

**SAVINGS AND LOAN
ANNALS 1972**

**United States Savings and Loan League
111 East Wacker Drive
Chicago, Ill. 60601**

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United States Savings and Loan League



A handwritten signature in cursive script, appearing to read "Sam".

PRESIDENT

FOREWORD

So QUICKLY DO PEOPLE assimilate higher standards of achievement once they have been reached that the savings and loan business' achievements in 1972 have been taken largely in stride. The fact remains, however, that 1972 was an unbelievable year in which all the "untouchable" records of 1971 were broken. Annual net savings gains of \$33 billion, mortgage lending activity of \$51.6 billion, net addition of loans in the amount of \$32 billion — all these figures substantially exceeded year-earlier performance, notwithstanding the contrary expectations of the experts. Total association assets rose to \$244 billion, passing the life insurance companies and leaving the savings and loan business second only to commercial banks among financial institutions.

With two such years occurring back-to-back, it would be easy for savings and loan managers, supervisors and trade association leaders to relax into the euphoria of the 1950s and to assume that all the recent problems of tight money, savings competition, earnings squeeze and stagnating home building were solved. An examination of this volume of *Savings and Loan Annals*, however, will indicate that no such relaxation has occurred.

While the savings and loan business takes great satisfaction in the performance of the business during the past two years, serious long-term issues remain to be dealt with. The kind of favorable money market which the business has been enjoying could disappear almost overnight, in addition to which new technology and systems in the money transfer area threaten severe competitive problems, almost without regard to the money markets. Without question, the business has strengthened its capability to meet and deal with competitive problems; but in today's fast-changing economy, there is no room for complacency.

The attitude of confidence mixed with concern which these facts call for is reflected in the U. S. League convention sessions and committee deliberations reported in the 1972 *Annals*. It is interesting to note, for example, that of the 10 topical forums included on the 1972 convention program, four covered topics which did not receive forum attention a year earlier. This programming is indicative of the fact that the savings and loan business now operates in an environment enlarged both in size and in the depth of the concerns which it must take into consideration. We no longer receive the automatic governmental sympathy that goes to "small business" for the obvious reason that collectively we are no longer small. And we confront issues such as electronic funds transfer system restrictions or consumer protests which simply did not exist as major issues a decade ago.

Thus, the speeches and deliberations reported in this volume touch upon many concerns and trends which are critical to the well-being of the savings

and loan business: inflation, money market rates, tax law revision, financial institution restructuring, access to the electronic money transfer system, consumer protection, equal employment opportunity, land development, overbuilding, service corporation activity, branch management and many others. These subjects are dynamic, not static; today's solution of a problem is subject to revision or reversal tomorrow as the key influences which affect our business change.

CONCERN IS NOT DEFEATISM

Concern, then, is a very legitimate note for any savings and loan convention to strike, no matter how prosperous the current operations of the business may be. However, concern is something quite different from pessimism or defeatism; for that there is no call whatsoever. Shortly after the money "crunch" of 1966 it became fashionable among theoreticians to discuss whether or not there was any longer a valid role for the savings and loan business. Seemingly, the structural difficulties with which we had to cope were overwhelming and incapable of being corrected, according to one school of thought.

That point of view has been put to rout by the more recent performance of the business. Today the question being discussed is "what" the proper role of this business is, not "whether" it has one. In great part this reversal of attitude flows from outside economic events — the curtailment of inflation and the impact this has had on short-term money rates — but it also can be traced to the work done in earlier years by management, supervisors and trade association leaders. Much of today's ability to cope arises from changes instituted by those who thought carefully about what was then the future for this business and is now the present.

It is this same spirit of forward-looking concern which you will find expressed in this volume of *Annals* and which will, I am certain, keep the savings and loan business strong and able to serve the public well in future years.

JOHN P. FARRY

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GENERAL SESSIONS

PRESIDENT'S ADDRESS

by JOHN P. FARRY, *President*

United States Savings and Loan League

Albert Lea, Min.

IT IS A GREAT PLEASURE for me to appear here today and to welcome all of you to this, the largest convention in the 80-year history of the United State Savings and Loan League. We are near the end of a record year of growth, surpassing the previous record set only last year. These back-to-back records have enabled the business to approach the huge size of \$250 billion as we meet here. Assets of this business now are larger than those of the nation's life insurance companies, and we now are the second largest group of financial institutions in the United States, second only to the commercial banks.

But time will not stand still. As this record year gives way to 1973, it already is clear that the coming year will be one with major questions for the savings and loan business.

It will be a year when the Congress will decide whether or not to extend the present system of ceilings on savings deposits.

It will be a year when the Congress will consider the general issue of tax reform. It is unclear at this moment what this consideration could mean in terms of the savings and loan bad debt formula. You can bet, however, that no one at the Treasury or in the Congress is going to recommend our taxes be reduced.

It will be a year when the legislative recommendations stemming from the Hunt Commission Report will be submitted for congressional consideration.

It will be a year when electronic funds transfer systems will begin to handle corporate payrolls and recurring monthly obligations, and when, we hope, the savings and loan business will make major progress toward becoming part of the electronic funds transfer system.

It will be a year when the Congress will again consider some of the legislative questions that remain unsolved from the current year, in particular the questions involving closing costs, settlement procedures and interest on escrow accounts.

This is quite an assortment of legislative questions for the savings and loan business, and their listing makes it clear that 1973 will be a pivotal

year — perhaps one of several pivotal years just ahead.

Obviously, these questions will receive considerable attention at this convention. In a speech to the convention tomorrow, Norman Strunk will discuss the potential revolution in operations that faces the business as a consequence of electronic funds transfers. The questions of major legislative interest will be discussed at meetings of League committees and the board of directors during the convention, and they will be reviewed at a legislative panel Thursday morning.

IMPACT ON LONG-TERM DIRECTION

The underlying importance of 1973 is this: It will see an intensification of efforts on the part of the savings and loan business to decide its future—to decide where we want to go and how we want to get there.

Of course, soul searching in the savings and loan business is nothing new. We have been in a process of rigorous self-examination ever since 1966 when we faced the first tight money crunch and first round of disintermediation. With the election behind us, I recognize that there is some apprehension at this convention that the Federal Reserve will tighten up just as it did after the election of four years ago. There is concern that, with huge government and credit demands, 1973 will see a repetition of the dreary disintermediation experience of 1966 and 1969.

Certainly, we live in an unpredictable age. It had been expected that the winding down of the Vietnamese War would mean a winding down of huge federal budget deficits and more progress in slowing inflation. But these expectations have not been realized so far. The cost of living continues to march upward. Cost of living increases have become so common a part of American life that they have even been built into our social security system. Obviously, we have a considerable distance to go in the fight against inflation.

As the Federal Reserve ponders its future policies, we hope it will recall that tight money did not stop inflation in either 1966 or 1969. Cooperation between the administration and the Congress on fiscal policy is essential to avoiding excessive reliance on monetary policy. Rather than travel down the tight money road again, certainly it would appear far more desirable to continue with a better mix of fiscal and monetary policies, and with some form of wage and price restraints until further progress is made in the battle against rising prices. Tight money and rising interest rates would aggravate the problem by accelerating the rate of increase in the price index, and thereby encouraging — if not necessitating — wage agreements well above the standards sought by the Pay Board.

HOUSING MORTGAGE MARKET PROSPECTS GOOD

In light of the improved prospects for peace and the reduced inflationary expectations which would flow from peace, I find it difficult to believe that the Federal Reserve will resort once again to a policy of excessively tight money. For this reason I look forward with some confidence to a reasonably favorable flow of savings into our institutions in 1973. This means that there should continue to be an ample supply of funds for American families wishing to buy homes and become homeowners.

Of course, the prospects for the housing and mortgage markets are bolstered still further by the progress that has been made in recent years in providing greater strength and flexibility for the residential mortgage market.

Six years ago, the savings and loan business began mapping and executing a strategy to make the business less vulnerable to chronic inflation. The impetus for greater flexibility in operations came from the business, from the Federal Home Loan Bank Board, past and present, and of course, from the United States Congress. These joint efforts have enabled the business to diversify our liabilities, broaden our lending activities and develop new sources of support for conventionally and federally underwritten loans.

No one would suggest that these actions necessarily provide full protection for the housing markets against new periods of credit stringency. Still, no one should feel that the mortgage markets are not a great deal more versatile and flexible than they were six years ago. In fact, the institutional restructuring of the mortgage market has been so massive in recent years that some savings and loan associations are concerned that these efforts to help "save" the mortgage market ultimately may produce significant new competition in the mortgage market.

In any case, the outlook in 1973 for the supply of mortgage funds is quite favorable. Indeed, there are questions in the minds of many here that the supply of funds may be greater than the demand for mortgage loans. This is not a new concern, and it certainly has been apparent to me as I have traveled around the country. Savings and loan executives are a conservative breed, and we are trying to make sure that the easy availability of funds does not create over-built situations, with a subsequent wave of foreclosures and losses that would put pressure on reserves.

While there is always some risk of overbuilding and lax lending practices, there so far is no evidence to indicate that this is a problem of any real magnitude in the single-family house field, although there are scattered reports of apartment overbuilding. One of the pleasant surprises of the past year has been the astonishing strength of the housing market. Loan commitments today remain at high levels, and this portends a continued high rate of building and heavy demands for mortgage credit.

STRONGER HOUSEHOLD FORMATION TREND

Clearly, most of us have underestimated the strength of the general housing market, and this miscalculation has been good news for everyone connected with the housing industry. The reason for the miscalculation is found in the statistics which were published recently by the Department of Commerce and which the U.S. League's Research Department passed along to me. Essentially, these figures show that instead of a growth in new household formations of 1.3 to 1.5 million as projected earlier, household formations actually increased almost 1.9 million between the spring of 1971 and the spring of 1972. This explains in great part the continuing explosion in demand for housing and housing credit in most parts of the country. On the basis of the revised government figures, there would seem to be good reason to believe that a high level of housing

and real estate activity will continue at least well into 1973, with a demand for mortgage credit roughly the same in magnitude as it has been in the past year.

This forecast should hold up even with a slight easing in housing starts that is expected by some analysts. If this easing materializes, it should not affect mortgage demand at our institutions to any appreciable degree. Many of this year's housing starts will become completions next year, and savings and loan associations will provide the bulk of the financing for the newly completed units. They also will provide the bulk of loans on existing homes that will be sold by people moving into the recently completed single-family homes and apartments. Therefore, mortgage lending by our institutions should be sustained even in the face of some decline in new starts.

When you couple the favorable outlook for savings with the continued heavy demand for residential mortgage credit, you have a situation where the savings and loan business appears likely to maintain healthy and strong growth, and with sufficient earnings to continue to build our reserves.

SPECIALIZATION STILL NEEDED

The picture I have drawn is one of basic optimism for the savings and loan business, and one of basic confidence that our institutions will continue to grow and progress. It is a kind of picture which strongly suggests, at least to me, that while our business should continue to seek change and greater flexibility in the period just ahead, there is no reason for this business not to retain a high degree of specialization.

There is a good deal of restlessness in the savings and loan business, and a feeling in some quarters that major changes in the structure of the institutions are essential.

But the scoreboard shows that we have moved through some very stormy periods in the past six years, and that we still have grown from roughly \$130 billion at the end of 1965 to nearly \$250 billion today.

The scoreboard shows that we have returned to the position in the savings market that we held before the two rounds of tight money and disintermediation.

It shows that we now serve a much larger share of the residential mortgage market than we did six years ago.

It shows a substantially improved interest earnings picture, as well as substantial payments of income tax to the U.S. Treasury.

Finally, the scoreboard demonstrates the viability and effectiveness of institutions across the land, and the ability of institutions of all sizes to participate in this progress. Unlike the commercial banking business, there has not been an undue asset concentration among a few dozen institutions, and all size associations should be reassured by their satisfactory adjustment to the major changes and challenges which have characterized recent years.

Despite the present healthy state of our business, this certainly is no time for complacency. It is obvious that some further changes and innovations are required. It is imperative, for example, that we gain a workable

and useful role in the electronic funds transfer system. While it is still unclear what mechanism will be developed for this purpose, it is essential that we have authority to have payroll items deposited in our institutions in addition, of course, to the ability to draw on deposits in banks for mortgage payments, systematic savings additions and other purposes.

We also urge that the Congress continue to maintain a system of interest rate ceilings on savings deposits. This business should not be expected to compete on equal footing in the matter of savings rates with a banking business that has vastly greater lending and investment authorities, and which controls and influences the destinies of countless commercial and industrial enterprises through its holding companies and trust departments.

The long-range question we must work to resolve is the direction in which our business will move in the years ahead. It seems to me that while retaining a high degree of specialization, we may wish to think seriously about acquiring some more flexibility on both the asset and liability sides of our business, and perhaps moving closer to the "family financial center" concept. This would strengthen our ties to our customers as the electronic funds transfer system expands. It also would free us from exclusive reliance on residential mortgage credit as a source of new loan business. And, it would be very much in the tradition of the savings and loan association as a "people oriented" institution.

There are many in the business who see our future as "full service real estate lenders." There are many who see it as "family financial centers." It will be recalled that the special U.S. League study committees headed by Hans Gehrke and Dick Gilbert saw no reason for the business to make a flat choice of either road to follow. Nor do I. There is no reason, it seems to me, for the business to be forced to take one path at the expense of the other. On the contrary, there should be enough flexibility to permit associations to determine their future operations in the light of variations in management philosophy and experience, and differences in competitive factors and needs of the markets they serve.

NEITHER CORPORATE FORM SUPERIOR

Inevitably, in the discussion of changing the savings and loan business, there has been a great deal of attention given to the subject of corporate form — and specifically in recent times whether mutual institutions should be permitted to convert to a stock form under a federal law, or under laws now authorized in 22 states. Without taking a position one way or another on the general question of conversions, it seems to me to be important to emphasize that the mutual and stock associations have worked side-by-side for many years, and that both have made contributions to the ability of this business to serve the American people. Because of this record of accomplishment, I would hope that no one in the business would approach this question with the attitude that one corporate form or another is inherently superior to the other. In fact, there is little in the record books to justify such a view.

As all of you know, the Federal Home Loan Bank Board has proposed a time-table for final promulgation of rules and procedures governing conversions. While leading members of Congress have not taken sides

one way or another on conversions, they have made it unmistakably clear that the Congress proposes to interest itself in this question to a substantial degree. While our committees and the League board of directors have yet to discuss this matter at this convention, I want to say from my personal point of view — the president is entitled to that, I believe — that I welcome this congressional interest. I regard it as completely appropriate in light of the fact that the major laws underpinning the modern American savings and loan structure — and responsible for much of our progress — were created by the United States Congress.

In my view, it is fitting that the Congress give this question full and adequate study to make sure that the rights of mutual depositors are protected, that prospective investors are fully informed, and that the flow of funds to the housing markets remains unimpaired. In my personal judgment, it would be a major mistake for the Board to move ahead with a conversion program without this type of congressional consideration and without congressional concurrence.

I am completely confident that — however this issue is finally resolved — careful congressional consideration also would help produce the development of procedures sought by the United States League to assure continuity for management and directors, to avoid disruptive “shock waves” for associations not wishing to convert, and the shifting of accounts from converted associations to other institutions in the hope of speculative advantage. In my view, these are key objectives we *must* continue to try to achieve.

What I have attempted to do today is to review briefly the questions that are before the business. I have suggested that I feel optimistic about the prospects for the business in the coming year. I also have attempted to suggest that we have made sufficient progress during the past six years that we do not need to make — and should not make — decisions about the long-term destiny of the business in a rash or hasty manner. Thanks to this progress, we have the luxury, so to speak, of being able to make these determinations under less pressure than at any time in recent years.

What has made the savings and loan business great? Its motivation has been to help housing and homeownership. It has functioned as a people-oriented and community-oriented business, which takes the funds of people in a community and re-lends these funds to others, for the benefit of both savers and borrowers, and to build better communities.

Now I think it is obvious that the Congress — which has done so much to aid this business over the years — is willing to help it secure the powers necessary to remain viable and moving forward. But the Congress is not interested in advancing the savings and loan business solely for the sake of the business. It is concerned primarily with the interests of the homeowner and potential home buyer. Thus, the decisions we make for the future of the business must be vested heavily with considerations of the public interest.

Considerations of this kind have dominated the history of the savings and loan business and opened the way for unprecedented growth and progress. They provide the guideposts for even more progress tomorrow and in the years to come.

A LOOK AT THE 93RD CONGRESS

by the HON. WRIGHT PATMAN

United States Congressman, Chairman

House Banking and Currency Committee

Texarkana, Tex.

YOUR BUSINESS IS NOW A LEADER in every sense of the word. Anyone who has been watching national television commercials knows that your business has more than \$200 billion in assets nationwide. This is a great deal of money, and it represents power. It also represents responsibility—public responsibility.

Housing continues to boom. We will end the year well over the 2 million mark for new housing starts, possibly as high as 2.4 million. The experts tell us that there will be a decline next year, but by historic standards it should still be a good year.

This increased home building rate has placed new demands on the available sources of mortgage credit, and it is my understanding that the demand for home mortgages will top \$64 billion before this year is out. This is a sizable jump from 1971 which fell just short of \$50 billion in mortgages. The forecasters indicate that the demand for mortgage money will be around \$60 billion next year.

Such heavy demand for credit indicates very clearly the need to keep money flowing into the housing market. It establishes the need to make certain that savings and loan associations, the nation's prime supplier of mortgage credit, get their fair share of available money.

We still have a very hazy and confusing set of monetary policies at work in Washington. There is still much timidity about putting the clamps on further interest rate increases and a great deal of confusion about the administration's plans to use monetary policy as a weapon against any future increases in the rate of inflation. The Federal Reserve Board still has its misguided theorists who believe that inflation can be combatted with high interest rates and tight money. These people must be watched closely in the coming months. With unemployment still hanging between 5.5% and 6%, i.e., 5 million people without jobs, it would be foolhardy for anyone to tighten up the money supply and to force another round of increases in interest rates.

