is insured by either FSLIC or FDIC, (2) the seller maintains at least a 50% interest in such paper and (3) the paper secures a mobile home located in a semi-permanent site within 100 miles of a home or branch office of the seller. Also, all mobile home chattel paper and participation interests therein were required to be sold only on a without-recourse basis. I hope you will take a look at the possibilities in this field because it does seem that the "immobile mobile" is here to stay.

'MOD ACT' WILL STRENGTHEN MORTGAGE USEFULNESS

I cannot leave the subjects of lending and investing without reference to the Housing Institutions Modernization Act of 1971, the "Mod Act." I ask you to consider this act as a whole with all of its 22 sections. It is a broad lending and investment bill, one which will make the mortgage corporation more useful. The Board is committed to preserving the continuity of management to maintain the flows of services to the public. This cannot be done if there is a big turnover of existing management. The Board is now devoting attention to the development phases of the savings and loan business, and I do not want to see our energy diverted to policing institutions which are in poor shape because of "fast-buck" operators. I should like to emphasize again that the reserves belong to the savers, and the stock, or voting trust certificates, or whatever, have to be issued to those savers and not to our favorite charity, or to the FSLIC. We cannot and will not trifle with the private

ownership of mutual institutions.

The last decade in our country has seen the growth of large enterprise in industry after industry. Yet our business has been operating in most parts of the country at a rather small average asset size. There is no ideal structure of the business, and the record year 1971 clearly shows that the present structure works well. However, we cannot ignore the increasing economic and market power of the commercial banks, particularly those operating in the holding company form. As a financial conglomerate, a commercial bank can offer a wide variety of services compared to those produced by specialized institutions such as the savings and loans. Nowhere is competition more acute than in the savings markets. There is also strong competition for mortgage loans. It is my conclusion that a banking holding company "mega-conglomerate" which would include a savings and loan subsidiary would tend to produce long-run socially undesirable results which would outweigh consumer convenience. How do you compete with a famous bank name and a plethora of services, with the mega-conglomerate combining the commercial bank, the mortgage company, the real estate investment trust, the factoring firm, the insurance company, the data processing organization, as well as the other savings and loan associations? This constitutes a most important public issue which I am sure will receive review and public discussion.

FHLMC WILL DEVELOP TRUE SECONDARY MARKET

The Federal Home Loan Mortgage Corporation has celebrated its first birthday and passed its first billion dollars in assets. The corporation relies upon the integrity of the federally insured lender, and its programs are designed to satisfy his needs. One of the objectives of the corporation is to develop and implement the kind of true secondary market which will allow mortgages to take a position equal to competing kinds of debt instruments within capital markets. This means that mortgages must be capable of being traded directly between originator and investor, simply and efficiently in a resale market, as opposed to being purchased by an instrumentality which has sold bonds to finance these purchases. Over the years the Federal Home Loan Banks and FNMA have been of great assistance to the housing markets as intermediaries between mortgage and capital markets. In its first operating year, the mortgage corporation infused approximately $850 million into the housing market by this intermediary process.

Furnishing a market for participations has been one of the many innovative contributions of the mortgage corporation. About $39 million in participations were purchased in September 1971 alone.

In 1971 we also sold what little whole loan FHA/VA inventory was on the shelves and was not already tied up in the GNMA bond trust. Our specialty, however, is the conventional loan, just as yours is.

And now for my announcement. I take great pleasure in this one, ladies and gentlemen—a milestone for 1972 and the mortgage market. You and I have talked for years, maybe even decades, about having a secondary market in conventional whole loans. I am very pleased to be

able to announce to you today the opening of that market. We will be mailing to you in the next weeks all of the relevant materials and details of the Federal Home Loan Mortgage Corporation whole loan conventional purchase program. Please then start your preparations for beginning operations early in 1972. The purchase program was designed with the involvement of many of you. I am thanking you once again for your contribution to the design of the instrument and the program.

In the single-family mortgage area, an over-the-counter program will provide for the variety of loans you make, including the new 95% conventional loan. We shall make a market in all these loans. In the multifamily market area there is a provision for purchasing over-the-counter loans on new and existing properties up to 80% of value and to a 30-year term, reflecting the Board's new regulations. There will be a new 24-month forward commitment called a maximum constant forward for multifamily loans that is unlike any commitment available before. That kind of forward commitment will provide your builders with a constant payment that can go down but not up and you, the lender, and the mortgage corporation, an interest rate that can go up but not down. The materials you will be receiving will lay out all the specifics on this commitment and on the other parts of the program.

The secondary market for conventional whole loans represents the beginning of a new era in the mortgage business, and we encourage you to get involved early.

The Phase 2 economic policies represent President Nixon's answers to the immense and interrelated problems which made up the wage-price spiral. The announcements of the past few weeks are indicative of the participative approach of the various commissions. The temptation to set down a series of edicts in Washington without consulting anyone has been successfully resisted, and the guidelines and the programs are being developed by the representatives of the sectors of our economy and the segments of our society most directly involved.

One of the first announcements was made by the Interest and Dividend Committee, asking that dividend increases be limited to 4%. The committee also concerns itself with interest stabilization, but it appears that Regulation Q and related controls on savings instruments will continue to be the responsibility of the four-member Interagency Committee on which the Federal Home Loan Bank Board has representation.

GOAL OF 2½% COST-OF-LIVING INCREASE SET

In the highly publicized major announcement of November 11, a goal of 2½% per year cost-of-living increase was set out by the Price Commission, not by the President and not by the Secretary of the Treasury. This limitation should be a boon to every household and family budget. In another area, the Cost of Living Council recently announced an initial group of exemptions from the post-freeze program. Notice the deregulation and decontrol activity of each of these entities of Phase 2.

Among those areas in which the freeze will no longer apply are

unimproved real estate, improved real estate with existing improvements and newly constructed real estate in which the sales price is determined after completion. For the time being most existing property rents are still controlled. Rents can now be raised only if improvements were made that cost half as much as the unimproved property was worth. New rental houses and new apartments that have never been rented before are exempt.

You probably noticed in the paper this morning that the consumer price index in October went up at an annual rate of 1.2%. In September the consumer price index went up at an annual rate of only 2.4%. These are the smallest increases in consumer prices that have occurred in four-and-one-half years. On a year-to-year basis, even, going back before the freeze, the increase is down to 3.8%. That is a long way from the 6% of 1969.

The emphasis is on deregulation and decontrol and exemptions from the freeze. These new committees are not new bureaucracies. They are being staffed by borrowing capable people from other agencies on a temporary basis with members of the Federal Home Loan Bank Board among them. Personally, I am hopeful that the temporary control of wages, rents and prices can prove successful.

Let me express my gratitude to the response of the U. S. League and of many of you in this business in bringing mortgage rates down. This is just the kind of business leadership which I hope will make rigid interest rate control unnecessary. These are difficult times. All of our institutions appear plastic, taking on new forms and weird shapes, but certain basic human drives and needs persist.

The year 1972 will be the first time ever when you will be putting two great residential mortgage years back to back. The '70s will be a great decade.

OUR FUTURE ECONOMY

by the Hon. John B. Anderson
United States Congressman
Rockford, Ill.

Last summer I became concerned as to why the economy had failed to respond to the President's "game plan." There had been some welcome abatement in the rise of the consumer price index early in the year, but the more meaningful and steady measures of inflation like the GNP deflator or the industrial prices component of the wholesale price index reflected a slight improvement which was hardly perceptible.

I raised this point with Dr. Arthur Burns, chairman of the Federal Reserve Board. As a lifelong student of our economy and dean of American economists, he readily agreed that the policy of fiscal restraint pursued by the Nixon Administration for nearly 24 months was precisely what the textbooks called for. If that policy has not been successful, it was because the private market had not responded to a cooling of demand in the conventional manner. The old rules no longer seem to be working. This would seem to call for a more unorthodox remedy.

Shortly after our discussion came the President's announcement of August 15. Already we have passed through the first phase of that policy, and the results have been dramatic, to say the least. After rising at an annual rate of nearly 5% during the first six months of this year, the wholesale price index has actually declined during the past two months under the freeze. While much uncertainty remains ahead concerning Phase 2, the decisions on pay, prices, dividends and profits made during the last two weeks by the various boards certainly suggest a determination to continue this success in the battle against inflation. I welcome this progress and would especially urge you who play such an important role in our economic system to continue to provide the cooperation and leadership that will be so necessary in this unprecedented excursion into peacetime wage and price controls.

However, I would also caution that direct controls cannot provide a total or permanent solution. They can suppress temporarily the symptoms of inflation but cannot get at the root causes. We were forced into this drastic program of controls because the old economic rules were

not working. The market was not responding. Unless we find out why and, perhaps more important, take the steps needed to get the market system back in working order, we may find ourselves unable to let go of the current anti-inflation machinery. In short, we may find ourselves saddled with bureaucratic controls indefinitely.

