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# FEDERAL RESERVE BULLETIN

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Board of Governors of the Federal Reserve System  
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# Recent Developments in the State and Local Government Sector

*Laura S. Rubin of the Board's Division of Research and Statistics prepared this article. Sylvia L. Lucas provided research assistance.*

The fiscal position of state and local governments has improved appreciably during the past year and a half. The turnaround from a small deficit in 1982 to a sizable surplus was due largely to increases in tax rates coupled with a strong economic recovery. Despite the improved fiscal position, real outlays for the sector as a whole were unchanged in 1983 as employment and capital spending remained weak.

The weakness in capital spending by state and local governments continued even in the face of a deteriorating domestic infrastructure that required repair and new construction. However, with improved fiscal positions, the generally strong trend of economic activity, and favorable conditions in capital markets, state and local governments now appear to be in a good position to increase capital outlays. Indeed, several cities and states have planned major bond offerings to support construction projects.

Municipal bond markets have remained fairly stable during the current economic expansion, despite the virtual absence of institutional investors and the uneven flow of new issues that resulted from legislative changes. Over the past year and a half, municipal bond yields generally have fallen relative to yields on other long-term obligations, and the level of interest rates is now well below the highs seen earlier in the decade.

## SECULAR TRENDS

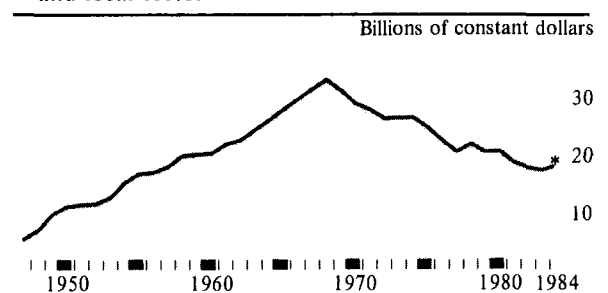
For the first two decades after World War II, the state and local government sector was characterized by rapid growth. Between 1948 and 1968, real outlays by the sector expanded at an average

annual rate near 6 percent, almost twice the pace of the private economy, and even during periods of recession strong increases continued. (Throughout this article growth rates are measured from fourth quarter to fourth quarter, except as noted.) However, the pace of growth slowed noticeably over the decade of the 1970s; and stagnation marked the early 1980s (table 1).

During the first postwar decade, much of the growth in real outlays was for construction (chart 1). Real expenditures for structures increased from about 14 percent of total state and local spending in 1947 to around 25 percent by 1954, and held that share through 1968. During that period, outlays for educational facilities and the highway system rose significantly. This was a period of rising birth rates, increasing real per capita income, and rapidly improving standards of living. Enrollment in public schools soared, necessitating the construction of new facilities. In addition, the federal interstate highway program, begun in 1956 and financed in part by federal grants to states, produced a surge in road construction.

Because capital outlays were so high, the combined operating and capital account of state

1. Real outlays for construction in the state and local sector



Annual data.  
\*First half, 1984; annual rate.  
SOURCE: U.S. Department of Commerce.

1. Growth in the state and local government sector, selected periods, 1948-84<sup>1</sup>

Percent except as noted

Item	Annual average			1983	1984 <sup>2</sup>
	1948-68	1969-79	1980-82		
Total nominal expenditures .....	9.9	10.5	7.9	5.6	10.3
Total real purchases of goods and services .....	5.9	2.6	-4	0	3.6
Real construction outlays .....	9.2	-3.8	-5.1	-6.7	21.4
Nominal revenues .....	9.6	11.5	7.2	9.6	10.6
Grants .....	12.6	15.3	.3	2.2	16.1
Own sources .....	9.2	10.7	9.2	11.3	9.5
MEMO: Surplus (deficit -) <sup>3</sup> (billions of dollars) .....	-2.5	.9	3.5	6.6	13.0
Factors in outlays					
Employment .....	4.5	3.3	-4	-4	1.3
School-age population .....	1.9 <sup>4</sup>	-1.3	-1.5	-1.1	-1.1

1. Annual growth rates measure changes from the fourth quarter of one year to the fourth quarter of the next year except as noted.

2. Growth is measured from the fourth quarter of 1983 to the second quarter of 1984 at an annual rate.

3. Operating and capital account.

4. 1960-68.

SOURCES: U.S. Departments of Commerce and Labor

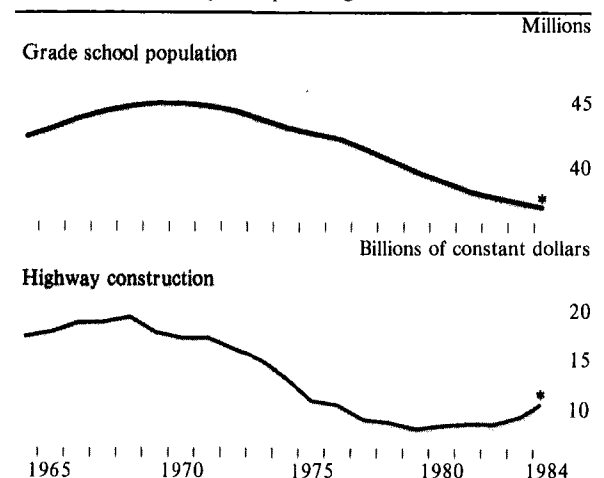
and local governments (as measured by the national income and product accounts) was in deficit in every year between 1948 and 1971. Expenditures continued to outpace receipts despite hefty advances in both federal grants and revenues from these governments' own sources (tax and nontax receipts). During the 1960s, federal grants financed about 20 percent of capital spending, and long-term municipal bond offerings financed 40 percent; the remainder was drawn from tax and nontax receipts, reserve funds, and short-term borrowing.

In the late 1960s, real outlays for construction were reduced. Building of educational facilities peaked in 1967; the grade-school population began to fall three years later and has since trended down steadily (chart 2). Highway construction also began to wind down in the late 1960s. Despite these reductions, total real outlays for the state and local sector continued to rise in the 1970s, albeit at a slower rate, as welfare programs became a major priority. Moreover, unlike the preceding period, the 1970s saw an increase in the rate of growth of revenue, as receipts from both federal grants and state and local tax and nontax collections picked up. The string of deficits was broken in 1972 when federal aid jumped nearly 30 percent, in part because revenue sharing was put in place. Deficits reappeared briefly during the 1974-75 recession, but in later years, surpluses climbed to \$10 billion. The surpluses were concentrated among local governments, while states hovered near fiscal balance during the period.

The public reacted to these large surpluses, in a period of rapid inflation and rising real tax burdens, with dismay. In 1978, voters in California approved Proposition 13, a constitutional amendment designed to reduce property taxes collected by local governments in that state, beginning a series of tax revolts that continued into the 1980s. Thirty-two states enacted legislation to reduce taxes or limit the growth of government.

From 1980 to 1982, the fiscal positions of state and local governments weakened, reflecting cuts in federal grants and two recessions. Federal aid

## 2. Indicators of capital spending

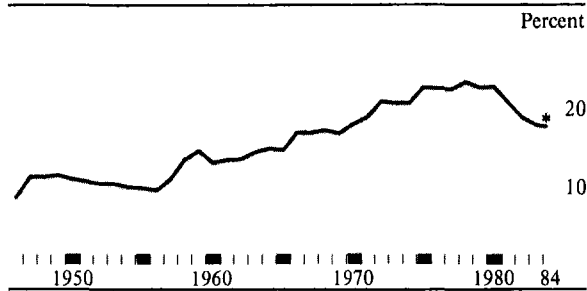


Annual data.

\*First half, 1984; annual rate.

SOURCE: U.S. Department of Commerce.

## 3. Federal aid as a percent of state and local revenue



Annual data.

\*First half, 1984.

SOURCE: U.S. Department of Commerce.

to state and local governments fell about 5½ percent in nominal terms between calendar years 1980 and 1982. Federal aid accounted for 18 percent of total revenue accrued by state and local governments in 1983, compared with 23 percent only three years earlier (chart 3). Much of the decline came in labor market programs as public service jobs provided by the Comprehensive Employment and Training Act were phased out; grants for all labor training and services fell from \$8½ billion in 1979 to around \$3 billion in 1982. In addition, major, lasting reductions were made in entitlement programs administered by state and local governments, such as welfare, medicaid, and school lunches. Other cuts in federal aid were in community development, highway construction, and revenue sharing.

Concurrently with cuts in federal aid, state and local governments weathered two economic recessions. The sector had only a temporary setback in the 1980 downturn; growth in receipts slowed in the second quarter of that year, and the surplus dwindled to near zero. The more recent recession, however, had a considerable impact on state and local fiscal positions. Despite a reduction in the pace of expenditures, a small deficit was recorded for the sector in 1982. It was largely a result of a sizable decline in the growth of tax and nontax receipts combined with the drop in federal grants for the year as a whole. The weakness was centered in the states, whose revenue systems are fairly responsive to aggregate economic activity. In contrast, local government receipts, which are dependent largely on property taxes, held up well in 1981 and 1982.

## THE 1983 RECOVERY

The fiscal positions of state and local governmental units quickly strengthened in 1983. The turnaround reflected both economic and political factors: not only did tax revenues benefit from a strong economic recovery, but also budget balancing (over a one- or two-year period) is mandated in every state except Vermont. Construction spending had been cut back as revenue growth slowed earlier in the decade and funds were shifted to current operating needs. Moreover, many governmental units limited labor costs, which account for more than half of the sector's purchases of goods and services. In 1983, 41 states either granted no wage increases to their employees or held pay hikes to 5 percent or less, and 40 states imposed hiring freezes or actually reduced their workforces.

Most of the tax hikes came during 1983, when 38 states raised at least one tax. Sixteen states increased personal income taxes, and many states raised major business taxes. In addition, general sales taxes, as well as taxes on cigarettes, alcoholic beverages, and fuel, were increased. With higher tax rates in place and tax bases on a cyclical upswing, states' revenue jumped \$7.5 billion in 1983. As a result, the operating and capital surplus for the state and local sector averaged more than \$6½ billion in the four quarters of 1983 and \$13.0 billion for the first two quarters of 1984.