The interest rate picture is not good. The prime rate has been moving up and appears likely to break the 6% mark at any moment. In fact, it appears that the big banks restrained themselves in the latter part of October to avoid embarrassing the President with a large increase in the prime rate just before the election. This restraint is now off, and it is my guess that the banks will be grabbing for more very soon.

Other interest rates are far too high. After the fantastic increases of 1969 and 1970, we allowed these rates to level off and stabilize at levels much too high to fuel the kind of expansion the nation needs. Many, if not most, of the interest rates are only about a point below the historic highs reached in the 1969-70 period. Mortgage rates nationwide are still above 7½% and in some areas the effective rate hangs around 8%. This is too high to allow low and moderate income families to afford new houses. It is too high to encourage builders to construct low income housing. Today we are getting more and more housing for the affluent, and little is being done for the lower income groups, largely because of the fantastically high price of money.

Thus, we must do something about high interest rates. We cannot accept 7½% mortgages as normal. We need to push monetary policy so we can return to the day of mortgage rates between 5% and 6%. A reduction to this level could give millions of families a fair chance to own a home.

We need interest rate reductions across the board. We need to make it cheaper for local governments, school districts and others to borrow. We need much lower rates on corporate bonds so that people can be put to work. At the federal level, we certainly need a reduction in the massive interest rate payments on the federal debt. These payments are already running at the annual rate of \$21 billion and I suspect that the new budget will show even bigger increases in this outlay.

NEEDED HOUSING LEGISLATION

Many of you were concerned that the Congress did not get a housing bill through in the last session. When the bill was finally reported by the Banking and Currency Committee, it was more than 400 pages long and contained provisions on every imaginable aspect of urban development and housing laws. The Rules Committee did not clear this legislation for floor action, and it became necessary for us to seek a simple extension of the basic housing authorities until June 30, 1973.

The housing bill represented many weeks and months of work in the committee, and I regret that we were unable to get passage before the Congress adjourned. There are some fundamental problems in housing legislation which have been ignored in recent years. The public and Congress are becoming more aware of the issues involved in these massive housing and urban programs and, and they are no longer willing to accept them blindly.

In the future, these issues will have to be discussed fully and the questions answered—answered in down-to-earth language, and not in the bureaucratic mumbo-jumbo which surrounds the programs carried out by the Department of Housing and Urban Development. The committee will have to find the means of developing a proper public understanding

of what is involved in these housing programs, and it will have to draft legislation which goes right to the point. This legislation will have to be based on the needs of the communities and the recipients of the housing, rather than on the needs of the industries which profit from these programs.

We must take a hard-nosed approach to these programs, eliminating the fat where it is possible and, by all means, exposing the scandals as they occur. Everyone wants housing, but this desire cannot be an excuse for papering over scandals and the operations of the fast-buck artists who have invaded such programs as FHA 235 and 236. Housing legislation will get much smoother sailing once the public and the Congress become convinced that we are performing a thorough audit of all housing programs and all operations of the Department of Housing and Urban Development.

It has been a mistake, in my opinion, to try to push housing and rural and urban development legislation in a single massive omnibus package. It is too much to expect the members of the House to pick up a 400 page bill and grasp all of its ramifications after only a few hours debate. In the future, I hope housing legislation is broken down into manageable subject areas so that it can be fully studied and considered not only by the Banking and Currency Committee but by the entire Congress.

OMNIBUS FEATURE DEADLOCKS HOUSING BILLS

It is difficult at this point, to set up a time schedule for housing legislation in the next Congress. There are undoubtedly varying views on the committee and we will just have to wait and see how the situation stacks up after the Congress is organized. It is a fact, however, that the housing programs expire June 30, and something will have to be done prior to this date. This could be another extension of existing programs, or it could be a more comprehensive legislative effort.

In recent years, there has been a tendency to try to include bank and savings and loan regulatory matters in omnibus housing bills. This, I am convinced, has been a mistake, and I think it is much better if the purely financial regulatory matters are kept separate from housing and urban and rural development legislation. I recommend this just as a matter of good strategy.

Without question, the Banking and Currency Committee has a heavy workload on tap in the new Congress. Undoubtedly there will be some who will be pushing the findings and recommendations of the President's Commission on Financial Structure and Regulation, the so-called Hunt Commission. This commission and its recommendations are, of course, one of President Nixon's gifts to the financial community.

HUNT COMMISSION A FAILURE

In my opinion, the Hunt Commission has confused and obscured many of the important issues that we must face on financial structure and regulation. The Hunt Commission was basically a failure. It does not appear to have gained any great support from anyone: savings and loan associations, banks or consumers. If these Hunt Commission regulations ever become law—and I do not think they will—the savings and

loan business would be placed at an even bigger competitive disadvantage than is true today.

Frankly, I would like to see the Hunt Commission report laid aside and forgotten, and the whole process started over again in open forums before the appropriate committees of the Congress. Your business, other businesses and the American public are much better served when these issues are raised in open sessions before elected representatives of the people. I do not think the interests of anyone were well served by the closed door sessions of the Hunt Commission. In any event, the Banking and Currency Committee will take a close look at any proposals which come out of this Hunt report. We are not going to allow this report or any part of it to be pushed through without allowing everyone to be fully heard.

COMPREHENSIVE INSURANCE PACKAGE DESIRABLE

The Hunt Commission notwithstanding, there is some important savings and loan legislation which I hope will have an early start in the new Congress. Most of you are familiar with legislation which would provide 100% federal insurance for the deposits of federal, state and local units of government in insured banks and insured savings and loan associations. Hearings on this matter were conducted this year, but unfortunately the committee was unable to take final action.

There is approximately \$30 billion in state and local funds deposited in the financial institutions throughout the nation. Nearly all of it is on deposit in commercial banks. In my view, there ought to be competition for these funds and they ought to be more evenly distributed among financial institutions. A provision for 100% insurance would create beneficial competition, and such insurance would force banks to start paying interest if they hoped to meet the competition. It does not make sense to allow the commercial banks to have a complete monopoly on these deposits.

If 100% insurance moves more funds into savings and loan associations, then we have helped housing. I am all in favor of that. In short, 100% deposit insurance will help local governments: They will benefit from the competition for funds through interest payments: the insurance will help the savings and loan business attract more funds; and the attraction of more funds will mean a greater flow of credit for needed housing. I predict that you will see favorable action on this provision in the next Congress.

VARIABLE INTEREST RATE AND CONVERSION CONTROVERSIAL

The 93rd Congress is almost certain to deal with two other areas of great importance to the savings and loan business: the proposals for a variable interest rate on home mortgages and for conversion of mutuals to stock companies. Both of these areas are controversial. The controversial aspects have been made more volatile by what I think are overly ambitious administrative proposals by the Federal Home Loan Bank Board. In my opinion, these issues require detailed study and open hearings in the Congress. They cannot be handled by administrative fiat.

Let us look at the variable interest rate question. Under this proposal the rate on a home mortgage would be allowed to vary with fluctuations in the cost of long-term borrowing. There are some very real problems with variable interest rates. I am fearful that they will shift the basic burden, and all the risk, from the lender to the home buyer. When the money market goes haywire, as it has been known to do, it appears that home buyers would take the entire brunt under a variable interest rate system.

Let me give you some examples: A person who took out a 30-year, \$25,000 mortgage in 1965 would have paid, as of July 1972, \$1,630 more under a variable interest rate. For a 1966 homebuyer with the same loan and terms, the extra payments would have been \$1,200. Anyone who obtained a variable rate, 30-year, \$25,000 mortgage in 1967 would have paid \$1,020 more than with a fixed rate mortgage loan.

The variable rate scheme also creates potential danger to the savings and loan business. Under such a program, it is possible that variable mortgages written when interest rates are at a particularly high point could lead to cash flow shortages if interest rates subsequently decline sharply. Also, the management of institutions might be all the more difficult and unpredictable if future rates of return on existing mortgages are uncertain. Finally, a healthy secondary mortgage market might be disrupted if the salability of mortgages becomes questionable as a result of the fact that rates are no longer fixed.

INTEREST RATES MUST BE MEASURED ACCURATELY

Before I could ever agree to a variable interest rate plan, I would need complete assurance that interest rate changes would be measured against a fair, accurate and reliable index. In addition, I would need to be assured that there would be a limit on the amount of interest rate increases and the frequency of these increases. It would also have to be demonstrated that the variable rate scheme would not create unsafe or unsound business practices on the part of savings and loan associations employing the device.

In short, I would never agree to the implementation of a variable interest rate program until it became absolutely clear that the public interest would be properly served, and that the savings and loan business would be protected. This has to be carefully considered and thoroughly aired before there can be any final legislative action. Caution is the word in this area, but I am willing to see to it that we have full-scale hearings on these questions and to give the business a chance to make its case, if a case can be made.

CONVERSION IS AN OPEN QUESTION

The same is true on the question of conversion. I am willing to hear this question out. In fact, there should be extensive hearings because the questions are sizable. The idea of conversion is obviously attractive to many associations. Many sincerely feel that this is the only ownership structure which will enable savings and loan associations to operate in the changing financial community of the 1970s. Perhaps this is so. I

really do not have the information to make a proper analysis of the claim.

Obviously, there are many problems associated with conversion. I could never favor the idea unless I were assured that there would be a definite and equitable manner to distribute stock purchase rights to the members, the present owners of the mutual savings and loan associations without giving anyone a windfall. I would also want concrete assurances that we were not setting up an ownership structure which might increase the possibility of greater concentration of financial resources in this nation. I would not want a structure that might make it easier for the big banks to move in and take over savings and loan associations around the nation. Consideration must also be given to what happens to key employees, the current leaders of this business, if we see wholesale abandonment of the mutual concept for stock ownership. The people in this business are dedicated to the basic purposes of thrift and home ownership, and I would not want to see this strength eroded by the manipulations of a handful of wealthy stockholders seeking a quick profit.

Frankly, I do not know what the final outcome of conversion legislation might be in the Congress. I am keeping an open mind on the concept. I am not committed to either side of the argument. I am willing to listen and to give everyone full hearings.

MONETARY AND GENERAL ECONOMIC POLICIES CRUCIAL

There are other major areas of interest for the savings and loan business in the 93rd Congress. For example, the law which allows flexible interest rates on savings, the so-called Regulation Q, expires, and the Congress must decide whether to renew this authority. Regulation Q, in the view of most savings and loan people, has been a bulwark against damaging outflows of funds from thrift institutions during periods of tight money. The Hunt Commission has raised new controversy about this law, and of course many bankers feel that Regulation Q should be permanently eliminated. Sometime early in the next session, the Banking and Currency Committee will have to take up these issues.

Variable interest rates, conversion, 100% public deposit insurance, Regulation Q, all of these are important issues for your business. But in the long run, monetary policy and general economic policies are really going to decide where savings and loan associations go—whether they prosper or whether they have to fight just to survive.

Unless we have stable monetary policy, and unless the people and their elected representatives have some say about these policies, we will always be in danger of new rounds of high interest rates, tight money and mis-allocation of credit. We need policies that will take into account the real needs of the people.

The savings and loan business needs to know that there will be a steady flow of savings and that there will be a stable flow of money for housing. We can assure this only if we have a monetary policy responsive to the people. In addition to your concern about the operating details of your immediate business problems, I hope you will study the broader questions of monetary policy, the Federal Reserve System and high interest rates. These issues are vitally important.

TEAPOTS ARE USED FOR TEA

by VIRGINIA ANNE TOLAR

Institute's 43rd Annual Speech Contest

First Federal Savings Association, Atlanta, Ga.

TERRY'S GRANDMOTHER HAD A TEAPOT that sat in an obscure corner of the kitchen cabinet. It was handled with great care, taken down only for the purpose of adding to or removing from its contents, and was lovingly patted as it was lifted to the back corner of the third shelf . . . just behind last year's crop of pickles, relish and chow-chow. No one remembered who chose this particular spot, but the whole family agreed that it was the perfect place for the family savings. Why they'd seen many a dream come true because of money that had been put in that teapot from time to time. Provided no one slipped any out, and provided there was no fire, and provided Grandmother's memory didn't fail her, she expected to be able to count out exactly what had been put in there, but never any more!

I first met Terry during the fall of his junior year at the state university. He was as modern and up-to-date as anyone around. He drove the brightest red, souped-up car, had an adorable blond girl friend and seemed so very ambitious and eager for life. There was absolutely no clue that he was related to the family with the teapot except for his perseverance in saving. Looking at his passbook, I could see that his account had started when he was still riding a tricycle and hating little girls. Things were a lot different for my friend, Terry. . . . He expected his savings to grow! He was coming by often now, making deposits, getting his interest posted and looking at that passbook as if every additional penny put him closer to some secret dream he was pursuing.

When the local paper revealed the picture of a lovely bride last year, we realized that Terry was married. Since his graduation from college and the acceptance of a job with East-West Airlines, Terry had saved more money than ever; and now, with the help of his new bride, saving became a family project. The baby was not expected until late spring, but already they were talking with us about setting up a trustee fund for the new baby, of saving for the baby's college education and a new car for him on his 18th birthday. It was beautiful! We were watching dreams come true for Terry and seeing him build new ones.

It has been a full year for Terry. He told us about the bonus he had gotten for coming up with a revolutionary idea for the airline industry, and it was with these funds that he purchased his first certificate. I remember his going over and over the interest rates to be sure that he was getting the absolute maximum interest for his investment.

Then there was the death of his father, a man we all loved and respected . . . and the need for immediate funds to take care of those expenditures involved. Terry was so thankful for the savings he had to fall back on.

And the baby came. With the coming of Terry Jr., our savings and loan association had a new customer (and was he cute!). His coming also brought into focus a dream of home ownership that his father had had for some time. So, for the next few weeks, while Mother carried the baby, Terry carried a roll of papers that we recognized as house plans. He was building a home, and discussing, arranging and planning with our Mr. Forsyth in the Loan Department. When the deal was consummated, we here at the savings and loan association were most pleased to see another dream come true for Terry.

Today Terry and his family live in a Cape Cod home at the end of a sunny, curving street, in a subdivision called Mt. Morey . . . the home financed through our association. Next year, he says, he'll furnish the living room and dining room just like they want it, but for now, he doesn't want to disturb his savings.

The teapot in Terry's home is used for tea. He's found a more profitable way to save and an easier way to make his dreams come true.

This is Terry's life. It's a good life . . . and our savings and loan association is so very proud to be a part of it. May we be a part of your life?

THE 1972 ELECTION AND OUR ECONOMIC FUTURE

by WALTER W. HELLER

Regents' Professor of Economics

University of Minnesota, Minneapolis, Minn.

AN EXAMINATION OF THE 1972 ELECTION and our economic future is an operation in Nixonomics and an inquiry into the economic philosophy and preferences of the reelected President. But that is only the beginning. Powerful as a president may be, he still operates within a system of political checks and balances and within crosscurrents of national and international economic forces and events that do not respond to the snap of a president's fingers; or even to the snap of the fingers of a powerful chairman of the Banking and Currency Committee. So in assessing the broad economic outlook in Mr. Nixon's second term, I will start with a brief examination of his preferences and then move on to a view of the whole spectrum of forces that are shaping your economic future.

I want to examine with you, at least briefly, the 1973 outlook and then examine the fears that have been besetting the economy and particularly the stock market. I want to look at the likely course of fiscal and wage-price policy and monetary policy, and in this process take a look at the prospects for achieving the \$250 billion budget target that the President has announced. We will consider the chances for avoiding a tax increase and for dismantling the wage-price controls and finally the possibility that we will maintain a favorable monetary environment for your business and for the economy.

Let us take a quick look at Mr. Nixon's preferences, if you will, in the economics field. What his economic policy instincts are is clear enough. If he had his way on controls, given his aversion to intervention in the market system and given his instinct for laissez faire, he would like to sweep those controls aside with one fell swoop. Secondly, on fiscal restraint or budget restraint, given his distaste for big government, for the very government that he presides over, he would like to cut and slash the federal budget and avoid a federal tax increase like the plague. I will come back to that in a moment.

He has, time and again, made clear that inflation is public enemy number one in the economic field. In the *Washington Star*, Garrett Horner

had a remarkable interview with President Nixon which was taped before the election on the correct assumption that he was going to be "landslide Nixon." Here are a few of the things he said, and rather than try to interpret him for you in my language, I would like to have him speak for himself. Horner reported that Mr. Nixon recalled having just come through a campaign in which he "didn't go out with a whole bag full of goodies." He made it clear there will be few social goodies in his second administration. Mr. Nixon took note of some suggestions that since he no longer is facing the problem of reelection he might be more free to advocate extensive social programs aimed at curing the nation's domestic ills. "Nothing," he said, "could be further from the mark."

Now let me quote selectively from other parts of that interview: "I'm convinced that the total tax burden of the American people has reached the breaking point. It can go no higher." Concerning domestic policy, Mr. Nixon will discard or trim down social programs set up in the 1960s that he considers failures largely because "they just threw money at the problems."

He stressed that he is going to thin out federal employees across the board, including the White House staff. The story notes, "As it has under most recent presidents, the White House staff has grown during Nixon's first term." Indeed after saying in 1968 that he was going to cut down the White House staff, he has expanded it by more than 50%. "But," he declared, "we can do a better job with fewer people. We have got to set the example on the White House staff."

Now, I would say to you, use that as a leading indicator: If Mr. Nixon cuts back the White House staff, then he is serious about cutting back the whole budget of the government. I would urge you to keep an eye on that particular indicator. He might just do it.

The President goes on to say: "In terms of the masses of civilian employees who are getting in the way of each other over in the Pentagon and around the country, they're going to have to take a thinning down." He made clear that he was talking about cutting some program work as well as workers out of such departments. And listen to this, because this has an impact on your business: the top ones that he mentioned were Housing and Urban Development, Health, Education and Welfare, and the Transportation Department. These, he said, "are all far too fat."

NO TAX INCREASE NIXON SAYS

The President made it clear that there will be no solutions of problems that require a tax increase. This is basic to his approach to future problem solving because, as he said, "more important than more money to solve a problem is the avoidance of a tax increase." Now, needless to say, I am not going to leave these statements totally unattended. I will come back to several of them in the course of my remarks.