Why do the old rules no longer seem to be working? Why did we experience this apparent sluggishness of response to conventional remedies? These are most difficult questions indeed. As an economic layman, I certainly cannot claim to present any definitive answers.

There have been some very important changes in the structure of the economy and in public attitudes over the last two decades that provide some clue to the economic difficulties that have led us on this uncharted course of peacetime controls.

First, and perhaps most important, there has been a decided adverse shift in what economists call the Phillips curve. The Phillips curve, as many of you know, is simply a shorthand designation for the apparent tradeoff between unemployment and inflation that seems inherent in modern free economies. To reduce unemployment, we have to tolerate more inflation, and vice versa.

George Perry, a leading economist at the Brookings Institution, has recently published a study which demonstrates in quantitative terms this worsening tradeoff in the contemporary American economy. According to his calculations, an unemployment rate of 4% (the full-employment target) was associated with a 2.8% rate of inflation during the 1950s. While this rate of inflation is higher than the ideal, it is one we could live with.

Perry calculates that today we can expect an unemployment rate of 4% to be accompanied by an inflation level of 4.5%—a 60% higher rate. To get inflation down to the 2% range would require levels of unemployment much higher than in the past—perhaps 10% or even higher. Clearly, neither of these alternatives is acceptable or even practical, yet this worsening unemployment-inflation tradeoff is an unyielding fact of life with which policymakers must contend.

There is another important change that compounds the difficulty. The American public, after a record decade of sustained prosperity, has become increasingly less tolerant of even mild levels of unemployment than it appears to have been in the past. The force of this changing public opinion has been to reduce the range of fiscal and monetary policies available to economic managers to fight inflation.

Without direct controls, more drastic fiscal and monetary restraint will be needed to reduce inflation. To survive politically, policymakers will have to apply an even lighter foot on the fiscal and monetary brakes. The implications of these new facts of economic life are not very reassuring.

One temptation will be to bite our lip and learn to live with permanent high levels of inflation, but when we recall the disastrous drop in our trade balance that occurred during the recent bout of sustained inflation, the folly of that course speaks for itself. We would soon find ourselves priced out of the international market, flooded with a torrent

of imports and sooner or later succumbing to short-sighted demands to build a protectionist wall around the U. S. economy.

Another equally unattractive temptation will be to resort to direct controls, rather than applying the old remedies of traditional monetary and fiscal restraint every time the price level begins to rise. Already, in fact, some journalists and politicians are suggesting that permanent controls might not be such a bad idea.

As one who firmly believes that a flexible price system and market economy are the most effective economic governors we can hope to devise, I submit unquivocally that permanent controls are a very bad idea. Each time we are forced to adopt controls, the self-adjusting force of the market will be undermined until one day it will simply be inoperative. Then we will have to acquiesce in a state-managed economy with all its omnious implications for our democratic form of government and the high standards of living obtained under our free enterprise economy.

MUST RESTORE DYNAMICS OF FREE MARKET

We will not have to rely on direct controls; we can keep the economy moving on a noninflationary growth by means of traditional fiscal and monetary policies if we can find ways to restore the true dynamics of a market. For years we have paid lip service to free enterprise while watching complacently as constraint upon constraint was engrafted on the free and flexible operation of the market. Our badly crippled economy has become like the legendary mule—we have to kick it in the head to gets its attention, as we did on the 15th of August. We are going to have to find ways to make the economic animal responsive to a lighter touch. This is the essential task before those who value and wish to preserve a free market economy in America.

There are certain factors which act as impediments and interferences with the market mechanism, reducing its flexibility and creating strong inflationary pressures. They have made the price system sluggish and tardy in responding to changes in supply and demand. In most cases these factors point quite readily to the reforms and structural changes that will be required to restore a viable market system.

The first of these market-undermining factors concerns the activities of government. We used to speak without much pause about our "democratic, capitalistic way of life" as if the two were completely harmonious and compatible. In the final analysis, they probably are, but political democracy and a free enterprise economy are not always congenial bedfellows.

By its very nature, a free enterprise economy is based on risk, competition, and the certainty of losses as well as profits, of losers as well as winners, and setbacks as well as successes. It is a dynamic process in which the alignment of forces is constantly shuffled, and in which resources move from one sector to another in response to changing demands and needs.

From a distance, it is a marvelous mechanism to behold and truly does provide, if operating effectively, more consumer satisfaction from any given bundle of resources, than any system that has yet been devised or proposed, but, alas, as economic men we are not only spectators on the sideline but also day-to-day participants in its constant succession of change and self-adjustment. Although losses of jobs and profits due to shifting consumer demand, technological breakthroughs that displace old processes and methods, and other competitive advantages appear from a distance to be part of the normal process of economic adjustment, they do not, in many cases, appear to be such beneficent developments from the viewpoint of those directly affected.

SPECIAL INTEREST LEGISLATION HAS WEAKENED ECONOMY

Those who are forced to bear the burden of adjustment under this system often look for scapegoats and turn to government for relief and protection. As a result of pressure from different groups, special interest legislation has taken a heavy toll on our economic system. The Davis-Bacon Act setting a floor on wages on federally funded construction projects is a potent example of this kind of unwise interference with the market. The law was passed in the early 1930s as the economy sank into the Great Depression and was justified as necessary to keep wages from falling to dangerously low levels. There may indeed have been a rationale for such a floor at that time, but, like most special legislation, it stayed on the books long after the need had disappeared. You will recall the anguished howls that were raised when the President suspended it briefly.

As prosperity returned, the act was transformed from a basement floor to an elevator that could move in only one direction—up. The general accounting office has recently published a study of nearly $80 billion of federally supported contracts over the last decade that shows that the government paid nearly $8 billion too much because of faulty administration of this law. Not only does this represent a huge, unnecessary expense to the taxpayers, but also—more importantly—it suggests that this law has tended to lock in the highest union wage rates wherever it is applied, with a consequent spill-over effect on private construction generally.

Another example occurs in the freight transportation industry. By requiring railroads to maintain considerable excess capacity and by keeping long-haul rail freight rates inordinately high in order to keep trucking competitive, the ICC has added billions of excess dollars to the annual transportation bill of the nation.

Our current system of oil import quotas adds nearly $5 billion annually to fuel costs to the consumer and provides additional protection from the rigors of the international market to an industry which is already protected through the current system of state production controls.

Together, these two programs have gone a long way toward making the petroleum industry a government-aided cartel rather than a competitive private market.

Recently a bill was introduced to prohibit nonfarm corporations from engaging in the production of agricultural commodities. Here again is a

measure likely to do more harm than good. To attempt to restrain a trend toward the development of a technical, capital intensive industry will in the long run promote economic inefficiency and the misallocation of resources, thus exacting unnecessary costs from the consuming public.

Another measure was recently reported out from the Education and Labor Committee to raise the minimum wage from $1.60 to $2.00 per hour by the end of next year. This would increase inflationary pressures in the economy directly by adding to the wage bill of employers with large numbers of workers below the $2.00 level. Indirectly, it would encourage workers above the minimum to push for higher wages in order to maintain traditional differentials. It would also encourage employers to adopt labor-saving devices, thereby reducing the number of low-skill job opportunities available. When we already have unemployment rates above 18% for workers under 20 and as high as 30% in many ghetto areas, there is some question about the rationality of a measure that would raise those rates even higher.

Heavy-handed tampering with the market mechanism is not the solution for augmenting the income of our low-income citizens. A better answer is a system of income supplements through the President's family assistance plan.

Let me now turn briefly to two additional areas in which the private market has been seriously eroded. The first concerns the imbalance of bargaining power between employers and unions that has developed over the years in many sectors of the economy. During the last few years wage rates have been rising about 7% annually and from 10% to 12% annually in the case of new union contracts in the construction industry.

Obviously, the problem is much easier to identify than the solution. Many suggest such customary panaceas as removing the union exemption from the antitrust laws, compulsory arbitration and a national right to work law. I never cease to be amazed when businessmen and industrialists propose these measures with boundless enthusiasm as the solution to their wage problems. The point is that these proposals simply are not in the cards for the foreseeable future. The labor committees in Congress are stacked with entrenched pro-labor incumbents who are not even slightly disposed to consider these proposals, let alone act favorably upon them. If there is to be a solution—and we desperately need one—we are going to have to find a more politically realistic approach.

PRODUCTIVITY MUST BE INCREASED

In my view, the approach must center on the question of productivity. Productivity has been declining with the result that unit labor costs increased by over 5% annually. Such increases can find outlet only in higher prices or lower profits.

This problem can be dealt with partly by changes in our tax laws designed to encourage more capital formation and by modernization of industrial plant and equipment. The tax bill that was passed in the House a month ago which restored the investment tax credit and maintained the ADR (asset depreciation range) system is an important start.