The improvement in the fiscal positions of state and local governments in 1983 was unexpected. When budgets were planned and tax proposals set forth during the late winter and spring of 1983, the outlook appeared dismal. Sizable tax increases were considered a necessity, and plans were made to slow outlays. These policies, it was hoped, would result in balanced budgets, or perhaps small surpluses, in the year ahead. The surprise came from the strength of the economic recovery. At the end of 1982, many private forecasters had been expecting real growth over the four quarters of 1983 to be 4 percent or less; in fact, real gross national product moved up about 6¼ percent. With retail sales, as well as personal and corporate income, expanding more rapidly than anticipated, rising tax receipts pushed up surpluses.

The unexpected strength of economic activity during 1983 and the lag between plans and implementation explain the coincidence of large budget surpluses and weak capital outlays. Indeed, capital spending by municipal units appeared especially low in light of the attention given in recent years to the problems of sustaining the domestic infrastructure. It is widely believed that many of the nation's highways, bridges, sewers, and airports need restoration and modernization, but state and local governments had not yet begun to meet this challenge early in the 1983 recovery. However, given improved fiscal positions, capital spending programs are expected to be a major priority in the years ahead. Moreover, additional funding for improving highways will be forthcoming as a result of the Surface Transportation Act, federal legislation that raised gasoline and diesel fuel taxes by 5 cents per gallon beginning in April 1983. Funds raised by this tax will be used by state and local governments for federal highway repair and public transit.

Facilities in greatest need of repair and upgrading include urban roads and the interstate highway system, as well as waste water treatment plants and many municipal water and sewer systems. Also in need of modernization are public transit systems, and airports.

Funds to rebuild the infrastructure will continue to be derived from a variety of sources—borrowing in the tax-exempt market, the revenue from governments' own sources, and federal grants. Only a portion of the recent surpluses is likely to be used for capital outlays in the near term. Instead, these funds are expected to replenish reserves drawn down during the recession, to provide rebates to taxpayers, and to permit tax reductions; earlier this year tax rates were reduced in several states, including Michigan, Nebraska, and Pennsylvania. In addition, some state and local employees may benefit from catch-up in pay, and outlays for services may increase.

#### *BUSINESS CYCLES AND STATE AND LOCAL ACTIVITY*

The strong upward trend in the activity of the state and local sector before the 1980s was not interrupted by the cyclical ups and downs typical

of other sectors of the economy. During the six postwar downturns preceding 1980, real purchases by state and local governments grew an average 7½ percent, and they were especially strong during the earliest recessions. After 1980, however, the sector appeared less resilient during periods of weakness: real outlays in the sector fell 0.2 percent during the brief 1980 downturn and were flat in the last recession.

Spending behavior during recovery periods has also changed dramatically. Before 1980, real purchases of goods and services by state and local governments continued to grow during recoveries, expanding between 2½ and 8½ percent in the first year of postwar recoveries. But the year after the trough of the 1980 recession, real purchases actually fell about 1¼ percent, and they were unchanged over the first year of the most recent recovery. The failure of spending to grow in the 1980s stemmed primarily from two factors already discussed: the reduction in outlays associated with the sharp drop in federal grants and the continued decline in spending for construction that began in the late 1960s.

#### *FINANCING STATE AND LOCAL OUTLAYS*

State and local government outlays are financed through tax receipts, federal grants, and a variety of nontax sources—for example, motor vehicle registration and license fees, rents and royalties, and various fines. When receipts exceed expenditures, excess funds are often placed in special reserve funds that can be drawn down when revenues are relatively low.

When state and municipal government treasurers are threatened with a deficit in their current operating accounts, they have a variety of recourses. Initially, a shortfall may be covered by drawing down reserve funds while attempts are made to hold the line on spending. Legislatures also may try to raise taxes if they think the imbalance will persist. For temporary cash needs, state and local governments may borrow in the short-term tax-exempt securities market by issuing notes, usually with maturities of a year or less. Notes issued in anticipation of receipts from taxes or other revenue flows have been dubbed tax anticipation notes (TANs) and revenue anticipation notes (RANs).

### *The Municipal Bond Market: External Financing of Capital Expenditures*

In order to finance public construction activity, state and local governments issue a substantial volume of long-term debt each year, in the form of general obligation and public-purpose revenue bonds. General obligation bonds typically must be approved by public referendum and are backed by the taxing authority of the governmental unit. In recent years, revenue bonds have become increasingly popular. These bonds generally do not require a referendum, and they are backed by the flow of revenues generated by the completed structure—for example, user fees, in the case of water, sewer, and electric facilities, and tolls, in the case of highways and bridges.

Chart 4 shows construction outlays in nominal terms by state and local governments and borrowing in the market to obtain new capital for public purposes. While capital formation trended up over the 1970s, gross bond volume remained relatively stable until 1982. State and local bond issuance was reduced somewhat in 1979 and 1980, reflecting the steady rise in municipal bond interest rates that began during the summer of 1979. Municipal bond rates moved down in 1982 as other credit market conditions eased, and the lower rates were accompanied by a sizable volume of bond issues.

While both construction outlays and gross offerings of public-purpose bonds generally have trended up in the postwar period, movements in the two from year to year have differed. Proceeds of bonds sold to finance capital construction do not have to be spent on the project itself

for three years. During that time, governmental units can make alternative investments and earn arbitrage profits on the spread between tax-exempt and taxable yields. This lag between bond sales and construction outlays influences their relationship. In addition, movements in construction spending are associated with changes in federal grants. For example, a rise in grants may result in increased outlays for structures without a need for additional bond financing.

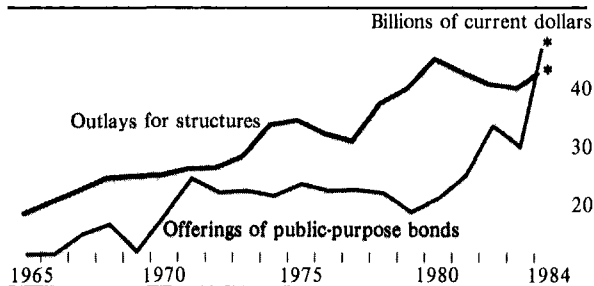
Legislative changes can also influence the timing of municipal bond financing. This influence was particularly evident in the first half of 1984. As explained below, during that time offerings of private-purpose tax-exempt bonds were unusually low as issuers awaited congressional extension of issuing authority and clarification of new restrictions. With that supply of bonds temporarily reduced, offerings of public-purpose bonds, notably for education and transportation needs, surged, rising considerably more than outlays.

### *Private-Purpose Bonds*

The total volume of tax-exempt bonds represents not only governmental funding needs, but in recent years, an increasingly large volume of private-purpose revenue bonds, securities issued by state and local government authorities on behalf of private individuals or businesses. Officials and issuers argue that the tax-exempt status of these bonds is legitimate because funding these private investments fosters expanded economic development, more jobs, higher incomes, and a broader tax base in the local area. In addition, new facilities and housing are seen to contribute to a higher standard of living in the community. Nonetheless, the primary direct beneficiaries of these bonds are specific individuals and businesses rather than the general public.

Private-purpose municipal bonds derive their tax-exempt status from various provisions in the Internal Revenue Code. The bulk of these bonds is sold to finance housing, industrial development, student loans, and certain private nonprofit organizations. Table 2 illustrates the growing importance of private-purpose bonds in the market for long-term tax-exempt securities. In 1975,

4. Municipal bonds and construction



Annual data.

\*First half 1984; annual rate.

SOURCE: U.S. Department of Commerce and Federal Reserve Board staff estimates.



## 2. Long-term tax-exempt offerings, 1975-83

Billions of dollars except as noted

Purpose of offering	1975	1976	1977	1978	1979	1980	1981	1982	1983
Total <sup>1</sup> .....	31.3	35.0	46.8	49.0	48.1	54.9	56.7	85.8	93.3
Refunding bonds.....	.9	3.5	9.6	9.3	1.9	1.6	1.2	3.8	14.0 <sup>2</sup>
New capital.....	30.4	31.5	37.2	39.7	46.2	53.3	55.5	82.0	79.3
Public purposes.....	23.6	22.4	22.6	22.0	18.7	21.1	25.1	33.6	30.0
Private purposes.....	6.8	9.1	14.6	17.7	27.5	32.2	30.4	48.4	49.3
MEMO: Private-purpose bonds as a percent of new capital.....	22	29	39	45	60	60	55	59	62

1. Data from *Bond Buyer* adjusted to include privately placed small-issue industrial development bonds.

2. Public Securities Association.

SOURCES. *Bond Buyer*, U.S. Department of the Treasury, and Federal Reserve Board staff estimates except as noted.

these bonds accounted for less than 25 percent of state and local borrowing for new capital; by 1983, their share had grown to 62 percent. Steady advances were apparent for most categories, with spectacular increases in single-family housing bonds and small-issue industrial development bonds (IDBs) (table 3); these two types of bonds are discussed in considerable detail in the accompanying appendix. In 1983, single-family housing bonds and small-issue IDBs made up half of private-purpose issues. Multifamily housing projects and private nonprofit hospitals also received substantial amounts of funding.

In recent years, the Congress and the administration have become increasingly concerned about the use of private-purpose bonds. First, these issues may represent some abuse of the original intent of the tax-exempt feature of municipal bonds—that is, that state and federal governments not hamper one another's activities. Second, because funds are being raised in the tax-exempt, rather than the taxable market, the large volume of private-purpose bonds represents a substantial revenue loss to the U.S.

Treasury. Third, the increased supply of these bonds in the tax-exempt market exerts upward pressure on interest rates for all tax-exempt securities, thereby raising the cost of borrowed funds for public purposes by state and local governments.