Finally, from an earlier commentary about relative emphasis of inflation and unemployment, he said, "I consider the battle between higher prices and higher taxes to be the major domestic issue of this presidential campaign." And he did not mention unemployment in that connection.

In trying to make a realistic assessment of the kind of economic environ-

ment in which we are going to be operating, we have to ask ourselves: How much of Mr. Nixon's preferences, of his desires, is he likely to get in the next one, two, three or four years?

First, even if Mr. Nixon were a czar instead of a president, and even if he now felt beckoned by the history books rather than the next election, I wonder how much of this philosophy he actually would put into practice in the economy. Unlike foreign policy, where he has been a shaper of events, you will notice that his domestic economic policy largely has been shaped by events.

Secondly, he is not a czar. There have been comments about the election that say that it was not so much of a great victory for Mr. Nixon as a great defeat for Mr. McGovern, and there is a great difference between those two. The comment on the front pages of the *Miami Herald* this morning may be prophetic: "Landslide Tactics Irk the GOP Faithful." Despite President Nixon's landslide victory, Republican Party leaders from the capital to the court houses are eyeing the White House with burning resentment and the future with trepidation because it was a personal victory, not a party victory." *Business Week* on Friday put it this way: "The voters managed to give Nixon a landslide without giving him a mandate." And I am quoting, as you see, the most impeccably respectable sources.

The Democrats in the 93rd Congress, instead of being humbled and forced to follow Nixon's lead on budget cutting, on tax reform, on measures to attack stubborn unemployment levels, will be stronger and more feisty than ever. And, I wonder if you are aware that the 13 incoming senators are 22 years younger on the average than the 13 they replace?

I do not mean to suggest after you have listened to Chairman Patman that you have to be young to be feisty—let me make that perfectly clear! But you probably would guess that he is the exception rather than the rule—that 22 years on the Senate side are going to make a difference.

NIXON MAY HAVE TROUBLE PUTTING PROMISES INTO PRACTICE

Apart from a feisty Congress, there are a lot of stubborn institutional and economic forces that a president has to contend with in trying to put his economic principles into practice. There is the independent Federal Reserve, sometimes too independent, which never stays in a president's hip pocket. It may start out there, but once those fellows get over to Constitution Avenue they are pretty independent—even of the Congress on many occasions, as Mr. Patman would attest.

Secondly, there is the propulsive force of the past year's fiscal and monetary stimulus, of budget stimulus and monetary expansion, which pretty well predetermines the economy's path in the next 10 to 12 months.

Third, there is the momentum and thrust of government spending programs that make cutbacks excruciatingly tough. Not that Mr. Nixon will not try to cut back the \$250 billion; not that his heart is not in it; not that he could not do it with a meat axe, but the cards really are stacked against him, as I will illustrate later.

Finally, there is the genie of price and wage controls. Once you call him out of the bottle, wishing alone will not stuff that genie back into

the bottle. It is interesting and important to "psych out" a reelected president on economic policy; but a realistic appraisal of the economic outlook in the next few years requires a balanced look at the whole matrix of forces that will determine our economic future, not just White House economics.

Let me turn then to a quick look at the 1973 outlook and the rest of 1972. The yeast of the budgetary deficits and stimulative Federal Reserve policy will keep the economic dough rising and rising briskly. I should think, in 1973. The prospect of a \$100 billion gross national product (GNP) advance this year moved from hope to reality on August 15, 1971, when the President really stunned and shocked the country with his complete about-face in economic policy.

He discarded his previous game plan and adopted a three-ply plan of: (1) checking the wage-price spiral with a freeze and Phase II, (2) stimulating the economy by cutting taxes and turning on the election year spending spigots, and (3) stopping the international dollar hemorrhage by cutting the dollar loose from gold and then devaluing the dollar. By the way, that does show that a president has considerable clout and power in economic policy. One cannot deny that, but it shows as well that he is often forced to go against his preferences in economic policy. It reminds us that to appraise what Mr. Nixon's economic policy will be in the next two or three years requires us essentially to predict the unpredictable; and Mr. Nixon has been unpredictable in the past four years.

It reminds us also that circumstances alter cases; Mr. Nixon changed his tune and here we are today, in part as a result of that decision, enjoying the vigorous recovery that was lacking until his turnaround. As I have been saying for many months, I would think that this would keep the economy moving briskly throughout the rest of this year and well into 1973, whoever was elected. The serious question marks will arise in 1973 and in 1974 because, then, the problem of inflation and high interest rates and the rest will have to be faced.

As I am sure you are aware, the way an economist "gets it all together" is through his GNP forecast. This is the way you can keep score on our appraisals of the economic situation.

VIGOROUS EXPANSION LIES AHEAD IN 1973

Nineteen months ago, when I spoke to the Detroit Economic Club, I had the temerity and what some of my colleagues may have thought was the audacity to say the following: "My preliminary appraisal for 1972, plugging in the new policy initiatives I anticipate, foresees our first \$100 billion advance in history." What I had in the back of my mind was that two politically attuned gentlemen like Mr. Nixon and Mr. Connally were not going to sit there and see the economy stick in the mud during an election year. I went on to say, "Starting from roughly a \$1.050 billion GNP in 1971, I arrive at \$1.150 billion for 1972 by the relatively modest route of 6% to 6½% real growth and about 3% to 3½% inflation." That was at a time when our actual growth was 1% in real terms and inflation was running at 6½%.

Now what is my current reading as to how we will come out of 1972?

Very briefly, I think we will come out with just about a 6.3% real growth and a 3.2% price increase; and that is a tremendous improvement over 1971. But what is more important to you, I am sure, is where the forecasters are now looking for 1973. My forecast in this case is close to the consensus forecast. It says that we will be moving in 1973 at about the same pace as in 1972; that is, a good, vigorous expansion lies ahead of us. Again, I would expect perhaps 6.2% real growth and not more than 3.5% inflation. Now on a bigger base that means a \$110 billion GNP advance next year as against \$100 billion or so this year.

And what about profits, profits after taxes? They went up 13% in 1971; they are going up about 17% this year, and I think they will go up another 12, 13, 14% next year. That is three years in a row averaging a 15% annual increase in profits after taxes.

What about unemployment? Well, that is the sticky point. I do not think it is going to get below 5¼% this year, and we will be lucky to be much below 5% by the end of next year, maybe 4¾%. I recognize the sad fact that unemployment is the last thing to respond in an expansion.

It is not only the numbers that are important in your economic outlook, it is the fact that as far as I can see over the next eight, 10 or 12 months, there are no signs of significant excesses developing in the economy. We start 1973 with considerable slack still left in the economy. First, we have 4½ million unemployed and only half the job vacancies in manufacturing that there were three years ago. Second, manufacturing industries are still operating at about 80% of capacity, and they like to operate at 90% on the average. And third, new Department of Commerce figures show that there still is what we economists call a \$50 billion output gap. In other words, if the U.S. economy were operating at full tilt, at full employment, this great economy of ours would be producing \$50 billion more goods and services per year than we actually are.

The other part of this absence of excesses is that the major sectors in the economy are in a steady expansion, not in an unsustainable boom. Look at consumption, for example. To be sure, people have cut their savings rate from 8% of their after-tax income to about 6½%, but there is no consumer binge—they are just confident and they are spending.

Secondly, there has been a moderate pace of growth in inventories. We are beginning now to get an acceleration, but it has been well paced. Third, plant and equipment—we are having an increase of about 10% in capital spending by business this year. The new McGraw-Hill survey published Friday shows another 10% next year. As a matter of fact, they interpret 10% to mean 14%. I will leave that as it is.

Housing is of some slight interest to this audience. Demographic trends plus the money supply and demand situation will keep housing from sagging. Two million new starts looks like a sensible forecast for next year. Savings will continue to flow into your institutions at a good clip in 1973. With a favorable picture as to the flow of funds, I would expect mortgage rates to hold fairly steady, maybe with a rise of ¼% next year.

What about government spending? State and local governments are temporarily in clover, but I emphasize, temporarily. They enacted numerous tax increases a year ago, and now they are getting the benefit of the

increases, plus the economic recovery, plus revenue sharing. Everyone is going to say that the problems of state and local government financing are solved; they are not solved. But, for the next year or two, maybe three, their fiscal problems are certainly eased as compared with the pressures they have been going through for the past 10 years.

What about the end of war in Vietnam? Is that going to cause a sudden adjustment in the economy and a cutback of defense spending? Not on your life. If you have looked carefully at the Nixon budget projects for defense—as both Brookings, a liberal institution, and American Enterprise Institute, a conservative institution, have done—you will see they both agree that under the Nixon program defense spending is projected to rise from \$77 billion this year to \$100 billion by 1977. In other words, there is a one-third increase in defense spending programmed even with the end of war in Vietnam. My guess would be the end of war in Vietnam would be a psychological plus and not an aggregate-demand minus.

Is there a chance that all this will be upset by international developments, by the balance of payments and balance of trade? All I can say here is that the theme ought to be "Going My Way." Things are going our way at the present time. We lament our inflation here but it is running at 3¼% while the average inflation in the other 22 countries of the Organization for Economic Cooperation and Development, our trading partners and competitors, is 6% and programmed to rise in 1973 unless they take drastic measures. Our costs are rising much less rapidly than the rest of the world.

Also, the full effects of our devaluation on imports and exports have not been felt. The return on our foreign investments will rise from \$8 billion this year to \$14 billion in 1976. My guess is that our international financial position is going to prove materially and not be a restraint on domestic policy.

So much for the good omens. You must have concluded by now that everything is rosy. Let me put on my rather darker glasses. Ask yourselves, "Why, in the face of the essentially optimistic picture just painted on the domestic and international fronts, is it that until the past 10 days the New York stock market has been hesitant; so uncertain, backing and filling, responding only to the Kissinger syndrome, rather than to the underlying optimistic outlook for the economy?"

SOME NEGATIVE INDICATORS

I think that the market has been held back by two sets of anxieties, or fears or worries. One, the fear of the reappearance and resurgence of inflation and along with it the fear of excessive government deficits on one hand and cost-price push on the other. And then, the second fear, (as I have appraised it in talking with members of the investment community) is a premature stop in our expansion and our expansionary policy; a premature tightening of the monetary brakes; a premature tightening of the fiscal brakes and possibly the wage-price controls.

Farther out, I think they are afraid of a tax increase. They do not believe that there will not be one. There are, then, these two conflicting

sets of fears: inflation on one hand, a premature stop of the economic expansion on the other.

You are all worried about inflation; but let me ask you, what really worries you? First of all, it cannot be the current indexes because the current indexes except for food, even though we have had a bad trip on inflation, are pretty favorable. The deflator, the GNP deflator, is doing fine—only about 3%. The cost of living index, in spite of a momentary upturn, is doing much better, especially when you get into the non-food area which is the part affected by stabilization policy. It is certainly better off than a year ago. Only food and wholesale prices are misbehaving.

You may think that I am making a defense of the Nixon Administration. I am, on the price front—one has to tell it as (not like) it is. Something certainly is slowing down the inflation in this economy. We are in the midst of a period of remission rather than of a final solution on inflation, and perhaps that is what is worrying people.

Let us ask ourselves whether we are about to run into a new excess — demand inflation — and whether I am being a Pollyanna by citing the current statistics. With considerable slack left in the economy, we can take a good deal of fiscal and monetary stimulus without having it take off and run into price increases. I do not think we are on the verge of a new demand-pull inflation.

We do have an inflation-prone economy in the sense that if we want to maintain a strong expansionary, full employment economy, we are also going to put upward pressure on wages and prices. Are we going to add to that pressure excessively by continuation of federal deficits as the economy nears full employment? Federal deficits to help put starch in a flabby economy are acceptable, but not big deficits at full employment.

NIXON MAY PARE BUDGET TOO MUCH

Can President Nixon pare his budget down to his goal of \$250 billion for the current fiscal year? For that matter, should he, under present economic circumstances? Does he have a budget meat axe or cleaver or a surgeon's scalpel that can cut \$8 to \$10 billion out of this year's budget? That is a very large number when you consider that so much of the budget is uncontrollable.

You cannot refuse to pay interest on the debt. You cannot refuse to pay those revenue sharing dollars to state and local governments. You cannot refuse to pay social security payments. You cannot dismantle the defense establishment overnight. When all is said and done you have about \$70 billion to work with. He is trying to cut \$8 to \$10 out of \$70.

Unless Mr. Nixon is willing to cut his defense spending plans sharply (and remember, under his previous budget, they are scheduled to rise by nearly a third in the next four years) I doubt that he can impound enough of the money that Congress has already appropriated to do the job.

Look at the counterpressures. I do not have to go beyond your own business. Look at this headline from the *Wall Street Journal*. "Home-builders and Lenders Ready to Battle to Shield Subsidies from Nixon's Budget Axe." That was based on the Anthony Downs' study cosponsored by the National Association of Home Builders, the National Association

of Mutual Savings Banks and the U.S. Savings and Loan League. In other words, there is a fight against the cutbacks that Mr. Nixon is talking about, and you for one carry a lot of clout. Though he is dead serious about his cutback efforts—let no one doubt that—I would think that he will find it somewhat difficult to accomplish. So, my conclusion is, he will huff and he will puff and yet I doubt that he will blow housing down very much. Whatever he presents in January, I doubt that the fiscal 1973 budget outlays will end up at \$250 billion, just as a matter of reality.

Now, it so happens that I think he should not overdo cutbacks this year. With slack in the economy, with unused manufacturing capacity, with capacity even in your business that will not be fully used next year, I feel that it would be a mistake to slam on the brakes too suddenly. But we do have to apply the fiscal brakes gradually as we get back to full employment.

TAX INCREASE BY 1974?

Will Mr. Nixon be able to avoid a tax increase? I would answer that with eight words: He hates taxes, but he hates inflation more. We do not need a tax increase in 1973, but with full employment finally coming around the bend—I will not say it is just around the corner—in 1973-74, this country cannot afford to continue deficit spending. If the President cannot cut spending enough, he will have to face up to the tax increase issue by 1974 if he wants to be responsible.

It is not just Democratic critics who come to this conclusion. Listen to Senator William Saxbe of his own party. He says: "I think we're living in a dream world on taxes; I don't think the President is being altogether honest with the people when he says there won't be any new taxes." Or look at it from the standpoint of his former economic adviser, Paul McCracken, who was quoted in the *Wall Street Journal* as saying: "Nixon probably will have to raise taxes despite his campaign vow." If Mr. Nixon is going to face the facts and balance the budget at full employment, chances are he will be thinking very seriously about a tax increase about this time next year.

If Mr. Nixon really wants to serve his own philosophy on government spending and enter the history books at the same time, he should work with might and main not just on the budget but on the budgetary process. He should be working on one hand toward a five-year budget rather than a one-year budget, so that when a proposal is made we know what it is going to cost five years out, not just this year.

Secondly, he should cooperate with the Congress in developing a congressional procedure by which they can look at the whole picture. The trouble is, the appropriations committees look at one appropriation and then another without operating within an overall framework—within any kind of a cap on expenditures. I think it vital that the Congress develop an overall procedure which would rationalize the individual appropriations they make, especially in terms of the total impact on the economy. For that they will need new organization, new procedures, and a much bigger and better staff to match the White House in carrying out the budgetary process.

I would only add one note to the tax picture, and that is, I think there is a misconception being generated that the U.S. government has been growing by leaps and bounds in the last 20 years. But the numbers show the following: In 1953, federal spending was 21% of the GNP; in 1963 it had fallen to 20%; in 1973 it will be all the way back up to 21%. I am sure the current rhetoric in the campaign could have given you the impression that the federal government had been expanding like mad, when actually it has been expanding no faster than the economy as a whole. This is not a plea for either lower or higher government spending. I just want to put the facts in perspective.

Before I close, what about monetary policy and wage price policy? Let us look at monetary policy. I do hope the Federal Reserve, while maintaining a responsible policy and a close watch on the economy, will not prematurely tighten up and bring on another credit crunch. This country does not need that. Most of all, the housing industry and the savings and loan business do not need it. I have a feeling Arthur Burns will be a major force for a responsible fiscal policy. He says repeatedly that he would like to see the \$250 billion figure reached. He is not sure that it can be reached, but if it is not, I will venture to predict that he would be on the side of a responsible policy that might call for a tax increase. He also will weigh in on the side of continued wage-price controls, my final subject.

WAGE-PRICE CONTROLS MUST CONTINUE

We are faced with a decision the President has to make within the next few weeks, namely, will he or will he not call for a continuation of the authority that expires on April 30 to maintain wage and price controls? There is a great deal of controversy and there is a great deal of, what shall one say, a battle for the President's mind on this subject. I believe, however, that as an economic realist he will recognize that 1973 is going to start generating quite a bit of cost-push.

Nearly 5 million workers are coming up for renewal of their contracts, in strong unions; 1972 was a breather, but in 1973 it is the top of the labor batting order coming up—autos, trucking, electrical workers, rubber, meat cutters. This is "murderer's row" with Leonard Woodcock, and the Teamsters and so forth coming up. Further, the productivity surge that has been helping us so much this year on costs, prices and profits will begin petering out later in 1973 as it always does in the later part of an expansion. So, given these cost-push pressures, I am prepared to predict that we will be living under continued wage-price controls, or at least wage-price restraint, through 1973. I do not think Mr. Nixon will fold the tent of controls completely and let big business and big labor quietly steal away. I think in his heart of hearts he wants to drop them, but in his head of heads he will see it as too dangerous a threat to his cherished goal of keeping inflation in check.

In this morning's *New York Times*, one of the lead stories asserts that the officials who operate the Nixon Administration's controls over wages, prices and rents are strongly disposed to narrow the program as a gradual step toward decontrol. They are also afraid, they have indicated in private

conversations, that the program is becoming excessively complex as more and more exceptions and regulations are issued. All I can say is, if that is their thinking, "Right on!" In other words, keep wage-price controls, but slim them down, focus them on the elephants, not the mice, focus them on big business and big labor, not on retail trade, and perhaps not on rent control, and maintain them where there is essentially a frustration of competition and where there is monopolistic pricing and monopolistic wage determination.