However, capital investment and modernization cannot do the entire job. Most economists who have studied the problem of growth in productivity tell me that almost one-half of the historic improvement in productivity has resulted neither from new technology and investment nor from improved education and skills among the work force. Nearly 50% of that growth has come from better and more efficient organization and the combination of the factors of production—labor, machines and materials. It is that truth which makes the whole question of the proper scope of collective bargaining and the prerogative of management so important.

As you know, our basic labor law requires employers to bargain over the wages, hours and conditions of employment. If we are to have any hope of returning to a situation in which noninflationary wage settlements are possible, the key area of conditions of employment must be redefined. The essential discretion over the introduction of new technologies and methods, location of facilities, planning of the work flow, manning requirements, and all the other factors which affect the efficiency of the productive process must be restored to management.

Such changes will not be easy because they will mean the displacement of jobs and workers. We will have to be imaginative enough to devise some kind of social quid pro quo: If it is in the public interest to eliminate practices which retard productivity, it is equally within the public responsibility to help cushion the costs to those who will be required to bear them in the short term. Unless we are willing to devise some kind of adjustment assistance program to provide displaced workers with transitional income maintenance, retraining and relocation assistance, we cannot expect much cooperation in our efforts to improve the productivity and efficiency of the economy.

BASIC INDUSTRIES SUBJECT TO RIGOR MORTIS

There is one final area in which the market system has gotten out of kilter over the years—the growth of excessive concentration and rigor mortis in some of our basic industrial sectors. For instance, in some highly concentrated industries like steel, competition has reached a fairly attenuated state. As a result, performance in terms of prices, profits, growth, technological advance and innovation, and competitiveness in international markets has not been very inspiring.

In the case of steel, much of the problem stems from excessive wage demands and from the policies of foreign governments, but a good share of the blame rests with the stagnant competitive environment within the industry. How else explain the fact that all the "majors" in lockstep plowed millions of dollars into new open hearth capacity for some 10 years after the oxygen conversion process had proved to be viable and more efficient in other areas of the world? Or that most of the majors built up substantial excess rolling capacity which provided a continuing overhead drag on their cost structures? One cannot help but

conclude that if the steel industry had been structured a little more competitively, this kind of self-inflicted damage might have been a little less pervasive and severe.

We must come to grips with this problem of excess concentration and competitive rigor mortis if our private market system is to be rejuvenated.

Let me conclude by pointing out that I do not think the future of our free enterprise system is bleak despite the current fact of governmental controls. We have arrived at the current impasse because over the years too many constraints upon the natural forces of self-adjustment and equilibrium in the market system have gone on unchecked. To avoid the unhappy prospects of permanent controls, we will have to take up the urgent task of beginning to dismantle these encumbrances and to allow the forces of competition in our country to take on new vigor and new dynamism.

The task will not be easy. As a nation we have been quick to stress the virtues of a free enterprise economy in the abstract but not equally ready to forego devising special protections and exemptions from the rigors of the marketplace. In the long run we cannot have both.

If the nation as a whole is to be persuaded that a free market economy is our best hope, it is incumbent upon you to provide the leadership, the candor and the intelligence to show the way. The public will not be easily deceived by high-flown rhetoric about the virtues of competition if that admonition is meant to apply only to someone else. Consistent application of market principles will be mandatory. In many cases, this will require that benefits enjoyed by some as a result of special protection will have to be forgone. In the short run this may involve significant costs and perhaps even sacrifices, but in the long run these changes will be well worth the price for the alternative is a government-run economy that will in the end impose far greater and more onerous burdens upon us all.

WHY POSITIVE THINKERS GET POSITIVE RESULTS

by DR. NORMAN VINCENT PEALE, *Pastor*
Marble Collegiate Church
New York, N. Y.

ONE REASON POSITIVE thinkers get positive results is that the positive thinker is a rare breed of man in that he is not afraid of a problem. As a matter of fact, he finds a problem exciting. He delights in taking hold of a tough, knotty problem and ripping it apart and putting it together again in the right manner.

As I go up and down the country meeting people everywhere, I have come to the conclusion that this phenomenon known as a problem is not the most popular in the land of the free and the home of the brave. Indeed, a great many people in talking to me about problems always seem to imply that a problem is inherently bad, whereas, on the contrary, if they were more philosophical, they would know that a problem can be inherently good.

When the good Lord wants to give you one of the great values in this life, how does he go about doing it? Does he wrap it up in a sophisticated package and hand it to you on a silver platter? Not at all. He is more astute and subtle than that. He buries it in the heart of a great, big, tough problem and watches you grow bigger as you take it apart and find what you might call the pearl of great price.

Many people say to me, "Wouldn't life be simply wonderful if we had fewer problems, or easier problems, or, better still, no problems whatsoever." May I ask you honestly, Would you and I be better off if we had fewer problems, or easier problems, or no problems whatsoever?

Problems constitute a sign of life. Indeed, I would go so far as to say that the more problems you have, the more alive you are. The man who has 10 good, tough, man-sized problems, is twice as alive as the poor, miserable, apathetic character who has only five. If you here this morning have no problems at all, I warn you—you are in great jeopardy. You are on the way out, and you don't know it. I don't want to throw any sour note into the meeting, but I have to tell you that you are going to have problems until the day you die.

Since when did American philosophical thinking become so sterile

and superficial as to assume that we are supposed to live in this world without problems? Our forefathers were a great breed of men. They had problems, but did they whine and whimper and crawl through life on their hands and knees, piteously holding up their hands to some so-called benevolent government asking that they be taken care of and relieved of all their problems? Not on your life. They stood on their feet like men, and they handled those problems, and they built the greatest economy in the history of mankind.

The question is, Has the breed run out? Have we grown fat and soft, not in our stomachs but in our heads, that we should think that there is something bad about a problem.

PROBLEMS HAVE A PURPOSE

Of course the world is full of trouble. It is now; it always has been and as far as anybody alive today knows, it always will be. This is for a purpose. Did you ever look in the mirror and ask yourself why you were born? This isn't very pleasant but it's important. It seems to me that the reason the good God has us born is so that at long last He might make men of us. The only way you become a man is to struggle with tough problems. The only way you have a great country is not for it to grow soft with the government handling everything with all of us relieved of difficulties. The only way you grow a strong citizenship is by making positive thinkers out of people who know that by their own intelligence and by the help of the good God, they can solve any problem they'll ever have to face.

When you get right down to it, I don't believe anyone is mentally healthy who does not accept this philosophy of a problem. If you want to know whether you are mentally healthy—in a very simplistic way—take a piece of paper and write down your reactions the next time a tough problem hits you. If you whine and whimper under it, maybe you had better get yourself a psychiatrist. If you say, "That's tough, but I think that with the help of the good God I can handle it," you can check yourself off as mentally healthy.

At my church here in New York City, there are 15 psychiatrists on the staff. In this way, we bring together scientific medicine and scientific religion. Between the two, we get a good many people well. In our clinic, we have every known problem—worry, fear, anxiety, marital problems, juvenile problems, alcohol problems, drug problems. You name it; we have it. But what would you think is the chief problem in a scientifically, religious, psychiatrically oriented counseling clinic at the heart of America's greatest city, over a period of 25 years in which 50% of the caseload is represented by men between the ages of 25 and 45—a problem common to highly organized American men of affairs?

It is a deep, inner, haunting feeling of inadequacy—that the individual doesn't have what it takes to overcome the hazards and cope with the problems of human existence. If those percentages hold good over the rest of the population, there are hundreds of thousands of people in this country today who do not believe they are capable of dealing with the problems of our time.

HOW DO WE MEET A PROBLEM?

How, then, does one meet a problem? How do we teach those in our clinic to do this? First, we teach them a good, healthy faith in God. Anyone with faith in God is in because he can think, and that is the important thing to do. We have a great many people in our country today who do not think. They react. It is a fact known to psychology that the human mind will not function and correlate when it is hot—only when it is cool, rational and factual can you think. When a person depends positively upon his ability to think, in my humble judgment he can handle any problem in this life. There are two kinds of thinking—positive and negative. The negative thinker does a very dangerous thing. He sends out negative thoughts and activates the world around him negatively. In accordance with the law of attraction that like attracts like, if you constantly send out negative thoughts, by the very nature of the case, you tend to draw back negative results.

The positive thinker sends out positive thoughts and activates the world around him positively. On the basis of the same law of attraction, he draws back to himself positive results. The positive thinker is one who sends out positive thoughts and who thinks coolly and rationally and who has faith.

WAGE AND PRICE GUIDELINES

Moderator: WILLIAM C. PRATHER

Panelists: THOMAS A. PFEILER, JEAN G. HARTH, L. JOSEPH SALM

U. S. Savings and Loan League

Chicago, Ill.

A SPECIAL GENERAL SESSION was held on November 22, 1971, during the 79th annual convention to consider the goals and structure of the wage-price control program. In view of the transitional nature of this material due to the fact that complete regulations had not been issued, these presentations have not been included in *Annals*. A Special Management Bulletin (#131) covering the subject was sent to U. S. League members December 9, 1971.