*Municipal Bond Volume in Recent Years*

Tax-exempt offerings for both public and private purposes have risen substantially during the past two years, following the peak in municipal bond rates in early 1982. Most of the increase was in revenue bonds (chart 5). Issuance continued to rise in 1983, as the lower level of interest rates sparked a large volume of refunding bonds. Another element was the provision in the Tax Equity and Fiscal Responsibility Act (TEFRA), enacted in 1982, that required all municipal bonds issued after January 1, 1983, to be in registered form; that is, issuers would no longer have the option of offering bonds in bearer form. Issuers and underwriters were concerned that

## 3. Tax-exempt offerings for private purposes, 1975-83

Billions of dollars

Purpose	1975	1976	1977	1978	1979	1980	1981	1982	1983
Total private-purpose offerings.....	6.8	9.1	14.6	17.7	27.5	32.2	30.4	48.4	49.3
Housing <sup>1</sup> .....	1.5	2.7	4.5	7.1	12.1	14.0	5.6	14.3	17.6
Single-family mortgages.....	*	.7	1.0	3.4	7.8	10.5	2.8	9.0	11.0
Private nonprofit hospitals.....	1.4	1.9	3.3	2.3	2.3	2.6	3.3	6.7	7.7 <sup>2</sup>
Student loans.....	*	.1	.1	.3	.6	.5	1.1	1.8	2.8
IDBs									
Pollution control.....	2.0	2.1	3.0	2.8	2.5	2.5	4.3	6.5	2.8
Small issues.....	1.3	1.5	2.4	3.6	7.5	9.7	13.3	14.7	13.6
Other <sup>3</sup> .....	.6	.8	1.3	1.6	2.5	2.9	2.8	4.4	4.8

1. Includes some IDBs for multifamily housing.

2. All private exempt entities.

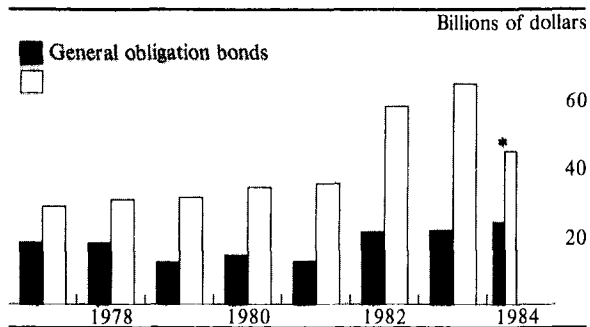
3. Includes IDBs for the following: mass-commuting vehicles, industrial parks, and facilities for local district heating and cooling, electric energy and gas, hydroelectric generation, sewage or waste

disposal, airports, docks, wharves, and sports and convention centers. Data before 1983 are staff estimates.

\*Negligible.

SOURCES. *Bond Buyer*, U.S. Treasury Department, U.S. Department of Housing and Urban Development, and Federal Reserve Board staff estimates.

## 5. Total municipal bond offerings



Annual data.

\*First half, 1984; annual rate.

SOURCE: Public Securities Association.

registered bonds would not sell as well as bearer bonds and sought to market a large volume of bonds before the requirements went into effect. The result was an increase in tax-exempt offerings near year-end 1982. When the effective date for registration was postponed to July 1, 1983, a second rush to sell bearer bonds prompted a surge in volume in the second quarter of 1983.

Offerings of private-purpose bonds, especially single-family housing bonds, student loan bonds, and IDBs, also surged during the fourth quarter of 1983. This increase reflected two provisions embodied in the Tax Reform Act of 1983, which was approved by the House Ways and Means Committee in October but was not passed by the Congress until June 1984. First, authority to issue single-family mortgage revenue bonds was due to expire at the end of 1983, and passage of the Tax Reform Act would have re-authorized these bonds for several more years. Uncertainty over when the Tax Reform Act would pass encouraged many housing authorities to market bonds in 1983 while they were still legal under the existing law.

Second, the act contained provisions that limited the volume of IDBs and student loan bonds issued in each state by setting caps on volume; in addition, it would have further limited the uses of funds, arbitrage, and depreciation methods. As the legislation was written, the effective date was January 1, 1984. Thus issuers preferred to come to market at the end of 1983 under the existing law: they were concerned that IDBs sold in 1984 might lose their tax-exempt status if and when the new law were enacted.

The rate of total municipal bond issuance was considerably lighter in the first half of 1984 than in 1983. During the first six months, volume averaged \$69 billion at an annual rate, compared with an average of \$83 billion in the preceding two years. During the lapse of legislative authority, issuance of tax-exempt bonds for owner-occupied housing was virtually nil, and the volume of IDBs was unusually light. Many of the IDBs that came to market earlier this year were refunding bonds. In some cases, however, issuers were assured by state officials that their offerings would be granted tax-exempt approval even under strict volume caps. Finally, some IDBs were issued either with mandatory "tax calls"—that is, they would be called if the tax-exempt status were denied—or with alternative, higher rates that would be paid if the bonds became taxable.

In late June, the Congress finally passed the Deficit Reduction Act of 1984, which extended authority to issue tax-exempt single-family mortgage revenue bonds and set out new restrictions on IDBs. Following passage of the act, offerings of both types of bonds came rapidly to market. Because housing bonds were not legally authorized until the President signed the bill into law, they could not actually be delivered, and the bond indentures contained language to that effect. The bill was signed in mid-July, and around \$7 billion of these bonds were sold by the end of September.

Industrial development bonds also became an increasingly important element in the volume of municipal bonds issued during the summer. Because IDBs are much harder to identify, precise data on their volume will not be known until special reports, as required by TEFRA, are filed and tabulated. Nonetheless, some analysts estimate that at least \$3 billion to \$4 billion of IDBs were marketed in the third quarter.

Partly because of this surge in single-family mortgage revenue bonds and IDBs, the total volume of municipal bond issues jumped to an estimated monthly average of about \$7.0 billion in the third quarter compared with \$5.7 billion per month during the first half of the year. Offerings were also bolstered by both private- and public-purpose bonds that came to market on accelerated schedules to take advantage of a decline in interest rates in July and early August.

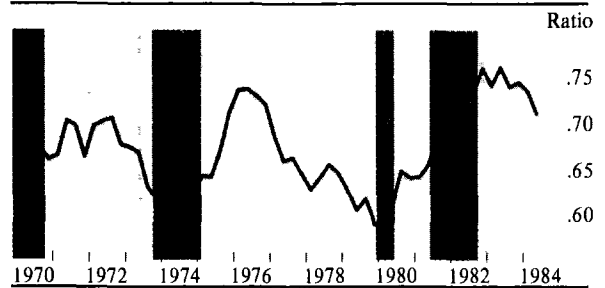
*Municipal Bond Rates*

Interest rates on general obligation municipal bonds peaked just above 13¼ percent in January 1982 after rising steadily during the preceding two years (chart 6). Interest rates fell throughout 1982, bottoming out at about 9 percent in April 1983. Over the next year rates generally remained in the range of 9½ to 10 percent. Then in May 1984, rates rose to about 10½ percent, reflecting the firming in the Treasury and corporate securities markets as well as anticipation of the increased supply of private-purpose tax-exempt bonds that might occur when legislative restraints were removed. During the summer months, rates averaged below 10¼ percent.

Interest rates on tax-exempt bonds do not necessarily move in tandem with those on taxable securities. Indeed, the ratio of yields on tax-exempt bonds to those on taxable bonds has a cyclical pattern that is influenced by the behavior of property and casualty insurance companies and commercial banks—the major institutional investors in municipal securities (chart 7). In the past, these institutions frequently stayed out of the tax-exempt market during recessions as lower profits reduced their need to shelter income. With reduced demand by these institutions, the ratio of tax-exempt to taxable yields had to be higher to attract individual investors. As earnings improved, these institutions would increase their purchases of tax-exempt securities.

Unlike earlier expansionary periods, the 1983–84 recovery saw little activity by institutional

7. Ratio of yields on tax-exempt bonds to taxable bonds<sup>1</sup>

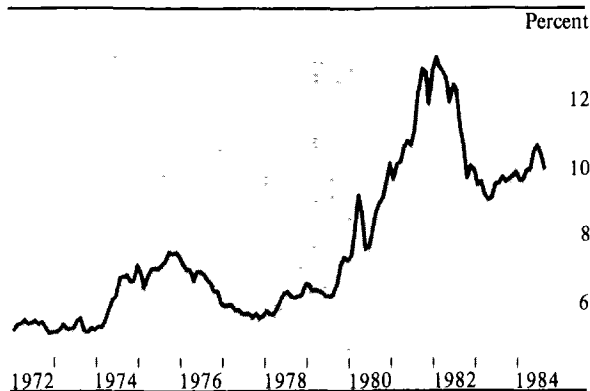


1. Quarterly data; ratio of the index of 20-year general obligation bonds published by the *Bond Buyer* to the index of recently offered A-rated corporate utility bonds published by the Federal Reserve Board. Shaded areas denote recessions.

investors in municipal markets. Property and casualty companies have experienced unprecedented underwriting losses since 1979. In addition, commercial banks have enjoyed less tax benefit from investing in municipal bonds than in the past. Before 1983, banks could use borrowed funds to buy tax-exempt bonds and fully deduct their interest costs. However, TEFRA changed that by allowing only 85 percent of costs incurred to be deducted, thereby reducing the incentive for banks to invest in municipal bonds. The Deficit Reduction Act of 1984 reduced this proportion to 80 percent.

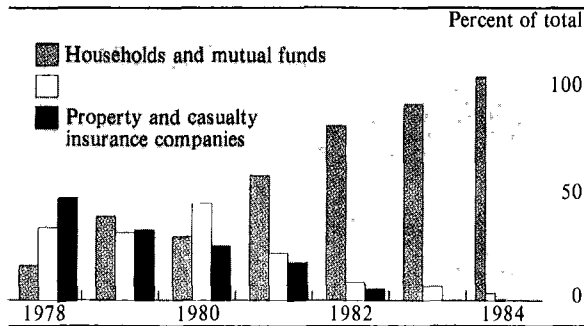
In contrast, purchases of municipal securities by households, directly or through tax-exempt mutual funds, rose substantially during the recent expansion (chart 8): mutual funds' holdings of municipal securities rose by nearly \$15 billion at an annual rate in the first half of this year, compared with about \$10 billion in the preceding two years. Mutual funds probably have grown rapidly in part because they have given individual investors access to the tax-exempt market that might have been closed to them because they lacked the resources or expertise to buy individual bond issues directly. Through the mutual funds individual investors can earn tax-exempt interest income on a diversified portfolio. Moreover, in recent years tax-exempt mutual funds have been able to offer individuals increased liquidity and various transaction capabilities, such as check-writing and exchange privileges with other mutual funds. Much of the rise during the 1980s has been in mutual funds that invest in short-term tax-exempt securities, including tax-exempt notes and commercial paper.

6. Municipal bond yields<sup>1</sup>



1. Monthly data; the index of 20-year general obligation bonds published by the *Bond Buyer*.

## 8. Purchases of state and local government obligations by major market participants



Annual data. Government obligations include net offerings of short- and long-term issues.

\*First half, 1984; annual rate

SOURCE: Federal Reserve flow of funds accounts.