I think you have to figure in your future thinking that wage and price controls have become, not a way of life, but a fact of life. The moment Mr. Nixon, on August 15th last year, put in a price freeze, wage-price controls became a bipartisan fact of life. Even when they are not in effect, big business and big labor will know there is a threat they will be put back into effect, and I hope that is going to introduce some moderation in future wage-price behavior.

I remember a statement by Al Capone—not that I am a great admirer of his, but he had an instinct for the bon mot—when he said, "You can get so much further with a kind word and a gun than with a kind word alone." Indeed, we have added to Federal Reserve policy and budget policy a potent new weapon in running this economy: wage-price policy.

When you look at the wage-price field and the credit field, you can only conclude that government willingness to intervene has been increasing over the years. Look at the way Arthur Burns moved in and said to the bankers, "We aren't going to impose those direct controls unless you let that prime rate go above 6%." He has the big club of direct control power in the closet. With that hidden persuader, he can go out and be pretty effective in "voluntary controls" and "voluntary restraint" if he wants to. The tools are available to do the job if our Federal Reserve authorities and the White House really have the stomach for doing that job.

1974 MAY BRING SLOWDOWN

In summary, I have said the following: First, with the push that Mr. Nixon finally gave the economy last year, after giving up his old game plan, the economy will move forward quite strongly in the next 10 to 12 months. Secondly, with the slack in our economy and its prodigious productive potential, I think there is substantial headroom for expansion. I do not think we are right up against demand-pull inflation.

Third, there is the danger that we might tromp on the brakes too early and drop the wage-price controls too soon. I hope that Mr. Nixon and Mr. Burns, remembering the 1959-60 parallel when they were on the other side on the fence trying to convince Bill Martin and Ike not to slam the brakes on, stay in perspective on this question.

Fourth, we are still in a period of remission on inflation, and it will be held back in 1973 by slack and by modified controls. But in all candor, I must say that a year from now, I doubt that I could give as sanguine and optimistic a picture. Unless we follow the right and responsible policy paths, we will be facing the ticklish combination of an economic slowdown (not a recession) in 1974, combined with a new surge of inflation. I hope we have the guts and intelligence to cope with those dangers.

ELECTRONIC FUNDS TRANSFER SYSTEMS— CHALLENGE TO THE SAVINGS AND LOAN BUSINESS

by NORMAN STRUNK, *Executive Vice President*

United States Savings and Loan League

Chicago, Ill.

SEVERAL HUNDRED TIMES a week the Federal Home Loan Banks receive telephone calls from their member associations requesting advances, with the proceeds of the advance to be deposited in the association's demand deposit account at the Home Loan Bank. This is an electronic funds transfer. Several hundred times a day business firms transfer money by wire from one city to another using the commercial bank wire or the Federal Reserve funds transfer switch. This is an electronic funds transfer. Every payday hundreds of thousands of employees, including about one-half of the employees of the U.S. League, have their pay automatically credited to their checking accounts in a bank. This is an electronic funds transfer. Every month thousands of individuals have their mortgage payments and their automobile loan payments made automatically by a pre-authorized transfer from their checking accounts to their loan accounts in the same bank. This is an electronic funds transfer. In many banks a certain amount each month is transferred from an individual's checking account to his savings deposit. This is an electronic funds transfer.

For the last 10 years, savings and loan people have been hearing about the coming of the checkless society and have rightfully been worried about it. Most savings and loan people thought that it was sufficiently far down the road, that by the time it really would have an impact on the savings and loan business, they would be safely retired and living on their pensions. For many of those in the business 10 years ago this was a safe assumption. It was a safe assumption for many five years ago, but it is not a safe assumption for most of you in this room today.

Actually, there is nothing on the horizon that has the potential of so radically changing the savings and loan business—and severely damaging it—as a change in the money and payments system in this country. It is, of course, one of the responsibilities of the U.S. League to look and plan ahead in order to prevent disaster from overtaking this business. Our record on that, I think, has been at least satisfactory, if not more than that.

Because developments in the payments system and the electronic transfer of money have the potential for such great impact on our business, the U.S. League has been studying this question and working on it for a long time. It is my purpose today to bring the business generally up to date on this subject, to indicate some of the problems involved and our course of action relative to it. I cannot today assure you that we have all the answers or that adjustments can easily be made for each of your institutions to a new world; but I do want, in effect, to inform you of what is going on and what is being done about it.

EFTS CHANGES BUSINESS IN FOUR WAYS

Now, what do we mean by electronic funds transfer? It means things to a business corporation or to a commercial bank and to the check clearing system that do not necessarily concern us. To the savings and loan man it means changes in the payments system that relate to family finances. I think it affects us in four different ways.

First, the electronic transfer of funds has the potential of eliminating many, if not most, of the paychecks in this country and sometime later social security checks, veterans pension checks and even welfare checks. Paychecks for industry will be phased out through SCOPE-type programs such as are now in operation in California. SCOPE is an acronym for Special Committee on Paperless Entries. It was a project of the large banks in California, the Los Angeles and San Francisco clearing-house associations and the Federal Reserve Bank of San Francisco. Basically, it means an automated clearinghouse operation. Its first objectives are to improve the payroll services that banks can render corporations so that all employees of a corporation can have their checking account credited with their pay, say, at 9 a.m. on the morning of payday regardless of whether the employee has his or her checking account in the bank that does the payroll services for the corporation. Employees, of course, should like this. It will save the employee the time of walking to the bank and depositing his paycheck or sending it in by mail. It will eliminate the possibility of loss of the paycheck, but it also prevents the employee from taking that check to a savings and loan office for deposit or to be cashed. SCOPE handling of payrolls also can mean that many corporation employees without a checking account today will have a free one tomorrow.

Operationally, the first SCOPE project, in California, has been ready to go since October 16, but as of today no more than a mere handful of items have actually been processed through the automated clearinghouse. The California banks are taking a slow, careful approach to marketing such a revolutionary change in the payments structure, and the California SCOPE committee itself has set modest goals for the program's first five years. The bankers in California, however, are virtually unanimous in their belief that paperless processing such as SCOPE offers will in time become an accepted part of the American financial scene.

Second, electronic transfers of funds mean a substantial increase in the use of pre-authorized payments for the payment of recurring monthly items; initially, those monthly bills where the amount is the same each month, as in a mortgage payment or a rent payment, and later where

the amount may vary from month to month, as in a utility bill. Many of your borrowers and some of your savers are getting started with pre-authorized payments under the Tran\$matic program. Tran\$matic today uses paper, because involved in it is the preparation of a type of check that goes through the bank clearing process. Under SCOPE handling of Tran\$matic payments, the piece of paper will not be created but rather the association will give its commercial bank a computer tape that includes all of the information on the loan payment. Through electronics, then, the checking accounts of all your borrowers who are on the pre-authorized system will be automatically debited a few minutes after the computer tape is delivered by you to the bank, and the total of the monthly loan payments deposited at the same time in your association's bank account. This means not only the elimination of paper but also of most of the people in the loan collection process and elimination of the float in your mortgage collection operation—all eliminations in your favor.

Thirdly, electronic funds transfers mean the use of a plastic card, like the credit card, but with a magnetic stripe on the back of it and a terminal through which payment can be made for goods and services. The card can (and might, in time) replace large volumes of checks and cash from the payments system in connection with merchandise and services purchased. We call this the third-party transfer system. Commercial bank experiments with this type of payment are being conducted in the area of Columbus, Ohio and in Nassau County, Long Island. While the hardware and software for this have now been developed, and the banks involved in the experiments talk optimistically, in my view, the development of an electronic funds transfer system to the point where it would replace the checking account as a way for people to make payments for goods and services is a long way off.

Ultimate development contemplates combining the 45 million outstanding bank charge cards with about 80 million checking accounts. It contemplates terminals in most retail stores which are hooked into big computers in a huge, nationwide electronic computer network. If such a system ever did get developed, of course, it would mean that a demand deposit account would become even more convenient than it is now, and the full service bank would have even more services for people.

Finally, electronic transfer of funds means that savings and loan depositors will do business with the association through the use of the fully-automated, so-called 24-hour branches where depositors can make withdrawals, deposits, and payments on loans or get cash any time of the day or night by use of a savings and loan Identification/transaction Card. Conceivably, someday a depositor of yours will be able to make a deposit or withdrawal through the facilities of any other savings and loan association in the country via a computerized on-line network functioning nationwide, possibly through the Federal Home Loan Banks. This fourth phase of electronic funds transfers requires no new law nor any new arrangements with the banking system, but it does mean the replacement of your savings passbook with a plastic card and the mailing of a quarterly statement to your depositors.

To recapitulate, the electronic transfer of funds will probably affect the

savings and loan business in four ways: First, paychecks will be phased out and employees paid through the automatic deposit of their pay into their checking or savings accounts. Second, pre-authorized payments will become increasingly accepted, as Tran\$matic pre-authorized payments are becoming accepted in many sections of the country today. Third, electronic transfer of funds will mean a growing use of plastic cards by people in making payment for goods and services. And, finally, an electronic system will mean use of fully automated branch offices.

SPECIAL EFTS STUDY COMMITTEE

As you have a right to expect, the U.S. League has not been ignoring the problems that electronic funds transfer can create. In addition to lending support to the Tran\$matic program, we have had a special committee studying the various electronic funds transfer programs and their possible impact on the business; special consultants have been working with us on the problem; and, we are currently assembling staff personnel who will specialize in this area. The Controllors Society, of course, has long been concerned about the technical aspects of electronic fund transfers.

Before I detail the U.S. League efforts more specifically, let me explain to you what has been involved in our efforts. There has been much talk for the last 10 years about the checkless society, and there was even talk about the cashless society. A more likely development, however, is toward a less-check society. The banking business now processes some 23 billion checks a year. The banking system has come as far as it can under its present system in automating the handling of checks. The MICR encoding system has been of a tremendous value, but the next step must be to cut down on the use of the check itself. The logical targets are the paycheck and checks written for the payment of recurring monthly items.

At the same time, the credit card has come on the scene. It has been a natural device to bring more people into the orbit of the commercial banking system. Combining the credit card as you know it today with a magnetic stripe on the back and terminals that are already in production greatly expands the potential of this piece of plastic.

You may remember that in 1967 and 1968 we were pushing in Congress the Federal Savings Institutions Bill which would have given savings and loan associations consumer credit authority and a modest entry into the checking account system in this country. When it became evident that Congress was not going to pass the Federal Savings Institutions Bill, we drafted a set of amendments to the federal savings and loan law which became part of the Housing Act of 1968. It was this action which gave associations authority to accept deposits, pay interest and issue subordinated notes. The last sentence of the new Section 5(b)(i), written by Congress in 1968, reads as follows: "Savings accounts shall not be subject to check or to withdrawal or transfer on negotiable or transferable order or authorization to the association, but the Board may by regulation provide for withdrawal or transfer of savings accounts upon nontransferable order or authorization." This did not give us authority to have checking accounts as the banks have them, but it does provide the legal basis for our being in the third-party transfer business whenever it becomes appropriate to

do so, and whenever the federal agencies will let us.

Meanwhile, bankers have been developing a SCOPE system in California and a parallel development has been underway with the Federal Reserve Bank and commercial banks in Atlanta, known there as the COPE Committee. The California savings and loan people have been in constant touch with the SCOPE development, the contacts being coordinated, of course, by the California League. The Atlanta savings and loan people have been in communication with the banks and the Federal Reserve officials in Atlanta. Thus far, the banks in both Atlanta and California have insisted on treating savings and loan associations as they would treat any other customer of the bank and, more importantly, there has been no apparent disposition on their part to permit our institutions to be on the receiving end of any part of the payroll when paychecks are eliminated. Thus far, the banks have been insisting that all of the paycheck must go to either a checking account in a bank or a savings deposit in a bank.

This attitude on the part of the banks has some rather frightening implications, and it also has, in our view, some restraint of trade aspects. It is the sort of question that we hope the House Banking and Currency Committee will look into next year when hearings are held on this general question, as suggested last month by Congressman St Germain, chairman of the Subcommittee on Bank Supervision and Insurance of the House Banking and Currency Committee.

While the banks have been developing SCOPE and experimenting with third-party transfer systems, we have been developing a pre-authorized loan payment system and a pre-authorized savings system under the Tran\$matic label. It has been our conviction that pre-authorization was in our future, and the sooner we got started in getting our mortgage customers on a pre-authorized payment basis the better off we would be in many ways. I have said many times that if the savings and loan business is not willing to make the changes in their internal operations involved in Tran\$matic then I do not know what will save the business when significant changes in internal systems will be required by EFTS in the years ahead.

We have had real problems in getting the commercial banks to accept the Tran\$matic system. Bankers had dozens of excuses not to process Tran\$matic drafts, but with constant work and with some help by the Department of Justice and Congressman Patman, all of the banks of any significance now have agreed to accept the Tran\$matic drafts. Charles Borsom and his group, the California League and the officers of some of our larger associations did some very effective work on this problem.

ASSOCIATIONS MAKE PROGRESS WITH TRAN\$MATIC

First Federal Savings of Lincoln, Nebraska, now has over 50% of its mortgage payments on the Tran\$matic program. First Federal of Rockford, after about a year of effort, now has 30% of its loans on Tran\$matic and is writing 93% of all new loans on this program. This association happens to be on-line with the Federal Home Loan Bank computer in Chicago. With 30% of all loans on Tran\$matic, First Federal can now move into a system whereby its commercial bank in Rockford, which has been creating the Tran\$matic drafts, will, as a byproduct, prepare punch cards to be

delivered to the on-line center at the Home Loan Bank. The result will be that with one-third of its loans, the First Federal of Rockford has eliminated all paper, all postage, all teller time and virtually all personnel time, and, of course, all the float against them in connection with loan payments. If a loan is due on the fifth of the month, the payment is made on the fifth of the month. One of these days the association will have 70% of its loans on Tran\$matic, and virtually all the costs involved in the loan collection routine will largely be eliminated.

I do not understand why more of you have not seen the possibility of cost savings and improvement in cash flow with the Tran\$matic system, and pushed your loan department personnel to put your borrowers on the pre-authorized system.

The savings banks in the East have the same worries that we have had as to the effect of electronic funds transfers and third-party payment systems. We have been in close touch with the savings bank leadership. In a few states, savings banks have a demand deposit authority. As many of you know, in Massachusetts the savings banks (as a result of a court decision) have, since August of this year, been issuing a type of check, a negotiable withdrawal order, on their regular savings accounts. People in Massachusetts can, in effect, have a 5¼% interest-bearing checking account. (The savings banks in Massachusetts are not insured by the FDIC and not subject to Regulation Q.) This has very significant implications with respect to the future of the co-operative banks and the federally chartered associations in Massachusetts. Savings banks are doing basically what the Congress gave savings and loan associations authority to do when in 1968 it wrote into the law the sentence I read to you earlier.

PLASTIC CARD EXPERIMENTS UNDERWAY

Third-party payment systems inevitably mean the substitution of plastic for the passbook account. The saver gets a statement once a quarter. First Federal of Lincoln has a program right now to phase out its passbook accounts into statement accounts.

Electronic funds transfer systems may eventually involve the universal use by savings associations of a plastic identification card with a magnetic stripe. A number of our technical people have been working with a committee of the Mutual Savings Banks known as the MINTS Committee (Mutual Institutions National Transfer System) on specifications for the encoding on these cards. Very significantly, these people were joined by representatives from the ABA's bank card division and a representative of the credit union business in a meeting last month to discuss specification encoding standards for credit and ID cards. Representatives of the four businesses, ours, savings banks, commercial banks and credit unions, have agreed upon a common encoding standard which you will want to follow when you issue identification cards in the future.

A few savings and loan associations have installed cash dispensing machines similar to those exhibited here in the business show. Most require a plastic card with a magnetic stripe to activate them. The job you will have if you install these machines is to get the plastic ID card in the hands of your customers.

The Federal Home Loan Bank Board recently authorized associations to operate 24-hour fully automated branches. Commercial banks in some cities have done this. This also requires a plastic card using a magnetic stripe. Twenty-four-hour teller stations, of course, increase the convenience aspect of the savings and loan business. In the state of Washington the savings and loan people want to have cooperative 24-hour fully automated branches wherein the depositors of Metropolitan Federal, for example, could do their business at the 24-hour branch of the Pacific First Federal or vice versa, or at a mutual savings bank office. Associations would be hooked into a common on-line computer system, if they received permission from the FHLBB to operate this type of multi-association branch.

We have tried to keep you informed about all this through my *Bulletin* and articles in *Savings and Loan News*. Federal Reserve Governor George Mitchell recently referred a banking audience to the *Savings and Loan News* article on the Atlanta COPE project as the best source of information.

EXTENSIVE COMMITTEE WORK EXPLORES FUTURE

We, of course, have been working with committees on all this. Last year President Eaton selected a committee of savings and loan executives under the chairmanship of Roy Blount of Decatur, Georgia, to consult with an academic team at Northwestern University which previously had done work in this field for the ABA.

It is obvious that the whole subject deserves the full time and attention of several U.S. League staff people, and that efforts of the staff and the research should be assisted by a small coordinating group of association executives. We have hired one person for this new staff and we expect to hire others. We have market research in mind with respect to pre-authorization and other phases of EFTS.

We will have two basic committees working on this problem. One will be known as the EFTS Research/Planning Committee and the other the Legislation/Legal Strategy Committee. Both committees, for coordination purposes will be headed by Roy Blount of Decatur.

Involved in this whole question is the possible necessity for our institutions to get from the Congress a demand deposit authority in order to be in the third-party transfer system. In this instance, I think the Hunt Commission was in error when it equated third-party transfers with checking accounts. The Hunt Commission said that for us to have a third-party transfer authority it would be necessary for our institutions to become members of the Fed. The fact is that most commercial banks are not members of the Fed. As I have indicated, the savings banks in Massachusetts are now using a type of check which is being cleared by the commercial banks, and there is no suggestion yet that these savings banks will have to join the Fed in order to have their negotiable orders of withdrawal clear through the Fed system.