TOPICAL FORUMS

ADVERTISING FORUM

Norman M. Jones, Fargo, N. D., presiding

CONSTRUCTIVE CRITICISM OF SAVINGS AND LOAN ADVERTISING

by William D. Tyler, Creative Consultant
New York, N. Y.

SINCE I ACCEPTED the hazardous task of critiquing your advertising, I have studied several hundred of your ads in the past six months. The result of all this is the somewhat less than brilliant observation: Your advertising, by and large, is fairly good. I could not say anything more withering if I tried. In this day when the competition for advertising attention is more fierce and formidable than ever before, that is a damning indictment. Saying that your advertising is only fairly good is almost like saying that it is going to be overlooked. Never has there been so much advertising and never before have people developed such resistance to it. So insistent, so obtrusive, so ubiquitous is advertising today that people have had to build up defenses. Otherwise they would have gone out of their collective minds.

I have directed my attention toward focusing on two goals: One is to point out the areas where I find your advertising weak. The other is to show how I would go about strengthening your advertising.

First, remember that I am conscious of the fact that you do not have the biggest advertising budgets in the world so you cannot command the services of the very top creative people and agencies in most cases. Second, keep in mind that I am not saying you are doing a bad job—just one that can be done better, and, in my opinion, must if you are to get your money back.

Let us break savings and loan advertising down into categories. The first is rate advertising which seems to be the biggest category. You do a good job of making the most of your 6% figure, but you do not go far enough with "big six." You are failing to translate that figure into human values—into what it can mean to a saver. The figure "6" is a cold figure. It is up to advertising to demonstrate and illustrate and dramatize what this figure can mean to a saver.

I have selected some rate ads that appeal to me. [*At this point, Mr. Tyler showed slides of advertising by savings and loan associations. He concluded the showing of this series by pointing out that savings and loan associations have not dramatized their competitive advantage adequately in their rate advertising. Too much has been left for the reader to fill in.*]

[In another series of slides, Mr. Tyler pointed out that it is more desirable to emphasize specific goals than platitudinous principles.]

In studying your advertising, I was astonished to find how little you were involving the community. Tie your institution in with the community and its goals as tightly as possible. Select some local project or public service and get yourself known as the backer or sponsor of that effort. Failing that, appeal to local pride in some way that stamps you as a community leader. Make people think of your institution as a public benefactor.

The category of localizing advertising to make your institution a vital part of the community brings you close to institutional advertising which is the kind used simply to impress the community. These ads I think are not worth running.

The next category is lightness, and I do not see much of it in your advertising. Here is a good example. [*A slide illustrating this category was shown.*] This is a key problem for financial institutions. The common man finds them frightening. He wants to save where he will be welcomed, not patronized. Show him an association that is human as well as big and secure, and he'll take his business there. [*A series of slides was shown at this point.*]

An effective approach which I have not yet seen is for an association to work out comparative tables—the accrual of 6% interest savings accounts versus the same amount in common stocks over the same period of time. Am I right in thinking that you will come out ahead of either the Dow-Jones industrials or the average for all big board stocks? I think I am. This is important because there is an idea abroad that stocks win out in the long pull which is a misapprehension.

Let us turn to the painful subject of premium advertising. This is painful because premiums do increase the cost of advertising. Most painful of all, they can serve just to move savings back and forth between institutions with greedy savers gathering up premiums. There is a way to use premiums that makes sense and can be profitable. Before considering this, let me show some slides illustrating effective advertising of premiums. [*Slides were shown.*] Premiums can provide that extra which will cause a customer to pick yours over other institutions.

The final category deals with the problems of special inducements which can win customers from competitors. [*Here slides illustrating the use of special inducements by associations were shown.*]

To sum up, I have faulted you for failing to dramatize, to humanize, to translate your big six into the kind of reward men and women are looking for—the chance to retire earlier, to own homes sooner. I have criticized your use of one-time premiums. I beg you to dig a little harder to come up with reasons for choosing your institution over others. My final plea is for greater friendliness in your advertising. This could be a determining factor in your tug of war with the commercial bank for the savings customer. It could be the one extra factor you supply that turns the tide in your favor. The kind of advertising that will turn the trick are those ads with gentle humor, with lightness and dignity, easy going, conversational, unself-conscious.

DIRECTORS FORUM

John H. Randolph Jr., Richmond, Va., presiding

WHAT CAN BE DONE ABOUT DECLINING URBAN AREAS?

by Floyd H. Hyde, Assistant Secretary

Department of Housing and Urban Development

Washington, D. C.

THIS HAS BEEN DUBBED the era of the insoluble. It is easy enough to make a case for that opinion. There are many problems, and when we solve some, others spring up to take their place. Complexity will get you in the end, goes the argument.

It is an ancient argument, perennially seductive, moving many to the decision that complexity must be fled for simplicity. I think the fear of complexity is an enemy. For instance, consider the city. It is certainly complex, but its problems, I am convinced, are not insoluble.

We are an urban society. In Lewis Mumford's language, the city is no longer mainly a magnet; it is a container. We are in it; it is where our problems are; it is where we must solve them. The flight to simplicity may have its attractions, but the action is in the other direction. The Bible may have begun in the garden, but it ended in the city.

I do not think this is the era of the insoluble. Declaring society an absurdity may be tempting at times; as when one realizes that this country spent $19.9 billion in 1969 on tobacco and "personal care," which includes cosmetics, perfume and underarm deodorants; but only $3.4 billion dollars on the entire HUD budget. The order of our priorities is indeed discouraging and so is our unwillingness to confront problems. Consider, for instance, the fact that lead-poisoning kills and cripples more children than did polio before the arrival of Salk vaccine; 400,000 children are poisoned annually. These and the many other examples you and I could add to the list must, I am convinced, be read as horror stories which make us angry enough to move ahead, rather than to succumb to seeming absurdity with the inevitable result of apathy and inaction.

Individually in your own communities and collectively as a business, savings and loan associations are a major factor in the production of housing. In national public policy housing has long been equated with community development. National housing programs—from the indi-

vidual homeowner mortgage insurance program to the present rather sophisticated assisted housing programs for low- and middle-income residents—constitute a major segment of HUD's urban programs.

HOUSING QUALITY RELATES TO NEIGHBORHOOD VIABILITY

Yet I think this traditional equation of community growth with housing production tends to beg some very real community development issues. After all, a community is merely a group of people living in association with one another. As such, shelter is just one of the needs of the people who make up a community. Further, we have proved again and again that the quality of shelter is directly related to the quality of many other kinds of goods and services—schools, health facilities, access to business and employment opportunities, access to consumer commodities and access to creative leisure activity. Then, too, as you need not be reminded, the quality of housing is closely related to the viability of the surrounding neighborhoods.

Although the close relationship between housing and other aspects of a healthy community seem self-evident, the federal government has not traditionally viewed the subject from this perspective. Our past national strategies have been single-shot in their approach. Housing problems were to be solved by "housing programs." Education problems, health problems, employment problems, transportation problems were all to be solved by separate "programs" bearing those labels. Clearly this fragmented approach has not solved our critical problems, in housing or any other individual area.

The contrast between the fragmented programs of the past and the series of proposals the President has put forth over the last 10 months could not be more marked. Rather than being one-shot, single-purpose programs, these offer a totally integrated approach in which federal funds will reinforce a community-level decision-making process. Let us look for a moment at how the proposals which the President has made would reshape the way in which community development problems are approached.

The first proposal made by the President focuses on the organization of the executive branch of the federal government. This reorganization plan would consolidate seven existing departments concerned with domestic programs into five departments arranged along functional lines.

Of particular interest to all of us is the creation of a Department of Community Development. Within that department will be brought together all relevant community-building tools—including special revenue-sharing programs for urban community development, rural community development and transportation. This will provide the first opportunity in the nation's history to integrate the vital resources flowing from the national government into large and small communities to achieve a balanced growth pattern.

Secondly, the President has advocated a new and global approach to planning for community development. We are now shaping the broad outlines of an overall national growth policy intended to bring future

growth in population, economic activity and resource utilization into more appropriate balance. The challenges posed by this task were summed up in a report prepared by the national goals research staff, established in the White House by the President. That report states: ". . . pursuit of a national growth policy may be characterized as both a search for coherence among the many activities of our society and a search for actions supportive of the human values and qualities which we would most hope to further."

To strengthen state and local planning capabilities and enable these levels of government to take their rightful places in shaping a national growth policy, the President has requested Congress to authorize a HUD-administered planning and management assistance program. This would make $100 million available to further state and local planning efforts.

REVENUE SHARING WILL PERMIT GREATER FLEXIBILITY

A third major category of Presidential initiatives is the series of revenue-sharing measures which will enable states and localities to administer development programs in a much more flexible and innovative way. The amount to be returned directly to state and local governments will initially be pegged at $5 billion but will grow as the federal revenue base expands. Use of the money will not be tied specifically to any particular problem area but will be determined entirely by states or localities on the basis of their own priorities.