### Other Developments

Despite a variety of institutional and economic changes, the municipal market has remained relatively stable. The registration requirement has not resulted in a noticeable change in the market. Although legislative changes interrupted the flow of bonds, yields appeared to move about as expected relative to yields on other long-term obligations, and issuers have been able to successfully sell bonds that previously had been withheld from the market, such as single-family housing bonds.

Moreover, tax-exempt markets in the aggregate do not appear to have suffered long-term repercussions from the default of the Washington Public Power Supply System (WPPSS) during the summer of 1983. On the other hand, several utilities with nuclear power plants under construction have been plagued by serious financial problems owing to cost overruns, construction delays, and heavy debt burdens. It has been estimated that bonds issued by troubled utilities have been trading at large interest-rate premiums—as much as 400 basis points—for some time. However, municipal utilities that do not have nuclear plants under construction and issuers of other types of municipal bonds seem to have been unaffected by the developments surrounding WPPSS.

### CONCLUSION AND OUTLOOK

During the first year of the current recovery, real outlays by state and local governments were

unchanged. This weakness came in the face of an improving fiscal position throughout the year. However, in early 1983, legislative bodies were planning tax increases and spending cuts and did not anticipate either the strength of the economic recovery or the rise in surpluses that resulted. Clearly, 1984 has been different: real purchases were up 3½ percent at an annual rate over the first two quarters of the year as real construction outlays advanced 21 percent.

Moreover, issuance of public-purpose bonds appears to have risen in the first half of 1984, after a decline in 1983. Plans are being made to undertake major capital projects. Much of the funding, especially for highway repair, is expected to come from federal grants. However, several states and cities, including Connecticut and Alabama, and Houston, Texas, have already announced plans for major bond offerings. The proceeds appear to be targeted at roads and bridges, although the Houston program also calls for spending on sewer and drainage projects and park improvements.

Furthermore, growth in the state and local sector is likely to accompany continued expansion in economic activity. The lack of growth in spending in the early 1980s stemmed primarily from two factors. First, revenue growth was down: federal grants fell significantly in nominal terms between 1980 and 1982, and then trended up only slowly, and receipts from tax and nontax sources slowed somewhat. Second, outlays for construction had been trending down since the late 1960s, largely in response to the end of the postwar baby boom, and by 1983, these real outlays were at about the same level as in 1956.

Neither of these factors is expected to remain in force. Federal grants, in nominal terms, rose 16 percent at an annual rate in the first half of this year and are expected to continue trending up. In addition, in light of strengthened fiscal positions and heightened concern about the infrastructure, real outlays for construction are likely to expand. This outlook depends on three key factors: the maintenance of a strong tax base produced by steady economic growth; stable capital markets to permit bond financing; and a steady level of federal support.

*The appendix begins on the following page.*

*APPENDIX: PRIVATE-PURPOSE BONDS**Single-Family Mortgage Revenue Bonds*

Municipal bonds issued to provide funds for owner-occupied housing were virtually unknown until the late 1970s. Then between 1978 and 1980, as interest rates on long-term, fixed-rate mortgages rose steadily, state and local housing authorities began to raise increasing amounts of funds in the tax-exempt market with the intention of distributing the proceeds to homebuyers at interest rates substantially below those on conventional mortgages. During this time, there were essentially no federal restrictions on these bond issues.

The volume of single-family mortgage bonds rose to \$10½ billion in 1980, accounting for almost 20 percent of total municipal bond offerings that year. Lawmakers became alarmed about the volume of these bonds and their possible abuse, and in December the Congress passed the Mortgage Subsidy Bond Tax Act of 1980. Its purpose was to limit issuance of single-family mortgage bonds. Provisions confined borrowers to first-time homebuyers and set limits on prices of homes that could be financed under these programs. Each state was subject to a volume cap, and rules were set to prevent state and local governments from accruing arbitrage profits. Finally, a sunset provision called a halt to the issuance of new bonds for owner-occupied housing after December 31, 1983.

In 1981, the year after enactment of this law, bond volume dropped precipitously, reflecting the strict arbitrage limits as well as high interest rates. The arbitrage restriction allowed a differential of only 100 basis points between the rate on the mortgage revenue bonds and the actual mortgage interest cost. Often this spread was not enough to cover administrative costs, requiring state and local governments to subsidize these bonds. Some preferred to suspend bond offerings. In addition, bond volume was reduced in 1981 in the face of extremely high interest rates. By October of that year, the rates on 30-year conventional, fixed-rate mortgages had soared to nearly 18.5 percent. The housing market was at its lowest level in the postwar period, and even with the savings on mortgages funded through

mortgage revenue bonds, many potential first-time homebuyers either could not qualify for a loan or simply were not interested in buying a house at relatively high rates.

In 1982, the volume of bonds issued for owner-occupied housing swelled. This development reflected primarily the decline in mortgage rates throughout the year and the corresponding improvement in the housing market. In addition, a provision in the Tax Equity and Fiscal Responsibility Act of 1982 (TEFRA) relaxed the arbitrage restriction from 1 percent to 1⅛ percent for all bonds issued after September 3 of that year.

Offerings continued to rise in 1983, especially in the second half of the year, when housing market activity advanced and the authority to issue bonds for owner-occupied mortgages neared its expiration date. Efforts under way in the Congress in the final months of 1983 to extend authority for these bonds beyond the sunset date were not successful. However, in June 1984, the Congress enacted new tax reform legislation that re-authorized these bonds until the end of 1987.

Issuance of single-family mortgage revenue bonds surged during the summer of 1984. It has been estimated that about \$7 billion worth of these bonds was sold in the third quarter. Nonetheless, total volume for the year is expected to be less than the \$11 billion offered in 1983. In part, the reduction is expected because issuance of these bonds is permissible during only half the year. In addition, housing activity has slowed, and the pool of homebuyers eligible for these loans has shrunk. Finally, the new legislation provided federal tax credits as an alternative to funding mortgages through tax-exempt markets. Some housing authorities may prefer to offer these credits.

*Small-Issue Industrial Development Bonds*

Industrial development bonds (IDBs) are issued by state and local governments on behalf of private businesses to finance industrial and commercial facilities. Interest on these bonds is exempt from federal taxes when the proceeds are intended to fund certain activities, including industrial parks, some hydroelectric generating

properties, qualified mass-commuting vehicles, pollution-control facilities, and residential rental property. Presumably, these projects were allowed tax exemptions because they were considered to have substantial external economies, or social benefits. Moreover, it may have been felt that permitting their construction using tax-exempt funds would provide the incentives needed to get them built.

One type of IDB that has gained tremendous popularity is the small-issue IDB—an issue of no more than \$1 million (\$10 million when certain capital expenditures are included). These funds have to be used in conjunction with the acquisition, construction, or improvement of a single depreciable property. At first, few limits were placed on the type of activity that could be supported, and the volume of new small-issue IDBs grew steadily through the late 1970s and early 1980s. It reached nearly \$15 billion in 1982 and accounted for almost 18 percent of all tax-exempt bonds issued to fund new capital in that year compared with 4 percent in 1975.

As was the case for housing bonds, legislators became concerned about the growing volume of small-issue IDBs. Moreover, like the projects supported by bonds for owner-occupied homes, those funded by small-issue IDBs appeared to offer minimal external economies, defying the intent of the tax exemption. As a result, TEFRA placed specific restrictions on small-issue IDBs. The legislation tightened depreciation allowances, disallowed the combination of small-issue IDBs with other exempt activities, and listed activities not considered exempt. Finally, a sunset provision cut off small-issue IDBs after 1986.

The volume of small-issue IDBs fell only slightly in 1983, and in 1984 lawmakers set up further limitations. Provisions contained in the Deficit Reduction Act of 1984 set state-by-state volume caps on total IDB issuance, limited a principal user of small-issue IDBs to \$40 million in bonds outstanding, and added to the list of prohibited uses.

# Profitability of Insured Commercial Banks in 1983

*Deborah J. Danker and Mary M. McLaughlin of the Board's Division of Research and Statistics prepared this article.*

The profitability of commercial banks declined again in 1983 as the industry's reported returns on assets and on equity fell to 0.67 and 11.2 percent respectively. Moreover, 48 commercial banks failed, and about 10 percent of the remaining banks ended the year with net operating losses despite the strong rebound in economic activity that had begun in late 1982.

The major factor contributing to reduced profitability was an increase in loan-loss provisions, occasioned in large part by the lingering effects of recession and by interest rates that remained high, even after a drop of about 2 to 3 percentage points on average. While not as sharp as that in 1982, the 1983 increase in loan-loss provisions brought the figure up to almost one-half percent of total net assets. Relatively hard hit were the agricultural banks, whose customers not only were affected by high interest costs, but also were faced with depressed commodity prices and reduced export demand associated with the strong dollar. Provisions for loan losses at these banks increased by almost half, to 0.59 percent of total net assets. International loans also played a role in credit quality in 1983; provisions against loan losses attributable to international business were increased more than 60 percent at banks with foreign offices.

A modest shrinking of net interest margins also contributed somewhat to the overall decline in industry profitability in 1983. The size of the change in these margins varied from group to group, depending on the alignment of the maturi-

ties of the assets and liabilities of the banks and on the impact of flows into money market deposit accounts (MMDAs) on the structure of their balance sheets. For example, the 13 money center banks managed to increase their interest margin several basis points, largely by limiting interest expense. As a group, they attracted heavy inflows of funds into the newly authorized MMDAs at the beginning of the year, which enabled them to cut back significantly on higher-cost managed liabilities. Smaller banks, with far fewer managed liabilities to run off, did less well. In fact, the smallest banks—those with total consolidated assets of less than \$100 million—experienced a relatively large decline in net interest margins. While gaining a lot of deregulated retail-type deposits, these banks also experienced a decline in lower-cost regulated deposits that exceeded the drop in managed liabilities. So even though the further deregulation of deposits in 1983 appeared to have little effect on the interest margin for the industry overall, it appeared to affect individual banks and groups of banks substantially.

Approximately offsetting the slight deterioration in the industry interest margin was a narrowing of the gap between noninterest expenses (excluding loan-loss provisions) and noninterest income. Increased fee income was an important factor in this development and suggests a continued trend toward "unbundling" of banking services, as well as an intensified effort to generate income from off-balance-sheet activities after regulators moved to tighten capital-asset guidelines. On balance, with higher fee income offsetting the lower interest margin, net operating profits in 1983 declined almost as much as loan-loss provisions rose. An improvement in capital gains on security transactions tempered the decline, leaving aftertax profits in 1983 down 4 basis points as a percent of total net assets.