The savings banks, of course, are moving into a paper system. There are many who think that our business would be foolish to follow the banks into a paper system when the banks are trying to get away from paper. Possibly we can leapfrog into a full electronic system.

I dislike leaving my audience dangling in midair about the solution

to a problem vital to our business, but that is necessary in this instance. The fact is that we do not yet have all of the answers. We think we know the shape of the problem, but we do not know the extent of its impact.

I am concerned about many aspects of it. I am concerned particularly about its effect upon the smaller institutions, just as the American Bankers Association is concerned about the effect of a new money and payments system upon small banks. If we could be assured that over the years we would have what the economists call an upward sloping yield curve: that is, low interest rates on the short end of the maturity scale and high interest rates for longer term debt instruments, and if we could be assured of always being able to pay a higher rate of interest for savings deposits than the commercial banks, I would not be too concerned. I do get concerned, however, because there is no way I can guarantee that year in and year out the savings and loan business will have the kind of pricing advantage over the commercial banks that it has had in the past, and I cannot guarantee you that the commercial banking system will not become more competitive, which might mean that present rate differentials would be inadequate.

On the other hand, thinking in terms of the priorities involved gives me greater confidence. First we must deal with the application of payrolls in the SCOPE program. I think this problem can be solved without much in the way of new law, although perhaps not to the complete satisfaction of the business; and it can be solved without too many new computer programs or internal procedures.

The second priority is in connection with pre-authorized loan payments and pre-authorized systematic savings programs. We clearly do not need any new law on that, only a determination on the part of savings and loan executives and people in your loan departments to sell the pre-authorized payment system.

To the extent that our business wants to use the fully automated, 24-hour branch, you need only the merchandising of plastic ID card accounts. That is up to you.

The third-party payment system is the most complex and most difficult to solve, but fortunately it is much further down the road than electronic funds transfers in payrolls and loan collections.

The changes coming to our payments system in this country pose great challenges for the U.S. League, savings and loan executives and the Federal Home Loan Bank Board. But they also pose challenges to all who have a stake in preserving the health and vitality of the savings and loan business, and flows of credit to the home mortgage market. That brings in the U.S. Congress.

I have great confidence that Congress will not sit by and see the computer and a new payments system reduce the effectiveness of our service to the home builders and home buyers of America. I hope that Congress will not let a commercial bank monopoly of checking account services to the American people be automatically used to freeze us out of a computerized funds transfer and payment system in a manner that would harm our business and render it ineffective.

THE BRAZILIAN SAVINGS AND LOAN EXPERIENCE

by JOSE EDUARDO DE OLIVEIRA PENNA

Director, Banco Nacional de Habitacao

Rio de Janeiro, Brazil

I SHOULD LIKE TO TALK about the Brazilian savings and loan system, the National Housing Bank and our urban development problems. This year has been a turning point in the population growth trend of our country. While the total population has reached 100 million, the rural population is beginning to decrease. This means that no longer will the greatest number of people live outside the Brazilian villages and cities. From now on, the Brazilian cities will be growing faster than the total population of the country. There will be an increase of 2.7 million, or 4.7% per annum, in the cities. The growth rate in the larger cities will be 5% a year, reaching 400,000 in a megalopolis like San Paulo.

To cope with this growth and to try to ease the pressures and needs of such a tremendous movement, the Brazilian government put together the Housing Plan. It was designed as a systems approach to a national problem with enough flexibility built into the law to permit the creation of new systems as new situations develop.

This has not been an easy task, nor can all the problems be solved, but we do want to testify that a great deal can be done to reduce the human hardships involved in a process that signifies the change from rural to urban status of 1.2 million people per year. The power created by the process itself can be used to generate enormous resources.

Of the Brazilian economy, 82% is now urban as is 58% of the population. Per capita gross national product is around \$500 (U.S.), reaching \$2,500 (U.S.) per family. The Brazilian economy is growing at a rate of 10% a year in real terms. Last year it increased more than 11%. This means that Brazil is fast leaving the underdeveloped stage and is entering the situation of a country with enough resources and production to provide for its people a decent living standard and the fulfillment of the basic human needs and aspirations.

With an urban population one-fourth that of the United States, Brazil is making progress. Cars are being produced at an annual rate of 600,000

with an increase of 20% a year. Steel is being produced at a rate of more than 6 million metric tons per year with production increasing more than 10% a year. All sectors of the economy reflect progress.

To reach this stage, a great deal had to be done in a country that had stopped savings and growth in 1963, with an inflation of 100% a year, without foreign reserves and without the confidence of either Brazilian or foreign people.

First, confidence of the people in the government and institutions had to be reestablished. In the case of the financial sector, that confidence had to be achieved by the use of a readjustment clause for the savers and for the borrowers. [The readjustment clause is a measure adopted within the system in order to correct the effects of inflation.] It was achieved in spite of people who fallaciously said that to use a readjustment clause was to accept inflation and to incorporate it into the economy and increase its rate. Just the opposite occurred—the rate of inflation is coming down from over 100% in the first few months of 1964 to an estimated 15% this year.

The fact is that if inflation exists, and this situation is recognized in financial contracts, a basic financial assumption is reestablished that future payments will be made with money of buying power equal to what existed at the moment the contract was signed.

If inflation exists and a readjustment clause is not used, what happens is that people start to make forecasts of the probable future rate of inflation and try to incorporate these estimates in the values of the contract, disguised as an increase in price or interest rates. The only thing you can be sure of in such circumstances is that someone is going to lose, because real inflation will not meet exactly the forecasts and also because people usually are unaware of what they are really gaining or losing.

As a personal aside, I should like to say that I have never understood why in a country like the United States, so preoccupied with fairness to the consumer (and savers are consumers), such a clause has not yet been adopted. Why truth in lending without truth in savings?

For us, there are many more savers than home buyers which means that the underdog is the small saver—not the luxury home buyer.

The readjustment system we adopted is based on the readjustment of the outstanding balance of the loans and accounts and not on the fluctuation of the market interest rates. The monetary correction of the values is based on the quarterly change of the general wholesale price index. The point is that debts and savings accounts both must keep their buying power. In a country with 5% inflation and a 9% mortgage interest rate, for instance, this could mean mortgages of 14% plus readjustments, thereby causing a much lower monthly payment in the early stages of loan repayment when the unit of currency is worth more.

GROWTH IN SAVINGS, INVESTMENT STIMULATED

This system has been in use in our country for the last eight years, with problems and difficulties of course, but with tremendous results in stimulating growth in savings and investment, in creating jobs, in spurring political independence and well-being for people even in poorer regions.

After the legal and institutional framework had been laid and existing financial contracts dealt with fairly, a great deal had to be done to train manpower to operate the newly created systems and to reeducate the people in general in the savings habits they had lost because of the inflation in the years that preceded 1964.

TV and public relations techniques were used to reestablish savings habits and were effective in changing the figure for new real financial savings from minus 3.2% of the gross national product in 1963 to a plus 15.9% in 1971. The outstanding balance of financial savings, not including stock shares and funds for transfer payments, rose from \$500 million (U.S.) in 1963 to \$11.2 billion (U.S.) in June 1972.

The savings and loan system created in 1966 is one of the sectors of the Brazilian financial structure that is growing for the benefit of the people, providing a good place for keeping the wealth that is needed to finance the housing and urban needs of our country. In building the savings and loan system we were helped, not only by American money but by American friends. Among these are Stanley Baruch, Bill McKenna, Norman Strunk, Bruce Ricks and Preston Martin.

BRAZILIAN SYSTEM: STOCK, MUTUAL, GOVERNMENT

The Brazilian savings and loan system comprises three different types of institutions: stock, mutual and government. From its start in 1966, it has reached \$2.5 billion in total assets, 3 million savers as of October 31, and 86 institutions with 1,300 branches including the old branches of the Caixas [associations] that have been modernized. The amount of new savings collected each month is nearly \$100 million (U.S.), and new savers are incorporated into the system at a rate of about 1 million per year.

Our goals are to reach 20 million savers by 1980 with \$5.5 billion (U.S.) of savings and total assets of \$7.0 billion (U.S.). If these goals are met, each Brazilian urban family will have 1.25 passbook savings accounts instead of four families per account as it is today.

Even though these resources seem big for us, they will not be sufficient to finance all the urban needs of our country. We need to build more than 7 million homes during this period, and some of these are for people who cannot pay the market interest rates charged by the savings and loan system.

For the financing of the housing needs of low income people and for water supply and sewage systems, the National Housing Bank of Brazil in addition to being the central bank for the savings and loan system, is the trustee of a workers' fund that collects every month corporate deposits for severance payments the equivalent of 8% of total payrolls of the private sector. This fund is used by the Housing Bank to provide liquidity and expansion loans to the savings and loan system and to finance low and medium cost housing.

Through an internal subsidizing mechanism, housing loans are made according to a scale that ranges from 1% a year plus readjustment, for the smaller loans, to 10% a year plus readjustment, for the bigger loans. In a certain way the families with higher incomes pay more so that the low income families pay lower interest charges, and the bank averages a

return that is sufficient to pay administrative costs and to generate the necessary reserves. Today the National Housing Bank is an institution with total assets of \$2.7 billion (U.S.) and \$350 million (U.S.) of equity.

The need to provide urban land with water and sewage facilities has pushed the bank into backing a sanitation financing system that operates in each state with local participation, whose goal is to furnish good water to at least 80% of the Brazilian urban population by 1980, instead of the 50% now benefited by this service.

From the sheer pressure of trying to solve the problems of housing, the bank is expanding into the area of urban development. How is it possible to clear the favelas [slums] without getting into urban mass transportation systems? How is it possible to reduce the housing costs without a land policy? Or without fiscal and financial instruments, to reduce speculation to reasonable levels? How is it possible to accommodate each year not only the 1.5 million born in the cities but also the 1.2 million who move from the rural areas? How is it possible to provide food, shelter, jobs, education, health, recreation to this mass of people without rationalizing public and private investments in the urban areas?

It must be remembered that the Brazilian economic and urban policies are based on the belief that private enterprise is the best means to reach social goals; that market mechanisms, even if guided by government regulatory powers, are the most efficient way of coping with the challenges that are presented every day to the Brazilians.

We can say that we have not been let down in our belief in private enterprise as an instrument of a society to develop itself. Everything that is now happening shows the impartial observer that in the future this situation is going to remain unchanged. We are now calling on private enterprise—financial and real estate private enterprise—to tackle two new problems: the development of (1) new towns and (2) existing and incomplete parts of the cities. These two new projects try to minimize the social costs of rapid urban growth, so that enough resources are left to other productive investments, the savings and loan systems being expected to play a decisive role in these resource-savings programs.

As always, the profit motive will be used, but curbed by competition so that the consumer will be protected. For this reason, the system has been recently authorized to finance all the needs of the community, including the construction of shopping centers, medical offices, schools, and so on, so that the new and old areas become better places in which to live, to work and to play.

Brazil is the host country for the XIII World Congress of the International Union of Building Societies and Savings Associations to be held in 1974, August 19-24, in Rio de Janeiro. This is a very important meeting for us as the 10th anniversary of the National Housing Bank will be August 21, 1974, and the Brazilian Savings and Loan System will have completed its eighth year. The thousands of people who we hope will come from all over the world to Rio beaches but also to the workshops on savings and housing, are going to benefit themselves by staying in an agreeable city. But we also are going to benefit—our system and our country—by the prestige and advice the participants will bring to us.

THE GREAT PARTNERSHIP

by STANLEY WARANCH, *President*

National Association of Home Builders

Washington, D.C.

IN THE NEARLY THREE DECADES since the end of World War II, the home building and savings and loan businesses have been partners in one of the most dramatic achievements of our times—the creation of the best-housed nation on earth. It has been a great adventure, and a great partnership. Through the bad times and the good we have been complementing each other's endeavors. I can say that both of our businesses have been innovative in the tremendous continuing demands and needs of American families, resulting in continually more sophisticated lending and housing organizations. The current housing market is larger and more diverse than ever before; more demands are placed upon us in the effort to reach that goal of decent housing for all citizens. I am confident that the partnership we have forged between our two businesses will see us to the realization of that goal.

It is in the spirit of that partnership that I would like first to speak briefly to your own particular province of lending. I speak from the builder's point of view in his dealings with savings and loan associations; and, I believe, that as partners we should speak frankly. We are now moving toward the end of a second year of housing starts of more than 2 million units—back-to-back record years unlike anything in the housing industry's history.

During this period, the Federal Home Loan Bank Board in our minds, has been creative, dynamic and aggressive. Builders, disenchanted with the cumbersome processing delays which have encrusted the government housing programs, are turning more and more to conventional financing.

For example, the permission to originate 95% conventional loans creates for the first time a viable alternative to FHA. Yet many of our builders complain that many savings and loan associations around the country still have not chosen to offer 95% loans at reasonable rates. And this reluctance extends, according to reports I receive from members, to the making of 30 year loans. Savings and loans have the authority to make these loans and our builders would like to see more of them doing just that.

In the secondary market, facilities such as Fanny May and the Mortgage Corporation are designed to improve the timing of an association's cash flow. But I understand that only 400 of the 6,000 associations are currently dealing with the mortgage corporation which was created specifically to encourage savings and loan's involvement. I would like to leave those few thoughts with you as examples of how the builder sees that cooperation and coordination between our two great industries can be improved and broadened.

At no time in this industry's history have home builders been more sensitive, more responsive and more involved in the needs of good planning, good design and good land use, all within the constrictions of cost and financing for families at every economic level. And at no time in the phenomenal growth of our industry since the end of the war have the problems it faces been so large, so varied and so complex.

Too often, the intermixture of broad social, environmental, economic and employment issues is labeled a housing problem by political leaders and those influential in molding public opinion and attitudes, thus influencing the American public. We are all well aware of how these problems were brought to the fore in the recent presidential campaign. We have growth and non-growth movements. The non-growth adherents create the most formidable barriers to orderly and planned growth. The poor and the minorities are either priced out of the suburbs or kept out through ingenious varieties of exclusionary devices.

Along with these, the building industry will continue to face in the years ahead major issues affecting the costs of its product, the availability of mortgage money, the unwise restraints of land use, archaic building codes unrepresentative of the increasing body of technology which the industry seeks to employ, environmental regulations and restrictions, an energy crisis of increasing proportions, and wage and manpower problems. Further, the role of government in housing is once again undergoing a most searching examination.

HIGH LEGISLATIVE PRIORITY IN NEW CONGRESS

This examination of the government role in housing undoubtedly will be a top priority item in the 93rd Congress when it convenes in January. As you know, major pieces of housing legislation went through much debate in the late 92nd Congress, but never got to the floor of the House. The Senate passed a good bill early in March, but the one produced by the House Banking Committee never got through the House Rules Committee, perhaps fortunately. It had provisions that I am convinced were unworkable and would have done more harm than good.

HUD Secretary George Romney has laid the basis in recent speeches for what probably will be a massive reassessment of policies and goals within the national framework. Unfortunately, his remarks have been misinterpreted in parts of the press as advocacy for complete federal withdrawal from the field. I would like to point out that he thoughtfully laid out five long-range basic policy alternatives and their implications for the consideration of all concerned.

Basically, these alternatives as the Secretary outlined them are: first,

termination of direct federal role in housing; thus the end of subsidy programs and privatization of FHA. Second, radical decentralization of the federal housing role to the states. Third, partial decentralization of the federal housing role to the states, and fourth, partial decentralization of the federal role to the states and metropolitan housing agencies. The fifth alternative is an incremental change in present programs and the intergovernmental delivery system. This would mean, according to Romney, more state and local involvement; timetables and deadlines for metropolitan fair share of low and moderate income housing, and subsidies allocated on a priority basis to those metropolitan areas which carry out their plans.

These are alternatives he suggested. As for the current subsidy programs, he said that we cannot just wash out Sections 235 and 236, which provide subsidies toward home ownership and rentals, but will need a transition period. This statement brings me to our involvement, yours and ours, in the study recently completed by Anthony Downs, the independent and respected housing consultant, on the subsidy programs and recommendations for the future.

DOWN'S' STUDY BASIS FOR POLICY, TESTIMONY

Downs' study is now being analyzed by your staff and officers as well as ours. I will not attempt to give you the details. That would be an impossible task in any case in view of the depth of the study. But at the risk of being self-serving, I will tell you that this independent study found in one specific that the 235 and 236 programs under which some 600,000 units for low and moderate income families have been built in the last four years are, on balance, effective instruments for meeting the key objectives of housing subsidies. These are but some of the advantages found in the programs. The study, I am sure, will serve as basis for formulating policy and testimony of both of our organizations in the coming legislative year.

Under the guise of protecting the environment, local governments resort to measures which, in effect, would attempt to stop growth of any kind. Zoning and land use controls are abused. Sewer and water moratoria are declared; classes of citizens are denied use of land and thereby housing. Planning, in too many cases, becomes planning to preserve the past. There is an increasing tendency toward the idea that the only way the public can influence the use of land and its future development is for the public to own it. But it is not the public which would own it, but government, and therefore such land would again be subject to pressures working against the public.

From Florida to California the moratoria are spreading. As a matter of fact, the moratoria affect the entire areas of those states and are being repeated in county after county in the intervening geography. In Florida, it is a sewer connection moratorium; in California it is because an environmental impact plan must be submitted with all construction. Obviously, rational long-range planning is necessary, imperative in fact, when your business and my industry are confronted with the publicly proclaimed attitude encountered in Oregon where its officials say come and visit—but

don't stay.

By far and away the most critical problem we are encountering today and are likely to encounter for a long period ahead is the soaring prices and shortages of lumber and plywood. For example, in just a year's time, if we take only a median FHA home selling at \$25,000, the price of the lumber and plywood in that house has risen by about \$900. Lumber is under price controls, but singularly manages to escape them.