In addition, we are seeking to bring sense out of the chaos of federal categorical grant-in-aid programs by grouping some 130 such individual, single-purpose programs into six special revenue-sharing measures. These include urban community development, rural community development, manpower training, education, transportation and law enforcement.

Under the special revenue-sharing proposal for urban community development, the present urban renewal, model cities, neighborhood facilities and rehabilitation loan programs will be folded together. Funds may be used for any of the statutory purposes of the categorical programs being folded in, including the broad purposes of the model cities program. Funds will be distributed under the urban community development program to local governments within metropolitan areas on a largely automatic basis. That distribution will be governed by a formula of need which takes into account population and poverty indices, including housing conditions and overcrowding.

In addition to the funds to be distributed on a formula basis, a small proportion of urban revenue-shared funds would be distributed by the federal government to localities with special needs or special performance capabilities and to smaller areas within and outside major metropolitan centers with problems of an essentially urban character. To ease the transition from the present programs for communities which have been receiving HUD funds but would not be eligible for formula allocations under urban development revenue-sharing, the President has asked for a special $100 million fund.

A statement of projected uses of such revenue-sharing funds will be made by the recipient locality. However, such statement will not constitute either a plan or a project application in the present sense of the terms. The community will be free to undertake its programs without further federal review either to delay or second-guess a community's decision makers. The federal government will no longer require a multitude of separate applications so cumbersome that they are not read. No longer will communities have to wait for years for a project to be approved, as has happened under current categorical programs.

While proposing this revolutionary approach to the distribution of federal resources, we are acting within the current legislative framework to bring programs together, reduce application requirements, decentralize the current federal review functions, and in other ways bring even the present set of programs more in conformance with local needs.

For instance, the Department of Housing and Urban Development already has reorganized its administrative structure to bring under the same unit of HUD the urban renewal program, model cities, water and sewer grants, open space land grants, neighborhood facilities grants, rehabilitation loans and grants, and public facilities loans.

This internal reorganization is now a fact at both the Washington and field levels. It gives HUD officials an opportunity to negotiate with local community leaders, headed by the mayor, concerning the full array of HUD community development and housing tools. This process—the annual arrangement process now being tested in a limited number of cities—provides flexibility at the local level, so that the mayor can receive the right programs in the right sequence to meet the needs that the community, not HUD, has identified as its priority needs.

As you can readily see, the sum of these proposals is not just to change the way the federal government goes about its business, but to change radically the entire approach to developmental problems. Flexible funds without tight categorical restrictions, removal of federal dictation of program design and implementation decisions, and a dramatic shift in decision-making to the state and local level all open up entirely new possibilities for encouraging balanced community growth.

As power flows out of Washington and back to state and local community leaders, you as leaders in your own communities will face many new challenges. You will be called upon to resolve many of the current issues which we have found insoluble by the categorical pigeonhole method the federal government tried in the past.

First, we have yet effectively to achieve cohesion within central city communities. There are those, including some in the real estate business, who would like to ignore the problems of the central city. They would have us recreate the walled cities of the Middle Ages, only this time the walls would be intended to protect people outside the central city boundaries, rather than inside as in medieval times. It does not take much analysis to see that this is not an effective solution. The deterioration of one part of a city—one part of our national community—cannot continue simultaneously with the security of the rest. Ironically for the advocates of the new walled cities, central city issues like crime, drug abuse and others seem to have already vaulted over city lines and now pose at least psychologically greater torment for those outside the central city than for those remaining inside.

Second, under the revitalization of local decision-making which will result from the proposals the President has made, local leaders must devise effective strategies to impact the growth process in the "outer city." The rapid urbanization of the metropolis' outer ring is creating tomorrow's cities. If this physical growth proceeds in a random or irrational fashion, it will inevitably produce tomorrow's "urban crisis." Then, too, impacting the growth of the outer city is intrinsically linked with solutions to the problems of the inner city. In fact, the two are indissolubly joined.

QUALITY OF COMMUNITY ENVIRONMENT MUST BE SOUND

Third, local leaders, acting with the support of federal resources, must ensure the quality of the community environment—fresh air, pure water and clean streets, and the economic factors which characterize a sound community environment. These include such elements as the flow of investment capital, the springs of job creation, the climate of entrepreneurial opportunity and the ways in which these factors are made available to all segments of a community's population.

These are just three of the challenges that now must be met by reinvigorated local leadership. I should like to draw attention to another dimension of the challenge to local leadership.

In the past, we have tended to draw a line in both our rhetoric and in our programs between public and private sector leadership. I submit that the advent of revenue sharing and the changes that will be brought about by the President's other proposals will show that this line is an artificial one. The provision of so-called "public services"—education, law enforcement, fire protection and the like—is largely influenced by private sector factors, such as the governmental tax base and the initiative taken by private developers. On the other hand, the forces which impinge upon private sector decision-making often arise out of public policy. Whether a neighborhood is a good place for new private investment depends upon the transportation network, the state of the educational plant and the provision of other public goods.

With the advent of revenue-sharing, the need for those both inside and outside public office to assume positions of community leadership is even more important. The local decision-making process must involve all segments of the local community. No one should either deprive himself nor be denied a voice in this dialog. Thus, the challenge is a challenge which you face both in your role as civic leaders and in your role as members of the financial community which sustains the housing industry.

Let me quote from Servan-Schreiber's *The American Challenge:* "Americans are not more intelligent than other people. Yet human factors—the ability to adapt easily, flexibility of organizations, the creative power of teamwork—are the key to their success. Beyond any single explanation, each of which has an element of truth, the secret lies in the

confidence of society in its citizens. This confidence often seems rather naive to Europeans, but America places it both in the ability of its citizens to decide for themselves, and in the capacity of their intelligence." Those are heady words, but, frankly and enthusiastically at the same time, we in Washington have no choice but to believe that there is, "out there" at the local level, both competence and the willingness to be the problem-solvers our society needs.

Finally, let me express my firm belief that not only must our cities be saved, but that they can be saved. Even though I am daily exposed to the physical and human decay in our cities, I am still one who has not lost hope. I will never be discouraged of hope in the human spirit, for the spirit and soul of man is what distinguishes him from all other kinds of life. I, for one, say that the spirit and soul of America is not dead. We can indeed offer not just hope, but we can move toward fulfilling the dreams and desires of all Americans.

WHAT THE 'DIRECT' IN DIRECTOR MEANS

by Walter E. Erikson, Partner

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ALTHOUGH THERE ARE diverse opinions on the role to be played and the function to be performed by boards of directors, it is universally agreed that election to the board is an honor, the type of recognition sought after by community and business leaders. It is also generally agreed that the role of bank director is filled with challenge, more so perhaps than most other directorships. The savings and loan and cooperative bank director, constantly and continuously, is socially, morally, economically and, in many respects, legally responsible for the satisfactory operation of his institution. In my opinion, directors of financial institutions occupy a fundamentally more important and exacting position of trust than those who direct other types of enterprise. Certainly, they are trustees of a public as well as a community interest.

A mutual institution is, of course, a corporation owned by the shareholders (or depositors in a federal association) and a corporate form that operates through representative management, making it possible for a great many shareholders to operate a business. It is impractical, however, for shareholders or depositors to conduct a business directly, nor could they do so effectively. Therefore, the power of control is exercised by the board.

More specifically, the primary obligations of the board are (1) to promote the best objectives of the institution, the business and the community, (2) to safeguard the assets and rights of the institution and (3) to account to the shareholders or depositors. How can directors best discharge these three obligations? It has been said that to define a director's job is to miss its special flavor. A director is called a director but he should not direct, at least in terms of administering or managing the institution's day-to-day operations.

I like to think of a board of directors as a cabinet of advisors who will examine many proposals with an objective and constructively critical, but not hostile attitude; and as the Supreme Court of the institution, the court of last resort to which unresolved organizational problems and policy questions are referred. This latter responsibility is one that directors seldom escape. Many critical problems can be resolved by directors through the use of effective management techniques.

EXECUTIVE, NOT DIRECTORS, MUST EXECUTE POLICY

In my judgment and in the judgment of many others, one of the most important responsibilities in the discharge of obligations of the director is the selection of competent operating management. Directors must indeed establish and direct the policies of the institution, but they also have a duty to refrain from becoming involved in the day-to-day execution of established policy. The carrying out or executing of policy set by the board is the responsibility of the full-time executive officer, and he or she has a right to adequate authority and freedom from undue interference from directors.

In view of the nature and extent of authority and responsibility that must rest with the executive officer and other top officers, they should represent the best talent available, giving consideration, of course, to the salary scale appropriate to the size of the institution and also to succession of personnel within it. Therefore, the inescapable conclusion that must logically be reached is that one of the foremost duties of a director is to select competent officers, develop an effective management team and provide for appropriate management succession. Competent management must be chosen and then allowed to manage.