NOTE: Nancy Bowen and Chinhui Juhn provided data processing and research assistance.

## INTEREST EXPENSE

Influenced by the lower average level of market interest rates in 1983, interest expense at commercial banks declined 1.66 percentage points, to 6.36 percent of total consolidated assets, as shown in table 1. The sharp decline in market rates that had occurred during the second half of 1982 was much larger than the upward drift of rates during 1983, leaving average market rates in 1983 below those of the previous year by several percentage points. Rates on certificates of deposit (CDs) at commercial banks fell more than many other market interest rates as the premium on bank liabilities lessened with some easing of market concern about exposure on energy and foreign loans: the margin of rates on bank CDs over rates on Treasury bills of similar maturity narrowed about 100 basis points on average in 1983.

The decline in overall interest expense at commercial banks, however, was smaller than that in market rates. The fixed-rate nature of a portion of banks' deposit liabilities, due both to long-term time deposits and to binding interest rate

ceilings on, for example, passbook savings, limited the drop in interest expense. This limiting factor was less important at larger banks, which had a higher proportion of their liabilities in large, short-term deposits tied to money market rates. As the chart shows, the decline in interest expense generally steepened with bank size: money center banks posted the largest decline, other large banks showed the next largest, then medium-sized banks, and finally, the small

1. Income and expense as percent of average net assets, all insured commercial banks, 1981-83

Item	1981	1982	1983
Gross interest income	1.85	1.79	1.59
Gross interest expense	8.75	8.02	6.36
Net interest margin	3.07	3.17	3.23
Noninterest income	.99	1.05	1.12
Loan loss provision	.26	.39	.27
Other noninterest expense	2.76	2.91	2.95
Income before tax	1.91	.91	.84
Taxes	.21	.1	.18
Other	.04	.03	.00
Net income	.76	.71	.67
Cash dividends declared	.30	.31	.33
Net retained earnings	.46	.40	.34
Ratio: Net interest margin to taxable equivalent <sup>1</sup>	3.28	3.55	3.81

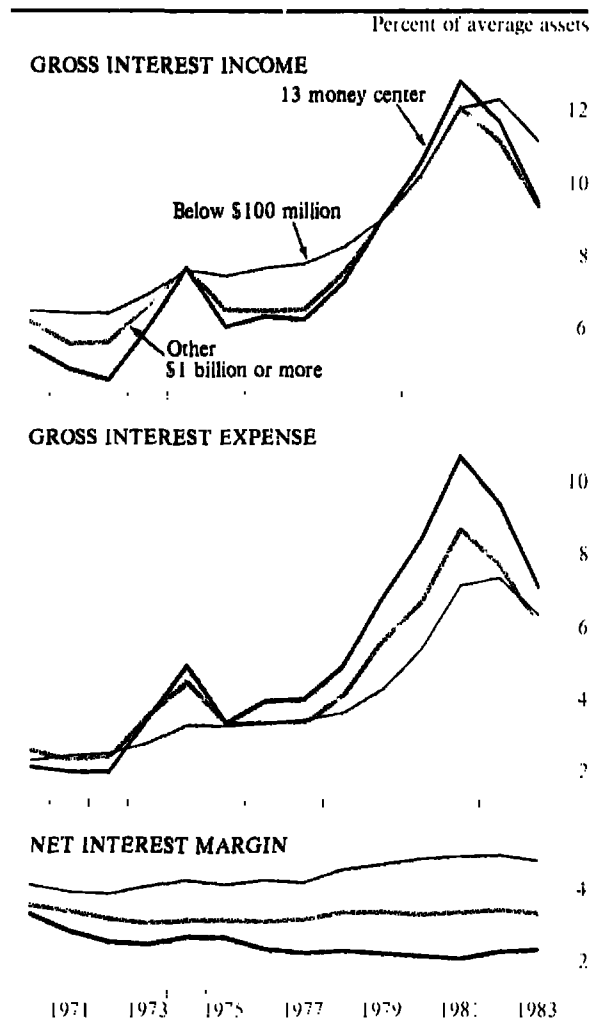
1. Average assets are fully consolidated and net of loan loss reserves; averages are based on amounts outstanding at the beginning and end of each year.

2. Includes all taxes estimated to be due on income, on extraordinary gains, and on security gains.

3. Includes security and extraordinary gains or losses (before taxes).

4. For each bank with profits before tax greater than zero, income from state and local obligations was increased by  $(1 - \tau) / (1 - \tau_s)$  times the lesser of profits before tax or interest earned on state and local obligations ( $\tau$  is the marginal federal income tax rate). This adjustment approximates the equivalent pretax return on state and local obligations.

## Components of interest margin



Size categories are based on year-end consolidated assets of each bank.

Gross interest income is adjusted for taxable equivalence. Net interest margin is gross interest income adjusted for taxable equivalence minus gross interest expense.

Data are for domestic operations only, 1976 when foreign office operations of U.S. banks were consolidated into the totals.



2. Selected financial liabilities as a percent of total assets, all insured commercial banks, 1981-83<sup>1</sup>

Average during year

Item	Domestic offices			Fully consolidated offices		
	1981	1982	1983	1981	1982	1983
Deposit liabilities	75.9	74.6	74.7	78.6	77.7	77.7
In foreign offices				15.8	15.0	13.5
In domestic offices	75.9	74.6	74.7	62.8	62.7	64.2
Demand deposits	25.1	20.7	19.3	20.8	17.4	16.5
NOW accounts	2.9	4.1	3.8	2.4	3.4	3.2
Large time deposits <sup>2</sup>	17.2	18.4	15.5	14.2	15.4	13.3
Other deposits <sup>3</sup>	30.7	31.5	36.2	25.4	26.5	31.1
Other selected financial liabilities	10.9	11.3	11.2	9.8	10.3	10.3
Gross federal funds purchased and repurchase agreements	9.1	9.5	9.1	7.5	8.0	7.8
Other borrowings	1.8	1.8	2.1	2.3	2.3	2.5
MEMO						
Money market liabilities <sup>4</sup>	28.5	30.1	27.0	40.2	41.0	37.5
Average assets (billions of dollars)	1,603	1,763	1,939	1,940	2,100	2,259

1. Percentages are based on aggregate data and thus reflect the heavier weighting of large banks. Data are based on averages for call dates in December of the preceding year and in June and December of the current year.

2. Deposits of \$100,000 and over.

3. Including savings and small time deposits, MMDAs, and Super NOW accounts.

4. Large time deposits issued by domestic offices, deposits issued by foreign offices, subordinated notes and debentures, repurchase agreements, gross federal funds purchased, and other borrowings.

banks. Small banks as a group tend to have more retail-type deposits and their liabilities tend to have longer terms; their money market liabilities represent just 11 percent of total assets, compared with 63 percent at money center banks. Small banks, therefore, have experienced less variability in interest expense in the past than have the larger banks; their expenses rise less when market rates rise and fall less when market rates fall.

An additional factor affecting commercial bank interest expense in 1983 was the change in the structure of liabilities as banks and their customers reacted to the introduction of new types of accounts. The most important of these was the phenomenally successful MMDA introduced in mid-December 1982; initially, promotional efforts led to interest rates that averaged 10.6 percent, about double the 5¼ percent rate offered on NOW and savings accounts. In addition to the MMDA, the Depository Institutions Deregulation Committee authorized the Super NOW account, effective in January 1983. Established after the Garn-St Germain Depository Institutions Act of 1982, both accounts were free of interest rate ceilings provided depositors maintained an average minimum balance of \$2,500. Of the two, the MMDA was the more popular, attracting \$213 billion to commercial banks by June and \$226 billion by the end of 1983. Super NOWs, which had broader check-

writing privileges but were typically offered at rates about 100 basis points below those on MMDAs, stood at \$23 billion by midyear and \$29 billion by December 1983.

The increase in MMDA and Super NOW balances generated a significant shift in the structure of banks' liabilities from 1982 to 1983. As shown in table 2, about 4½ percent more of the industry's assets were funded with retail-type savings and small time deposits, MMDAs, and Super NOWs (the "other deposits" category). Offsetting the increase in this category was a large decline in money market liabilities, equal to 3½ percent of consolidated assets, and a smaller decline, of almost 1 percentage point, in the demand deposit share. The drop in money market liabilities was concentrated in the large time deposit component and reversed the upward trend of recent years, leaving managed liabilities at about the 1979 level of 37.6 percent of total assets. The decline in demand deposits as a fraction of assets, by contrast, continued the trend in that series and in fact was more gradual than in the past few years.

The rapid growth of balances in the newly authorized accounts was also associated with shifts in the shares of various types of deposits within the growing retail-type category of "other deposits." Within this category, savings balances declined, the last of the tax-exempt All Savers Certificates matured, and balances in

3. Rates paid for fully consolidated liabilities, all insured commercial banks, 1981-83<sup>1</sup>

Percent			
Item	1981	1982	1983
Interest-bearing deposits	13.38	11.94	9.13
Large negotiable certificates of deposit	16.42	14.14	8.90
Deposits in foreign offices	17.34	14.87	10.32
Other deposits	10.02	9.75	8.79
Subordinated notes and debentures	10.01	9.99	10.01
Gross federal funds purchased and repurchase agreements	17.52	12.83	9.69
Other liabilities for borrowed money	14.42	13.22	12.12
Total	13.86	12.08	9.29

1. Calculated as described in the "Technical Note," FEDERAL RESERVE BULLETIN, vol. 65 (September 1979), p. 704.

individual retirement accounts and Keogh plan deposits rose. Small time deposits diminished in importance through the first half of the year but then rebounded in the second half, in part as a response to the deregulation of most such deposits in October.

In the aggregate, the change in the structure of liabilities implied more dependence on retail-type deregulated deposits and less on money market liabilities and on deposits (including demand deposits) subject to fixed interest rate ceilings or not eligible for interest. The effects of these changes on the interest expense of a particular bank or group of banks depended largely on the relative declines in the more costly managed liabilities and the less costly regulated deposits (see appendix table A.2). At one end of the spectrum, the money center banks as a group reduced their money market liabilities substantially, by 4.2 percent of total assets, while running counter to the industry trend by actually raising the share of demand deposits. By con-

trast, the small banks, with fewer managed liabilities to run off, cut their money market liabilities by just 1.4 percent of assets. Their demand deposit balances continued the strongly downward trend of recent years, and on average balances in regular NOWs also shrank. In part reflecting these differences in balance sheet changes among banks of various sizes, the decline in interest expense at the small banks (1.02 percentage points) was less than half that at the 13 money center banks (2.31 percentage points). Interest expense nevertheless remained highest at the money center banks because of their still-high ratio of managed liabilities to total liabilities.