Most of you are familiar with the Cost of Living Council's on-again, off-again controls of lumber firms, under which some 200 lumber firms records are being looked into by the Internal Revenue Service, that Price Commission officials have been told of gimmicks, shenanigans and so-called inventive distribution channels. Nevertheless, prices continue to rise. In addition to meetings with forest products representatives on several occasions, sessions which proved useless from our point of view, I have personally taken the situation to Director Donald Rumsfeld of the Cost of Living Council and written to the President. The single exception, the glaring exception, to what appears to be a successful effort to dampen inflation is in the area of lumber. And it threatens the validity of the whole stabilization effort.

HOUSING AT CROSS-ROADS

With all of its problems, the industry probably will start in the range of 2.25 million to 2.3 million units this year, topping last year's record of 2,084,500 units. But this unbelievably high rate of production cannot be sustained and we will be entering 1973 at a declining pace. The flow of funds into your institutions, however, is continuing surprisingly strongly, and the generally economic recovery is healthy. But there will be other demands for money and capital, and the federal government undoubtedly will not be giving the same attention to housing as it has exhibited over the past two or three years. Housing may have served its purpose, at least during this cycle.

Regardless of the non-growth movement, zero population proponents and environmental concerns, the nation will continue to grow. This would seem to put our industry at a cross-roads. More is being demanded of it than ever before. We must, however, meet those demands and needs. In partnership with the savings and loan institutions, I am confident we shall

THE FUTURE IS NOW

by PRESTON MARTIN, Chairman

Federal Home Loan Bank Board

Washington, D.C.

THE END OF THE FIRST TERM of President Richard Nixon and the beginning of a second term is surely such a milestone in our business lives as to warrant both an *ex-post facto* summary of the past four years and an *ex-ante facto* comment about the next four. Redskin Coach George Allen's famous one-liner when he came to Washington two years ago comes back to me: "The future is now," he proclaimed. I think that in a very real sense this is also true for savings and loan associations and the FHLBB governmental conglomerate. It may be productive first to review major actions taken by this Board during the past four years; and second, to consider how these may be translated into the future.

In the next four years the structure of financial institutions in this country will be radically reshaped. Congress cannot fail to respond to the tremendous progress made during the last four years. The strength and adaptability of the savings and loan business and of the FHLBB agencies are two of the most important factors to take into account in reshaping our institutions. This very strength and this very adaptability are the major reasons why housing has broken every record and lifted the quality of shelter of the American people to unprecedented levels.

BUSINESS EXPANDS, MAINTAINS PRICE STABILITY

The output of the savings and loan business is lending, and I would be hard pressed to name any other major United States business which has expanded its output as much during this time, while maintaining price stability. Of course the Board and its component organizations can be further improved. Certainly the business has much yet to do to meet the complete needs of communities in today's vastly different world. I hope the Congress, in developing the next four years of legislation, will make a balanced evaluation of the record of the last four years of our present financial system's performance, specifically of our savings and loan and Bank System. Only in that way can we conserve the best elements of today's system while widening and deepening the legal action space of the business during the next two sessions of Congress. No one can accuse me or my associates of a mere defense of the status quo, but I happen to believe that "conservative," and "to conserve" have real merit today.

The FHLB System turned 40 years old this year. Most of us can remember, and can comment with some authority on, Walter Pitkin's 40 year old best seller of 1932, *Life Begins at 40*. Its underlying thesis was that "the best is yet to come." If my projections today fail to hit that mark within the next few years, we can hedge by taking comfort in Mr. Pitkin's follow-up book, which you may not remember. It was titled *Life Begins at 50*.

If the future is now, let us see where we are now, and where we stood when my colleagues, Carl O. Kamp Jr. and Thomas Hal Clarke, and I came to Washington in 1969. In January 1969, savings certificates amounted to 25.5% of savings. Almost all were for one year or less. At the beginning of October 1972, certificates amounted to 48.8% of savings. More than 33% had maturities over one year; only 15% were for one year or less. Disintermediation is thus less of a threat today.

Savings and loan associations are paying tens of millions of small savers 6% on their savings, at a time when inflation is running less than 3%, so the real return on their savings beats early 1969. Remember that 1968's inflation was over 4½% on a December-to-December basis, and the saver was getting 5% or less.

Is there a future in the savings market? I argue that the Nixon Administration's fiscal policy and the monetary policy of Chairman Arthur Burns and his Federal Reserve Board colleagues will produce a much lower rate of price increase in the next four years compared to the last four. Last quarter's money supply growth dropped to 4.7% at an annual rate, for example. Bankers Trust dropped its money market formula in setting the prime. Less inflation has to have savings market effects if you compete adequately for your market share.

WILL EXPANSION CONTINUE?

Can you compete? Recent experience strongly suggests that the business may have recovered at least some of its lost share of the savings market from the low periods of the middle 1960s. This cannot be certain until the next tight money period sends the commercial banks back into the savings markets with all of their available tools. Even in those situations, new marketing and merchandizing approaches may be effective in holding on to more of a market share next time, than was possible in 1966.

Let us look at that 1966-1967 period, comparing savings and loans to commercial banks, mutual savings banks, credit unions and savings bonds. Assume for a moment that the total savings gain for those institutions defines the savings market. The savings and loan share in 1966-1967 was 21.8%. Now, let us look at the last two years. Taken quarter-by-quarter, savings and loan's share of the savings market as defined did not fall below 36%, and it appeared to run from 40% to 45% for the 24 months of 1971 plus 1972 (interest and dividends included).

The average yield on mortgage portfolios was 6.24% in mid-1969, compared to 7.01% in mid-1972. That, of course, is how you are able to pay the saver so much more on his deposits. (Remember when we could not call them "deposits"?) I would expect the weighted average yield to climb further to at least 7.10% by year end. Given another three

years of adequate growth and reasonable earnings, modification of Regulation Q may be feasible. It is certainly not feasible today. The regulatory framework restraining interest rates is working to keep mortgage interest rates from escalating the way some short-term rates are doing. Regulation Q ceilings keep down costs, but under those ceilings, savings and loan associations are providing the small saver with the highest real rate of interest, after deducting inflation, that he has had in a decade.

Net new savings and loan savings (excluding interest) stood at \$859 million for the first half of 1969. During the first half of this year \$13.75 billion was recorded, an incredible rise to 16 times 1969's volume; or, as one of our economists says, "rapidly approaching infinity." More importantly, insured associations made loans totaling \$11.3 billion in the first half of 1969 and doubled this to \$22.6 billion in the same period in 1972. One of the most important considerations, if the future is now, is the amount of loan commitments currently being made. These totaled \$3.7 billion as of January 1969. They are up 222% to a record \$11.9 billion at the close of September 1972.

UNLIMITED EXPANSION MAY CAUSE PROBLEMS

While these figures are dramatic, I am not for growth just for its own sake. Rapid growth produces a certain proportion of bad loans and investments in any kind of financial institution. This growth period likewise will produce some bad results, but we are all a little older, maybe a little wiser, and it looks as though we will handle that problem a little better this time. I am arguing that the business is filling a social need at a time when other financial institutions are shifting away from mortgages.

Savings associations have expanded their shares of the mortgage market as FHA has gone through the throes of reorganization. Conventional financing has filled a gap formerly handled by FHA lenders. Some of the credit gap comes from other lenders' portfolio broadening. Take the first quarter of 1972 as an example. Savings banks then were acquiring more corporate bonds (\$5.3 billion) than non-home mortgages (\$3.0 billion), and more of those mortgages than home mortgages (\$1.2 billion). (All figures are seasonally adjusted annual rates.) Broader investment powers, of course, tend to divert funds away from home mortgages when their rates are relatively low. In 1971, mutual savings banks acquired more dollars of bonds than of mortgages (all kinds), \$4.3 billion to \$3.9 billion.

I do not imply that this is socially undesirable. I just make the point that broader lending and investing powers should be evaluated in realistic terms. The mutual savings banks face geographic markets which are different from most of ours. They are using their broader powers in a responsible way.

Importantly, the mix of savings and loan portfolio additions in many cases has altered in the past three years: more construction loans, mobile home loans, nationwide lending, more apartment loans, condominiums and other new types of loans. Some institutions are actually bumping up against the 10% ceiling on nationwide loans.

Finally, the business has moved through the last monetary cycle with the utmost downside stability in lending. The present commitment volume

suggests that there may be a repeat in 1973, even if savings flows drop again. You went through the 1969 crunch lending just as in "normal" 1968. The Board is following the present commitment versus cash flow situation with great interest in its own planning. The savings and loan commitment level was a consideration in the Board's \$1.0 billion financing this month. It is in the public interest to maintain downside stability in mortgage flows within reasonable limits. This cannot be done without a strong secondary market for mortgages. The Bank System by itself probably cannot handle all of savings and loan credit demands next time. This is a \$240 billion business now, not a \$152 billion business, as it was at the end of 1968.

FHLMC CHANGES PICTURE

Another dramatic event has occurred since 1968. This, of course, was the birth of the Federal Home Loan Mortgage Corporation. Title III of the Emergency Home Finance Act of 1970 is the charter statute of the Federal Home Loan Mortgage Corporation. It was signed into law on July 24, 1970. The Mortgage Corporation now is doing \$1.5 billion to \$2.0 billion in loan commitment volume per annum.

Since the first directors' meeting in September, two years ago, the FHLMC has:

1. With the aid of FNMA, developed a more uniform conventional mortgage document which could be used by your associations and others who sell mortgage loans. This was an essential first step in making the mortgage competitive with bonds and other highly marketable "fixed value" investments.
2. Recruited and trained an operating staff of 150 people. Fifty are in the Washington office and the rest in the 12 regional offices.
3. Put into operation seven loan buying programs for FHA, conventional, single-family and multifamily properties which were designed and introduced with the help of many who are at this convention. These programs currently are producing on average a new loan volume at the rate of \$40 million to \$50 million a week.
4. Introduced three corporation sales programs for bonds, loans and loan participations. The corporation already has sold \$460 million of its participation certificates.

The Mortgage Corporation has operated at a profit at a time in which the normal spreads between interest rates on bonds and yields on mortgages and participations is far narrower than has been typical historically. FHLMC has been operated to minimize the risks inherent in dealing in these two markets simultaneously, the bond market and the mortgage market. How has this been done? By simultaneously buying and selling, or by financing as quickly as possible after purchase with maturities which match the averages of the pools of mortgages. Tom Bomar and his people have thus remained a marketing vehicle for savings and loan associations and not a mortgage warehouse. The retained earnings are a cushion to absorb future interest rate vagaries.

The president of the FHLBank in each district will be present at a Mortgage Corporation monthly board meeting in the near future, if he

has not already attended one. Furthermore, to stimulate the participation of the business in policymaking processes, I am pleased to announce today the formation of an FHL Mortgage Corporation Advisory Committee made up of business representatives. As soon as the proper clearances are obtained, the mechanics of this new entity will be given out in detail.

5. FHLMC has originated a continuing program of research and development to facilitate the establishment of a true national secondary mortgage market; the variable rate mortgage; a futures mortgage market; and the first looks at the complexities of a computerized national market exchange system. The first idea we hope you will use, and the next two could be implemented by any number of private institutions, with the Mortgage Corporation providing the results of its research and development.

These are not just exciting ideas. They are part of the Mortgage Corporation's work in progress toward helping the savings and loan business in its drive to change from a predominantly local, single-family home loan business to a nationally oriented multi-service business within the housing market.

OES, DEVELOPMENT IMPROVE STRUCTURE

Let me touch on two areas with which you have virtually month-to-month contact: examinations and supervision, and industry development. First, our Office of Examinations and Supervision has made numerous significant moves forward. Of primary importance in this area has been the publication of a new examination manual. This manual implements a new approach to examinations, an approach based on the concept of "examination by objective." It develops principles for determining the scope of each examination, and it builds programs that will facilitate the exercise of judgment based on individual situations. Further, the manual develops programs that will be acceptable to most (if not all) of the states as a basis for joint federal-state examinations. To date, almost 3,000 savings and loan associations have been examined under these new procedures, and overall the time period required per examination is decreasing.

Secondly, in the area of industry development, truly tremendous strides have been made, and nearly all of them are particularly relevant to savings and loan's competition for added shares of both savings and mortgage markets. The Office of Industry Development undertook two years ago to overhaul completely application procedures and concepts. This it did with imagination, initiative and dramatic effect. Scrapping old methods, OID now accommodates a 43% increase in application workload while decreasing average days processing time by 65%.

Many of your dollars have been saved, in terms of less costly application procedures. The processing time of branch office applications at the Washington level has been reduced from 96 to 35 days, and the processing time for merger applications has been reduced from 133 to 49 days. These cuts in time in Washington could not have been so dramatically reduced, of course, without the program initiated by OID to delegate responsibility to field offices. District Bank offices, especially certain supervisory agents, have contributed importantly to improving application processing at the FHLBank level where it belongs, and the information and advice they

pass along to Washington has greatly aided our decision-making.

Keep in mind the services and the improved status of your FHLBank, along with its somewhat higher costs. Better, bigger, quicker branch services are just one part of the bundle. Think a minute of the decisions obtainable now at your FHLBank compared to 1969. The innovative use of talents and dedication to purpose have created a new confidence in the government's decision-making process.

REGULATORY CHANGES HELP SAVINGS MARKETS

Between 1969 and the present, the Board has adopted 65 regulatory changes to facilitate and broaden savings and loan's lending powers to stimulate housing throughout the country. Fifty-three of these changes have come since September 1, 1970. These regulations are familiar, and a number of you have chosen to put many into practice. They range from mobile home financing to nation and statewide lending, broadened permissible activities of service corporations, land acquisition and development loans, household equipping, and 90% and 95% loans.

Other major regulatory changes have been aimed at savings markets. It was just in June 1969 that savings associations were given the authority to offer savers fixed-rate, fixed-term savings certificates up to five years in maturity. In January 1970, 10-year certificates were approved with eased restrictions on minimum denominations and prior deposit size. New rate ceilings were adopted about the same time.

Remember how the business avoided the then-threatened disintermediation from bunched certificate maturities? Many efforts were made to lengthen the maturity of advances, to increase their availability and purposes for an individual association and to encourage management to plan ahead to use advances. Your commitment level appears to rely in some part upon the new availability and types of advances.

You want to diversify your assets. The Board in 1969 increased the multifamily percentage of assets a federal savings and loan association could hold from 10% to 15%. In 1970, mobile home lending powers were broadened, and savings and loans were given liberalized lending powers for low rent housing. The following year the Board permitted federal associations to make 95% loans, as I have mentioned, and liberalized construction lending rules, extending at the same time the geographical lending limits to a 100-mile radius of each branch office, subject to state boundary constraints.

Frankly, the Board used the scatter-gun approach to broader lending and investing regulations. Each of us on the Board comes from a different region of this country, so we are much aware of the great variety lending markets savings and loan associations serve. For the next few years, you will be considering how to broaden your lending and investing powers further by means of statutory changes. In this process, it is time to review the broadening of the last four years to decide which of the new powers will be of most service to your communities. I say "will" because the demand for permanent home financing has been so great in most areas during the past four years that management has not been called upon to use all of the powers which with a little stretching could

fit its markets. Certainly a lot of the new kinds of loans will be given a trial by hundreds of boards of directors in the next four years. Let us not ignore the potential contributions to the community and to the bottom line of the wider real estate lending and investing proposals the Board plans to revive in the next year's legislative program.

In our efforts to recognize the need for financial institutions to go to the people instead of making the people always come to financial institutions, the Board adopted regulations July 1972 to permit satellite offices and limited branches. As Hal Clarke, who worked closely with the OID on this, wrote in our *FHLBB Journal* last June, these steps should go a long way "toward closing the convenience gap in relation to commercial banks." He added that "the satellite offices will be savings and loan facilities which combine convenience of place with convenience of time by providing continuous service at the most strategic possible locations. . . . The relatively low capital investment makes it an attractive test of an additional means to increase the viability of the savings and loan business in promoting thrift and housing financing."

OFFA AND FSLIC ADVANCES

I would now like to bring you up to date on two of our extremely active integral operations in Washington, the Office of Finance and Fiscal Agent and the Federal Savings and Loan Insurance Corporation. The Office of Finance was carved out of the Office of System Finance and Bank Operations in 1970. Within a year, its director had begun to tie together the many decision-making responsibilities in the asset management, debt management, and financial planning and forecasting areas. This has now been done with substantial cost savings for all of our constituent governmental institutions. Six months ago, in the area of portfolio management, the Board initiated a consolidated securities fund as a pilot program. The non-commingled funds are being managed as never before. The consolidated fund operation for six months (though it is premature to make a final judgment) shows cost savings from centralized management and reduced commissions from making a single net transaction for the commingled fund, as opposed to making numerous small transactions. Savings apparently will be in the millions of dollars annually.

The Board also has approved a new investment policy which has enabled all of the Bank portfolios to be managed more aggressively but with prudence. In addition, the new policy gives the portfolio managers in the FHLBanks and in Washington new goals, new incentives and understanding of the impact of good portfolio management on the earnings of the Banks. The latter has been salutary. I am pleased to announce that during the past six months, during a period in which Treasury bills have increased in yield by more than 1% and thus have declined in price, all of our portfolios have out-performed the market and have done so through application of intelligent money management techniques rather than through excessive risk taking.

In the area of debt management, we moved the Banks' fiscal agent from New York City to centralize all of our financial responsibilities in a single office in Washington, with substantial cost savings. More rigorous

performance standards were established to measure performance of securities dealers marketing our obligations. With this new intelligence we reduced the number in our syndicate from 350 to 160, cutting paper and handling costs appreciably. Dealing with the most efficient securities dealers maximizes the distribution of its securities to bona fide purchasers rather than to speculators, enhancing our ability to price our issues at more favorable rates. By "favorable" I mean that our spread above Treasury securities has been narrowed.