Whether due to lack of complete understanding of their duties or to lack of sufficient diligence, directors sometime fall short of the performance expected of them by supervisory authorities and as required by law. On the other hand, some directors take their responsibilities so seriously that they may actually impede the success of the institution through frequent inquiries and intervention in day-to-day operations. It is incumbent on you to apply good judgment in deciding where the function of directing ends and that of implementation begins.

Often this is a most difficult distinction to make. The goal, of course, is to develop a climate where the directors and officers constitute a team. If an officer or officers tend to dominate the board, the directors have it within their power to call a halt. However, the reverse situation poses a very difficult problem for the officers. Why do we have a board of directors? Why don't we have just one director?

A director-management team must be developed which will utilize the strengths of individual directors and officers and neutralize their weaknesses. Operating management may think it knows best and it may in fact know best about a particular problem under consideration. Yet the directors with their diverse backgrounds, experiences and contacts provide an excellent reservoir of expertise in appraising management proposals. The savings and loan and co-operative bank business benefits from situations where the majority of the directorates are comprised of outside directors; that is, they are not full-time officers of the institution. Their outside point of view is important and, properly applied, can be very helpful.

The executive officer should be responsible to the board for proposing, planning, administering, coordinating and controlling the institution's activities within the scope of basic policies established and authority delegated by the board. In doing so, he is accountable for maintaining the direction and momentum of the institution toward the objectives established by the board. This is obviously a full-time effort and represents responsibilities commonly associated with the title of president. Why is it then that the title of president is bestowed only on a fraction of managing officers? I can appreciate the prestige associated with this title, but most directors are principally occupied with other interests and can spend only a limited time in the institution, certainly not full time. The managing officer has been chosen; he should be capable and one in whom the directors have confidence or they have not fulfilled their responsibility in this area. Why not give him the title of president?

Determining objectives, developing goals and establishing progressive policies and programs are the most important responsibilities in the discharge of director obligations. Rather than discuss specific areas of policymaking, I should prefer to discuss more fundamental questions to be asked and answered in establishing policy.

I am thinking of such fundamental questions as:

1. What do we seek to accomplish and why?
2. What additional services can be rendered to shareholders in the community?
3. How can present services be improved?
4. What level of income is required to pay a competitive dividend in the future?
5. What kind of community relationships is the institution seeking to establish?
6. What is our public image? Do we know in what esteem the institution is held?
7. Is our available capital being invested to produce optimum net income?
8. What is our loan-up position?
9. How does our free capital position compare to others in the business?
10. Are we trading investment securities to improve net income, reduce taxes, improve surplus; or are the securities lying in a safe deposit box gathering dust?

11. How much does the institution require in terms of liquidity funds? Is excess uninvested liquidity costing precious income?
12. Have we given indepth consideration to how participating in loans with others or selling participations to others may improve net income?
13. Have we used our line of credit with the Federal Home Loan Bank to full advantage?

A careful written response to such questions will place a spotlight on available opportunities and result in improved operations. Notice I said in writing; I believe goals, objectives, policies and programs should be set forth in writing, made available to all concerned, reviewed periodically and revised as required. In a well-managed institution it is axiomatic that well-defined goals and objectives be established. Answers to questions such as I have raised will assist in developing proper goals and objectives. For example, some kind of public relations must be a specific objective, and once the objective is clearly stated, ways to accomplish it will suggest themselves by the dozen.

In these days of mergers, the existence of the institution itself is subject to debate. Is continued independence an objective? Answers to the fundamental questions will suggest whether independence is in the best interests of the institution, the shareholders, the community, and officers and employees. Perhaps your institution cannot grow, cannot compete, cannot pay shareholders or depositors reasonable dividends or interest, cannot provide the level of service required by a community, will lag behind in the future. Perhaps merger with another institution should be seriously considered. To delay merger in such a case could not be considered an intelligent fulfillment of directorial obligations. If continued independence is an objective, then definite plans must be formulated to accomplish it.

LONG-RANGE PLANNING SHOULD BE TOTAL EFFORT

Before leaving this subject, I would be remiss if I did not mention what I consider to be one of the most common managerial mistakes, which is the absence of a long-range plan. Long-range planning is probably one of the most effective and significant management tools, and every institution, no matter how small, should project its profits and financial condition for at least a five-year period. This is really a total management effort, which in itself is an advantage; both management and directors should know what portion of the financial market the institution has enjoyed historically, how much it is presently serving, and how much can be achieved in the future.

Assuming that long-range objectives have been determined and sound policies established which are clearly understood by the director-officer team, that the institution has been endowed with competent operating management which is permitted to manage, there are still the obligations required by statute and good business pratice which must be fulfilled on a day-to-day basis. Management must do its job, and the affairs of the institution must be conducted in a safe and sound manner. This responsibility can never be delegated. How does one maintain the

measure of control and fulfill all obligations in view of the remarks made thus far? There are, in my experience, at least eight tools which should be utilized in achieving the required measure of control.

1. Progressive policies and programs in writing. This has already been discussed to a limited degree. An additional important consideration in developing policies and programs is the development and implementation of an effective system of internal check and control. Directors are not required to be expert accountants and auditors and are entitled to rely on information given them by operating management whose integrity and competency is not under question. However, directors are charged with the responsibility of providing reasonable checks and controls over day-to-day operations of the institution. The primary responsibility for safeguarding the assets of the institution and for preventing and detecting errors and fraud rests on management. That is, proper internal controls must provide the first line of defense. You cannot rely wholly on examinations and audits by supervisory authorities and independent auditors.

2. Sound and realistic patterns of organization. The score card for business is its organization chart. It tells each member of the team the position he is playing, his authority, responsibility and area of operation. To be of any value, an organization chart must be in writing, must be known, understood and followed by all officer, supervisory and clerical personnel. In order to use personnel effectively it is necessary to develop team work. Too often, responsibilities, duties and authority are assigned to individuals on an availability basis with no regard to any logical organization pattern. Such a situation creates duplication of effort, poor communications, poor morale, commingling of functions and a tendency toward empire building.

Draw up an organization chart showing clear lines of authority and responsibility. Prepare written job descriptions for each position. Most important of all, see that the organizational plan and the job descriptions are effectively implemented. An organization chart and written job descriptions are effective tools regardless of the size of your institution.

3. Constructive personnel policies and practices. In the final analysis it is through people that business objectives are accomplished. To make any organization chart live, there must be people who have the necessary talents and traits, the ability to perform and the potential to improve. The growth in the co-operative bank and savings and loan business has created a demand for experienced personnel which far exceeds the supply. One of your more important responsibilities is to develop a personnel program designed to recruit qualified personnel, properly train and develop existing personnel, motivate personnel for maximum performance, promote deserving people today and provide for succession tomorrow, and to adequately compensate personnel for services rendered, both in terms of salary and fringe benefits.

4. Written and efficient procedures. A procedure set forth in detail, step by step, is the best guide to operating personnel in the accomplishment of their tasks. It permits officers and employees to refresh their

minds and minimizes the possibility of deviation from procedures and policies established by you, the directors. Contacts with many institutions have demonstrated overwhelmingly the value of written procedures as a major step toward achieving executive effectiveness and control.

5. Budgeting. Budgets are important for the control of income and are great time-savers for the director and managing officer. The basic objectives of the budget are to coordinate the efforts of the various departments or functions in the institution, to assist in the development of sound administrative policies, and importantly, to measure overall operative effectiveness. I spoke earlier of long-range goals and policies. Financial budgets are yardsticks to measure and control short-term or step-by-step progress toward your long-range goals. They provide a plan of operation for the next year, expressed in the language of figures. Without the opportunity to compare actual performance against previously established standards approved by the board, operating management is seriously handicapped in the pursuit of its objectives, and directors lose an important element of control.

6. Systematic and sustained inspection. Directors must, of course, inspect continuously and constructively to ensure that their policies are being carried out. Effort can be evaluated in terms of whether the results are in the right quantity, of the right quality, at the right time, at the right place and at the right cost.

7. Effective internal reports. The results of the previous six points are reflected in the internal reports, or should be. If I were to name a principal deficiency in today's co-operative bank and savings and loan management, it would be in the area of internal reporting. This is true even though good reports represent one of the best ways for officers and directors to achieve a measure of control over the affairs of an institution. A good report should direct your attention to where it is most needed and to where it would be most productive. The following characteristics are inherent in good internal reporting systems:

a. Reports should be timely, brief and designed to be readily understood by the non-accountants.
b. They should provide a record of actual performance with comparative data to indicate trends.
c. Budgets and projections should be incorporated in the reports so as to permit management to measure and evaluate operating effectiveness.
d. They should be designed to point out areas where prompt corrective action is required and indicate a course of corrective action.
e. They should serve as a basis for revising projections and goals.