## INTEREST INCOME

In 1983, interest income at insured commercial banks declined 1.69 percentage points to 9.50 percent of assets. Lower average market interest rates were of course the predominant factor in the decline—as they were in the case of interest expense. But the drop in income was tempered by the long maturity of many bank assets, securities in particular.

Commercial banks as a group expanded their holdings of securities, especially U.S. Treasury obligations, while cutting back on loans as a share of total assets (see table 4). In part, this change in asset composition was a reaction to the heavy inflow of MMDA and Super NOW funds early in the year. As noted above, the new accounts prompted a restructuring of bank liabilities, but the asset side of the balance sheet was

4. Portfolio items as a percent of total assets, all insured commercial banks, 1981-83<sup>1</sup>

Item	Average during year			Average during year		
	Domestic offices			Fully consolidated offices		
	1981	1982	1983	1981	1982	1983
Interest-earning assets	80.8	82.5	82.6	83.8	85.2	85.2
Loans	54.5	55.3	54.7	55.2	56.1	55.7
Securities	20.0	19.2	19.9	17.0	16.6	17.5
U.S. Treasury	6.4	6.1	7.4	5.3	5.1	6.4
U.S. government agencies	4.0	4.1	4.0	3.3	3.5	3.4
State and local governments	9.1	8.6	7.9	7.6	7.2	6.8
Other bonds and stocks	.5	.4	.5	.8	.7	.8
Gross federal funds sold and reverse repurchase agreements	4.8	5.2	5.0	4.0	4.4	4.3
Interest-bearing deposits	1.6	2.7	3.0	7.7	8.1	7.7
MEMO: Average assets (billions of dollars)	1,603	1,763	1,939	1,940	2,100	2,259

1. Percentages are based on aggregate data and thus reflect the heavier weighting of large banks. Data are based on averages for call

dates in December of the preceding year and in June and December of the current year.

also affected. The sudden inflow of funds was placed largely in securities—a typical adjustment, especially for smaller institutions with less scope to vary managed liabilities. Only a small portion of the inflow initially went into loans because the economic recovery had just begun and loan demand remained sluggish. By contrast, the Treasury's demand for credit surged, reflecting the huge federal deficit.

Small banks as a group continued to hold a higher proportion of assets in Treasury securities than did other banks, and they also showed the largest proportionate increase in these instruments. Small banks allocated an additional 2 percent of total assets to Treasury securities, which raised the share to an average of almost 12 percent. At the same time, these banks partially offset the acquisition of federal debt by decreasing their holdings of state and local obligations, leaving total holdings of securities only somewhat higher, at 31 percent of total assets. This share of securities in total assets was high, especially when compared with the 6½ percent at money center banks, and helped support interest income because the longer maturities of these securities guaranteed income through a period of falling interest rates. In fact, more than 80 percent of bank-held securities, but less than 40 percent of loans and 5 percent of other interest-bearing assets, had a remaining maturity of more than six months.<sup>1</sup> Small banks also held longer-term securities and longer-term loans than did large banks. Taken together, these portfolio characteristics limited the drop in interest income to 1.14 percentage points for small banks as a group.

Because their portfolios have a shorter maturity and loan rates tend to vary more with market rates, the money center banks posted the sharpest fall in interest income, down 2.24 percentage points to 9.26 percent of total assets. The drops in interest income at other large banks and at medium-sized banks were 1.73 percent and 1.20 percent respectively and thus fell between those at money center and at small banks and paral-

#### 5. Rates of return on fully consolidated portfolios, all insured commercial banks, 1981-83<sup>1</sup>

Percent			
Item	1981	1982	1983
Securities, total	9.27	9.96	9.83
U.S. government	11.38	12.19	11.79
State and local government	6.72	7.19	7.04
Other	11.54	11.64	11.14
Loans, gross	16.37	15.20	12.70
Net of loan-loss provision	15.83	14.39	11.76
Taxable equivalent <sup>2</sup>			
Total securities	11.73	12.49	12.06
State and local government	12.15	12.93	12.58
Total securities and gross loans	15.26	14.57	12.55

1. Calculated as described in the "Technical Note," FEDERAL RESERVE BULLETIN, vol. 65 (September 1979), p. 704

2. See table 1, note 4.

elled the ranking of declines in interest expense. Money center banks were the only group to increase the share of their assets held in loans; high growth rates in loans to foreign governments and official institutions and in security and real estate loans brought the share of loans in total assets to 61½ percent. Money center banks also increased their holdings of securities. The offsetting decline occurred in the share of assets allocated to interest-bearing deposits.

#### NET INTEREST MARGIN

In 1983, the net interest margin at commercial banks edged lower from the favorable levels of the previous year. The deterioration was by no means uniform either across banks or over the year. In particular, year-over-year comparisons actually showed some widening of the interest margin in the first half of the year, but a sharp narrowing in the second half left the margin somewhat lower on average for the year. In addition, some classes of banks (for example, the money center banks) managed to go against the trend and increase their interest margin for the year as a whole.

The deterioration in the interest margin in the second half of 1983 appeared especially sharp because in the comparable period in 1982 the interest margin had widened remarkably for many banks. The widening of interest margins in late 1982 had been associated with a steep drop in market rates that had pulled down the cost of bank liabilities somewhat more quickly than the

1. Six months was the remaining maturity if the asset carried a fixed rate and was the earliest possible repricing interval if the asset had a floating rate, as reported on Schedule J of the Call Report (June 1983).

income from assets. Consequently, even though the net interest margin at money center banks remained unchanged from the first to the second half of 1983, a comparison with the year-earlier period showed an improvement of 15 basis points in the first half and a much smaller improvement, of just 5 basis points, for the full year.<sup>2</sup> For most other banks, however, the deterioration in the second half of 1983 could not be attributed entirely to the unusual reference period. Indeed, the net interest margin at banks other than the money center banks narrowed from the first to the second half of 1983 as interest expense increased and interest income remained essentially unchanged.

The change in the interest margin from 1982 to 1983 was not uniform across bank groups. For example, small banks lost 16 basis points on average at the same time that money center banks gained 5 basis points. These relative movements narrowed the differences among classes of banks in 1983 (see the chart and appendix table A.2): the interest margin moved to 4.79 percent at small banks, 4.37 percent at medium-sized banks, 2.32 percent at money center banks, and 3.33 percent at other large banks.

The gap between the higher interest margin at agricultural banks and the somewhat lower margin at banks specializing in mortgage lending also narrowed.<sup>3</sup> The two groups are comparable because they consist largely of small banks, but their 1983 results differed markedly. The banks with large holdings of agricultural loans saw a particularly sharp drop in the return on loans and a concomitant fall of 22 basis points in their net interest margin. At the same time, mortgage-oriented banks showed a relatively small drop in the rate of return on their loans and ended the year with an increase of 16 basis points in

their interest margin—exceeding even the improvement at the money center banks. The small decline in the mortgage group's return on loans demonstrated the low sensitivity of real estate portfolios to interest rates despite the growing importance of adjustable-rate mortgages. Beyond the interest margin, asset quality was an important differentiating factor: loan-loss provisions were increased 18 basis points at the agricultural banks, but only 3 basis points at banks specializing in mortgages. On balance, net income rose at the mortgage-oriented banks and fell at agricultural banks. Nonetheless, the former remained somewhat less profitable, and the latter somewhat more profitable, than small and medium-sized banks in the aggregate.

#### LOAN LOSSES

Loan losses became a more significant factor in commercial bank profitability in 1983. While rising less than they had in 1982, both provisions for loan losses and actual net chargeoffs of loans continued to climb from their high 1982 levels. In the aggregate, loan-loss provisions increased 8 basis points, to 0.47 percent of total net assets, and loan chargeoffs (net of recoveries) jumped 11 basis points, to 0.66 percent of gross loans. Both these figures surpassed recent peaks.

Loan losses increased in 1983 as a number of sectors of the economy continued to suffer from the effects of the recent recession. Relatively high interest rates also added to repayment difficulties. Low commodity and energy prices adversely affected the agriculture and energy industries; agriculture also came under pressure as the high and rising exchange rate of the dollar impaired the competitive position of U.S. farm exports. And abroad, difficulties in several developing economies continued to hamper the servicing of loans to borrowers in those countries.

Loans written off as uncollectible (net of recoveries from loans previously charged off) rose at each group of banks, although by varying amounts among groups (table 6). In particular, the medium-sized and the money center banks did relatively well, adding just 4 and 6 basis points respectively to net chargeoffs as a percent

2. Net interest margin is calculated as the difference between interest income, adjusted for taxable equivalence on tax-exempt state and local securities, and interest expense, expressed as a percent of total net assets.

3. The mortgage group consists of commercial banks with at least a quarter of their assets allocated to loans secured by real estate; in 1983, this group contained 3,018 banks. The agricultural group consists of commercial banks with at least one quarter of loans at their domestic offices allocated to farm real estate mortgages and loans made to finance agricultural production; this group contained 4,055 banks in 1983.

## 6. Loan portfolio losses and recoveries, all insured commercial banks, 1982-83

Millions of dollars, except as noted

Year and size of bank <sup>1</sup>	Losses charged	Recoveries	Net losses		Loan-loss provision
			Amount	Percent of loans <sup>2</sup>	
<i>1982</i>					
All banks . . . . .	8,109	1,588	6,521	.55	8,291
Less than \$100 million . . . . .	1,578	308	1,270	.67	1,479
\$100 million to \$1 billion . . . . .	1,637	315	1,322	.60	1,642
\$1 billion or more					
Money center banks . . . . .	2,125	392	1,733	45	2,212
Others . . . . .	2,769	574	2,194	57	2,958
<i>1983</i>					
All banks . . . . .	10,456	2,056	8,401	.66	10,614
Less than \$100 million . . . . .	2,001	387	1,615	84	1,895
\$100 million to \$1 billion . . . . .	1,941	393	1,548	.64	1,927
\$1 billion or more					
Money center banks . . . . .	2,490	478	2,012	51	2,467
Others . . . . .	4,024	798	3,226	74	4,326

1. Size categories are based on year-end fully consolidated assets.

2. Average of beginning- and end-of-year loan balances.

of loans in 1983. Others did less well; both the small banks and the large banks other than money center banks increased their chargeoffs 17 basis points. Banks specializing in agricultural lending saw the worst deterioration—a jump of 26 basis points that left net chargeoffs at almost 1 percent of gross loans.