COST SAVINGS EFFECTED

We have utilized the auction technique for selling securities. Cost savings abound. For example, the staff analyzed the cost of engraving securities and found that our delivery price was 78¢ per note. We are now paying 7½¢ per note for quality work. Finally, we have substantially reduced the cost of our dealer concession per amount of debt sold. Based on the sale of more than \$2 billion of securities in 1972, the operational savings alone have totaled more than \$1.1 million or approximately \$100,000 per FHLBank, compared to 1969. Because of our debt extension program the actual dollars spent on operations in the sale of obligations are estimated at \$1.6 million in 1972. During 1969, in the process of selling more than \$8 billion of short-term debts, the System paid nearly \$13 million in commissions and operating costs.

The Office of Finance, working with the FHLMC, has sold debt to support purchases of mortgages in the Government National Mortgage Association Trust. This trust, now totaling \$1.3 billion and yielding 7.4%, is supported by a like amount of bonds with an average maturity of approximately 10 years, consistent with the life expectancy of FHA/VA mortgages in the trust. Some mortgage investors have utilized short-term debt to purchase long-term assets and have suffered gigantic earnings swings or losses because of that fact. Not the FHLMC trust. It has been financed with little of that risk and is yielding nearly a 1% profit annually before operating costs.

The Office of Finance has negotiated more than \$200 million of private placements for the trust in recent months at significant discounts from the public market. For example, Delaware River Port Authority purchased \$104 million of our obligations at 6% for eight years at a time when the public market was nearly 7%. This represents a saving of nearly \$1 million a year for eight years. Likewise, in 1970, the Office of Finance also took over operation of the Federal Savings and Loan Insurance Corporation investment portfolio. On average for the past six years the portfolio had underperformed a standard index by ½ of 1%. I am pleased to advise you that the huge portfolio is now booking income at slightly over 6%. A comparison of the current rate of return versus the historical rate of return reveals that the improvement in earnings of the FSLIC portfolio amounts to more than \$40 million a year.

At this point I would like to discuss the FSLIC in general and some of the innovations brought about in its operations. The FSLIC is organized along highly functional lines which closely parallel our principal problem areas. The FSLIC has strengthened its control over accounting and financial

activities and has developed a comprehensive automated Asset Management Information, Accounting and Cost System. The system is providing a higher level of control and accuracy in terms of the direction of FSLIC liquidation actions. New FSLIC staffers are equipped with real estate accounting and financial analysis skills.

Wherever possible in FSLIC cases, we intend to avoid cashing out savers. In recent history, only one association presented problems which we could not solve without liquidation. Nevertheless, we are prepared with an effective system of insurance payout to pay savers quickly should it be necessary, and we set merger support terms with this in mind.

FSLIC has improved the administration of loans made to savings and loan institutions to prevent default, the financial assistance agreements covering approximately \$400 million of assets, and the liquidation of assets to which the FSLIC holds title. In 1969 FSLIC held title to \$136.8 million of assets. Then, FSLIC established new directions in asset liquidation. Priority rankings, new techniques for establishing market value targets and an aggressive disposition program resulted in liquidations of \$31.1 million last year in the midwestern office alone. As a result of our 1971 liquidation performance, FSLIC effected a reduction of employees in its Westchester, Ill. office. We fully expect to continue staff reductions as we liquidate assets until we retain a relatively small cadre of highly professional liquidators.

During the past four years, the assets and reserves of the FSLIC have grown by nearly 25%. On December 31, 1968, over 17% of the Corporation's reserves were tied up in non-liquid assets. Presently, only 9% of reserves are committed to non-liquid assets. The conversion during the last four years of over \$148 million in real estate related assets into cash, has trimmed the Corporation to less than \$65 million in this category. Furthermore, greater opportunities will now be available to the Corporation for liquidating its remaining \$140 million investment tied up in receiverships by virtue of opposition to the Corporation's claim for post default interest. There will be less incentive to delay rightful payments to the Corporation as well as a removal of incentive to those who may feel a windfall profit can be made through FSLIC liquidation of receivership assets.

Add them up: liquidation of assets, retirement of loans and advances in Las Vegas, and default prevention measures. The Board is in the midst of a serious examination of the possibility of an important reduction in premiums, the cost of insurance to the savings and loan association.

BOARD TO CONCENTRATE ON THREE AREAS

Let us move from now to the future, and this Board's areas of opportunity when the 93rd Congress convenes in January 1973. First, we are continuing to examine the benefits and costs, including mortgage interest rate implications, of possible legislative proposals which emanate from the Hunt Commission recommendations.

I do not mean the whole package of recommendations. Frankly, we are concentrating upon the tax proposal, the asset and liability restructuring, and Regulation Q, in that order. This is the reason the Board believes

that the sequence of legislative change should be just that. You do not start with Regulation Q removal—it is a residual if it is modified at all, after the probable revenues and costs of tax, asset and liability changes are analyzed. Secondly, we will redraft the Savings and Loan Model Association Act, including the federal stock proposals. Thirdly, you are aware that the Board is considering a revision of the FSLIC's premium structure. We will have more to say about these at a later date.

Concerning other matters of considerable interest to the Board and Congress, I would like to mention a few recent proposals which the Board has the statutory authority to initiate but which various congressional leaders have indicated a desire to review before final action is taken.

Our proposed subordinated debenture regulations have been out on comment since October 6. We will be studying these comments. The Board, however, plans to move rapidly toward issuing final regulations in this area, probably before the end of the year. If you anticipate capital needs in 1973, you may want to start making your plans now to attract the capital we are confident will come from sources which typically have not provided funds to savings and loan associations. This includes possible mergers initiated by mutual institutions, which have presented convincing arguments to the Board as to the utility of subordinated debentures in acquiring capital-short marriage partners.

In the area of conversions, the Board is proceeding on its timetable adopted September 22 to end the moratorium on conversions from mutual to stock form by its target date of April 30, 1973. We welcome the indication by congressional leaders that they will hold hearings on this subject as soon as possible after the 93rd Congress convenes.

The third proposal which the Board feels will help stimulate the continuing flow of mortgage credit in 1973 is the variable rate mortgage. Certain legislators also have indicated a desire to study this proposal further. The Board, however, is confident that a conclusive case can be made to show that the VRM should improve your lending capabilities during periods of credit stringency, and at the same time benefit homebuyers and builders. The many comments on this proposal are in, including the strong endorsement made by the U.S. League. All are being carefully analyzed by the Office of General Counsel.

Another project, under study by FHLMC and the Board, is a futures market in mortgages. The Board finds this concept very exciting. You may have read an article I prepared on this for our October 1972 FHLBB *Journal*. Another will appear in the November *Journal*, written by the Mortgage Corporation's research director, Ken Plant. I feel this concept could have a major impact on the savings and loan business in 1973 and may eventually produce a multibillion dollar hedging operation. A futures market would dampen the cyclical variability in interest rates and shift money market risk from builders and lenders, to speculators who seek short run gains by predicting changes in interest rates.

I have occasionally been critical of those Cassandras among financial writers who even today say there is no future for this \$240 billion business with its 100,000 employees and its spectacular record of growth and service. I hope that some of their fears as to serviceability were laid to

rest by this year's farsighted and far-reaching Federal Reserve Board decision taking savings and loans off the "laundry list" for bank holding company acquisitions. In its statement, the Fed recognized the wisdom of Congress in setting up specialized institutions, both private and governmental.

I remain convinced that it is absolutely necessary politically for the business to make a much stronger showing in the moderate and low income area if we are to get the maximum benefits Congress can provide. Thus, I do not regret the Housing Opportunity Allowance Program experiment, although I do not favor funding it beyond its present expiration date. With the two HOAP programs I believe we demonstrated that subsidy funds can be administered without a vast bureaucracy, without committing the government forever to a stream of payments and to the benefit of families who would otherwise not attain home ownership.

Norman Strunk and Thomas Hal Clarke have had something to say about your future in the electronics payments system, with which I heartily concur. We must seek legislation on this subject in the next session of Congress as a matter of survival. You will have access to these payments systems, without doubt.

Finally, the FHLBB has to continue to have status in the highest councils of succeeding administrations. This is only one reason for the new location of the future FHLBB-FHLMC headquarters building. It will face 17th St. and many of the White House staffers in the Old Executive Office Building. It will bring our staff members home from their five scattered locations. It will be a symbol of the greatness of this business.

There is the list of what we like to look upon as some significant achievements accomplished since 1969, as well as some of our most notable proposals for the future. The savings and loan business today stands on a pretty firm foundation, winding up another record year in so many, many areas. I am confident that the business would not be so complacent as to merely sit on a back-to-back record of the three best housing years in history. If the best is yet to come, I would hope that a number of our new tools can be well utilized to build on this present foundation and make 1973 another banner year. If so, certainly the future is now.

I should be less than candid if I did not indicate to you that after seven years in government, I am beginning to feel a seven-year itch. I should like to read to you an announcement. At the White House daily press briefing, 15 minutes ago, my resignation as chairman and member of the Federal Home Loan Bank Board and the Federal Home Loan Mortgage Corporation was announced by the President and accepted. I shall leave December 1, 1972.

My future plans are not definite, but I shall continue to work for housing, and I pledge to you my best in the support of this great business in the future. I shall be in the private sector. The past four years have been immensely rewarding, certainly challenging, and I hope productive. President Nixon has given housing the highest priority. I have enjoyed my association with my colleagues, Carl O. Kamp Jr. and Hal Clarke and Tom Bomar, and also with the most able staff in Washington. I am sure they will continue to advance the concepts which are now on the drawing boards. Thank you for four great years.

SAVINGS AND LOAN LEGISLATION IN THE 93RD CONGRESS

Participants: *John P. Farry, Albert Lea, Minn.;*

Richard G. Gilbert, Canton, Ohio; Tom B. Scott Jr.,

Jackson, Miss.; Norman Strunk, Chicago, Ill.;

Carl Coan, Washington, D.C.; Paul Nelson,

Washington, D.C.;

Moderator: *Stephen Slipher, Washington, D.C.*

John Farry: I doubt that there are any subjects of more significant concern to our business in the next two years than those aspects of our business which will be considered by the 93rd Congress. Because what happens in the 93rd Congress is going to be so important, we have asked a panel of the most knowledgeable people in our business in the area of legislation to discuss with you this morning savings and loan legislation in the 93rd Congress. Steve Slipher, our staff vice president and legislative director of the United States Savings and Loan League, will serve as moderator of the panel this morning and will introduce its members.

Stephen Slipher: Thank you very much, Rip. In planning the convention, we did think that on this last day after so many committee meetings and all the speeches, it would be interesting to wrap it up and have a frank panel discussion, not only of legislation but also of some of the major problems we talked about this week, and some of the things that will be facing us as we adjourn our 80th convention. We do have the panel here and I will just quickly introduce them so we can get on to the discussion.

Our first panel member, Carl Coan, is the staff director of the Housing Subcommittee of the Senate. He not only has that distinguished title but he is in fact the staff man closest to Chairman John Sparkman on all housing matters and, of course, we know Senator Sparkman is Mr. Housing of the United States Senate. Incidentally, Carl, the first thing we want you to do is to carry back our congratulations to the senator for his overwhelming re-election. Mr. Coan, will you take a little bow here.

On the House side we have another veteran staffer—the highly respected chief clerk of the House Banking and Currency Committee. He works very closely with Chairman Patman who of course is so well known to this audience and who made such a great speech on this platform on Monday. Let us welcome the House Banking and Currency Committee director, Paul Nelson.

Next we have three familiar gentlemen. First, our president-elect who for many years has been considered one of the most skillful professional managers in our business and the type you would call a bona fide scholar of housing and finance, which is evidenced by his recent service on President Nixon's Commission on Financial Institutions. Unless he makes a complete fiasco of this panel, he will be installed as president of the U.S. League in about one hour—Richard Gilbert of Canton. Next we have a past president of the U.S. League. He is a distinguished attorney, although otherwise a very decent fellow, and he is completing his second year in the all-important post of legislative chairman—our good friend, Tom Scott of Jackson, Miss. The next man has sat at the hub of the savings and loan business for more than 20 years. There is more input to his office and output from his office than anywhere else in the savings and loan world. Many of the fine developments of our business today are the result of his planning and thinking, as we heard in his Tuesday address on electronic funds. He still has his brain working for the years ahead—Norman Strunk.

To get started here, I am going to ask Dick. Dick, you have been here all week. How would you size up the mood of our delegates—some of the things they are pleased and displeased about. What do you want to send us away from the convention thinking about?

Richard Gilbert: Of course, the big story of the convention is the chairman's resignation. That surprised many, although it had been forecast. However, I sense that the delegates are asking for some new legislation in certain areas. I also sense that they are thinking that there should be no legislation in other areas. Tom will talk in more detail about legislation we need and legislation we perhaps do not need.

I think that there is a concern on the part of the delegates with respect to the failures of some HUD housing programs and a lack of progress in other areas. Then, in chatting with people, I find a concern over the mounting work load of reports, of requirements that are being placed on our institutions and on our staff. For example, some of them were created by an overreaction on the part of agencies and the Congress with respect to consumerism, the truth-in-lending laws, closing cost paper work and the possibility of legislation governing closing costs. The Bank Secrecy Act, which many of us have not even studied yet, will place onerous workloads on us. I think that there is a growing knowledge and concern about electronic funds transfer (EFTS). Will we be in it, will we not be in it, if we do get in it, how do we get in it and when do we get in? I think that those are some of the things that I hear around the halls.

Mr. Slipher: Tom, to narrow it down to specific legislative questions, what are some of the key issues?

Tom B. Scott Jr.: Well, I would think that the rate control issue comes

first. Rate control expires early next year so the Congress will be looking at that matter and trying to determine whether or not an extension is in order. Of course we hope it is. Then we have been given advance notice that there will be hearings on tax reform, and of course we have a big stake in that. We feel that the tax formula which Congress worked out for us in 1969 is a good and equitable formula, and our position will be to try to retain it. Then, the housing bill that we all labored over, Congress in particular, was not passed in 1972; but the issues involved, including closing costs and escrows, are still very much alive. I would think that there is the question of the conversion of mutual institutions to stock institutions. This is a subject that Congress will consider. In addition, we have the laundry list of broader investment powers that we have been discussing for a number of years and will continue to try to get authorized in legislation. In order, then, Regulation Q, tax reform, housing bill, conversion to capital stock and additional investment powers appear to be the top priority issues.

Mr. Slipper: Now that is a long list, and a number of the items you have mentioned are not voluntary or problematical. In the case of Regulation Q, the law expires, and it must be acted on. The housing bill is a holdover, so to speak, and commitments have been made to hold hearings on these other subjects. What Tom is talking about is what is going to happen regardless of what we want to do or whether we initiate anything. That is just the number of balls that are going to be thrown at us. Norman, what is the League's Chicago office going to do to assist on legislation, and what are some of the other big problems that we will be working on?

Norman Strunk: We have, of course, been anticipating these things. We have been generally familiar with the probable shape of the Treasury recommendation with respect to tax reform relative to savings and loan associations. The Treasury, we think, will advocate a repeal of the bad debt arrangement, the bad debt allowance, Sec. 593 for commercial banks, savings banks and savings and loan associations, and will want to put all these institutions on a regular bad debt arrangement similar to any other corporation. Then Treasury would substitute a credit, either as a deduction from taxable income or as a deduction from the net tax, the amount of which would depend upon the extent of an investor's investment in mortgage loans. This same tax credit for mortgage investments would be available to all types of lenders. We, of course, are aware of this approach, we are aware of the general numbers and we have been doing a vast amount of research on this subject to determine the effect upon various institutions so that we will have the numbers ready when we see the precise shape of the Treasury recommendations, and Mr. Mills' committee gets into this question. We have all this on computer tape so theoretically we can just push a button and find the effect of a variety of tax credit proposals.

With respect to the closing costs questions and the interest on escrows, I would guess that these subjects are not going away. The League bothered you with a very extensive questionnaire which took a lot of your staff time to complete, but we now have all that information on computer

tape, readily available for the committees of Congress when these subjects come up again.

With respect to electronic funds transfers, also, we have been doing a vast amount of work, including many staff studies, so that we will be ready whenever this subject is an active one before Congress.

Finally, on Regulation Q, a number of years ago we published a so-called white paper on the subject, summarizing our case on the matter. We will now update that white paper and provide it to everyone who has an interest in the subject so that it can be used in discussing the matter with members of Congress.

Mr. Slipper: I think that may be something that is sometimes overlooked. Behind all of our testimony and all of our positions is a tremendous amount of research, and that is where the Chicago office comes in. They do the surveys and gather the material. If you cannot go to those committees and have facts to back up your argument, then you are not going to get anywhere. We do try to go in there with full credibility. We have talked about the general number of items, but, of course, we have had an election, too. Paul, you might tell us whether the election has changed the committee in any particulars, or how it affects the schedule. Precisely how do you see the schedule of the House Banking and Currency Committee for the next few months?

Paul Nelson: Let me mention first, Steve, that the composition of the House Banking Committee has not changed. It is precisely the same as it was in the last Congress, except for two Democrats and one Republican who retired.

As far as committee action next year, believe me, it is the members who decide, and not the staff. One thing to keep in mind is that the Congress will start on January 3 this time, rather than at the end of January, so it is quite possible that substantive action on legislation will be in order along about the first of February; but as we know, nothing is definite in the political world.

Along with the items that Tom and Norman have mentioned, I think that the committee will be looking into some other matters which are of concern specifically to your business. There is the matter of legislation which would allow savings and loans effectively to solicit public funds. Secondly, there is the check-cashing question, which many of you are familiar with, as well. I think, too, that the committee will probably get into a study or investigation of other items of interest to the business, such as, how the service corporations are working, and a look into the general savings and loan holding company question.

I would like to mention one thing more. When Steve and Norman come to visit us, the sole question on their minds is what they can do, or what they can tell us regarding your business. It must be kept in mind that the House Banking Committee covers a lot of other areas. Just to give you an indication of the committee's broad jurisdiction: It covers all international financial institution legislation; and it covers such matters as export control (the recent Russian wheat deal emanated from legislation that came out of the House Banking Committee) and much more you are familiar with. So, there are other matters and other pressures which

the committee has to concern itself with. But, you may rest assured that when Steve comes by he gets at least two minutes of the committee's staff time—whether he needs it or not!