8. Examinations and audits. The reports on examinations and audits by the supervisory authorities and independent auditors provide directors with an important measure of control. Certainly directors cannot safely disregard comments and criticisms contained in examination and audit reports. Subsequent examinations and audits cannot be regarded as a substitute for the exercising of proper internal controls in

the actual handling of transactions. A practical system of internal control must be established and implemented to serve as the primary safeguard against irregularities and as a check on the accuracy and reliability of accounting data.

As a CPA, I can state that we do make it a practice to review your system of internal check and control and to make recommendations for improvements to the directors. Personally, my experience has proved most rewarding, since the directors and executive officers have accepted my criticisms, comments and recommendations in the spirit in which they are given. By encouraging constructive criticism, you may get a great deal more from your independent audit effort.

It is my strong feeling that you should thoroughly understand all aspects of the audit report and the reasons for any comments and recommendations. If deemed advisable, there need be no reluctance for the managing officer or the board to meet with the auditor to discuss any aspects of his audit and related reports; in fact, I would encourage such meetings and dialog.

HAVE POLICY FOR DIRECTOR RETIREMENT

Developing a director-management team effort means creating a stimulating atmosphere providing each director and officer with ample opportunity for creative contribution. This requires a supportive rather than a defensive communication atmosphere. It requires that each individual contribute fully. Directors have a duty to see that the board is composed of members who are active, enthusiastic, ethical and who constantly contribute to the success of the association. Every board needs a definite policy for the retirement of directors. Some directors do not volunteer to withdraw, in effect thus putting their personal interests ahead of the association's. I realize that the question of when is a director too old to serve is a difficult one. Chronological age is one thing, physiological age is another and mental age is still another. The ideal board should have a preponderence of neither very young nor very old members, bearing in mind the French adage—"If youth but knew, if age but could." Again, much has been written on the subject of directors' retirement, and it is generally agreed that a fixed policy is essential.

I can think of few callings in public or private life that demand a greater combination of ability and virtue than that required of a savings and loan director. Someone once said that a bank director is a man who is 50% economist, 50% accountant, 50% management consultant, 50% philosopher, 50% behavioral scientist and 50% salesman. When these percentages are added together, it will be found that they total 300% indicating that yours is more than a man-sized job.

I congratulate you on being directors, it is an honor, a source of personal satisfaction to you and a challenging responsibility. If I have been successful in providing you with just a few answers to the question which I hope you ask yourself frequently, and that is "How can I be a better director and better serve my institution?" then I am most pleased.

IMPLICATIONS OF ELECTRONIC FUNDS TRANSFER SYSTEM

by Roy A. Blount, President
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WHILE THE TITLE OF THE TALK does describe the subject accurately, I want to talk about money. Money is the cash in your pocket. Money involves the checkbook your wife uses to shop. Money encompasses the bank credit or charge card you carry in your wallet. To serve its purpose, money must change hands, must be moved around. I want to discuss the movement, the transfer, of money by electronic means. The purpose is to suggest implications of these electronic developments for the savings and loan business and to alert you to responses which may arise or be forced upon you.

There has been a great deal of discussion of money and money-paying systems in recent years. Only within the last year or so has the situation cleared enough to reveal what the future may hold in the area of payment systems.

Plans have been completed to test a paperless funds transfer system in California and a number of other major areas across the country. These plans have been given a name, SCOPE, which stands for Special Committee on Paperless Entries. Through it participating banks ultimately will exchange payments, that is, money, electronically—without paper.

In a second development, the Monetary and Payment System Planning Committee—MAPS—of the American Bankers Association has concluded that the commercial banking system must develop and promote a new approach to the transfer of funds if the banking business is to remain competitive. Although a number of suggestions have been offered by the MAPS Committee, the one given top priority is the development of preauthorized and paperless payment systems.

Third, the Federal Reserve Board has issued a policy statement calling for basic changes in the nation's system of handling money payments. Only recently the Fed expanded its nationwide communications network for free wire transfers of payments in amounts of $1,000 or more. This opened the way for any business or individual anywhere in the country to make quick payment at no or low cost of any amount of $1,000 or more. In other words, it permits the buyer to provide the seller with the immediate use of funds. The savings and loan business and the U. S. League have not been idle as these commercial bank activities have unfolded.

In 1968 when Congress substantially amended the savings and loan

law a provision was inserted to the effect that savings account withdrawals could be effected by nontransferable orders or authorizations. That provision was the legal basis for the third party transfer regulation which was issued and then withdrawn last year, presumably because of Federal Reserve and commercial bank pressures.

PAYMENT SYSTEMS FOR SAVINGS AND LOANS

A few savings and loan associations have experimented with new types of payment systems. One goes by the name of "Pachek" and another by "Sav'r Spend." As I mentioned, the banks have suggested concentration on preauthorized payments. In this connection a most important concept that has been developed for savings associations is Tran$matic Systems which is a preauthorized payment system now operating successfully in our business.

The U. S. League has created a special committee to study thoroughly and objectively this whole area. I am privileged to be chairman of this committee. Our study group is working with a small but highly qualified faculty group from Northwestern University, Evanston, Ill. The Northwestern team has been working on the topic since midyear.

Why all this activity? What is wrong with our present payment system? What has prompted commercial banks to move in these new directions? There are several answers to these questions.

First, as might be expected, competition is one element. Each individual bank's desire to improve its services for its customers has generated some of the impetus toward change in the funds transfer system.

A second reason has been the development of technological "hardware" and "software"—machines, systems, relay networks—which have the capability of effecting vast changes in the way money is handled today.

The most important reason for this activity, however, is one which might not be readily apparent to anyone but a commercial banker. Simply stated, the present payment system depends primarily on checks, and the American economy has become so accustomed to writing checks that it has created a glut of paper. Last year some 22 billion checks were written. The Federal Reserve estimates that 435 million are written each week, more than two for each and every individual in this country. More importantly, those statistics only relate to today's check volume. All indications are that these numbers will double by 1980 unless some basic changes in the system are effected.

The writing of a check is only the first step in a long, complicated and expensive process of transferring funds from the check writer, the payor, to the recipient, the payee. Consider, for example, how a check written to a merchant here in New York will eventually find its way back to you in your monthly statement. It will be handled by the shopkeeper and deposited in his bank. From there, his bank may forward it to its correspondent bank where it will be handled again. The correspondent will probably send it through its Federal Reserve bank where it will be handled again. The Federal Reserve will send it to your Federal Reserve bank which in turn will send it, perhaps again through a correspondent, to your bank. It all adds up to a costly and time-consuming process. The delay between the time the check is written and the shopkeeper gets credit for it and the time when your account will be debited in your home town gives rise to "float"—a situation which is greatly disturbing to the Federal Reserve in terms of regulating the money supply.

How costly is the present, paper-oriented checking system? Perhaps a few statistics will put this in perspective. The Federal Reserve collects thorough cost analysis figures on its member banks. The average "small" bank is likely to have $10 million in demand deposits subject to withdrawal or deposit by check. It is also likely to have $12 million in time deposits, that is, passbook and certificate savings accounts. To handle the normal volume of transactions for $12 million in time deposits, this small bank will need less than four processing people. In order to handle the volume of transactions for the lesser, $10 million, in demand deposits, however, the bank will need 23 processing personnel. Almost six times as many people are needed to handle a lesser amount of money. The ratios are not substantially different for large banks. Thus the paper check transfer system is highly labor intensive. Just as it is for a savings association, the cost of labor is a commercial bank's greatest operating expense.

Faced with an increasing volume of checks being written and higher labor costs, seemingly the banks could mechanize more thoroughly the handling of these individual pieces of paper. Unfortunately, the mechanization of check handling seems to have gone about as far as it can. The MICR encoding system appears to be the ultimate in mechanization. It has been in effect for a number of years. Those little oddly shaped numerical characters located on the lower left-hand corner of the check have permitted the banks to handle more effectively a greater volume of paper. The ideal the banks envision actually will do away with paper all together. At its ultimate it would be possible for you to sit at home and by use of the telephone effect instantaneous payment of, for example, your telephone bill so that your account would be debited and the phone company's credited—all through electronic impulses.

'CHECKLESS, CASHLESS SOCIETY' NOT HERE YET

These sophisticated concepts have generated many lengthy discussions of the "checkless, cashless society." Despite this, it is fairly well agreed by all observers that the implementation of such a system is a long way off. Despite the problems the banks are having in handling the paper check, a special study sponsored by the American Bankers Association indicates that the present system can survive through the rest of this decade. This and other studies also generally conclude that the evolving funds transfer system probably will be, for a long time, a hybrid—a combination of paper and electronic systems.

What does all this mean to the savings and loan association? Money, of course, is our stock in trade, our product. We buy it from our sav-

ers and sell it to our borrowers. The present structure of our payments system has enabled us to get money from our customers. If our business is to survive and prosper we must make certain that any future payment system does not put us at a competitive disadvantage—or even exclude us—from continuing to accumulate the savings of the public. The commercial banks, in a sense, now "own" or at least administer the present funds transfer system. It is they who are seeking the changes and, as might well be expected, their focus from a competitive viewpoint is far different from ours. This was made patently clear in the ABA MAPS study which expressed considerable concern over our business' third party transfer power.