Provisions for future loan losses rose very much in line with banks' actual losses. The increases were smallest at the medium-sized and money center banks and largest at the agricultural banks.

The international business of banks became a more important factor in loan losses in 1983. For example, in 1982 commercial and industrial loans to foreign addressees accounted for more than 28 percent of gross loans at the 13 money center banks, but they contributed just 20 percent of the \$1.7 billion in net loan chargeoffs at those banks. But in 1983, chargeoffs of foreign commercial and industrial loans rose sharply to nearly 30 percent of the \$2.0 billion in net chargeoffs. In addition, loans to foreign governments and official institutions constituted a growing if still small component of chargeoffs; these loans rose from 1 to 6½ percent of total net chargeoffs at money center banks between 1982 and 1983.

#### *OTHER NONINTEREST EXPENSES AND NONINTEREST INCOME*

Relative to average assets, noninterest expenses increased slightly in 1983 for insured commercial

banks in the aggregate. The rise of 4 basis points, to 2.95 percent, represented a marked deceleration in the upward trend of recent years. Only money center banks showed a significant increase—nearly three times the national average—in this ratio; and medium-sized banks actually experienced a decline of 4 basis points. As a consequence, the ratio of noninterest expenses to assets at money center banks moved closer to the figures at other banks. The differences in changes in noninterest expenses were due mostly to movements in salary and employee benefit expenses. In particular, the money center banks expanded their staff only slightly, by 0.4 percent, compared with the industry average of 0.7 percent. These savings were more than offset by an increase in salaries and benefits per employee of 7.6 percent, which was about 1 percentage point higher than that at banks in other size classes.

Noninterest income grew twice as much as expenses in 1983 and increased across all sizes of banks. For most banks, the increase was accounted for by growth in fee income. As banks have "unbundled" financial services, a process probably hastened by deregulation, they have increasingly charged explicitly for services. At small banks, the rise in fee income came predominantly from deposit service charges. At large banks other than money center banks and at medium-sized banks, the deposit and other service charges accounted equally for the rise. At money center banks, the growth in deposit service charges was in line with the national average of almost 18 percent, but since such charges

## 7. Profit rates, all insured commercial banks, 1979-83

Percent

Type of return and size of bank <sup>1</sup>	1979	1980	1981	1982	1983
<i>Return on assets</i> <sup>2</sup>					
All banks.....	.80	.79	.76	.71	.67
Less than \$100 million.....	1.15	1.18	1.15	1.08	.96
\$100 million to \$1 billion.....	.96	.96	.91	.85	.84
\$1 billion or more.....					
Money center banks.....	.56	.56	.53	.50	.51
Others.....	.72	.66	.68	.63	.55
<i>Return on equity</i> <sup>3</sup>					
All banks.....	13.9	13.7	13.2	12.2	11.2
Less than \$100 million.....	14.1	14.2	13.6	12.7	11.2
\$100 million to \$1 billion.....	13.9	13.7	12.8	12.0	11.9
\$1 billion or more.....					
Money center banks.....	14.0	14.4	13.4	12.3	11.9
Others.....	13.5	12.7	12.9	11.9	10.4

1. Size categories are based on year-end fully consolidated assets.  
2. Net income as a percent of the average of beginning- and end-of-year fully consolidated assets net of loan-loss reserves.

3. Net income as a percent of the average of beginning- and end-of-year equity capital.

amount to just over 5 percent of noninterest income at those 13 banks as a group, the rise had little impact. Instead, improvement in noninterest income came mostly from other service charges and the undifferentiated "all other noninterest income." On net, the industry's spread between noninterest expenses and income in 1983 narrowed by 3 basis points from the previous year, approximately offsetting the reduction in net interest margin over the same period.

## PROFITABILITY, DIVIDENDS, AND CAPITAL

Commercial banks were less profitable in 1983 than in any year in the last two decades. The weighted average return on assets declined 4 basis points in 1983, and the average return on equity fell a full percentage point (table 7). Much

more noticeable drops in these measures occurred at small banks and at large banks other than money center banks; indeed, the year-to-year changes in profit rates for these two groups were the largest in recent years. In contrast, the profit performances of medium-sized and money center banks were similar to those in the previous year, with money center banks even showing an increase of 1 basis point in return on assets.

Despite the reduced profitability of the industry, the ratio of cash dividends on common and preferred stock to assets went up 2 basis points in 1983. Money center banks increased their dividends 5 basis points, considerably more than other banks, while dividends at medium-sized banks rose at about the average rate for all banks. Other large banks and small banks reduced their dividends slightly relative to total assets.

## 8. Sources of increase in total equity capital, all insured commercial banks, 1979-83

Millions of dollars, except as noted

Year	Retained income <sup>1</sup>		Net increase in equity capital		Percent of increase in equity capital from retained income	
	All banks	Large banks <sup>2</sup>	All banks	Large banks	All banks (column 1 - column 3)	Large banks (column 2 - column 4)
	(1)	(2)	(3)	(4)	(5)	(6)
1979.....	8,350	3,616	9,952	4,291	84	84
1980.....	8,859	3,843	10,828	4,567	82	84
1981.....	8,904	4,108	11,168	5,426	80	76
1982.....	8,410	4,055	10,865	5,304	77	76
1983.....	7,651	3,621	10,738	5,625	71	64

1. Net income less cash dividends declared on preferred and common stock.

2. Banks with fully consolidated assets of \$1 billion or more

Insured commercial banks retained about \$750 million less income in 1983 than in the year before, the second consecutive year of decline (table 8). Despite the drop in retained earnings, the industry's equity-to-asset ratio rose in 1983 for the first time in seven years as equity sales boosted bank capital. The aggregate ratio rose to 6.0 percent, with equity increases in excess of asset growth at the money center banks as the primary contributing factor. Over the year, the money center banks raised their equity capital more than \$2 billion, or about 8 percent. Although stock prices slid through much of the year, regulators' concern over capital adequacy and new guidelines for minimum ratios of capital to assets probably contributed to the banks' decision to increase equity.

#### *INSURED U.S. COMMERCIAL BANKS WITH FOREIGN OFFICES*

In line with the industry as a whole, commercial banks with foreign offices saw their net operating income fall about the amount that loan-loss provisions were increased.<sup>4</sup> Loan-loss provisions at these banks were raised by 0.09 percent of average consolidated assets, or almost 30 percent. The increase in loan-loss provisions was especially pronounced for loans attributable to the international business of banks; the foreign share of total provisions rose to 27 percent in 1983 from 21 percent in 1982. Nevertheless, profits from international business held up well as the interest margin widened on business with foreign customers, offsetting the deterioration in loan losses and other noninterest expenses. In the aggregate, banks with foreign offices reported that all of the 1983 decline in their return on assets was attributable to their domestic business (see table 9).

The behavior of net income attributable to foreign offices was similar to that of net income attributable to international business (which includes all business with foreign-domiciled customers, whether conducted in domestic or for-

4. This group includes 188 large insured commercial banks with foreign offices, or Edge Act or Agreement subsidiaries.

#### 9. Consolidated income and expense as a percent of average net assets, U.S. insured commercial banks with foreign offices, 1982-83

Item	1982		1983	
Gross interest income	11.11		9.07	
Gross interest expense	8.58		6.54	
Net interest margin	2.53		2.53	
Taxable equivalent <sup>1</sup>	2.79		2.75	
Noninterest income	1.17		1.24	
Loan-loss provision	.39		.48	
Other noninterest expense	2.56		2.62	
Income before tax	75		67	
Foreign offices <sup>2</sup>	.24		.25	
Domestic offices <sup>2</sup>	.51		.43	
Net income	55		49	
International business <sup>2</sup>	.18		.18	
Domestic business <sup>2</sup>	37		31	

1. See table 1, note 4.

2. See table A.3. Reflects amounts attributed to each class of business, giving full allocation of income and expense.

foreign offices). Profits from foreign offices also increased on the basis of some widening in the interest margin, in contrast to the declining profits and narrowing of 10 basis points in the margin at domestic offices. A factor contributing to the better performance of the foreign office margin was the relative absence of fixed-rate characteristics on their deposit liabilities; foreign offices have few long-term deposits and none subject to regulatory interest rate ceilings. As table 10 shows, interest income and expense both fell sharply at foreign offices, declining more than 300 basis points as compared with the declines of 155 basis points in income and 145 basis points in expense at domestic offices.

Separating these banks into two groups, the 13 money center banks on the one hand did relatively well, showing a slight increase in aftertax profits. The increase in profits attributable to

#### 10. Interest income and expense as a percent of average net assets, U.S. insured commercial banks with foreign offices, 1982-83<sup>1</sup>

Item	Domestic offices		Foreign offices	
	1982	1983	1982	1983
Gross interest income	9.80	8.26	12.59	9.56
Gross interest expense	6.77	5.32	11.40	8.36
Net interest margin	3.03	2.94	1.19	1.21
Taxable equivalent <sup>1</sup>	3.39	3.24	1.19	1.21

1. Approximated for domestic offices according to the method described in table 1, note 4.

their international business compensated for the decrease in domestic profits and lifted international profits to just over one half of aftertax income. Other large banks with foreign offices, on the other hand, experienced a deterioration not only in domestic profits but also—albeit milder—in international profits. As a group, net income at these banks declined 12 basis points, slightly less than the 14 basis points by which loan-loss provisions were raised. Increased capital gains on security transactions and an improvement in the balance of noninterest income and expenses offset a substantial narrowing of the interest margin at these other large banks.