Mr. Slipher: Carl, let us go back to the Senate side and see what your schedule is and some of the items as you view them coming up. You have a little different jurisdiction, but it is the same from our point of view.

Carl Coan: The big news as far as we were concerned was to get our chairman back in office again!

Now, as far as the committee is concerned, in terms of Democrats and Republicans we may come through with a 9-6 committee next year, rather than the 8-7 committee as we have had this year. It will be a more liberal committee, if you want to use that word. Actually, we do not operate on a partisan basis. Senator Sparkman is very good at working well with both sides; he is a great moderator; the debate may go on, and invariably he will come along and be the man who finally makes the decision. So, he does not work on a partisan basis. Nevertheless, we cannot deny the fact that in the coming year, there will be more representation on the Democratic side than on the Republican side.

Now, I do not know what this means to the savings and loan business. The mutual savings associations have a very good image in our committee and a problem may be as to whether or not that image can be maintained.

We will have a very busy year. We have holdovers. As you know, the housing bill did not get through. There was a great deal of interplay on that. On the Senate side, we were able to get the bill through very early. Then, when it got over on the House side, it ran into some problems. Now, our members were able to work through these things; or maybe the House members had more insight than we did. But, at any rate, when it got up to the last week of the Congress, and the House was about to come through with a bill which would have required a conference, we were rather relieved, to be very frank with you, Paul, that you were not able to come through and force us to sit down a week before the election and resolve those difficult problems!

A housing bill is going to be one of the Senate's high priority issues next year. We will probably get started very early in the year. I think, we will start off with some oversight hearings on the whole problem of FHA. Mr. Romney has been going around the country telling everybody how bad it is. We would like to bring up the administration officials and tell them some of the things that might be wrong with it, too. It may not be the legislation; it may be there are administrative matters, too. Maybe we need to talk with the administration on how we might correct some of those.

Mr. Slipher: Dick, a lot of these issues, such as Regulation Q and tax reform, were discussed by the Hunt Commission. You were a member of that commission. What is the status of the Hunt Commission Report, and what kind of follow-up is there going to be to it?

Mr. Gilbert: We know now that we will have a bill which will come from the White House and be presented to Congress, and our guess is that that will be presented early in the year, February or March. What

Congress will do with the bill is uncertain. The commission's recommendations will have administration support but perhaps not congressional support. Based on some early discussions about the bill, we sense that it will not be a piece of package legislation, and that was one of the major recommendations in the commission report. The thing that many bankers would like to see, for example, would be not just enabling recommendations for broader institutional powers but, in addition, embodiment of recommendations concerning taxation, Regulation Q and interest rate control. Because of the timetable of Congress in dealing with the forthcoming expiration of interest rate control on June first, some matters must be considered soon. Furthermore, different committees work on the various aspects covered in the commission recommendations. Both Howard Edgerton and I, throughout the deliberations of the Hunt Commission, kept saying, "Look, there is no sense in trying to get this in package legislation because different houses of Congress look at it, or different committees look at it. Therefore, we think there will be a bill embodying many of the recommendations but not all. We question what the congressional reaction will be and, of course, at the present time our business has not taken a firm stand as have some of the other groups. The League will look at the recommendations as they come out as legislative proposals, and we will endeavor to have them work to the advantage of our institutions. Of course, we must remember also that whatever comes forth has to work to the advantage of the country as a whole.

Mr. Slipher: Tom, talking about Regulation Q again, when the rate controls went in, we had pretty tight money and we had a chaotic market. It was fairly easy for Congress to see the need to put some controls in. Now we have had some awfully good savings years. How can we argue that we need controls when we have been getting so much money in? It is going to be a little bit different, or is it?

Mr. Scott: It is going to be different and more difficult. If we were always to be in the kind of climate that we are in right now, our savings flows would be too good to argue that we are entitled to rate control or a differential between ourselves and commercial banks. However, I like to believe that the Congress has as good a memory as you and I do; Congress will remember that savings rate wars are just disastrous. Moreover, rate wars tend to push the cost of mortgage money up because in the end the consumer must pay. Really, then it is not the savings and loan business that is being protection with Regulation Q, it is the borrower. I would hope that that kind of an argument before the Congress could be effective.

Mr. Slipher: I want to ask Paul Nelson about schedules and specifics. We heard a lot here including Norman's talk on electronic funds. I do not recall the banking committee ever doing anything about that or having any particular bill. Do you think they do have any interest in that? As a matter of fact, while you are talking, you might unload some of the other things that you hear around the committee halls that maybe we have not initiated, but are going to have to deal with.

Mr. Nelson: I think on the electronics funds transfer system—and believe me, Norman did not write this part of my speech—it is a matter of survival to the savings and loan business if you are not able to participate on a

proper and equitable basis. I do not think there is any question about that. I can say that as an economist, without even looking to my role as a staff member of the House Banking Committee. Congressman St Germain, the chairman of the Bank Supervision and Insurance Subcommittee, has committed himself publicly here, and in previous speeches to savings and loan groups, to hold hearings on the matter of electronic funds transfer systems. Representatives St Germain and Patman have directed the staff to do whatever work is necessary to recommend to the committee the proper way to proceed. Probably what will happen will be an oversight hearing or an investigation. At some point, there will have to be an umbrella of federal regulation, so that there is no question that all participants or prospective participants in the system will have a voice or place to be heard, and be treated on a proper and equal basis.

One more minor matter—we have discussed, or there has been reference made to, consumer items that will be affecting the savings and loan business. As you know, there is a whole host of items that many members think savings and loans should be doing which fall under the general category of "consumer items." I am sure they will be popping up quite frequently during the next two years of Congress.

Mr. Slipher: Carl, do you want to add something about questions raised by senators on your committee? I know that Carl is very patient with us, and the senators may talk about how nice we are, but they do have some questions that they wonder about us sometimes.

Mr. Coan: Steve, I think that this is a matter that needs to be said over and over. You have heard Senator Sparkman say this. Savings and loans must maintain their image. You might recall that when Senator Sparkman addressed this convention last year, he spoke about the basic purpose of a savings and loan association. That is, taking in the savings of the people, and returning those savings to the community, to build that community. And, he got a big cheer from the audience on that.

As we see the savings and loan system grow and get larger and larger, some of this original image is lost. The members of our committee, when they begin to think about legislation which would favor the mutual associations, bring these matters up. They think, we are struggling here with housing problems; we are providing federal funds to provide subsidies, interest rate subsidies; and we have gotten into a lot of difficulty with those programs this year. When they begin to think about the problems with our cities, they say: Here is a savings and loan association; it is doing very well; it is taking in the maximum savings in its history—and still the problems are not solved. How can we bring together these two disparate trends? The problems of the little people who are not getting the proper housing; the problems of the cities; and here the savings and loans, which are the primary lenders and the primary financial support for housing; how are we going to bring them all together and get a better working arrangement?

I think, Steve, when you come up to Congress, you must continue to prove yourself; you must demonstrate that you are doing the job that the members think should be done. You must keep in there, or you may find it difficult to get the new kinds of legislation that you will be looking

for in this coming year.

Mr. Slipher: Yes, and I think you would agree, Carl, that the people who raise these questions, whether you call them consumer advocates or public interest groups, get more numerous and vocal and influential every year. Norman knows this as one of the things that he has been talking to us about for a long time. We recognize that we have to deal with this. Norman, do you have any comment?

Mr. Strunk: Well, yes, I am glad Carl raised this point. We have to go before committees of Congress only for things we absolutely need. Regulation Q is the most obvious need in terms of affirmative legislative action for us. We have to go to the committees with clean hands, having done the kind of job that the members of Congress think we ought to have done, if we expect them to give us the kind of support we hope for. I was impressed with Federal Reserve Governor Andrew Brimmer's extensive speech some months ago arguing that our institutions were not making sufficient loans to black people in the inner city to justify continued support through Regulation Q controls. In a similar vein, it is hard for us to follow the instincts of some in the business and oppose all so-called consumer legislation on the one hand and then ask for legislation to help us on the other.

Mr. Slipher: Not only the ones you have already mentioned, but we hear the inevitable questions come back to us through senators and congressmen: How about interest on escrow, why are closing costs high, and a whole lot of these things. We can sit around the room here, and we can all agree there are good explanations, but they do raise questions in Congress. I hope one of the things the U.S. League has is a reputation for dealing and leveling with the Congress. Dick, we have talked about a lot of pessimistic things, but I know I am an optimist. You are, too. I hope you can close up the panel by telling us that in spite of a few troubles \$250 billion is not bad, and that we are still around here. You did not take on the job to dismantle the business, did you? You count on a vital year.

Mr. Gilbert: Barring a reversal in the next couple of minutes, I will be making an acceptance speech, and it will not have a resignation at the end of it. I do have great hopes for the future of this business and in the United States Savings and Loan League. We have been told that we will be going into high gear in January or early February with respect to what we are viewing as a legislative year, and as Norman and Carl pointed out, if we go into this with a good old building and loan philosophy in mind, we will come out of it all right.

BRICKS AND MORTALS IN THE CONSUMER AGE

by **STANLEY W.G. MORTON**

Chairman, Building Societies Association

London, England

BUILDING SOCIETIES IN GREAT BRITAIN were founded in the 18th century. Originally their members built their own houses, which gave the best possible consumer protection. Today we have an independent non-profit-making body, called the National House Builders Registration Council, which makes sure new house purchasers get a fair deal.

The objectives of the NHBRC are both to insure that no purchase of a new house need suffer financially from major defects or other disasters and to help improve building standards generally. Clearly the council's work is of great benefit to building societies because it is improving the standard of the new property mortgaged to them.

The council was set up because of criticism of private house builders, sometimes fair and sometimes unfair. I gather that there has been considerable criticism of building standards in this country, and while I am not qualified to comment on that, it is significant that one of Ralph Nader's men was in Britain recently looking at how the NHBRC operates. That is why my comments may be relevant to you.

The cornerstone of the operation is the establishment of a register listing virtually every house builder in the country. Before being put on the register each builder's work is inspected, and only if his standards are good enough can he be registered.

Registered builders must contract to comply with specifications laid down by the council, must permit spot-checks by the council's inspectors and must provide a two-year warranty against defects. Rights pass to successive owners of the house. The council also protects purchasers against defects which builders cannot remedy because they have gone bankrupt, and against defects arising, after two years and before 10 years are up, from faults in the load bearing structure. A simple conciliation service deals with 98% of all cases. Other work by the council includes setting up a housing research foundation and establishing a training school for house building inspectors. The cost of all this is less than 1/4 of 1% of the purchase price, which is good value for the consumer. Where builders do not comply with the specifications and standards laid down they can

be, and are, expelled from the register. This is the ultimate sanction.

Such an organization needs teeth, or why should all builders join? The teeth are provided by the building societies which are strongly represented on the council. Building society mortgages will be given only on new houses built by registered builders. If the builder is not on the register he will find it almost impossible to sell his houses. In other words, building societies are a vital element in the council and its work.

The growth of consumerism makes organizations of this sort more and more important. They protect the builder and the building society just as much as the public. The efforts of the NHBRC have insured that standards generally improve and that the whole industry gets a better image.

It would be presumptuous to suggest that our approach is the right one for the United States. It works for us and we have avoided both government control and consumer criticism. Should you wish to adopt something similar, modifications would be necessary.

A scheme could be established on a state-by-state basis, because climatic conditions vary so much that different standards are necessary in different parts of the country. Perhaps the FHA's housing inspectorate could be subdivided by states. As savings and loan associations operate within state boundaries, a state register of builders could be set up. A builder could join the register in a number of states.

Support from savings and loan associations and any other mortgage-providing bodies is essential. Cutting off the money supply to would-be purchasers of jerry-built houses is the best possible sanction against shoddy builders. The good builders and the consumers will appreciate your support.

It is well worthwhile for everyone interested in the well-being of house building to establish an independent body devoted to better standards. There are many improvements we can still make in Great Britain, but I think we have started on the right lines.

AMERICA—WHAT NOW?

by DAVID BRINKLEY

NBC News Commentator

Washington, D.C.

ONE OF THE LARGEST BLOCKS of American voters did not vote for Nixon and did not vote for McGovern. They stayed home and did not vote for anybody. There are about 140 million people in this country who are eligible to vote. A little more than half voted while 60 million stayed home. Those people who chose President Nixon were heavily outnumbered by those who chose nobody. By that standard, Mr. Nixon came in second and Senator McGovern came in third.

Why are so many people so uninterested or so disaffected or so alienated that they decline to take part in the political process—one of the few privileges we have left that does not cost anything? Some people did not vote for good reasons—they were traveling or they were ill—but still millions of people declined to take part in the only activity that all American people do together—the only one where everyone is absolutely equal. David Rockefeller has one vote, and the man who sweeps out his office has one vote.

In looking at this, we need to look beyond the election day itself, because what happened on November 7, of course, was the result of what happened weeks and years before November 7. On the basis of traveling in 40 states, talking to and listening to all kinds of people, of receiving mail from millions of people during 20 years on television, I might make some educated guesses. The primary reason so many people stayed home on election day is that they do not like the way this country is going. They do not believe that their political leaders pay any attention to them. They believe that their opinions are ignored. These feelings deserve to be taken seriously because to a great extent these people are right.

Last year, one of the research organizations went into 10 congressional districts and took meticulous polls of public opinion on 10 or 12 subjects. It followed this by examining the voting records of the congressmen representing these congressional districts to see how well they voted the real wishes of the people who elected them. This research revealed that in nine out of 10 cases the congressmen hardly represented them at all

Very often, in nine out of 10 times, the congressmen voted exactly the opposite of what the people in their home districts wanted. It is no wonder that in another survey last year when a sample of American people were given a list of 20 occupations and professions and asked which ones they admired and trusted the most and the least, politicians came in 19th.

Another poll may be interesting to you. In a survey taken this year among white middle class Americans, only 19% thought the government was doing a better job now than it was doing a few years ago. In private fields—business, finance, science, medicine—64% thought they were being served better now than they were a few years ago. People tend to have a far better opinion of private institutions—such as savings and loan associations—than they do of public and political institutions.

We all know that there are numerous faults and flaws and short comings in private industry in this country. We also know that generally it is responsive to the public's wants and needs. If people by one means or another let private industry know what they want, it will respond and, if possible, give it to them. If they want it in four different colors, it will be offered to them in nine different colors. If they want it in orange and purple stripes and able to make ice cubes while playing "Sweet Adeline," they will get that too. Needless to say, the American people do not get that kind of responsive service from their government. More than serving the public, government is serving itself. It is working ceaselessly to expand its budget, its staff and its power while doing very little for the American people. It is commonly said in Washington that in the war on poverty, poverty won.

QUESTIONS GO UNANSWERED

This is what the American people see when they contemplate their government. If they do not like it, who can blame them? Government takes a third to a half or more of the money they have worked to earn, and in return gives them very little or nothing. When they raise questions, their political leaders do not supply answers.

In a big country like ours, how long can free institutions last? Can they survive the shocks and strains they are subjected to? Can they survive in a country so frequently torn apart by racial and ethnic hatreds? Can they survive in a country we used to think of as a melting pot when we know now the melting pot does not melt? Can democracy survive in a country where political decisions increasingly are being made, not by 75 or 80 million voters, but by one mentally disturbed person with a gun? John Kennedy, Robert Kennedy, Martin Luther King, George Wallace — who will be next? Who will choose our presidents? The voters, making a positive choice, or killers making negative choices by deciding who will not be president? Can our institutions survive much more of that? How much more?

Can our country survive a presidency grown so powerful that it can start a war on its own, without the assent of Congress, and carry it on for years after most of the American people want it stopped? What assurance do we have that some future ambitious president, anxious to be

a hero, will not start another war? Can our institutions survive that? How many times can our institutions survive such situations?

Can our country survive with a legal system unable to protect its own people? A legal system so slow, so cumbersome, so complex, so expensive that it cannot deal with an avalanche of violent crimes. A system where 60% of violent crime is committed by repeaters, caught once and then released, where only a tiny percentage of the guilty — perhaps 1% — are ever punished at all. Can democracy survive that? And how long?

Can it survive a governmental system that taxes with outrageous unfairness? Can it survive the burden of expensive government which costs so much and produces so little?

Out of every six adults in the United States, one is now on the public payroll. Of the new jobs created in this country in the last five years, one out of two has been a public payroll job. In Great Britain, this figure is one out of 18 and in Japan, one out of 36.

All of these are questions which people are asking over and over again, to which they do not get answers. Not only do they not receive answers, they do not even hear their political leaders asking the questions.

People often write and ask why there is so much bad news on the air, why we point out the faults and flaws in the country. The answer is that we care so much for our country that we want to cure what is wrong.

The answer to all these questions may very well be "yes." A democratic country can survive and prosper and thrive. However, we cannot find too much evidence of this in history because no democratic country has ever faced this particular set of problems before. If we overcome these problems, we shall be the first to do so.

In his second term, Mr. Nixon says that he will try to do something about some of this. He will try to tame the bureaucracy. If so, I know that all of us, regardless of our party, wish him well. Looking back over the past 20 years, we find very little evidence that the government has done much about bureaucracy. All that is done efficiently is the collection of taxes—collecting not spending. During this time, governmental power has been expanding. Instead of doing what American people needed or wanted done, government has devoted itself to pushing people into doing what they did not want to do.

So none of us should be surprised that tremendous numbers of people did not vote, that masses of people in our country have a very low opinion of politicians. They feel that no one cares what they think, that the tax system is unfair, that the government is arrogant, remote and indifferent to their needs, primarily concerned with its own.

Senator McGovern essentially offered people more of the same—more taxes, more welfare, more bureaucracy, more people dependent upon government to do for them what they could do for themselves. We saw that his offer was overwhelmingly rejected. What he offered went directly against the mood and the wishes of the American people who want less—not more—of all that. Another election or two and perhaps the politicians will get the message. We hope it may be soon because we may not have too much time.