Let me give you an example of how one of the suggested approaches to the new funds transfer system could have serious negative implications for the savings and loan business. Let us look at the SCOPE project. Individual commercial banks already prepare payrolls for many business organizations. They may either send checks to the employees or automatically deposit their pay in their checking account if the account is at the particular bank. As an incentive to the employer and employee to do business with them the bank often offers "free" checking accounts. If all employees open a checking account at the bank preparing the payroll then no checks, no pieces of paper, have to be created by the bank. It merely credits each employee's account with the amount of his net wages.

But not all employees, of course, use the same bank. Here is where SCOPE enters. Now the SCOPE system uses magnetic tapes but ultimately will use electronics to distribute payrolls to any number of banks. Instead of a paycheck a paperless credit to the employee's account at his bank will be generated. SCOPE will save time and cost for the bank and employee involved and will give instant availability of his salary to the employee on payday. Since paychecks account for some 12% of all checks written in this country, the ability of the commercial banking system to develop automatic payroll deposits will go far toward reducing its paper burden. Not to be overlooked is the fact that some 70% of the families in this country have checking accounts and are familiar with how they work.

SCOPE OFFERS PREAUTHORIZED PAYMENTS

Single deposit payroll is but one aspect of the SCOPE project. The other is the concept of preauthorized payments for customers. This involves authorization given to the bank by the depositor to pay his bills for him at a predetermined time. Such an arrangement will work best with bills that are the same size and which must be paid on a regular schedule, for example, a mortgage payment. The customer signs a form preauthorizing the bank to debit his account each month. Acting on this authority the bank debits his account and credits the account of the lender. Again, this will be a paperless entry, since the employee's creditors may have their deposit accounts at other banks. The SCOPE project ultimately envisions an electronic interchange through a local clearing house arrangement. Use of magnetic tapes will be the first step

in the evolutionary process.

What are the implications for savings associations? First, the employee will never see a paycheck so that eliminates one opportunity for a savings association to be of service to him by cashing his check, accepting his mortgage payment or adding to his savings account. Second, banks intend to keep the preauthorized procedure within their own institutions. The borrower who wants to preauthorize his mortgage payment will have to sign the authorization right at the bank. Can you see how easy it will be for the bank officer to suggest to his depositor that a preauthorized monthly addition to his savings account at the commercial bank is a good idea? In a nutshell, the heart of the competitive fight is for the customer's dollars, his money. A system which permits the banks to get to the customer first at the time of deposit and at the time of payment will give them a powerful edge over savings and loans.

This is the description of one approach the banks have adopted or are adopting. It will be interesting to see what actually develops. The typical customer likes to play the "float." He may welcome the thought of having his paycheck instantaneously available to him by automatic deposit to his checking account. On the other hand he may well prefer to exercise control over his payments, particularly where they may be variable in amount or in order to make certain he does not overdraw his account.

'SUPER CHECK' IS NEW GIMMICK

Some banks have been involved in a number of other ideas for altering or eliminating the paper check system. There is, for example, the "super check" which is one check with a list of different payees imprinted on it. The customer merely indicates the amount, if any, to be paid to the payees, totals it up and sends it to the bank. The bank distributes the amounts—with all the paperwork—if the payee is a customer. There has been talk of developing a system whereby cancelled checks would not be returned to the writer. Another "bank of first deposit" scheme has been suggested. Here the paper check would stop at the first bank, and magnetic tape or electronic impulses would transfer the funds from that point.

Not to be overlooked in all of this too is the concept of the bank charge card. Up to now this commercial bank service actually has created a whole new paperwork system. The merchant imprints a sales slip, the customer receives a copy immediately and generally another copy when the bill is received. Then a check has to be written to pay for the items charged.

The banks see the credit card as an important part of the evolving funds transfer system. First and foremost, bank cards have put "plastics" in the hands of millions of American people. It is generally agreed that some similar device will be an important element in the evolving system. An experiment now being conducted in several parts of the country illustrates this fact. In Upper Arlington, Ohio, a suburb of Columbus, residents of that community now can go into their grocery stores and other shops, make their purchases and merely hand the sales

clerk their BankAmericard. The clerk inserts the card in a special terminal and dials some numbers on an attached telephone. A computer reads the card and the clerk hears a computer voice which tells him whether or not the purchase can be effected. If it can, the customer walks out of the store with the goods, having had his credit card account charged and the vendor's deposit account credited, all electronically. At this point the customer is merely adding to his outstanding balances under the bank charge plan. It is easy to see how simple it ultimately could be for the transfer to be made from his checking account. Even with this system, the purchaser only writes one check at the end of the month for the total amount charged against his card plan. If he wants to defer a portion of the payment he can do so by paying a finance charge for this privilege.

The Upper Arlington experiment is being duplicated in several other parts of the country. These are local experiments. The organization which handles the distribution of BankAmericard across the nation, however, is thinking bigger. It is about to engage in a nationwide program which illustrates in some respects the far-reaching implications of electronic funds transfers. The BankAmericard project will ultimately permit the card holder to go anywhere in the nation and yet by electronic means permit the local merchant to verify the authenticity of the card and get an authorization to effect the transaction in a matter of seconds through a nation wide interconnected system of computerized authorization centers. This represents an electronic approach to the handling of bank charge cards. Again, it is easy to see the parallels that exist between these plans and checking accounts.

TRAN$MATIC SYSTEM BEING USED

Earlier I said that the savings and loan business had also begun some activity in the funds transfer area. I mentioned the basic authority granted by Congress in 1968 and the special committee and study group which is now working. More importantly, I would like to describe briefly an approach to the problem which is now being used by over 300 associations across the country. Today over 300 savings associations are processing several hundred thousand preauthorized checks each month using the Tran$matic Systems approach. Tran$matic is a program which makes use of a customer's present checking account for preauthorized loan payments and savings additions. On the loan side the customer simply authorizes the association to draw a check on his account each month for the amount of his loan payment. The customer also authorizes the bank to honor such checks drawn by the savings association. The checks themselves are encoded in an identical manner to those that the borrower has in his checkbook. The institution which draws the check forwards it to the bank, and the cancelled check is returned to the borrower with his monthly statement. Over 6,000 banks across the country are now accepting these preauthorized checks.

For several reasons the importance of Tran$matic to the business cannot be overlooked. First, it is an answer to the commercial banks' express drive on preauthorized payments. Second, associations using Tran$matic have learned that it does work. Borrowers are willing to preauthorize payments, and a growing number of savers are using the same device for monthly addition to their savings accounts. The benefits to the savings association are many and include smaller postage costs, less paperwork, more predictable cash flows. Associations are learning that introducing new services requires more than a simple statement of their availability. A service like Tran$matic has to be explained and promoted. It must be implemented by the complete staff of the institution.

Rather predictably, Tran$matic has been viewed with a jaundiced eye by some commercial banks. Not all of them have agreed to handle the preauthorized checks. It is interesting to note that the U. S. Department of Justice has become interested in incidents of commercial bank resistance and on its own is conducting an investigation of the situation.

Where will this lead? At this juncture nobody really knows. Many questions have yet to be resolved. The technology, the hardware, for accomplishing electronic funds transfer is available, but the cost is great. The commercial banks are not fully agreed as to the best approach. The variety of experiments that are presently being conducted prove that. There are also important unanswered questions with respect to the effect of these concepts on the competition between banks—particularly large versus small. There is even controversy over the activities of the Federal Reserve in this area. The MAPS study specifically points out that the bankers want to control the funds transfer system and view Federal Reserve activities as a threat to such control. The Justice Department with respect to Tran$matic indicates recognition of the fact that there are broad public interest implications involved in the development and control of funds transfer systems.

CHANGES IN SYSTEM CHALLENGE TO DIRECTORS

The thrust of my remarks is to make one salient point. Change in our payments system is occurring. Such changes could affect dramatically the operations, and even the survival, of the savings and loan business. Such change presents a tremendous opportunity and responsibility on you as directors of savings and loan associations. Our business needs new ideas, new approaches and fresh thinking on this entire topic. As I have indicated, the League is doing its part in this respect, but you directors with your broad business and personal experiences are perhaps in the best position to give us assistance. How? Do this. Think of the funds transfer system. Think of how it presently affects your personal and business life. Think of how your life would be changed if some of the sophisticated concepts I mentioned today should become a reality. Such thinking can assist our business in two ways. First, it could produce the unique new idea or suggestion which might help our business find its proper niche in the evolving funds transfer system. Second, such thinking would, I feel certain, better prepare you to evaluate, and help implement, the changes in savings associations' services which will have to come if the savings and loan business is to grow and prosper.