As it has in the past several years, the level of total assets held at foreign offices fell—by about \$8 billion in 1983. Here, too, the money center banks were responsible for the trend, showing a drop of more than \$10 billion. The other large banks posted an increase in foreign office assets of about \$2 billion. One should note, however, that shifts of assets from foreign offices to international banking facilities (IBFs) would show up as a drop in foreign office assets and a corresponding increase in those at domestic offices

11. Assets and liabilities, U.S. insured commercial banks with foreign offices, December 31, 1983

Percent of total, except as noted

Item	Domestic offices	Foreign offices
<b>Total assets</b> (billions of dollars) . . . . .	1,012	382
Cash and due from banks . . . . .	12	30
Gross federal funds sold and reverse repurchase agreements . . . . .	4	*
Securities . . . . .	12	3
Loans . . . . .	58	51
Other . . . . .	14	16
Advances to affiliated offices . . . . .	3	9
<b>Total liabilities</b> (billions of dollars) . . . . .	943	381
Deposits . . . . .	71	81
Non-interest-bearing <sup>1</sup> . . . . .	22	4
Interest-bearing . . . . .	49	77
Savings and small time . . . . .	30	n.a.
Time of \$100,000 or more . . . . .	19	n.a.
Selected nondeposit financial liabilities . . . . .	17	5
Federal funds purchased and repurchase agreements . . . . .	14	*
Other liabilities for borrowed money . . . . .	3	5
Other . . . . .	12	14
Advances from affiliated offices . . . . .	4	9

<sup>1</sup> Demand deposits in domestic offices, non-interest-bearing deposits in foreign offices.

\* Less than 0.5 percent

n.a. Not available

because IBFs have been included in domestic offices.



## A.1. Report of income, all insured commercial banks, 1979-83

Millions of dollars, except as noted

Item	1979	1980	1981	1982	1983
<b>Operating income, total</b>	<b>149,795</b>	<b>190,109</b>	<b>247,932</b>	<b>257,188</b>	<b>239,255</b>
Interest, total	137,364	174,416	228,675	235,121	214,088
Loans	101,942	126,663	163,171	166,589	151,356
Balances with banks	10,561	16,035	23,935	23,857	16,738
Federal funds sold and securities purchased under resale agreement	6,106	8,750	12,236	11,316	9,198
Securities (excluding trading accounts)	18,755	22,968	29,333	33,359	36,797
U.S. Treasury and U.S. government agencies	10,630	13,400	18,037	21,022	24,204
State and local governments	6,928	8,131	9,671	10,612	10,618
Other <sup>1</sup>	1,197	1,437	1,635	1,725	1,974
Trust department	2,375	2,738	3,179	3,604	4,188
Direct lease financing	1,073	1,371	1,746	1,943	1,961
Service charges on deposits	2,517	3,173	3,905	4,573	5,399
Other charges, fees, etc.	3,635	4,352	5,302	6,203	7,267
Other operating income	2,831	4,059	5,116	5,715	6,351
<b>Operating expenses, total</b>	<b>131,950</b>	<b>170,675</b>	<b>227,714</b>	<b>238,016</b>	<b>220,229</b>
Interest, total	87,570	119,758	169,268	168,553	143,210
Deposits	71,693	98,130	138,977	141,097	119,839
Time CDs of \$100,000 or more issued by domestic offices	18,105	24,753	39,034	37,359	22,523
Deposits in foreign offices	24,523	34,941	46,696	41,746	29,021
Other deposits	29,065	38,436	53,248	62,029	68,295
Federal funds purchased and securities sold under repurchase agreement	12,218	16,707	23,786	20,618	16,438
Other borrowed money <sup>2</sup>	3,162	4,380	5,894	6,188	6,253
Capital notes and debentures	497	541	611	650	680
Salaries, wages, and employee benefits	21,465	24,565	27,927	31,218	33,636
Occupancy expense <sup>3</sup>	6,255	7,325	8,566	9,960	11,100
Loan-loss provision	3,764	4,453	5,059	8,291	10,614
Other operating expenses	12,796	14,573	16,962	19,953	21,661
Income before taxes and securities gains or losses	17,843	19,435	20,149	19,172	19,026
Applicable income taxes	4,736	5,009	4,611	3,639	4,091
Net securities gains or losses (-) after taxes	-350	-492	-861	-661	-15
Extraordinary charges (-) or credits after taxes	39	17	54	68	70
Net income	12,797	13,950	14,731	14,940	14,989
Cash dividends declared	4,449	5,091	5,831	6,529	7,338
<b>MEMO</b>					
Number of banks	14,352	14,421	14,400	14,121	14,074
Average fully consolidated assets (billions of dollars)	1,593	1,768	1,940	2,100	2,259

1. Includes interest income from other bonds, notes and debentures, and dividends from stocks.

2. Includes interest paid on U.S. Treasury tax and loan account balances.

3. Occupancy expense for bank premises net of any rental income plus furniture and equipment expenses.

A.2. Portfolio composition, interest rates, and income and expenses, insured commercial banks, 1980-83<sup>1</sup>

## A. All banks

Item	1980	1981	1982	1983
Balance sheet items as percent of average consolidated assets				
Interest-earning assets	82.9	83.8	85.1	85.2
Loans	55.4	55.2	56.1	55.7
Commercial and industrial	20.8	21.5	22.8	22.5
Real estate	14.6	14.4	14.2	14.1
Personal	10.6	9.6	9.2	9.2
Securities	17.0	17.0	16.6	17.5
U.S. Treasury	5.3	5.3	5.1	6.4
U.S. government agencies	3.0	3.3	3.5	3.4
State and local governments	7.8	7.6	7.2	6.8
Other bonds and stock	.8	.8	.7	.8
Gross federal funds sold and securities purchased under resale agreement	3.7	4.0	4.4	4.3
Interest-bearing deposits	6.8	7.7	8.1	7.7
Deposit liabilities	79.5	78.6	77.7	77.7
In foreign offices	16.0	15.8	15.0	13.5
In domestic offices	63.5	62.8	62.7	64.2
Demand deposits	24.0	20.8	17.4	16.5
NOW accounts	1.0	2.4	3.4	3.2
Large time	12.8	14.2	15.4	13.3
Other deposits	25.7	25.4	26.5	31.2
Other selected financial liabilities	9.2	9.8	10.3	10.3
Gross federal funds purchased and securities sold under repurchase agreement	6.9	7.5	8.0	7.8
Other borrowings	2.3	2.3	2.3	2.5
MEMO: Managed liabilities	38.4	40.2	41.0	37.5
Effective interest rates (percent)				
<i>Rates earned</i>				
Securities	7.88	9.27	9.96	9.83
State and local governments	6.03	6.72	7.19	7.04
Loans, gross	13.71	16.37	15.20	12.70
Net of loan-loss provision	13.19	15.83	14.39	11.76
Taxable equivalent				
Securities	10.23	11.73	12.49	12.06
Securities and gross loans	12.88	15.26	14.57	12.55
<i>Rates paid</i>				
Time and savings deposits	10.66	13.38	11.94	9.13
Large negotiable CDs	12.56	16.42	14.14	8.90
In foreign offices	14.03	17.34	14.87	10.32
Other deposits	8.10	10.02	9.75	8.79
All interest-bearing liabilities	11.10	13.86	12.08	9.29
Income and expenses as percent of average consolidated assets				
Gross interest income	9.87	11.81	11.19	9.50
Gross interest expense	6.78	8.75	8.02	6.36
Net interest margin	3.09	3.07	3.17	3.15
Noninterest income	.89	.99	1.05	1.12
Loan-loss provision	.25	.26	.39	.47
Other noninterest expense	2.63	2.76	2.91	2.95
Profits before tax	1.10	1.04	.91	.84
Taxes	.28	.24	.17	.18
Other	-.03	-.04	-.03	-.01
Net income	.79	.76	.71	.67
Dividends	.29	.30	.31	.33
Retained income	.50	.46	.40	.34
MEMO: Net interest margin, taxable equivalent	3.46	3.45	3.55	3.50

1. See notes to tables in the text.

A.2. Portfolio composition, interest rates, and income and expenses, insured commercial banks, 1980-83<sup>1</sup>-Continued

## B. Banks with less than \$100 million in assets

Item	1980	1981	1982	1983
	Balance sheet items as percent of average consolidated assets			
Interest-earning assets	89.4	90.8	91.0	90.9
Loans	55.9	53.6	52.5	51.4
Commercial and industrial	11.9	12.3	12.9	12.9
Real estate	20.8	19.6	18.4	18.0
Personal	15.5	14.0	12.9	12.3
Securities	27.8	29.4	29.6	31.0
U.S. Treasury	9.2	9.9	9.8	11.9
U.S. government agencies	6.3	7.4	8.4	8.6
State and local governments	11.8	11.5	10.9	10.0
Other bonds and stock	5	.5	.4	.5
Gross federal funds sold and securities purchased under resale agreement	5.5	5.9	6.4	6.0
Interest-bearing deposits	2	1.9	2.6	2.6
Deposit liabilities	88.1	87.5	87.1	87.8
In foreign offices				
In domestic offices	88.1	87.5	87.1	87.8
Demand deposits	26.7	22.5	19.0	17.0
NOW accounts	8	4.0	6.2	5.7
Large time	9.5	10.0	10.7	9.8
Other deposits	51.1	51.0	51.2	55.3
Other selected financial liabilities	1.4	1.7	2.0	1.5
Gross federal funds purchased and securities sold under repurchase agreement	1.0	1.4	1.7	1.2
Other borrowings	.4	.3	.3	.3
MEMO: Managed liabilities	11.1	12.0	12.8	11.4
	Effective interest rates (percent)			
<i>Rates earned</i>				
Securities	7.89	9.69	10.82	10.58
State and local governments	5.80	6.44	7.24	7.47
Loans, gross	12.43	14.90	15.35	13.70
Net of loan-loss provision	11.90	14.30	14.46	12.58
Taxable equivalent				
Securities	9.98	11.77	12.97	12.52
Securities and gross loans	11.60	13.79	14.48	13.26
<i>Rates paid</i>				
Time and savings deposits	8.81	11.21	10.97	9.15
Negotiable CDs	11.66	15.18	13.72	9.20
In foreign offices				
Other deposits	8.36	10.56	10.52	9.15
All interest-bearing liabilities	8.89	11.31	11.02	9.11
	Income and expenses as percent of average consolidated assets			
Gross interest income	9.67	11.49	11.71	10.57
Gross interest expense	5.36	7.13	7.33	6.31
Net interest margin	4.31	4.36	4.38	4.26
Noninterest income	.64	.69	.68	.70
Loan-loss provision	.26	.28	.41	.51
Other noninterest expense	3.12	3.23	3.30	3.28
Profits before tax	1.57	1.55	1.35	1.17
Taxes	.36	.35	.26	.23
Other	-.03	-.06	-.01	.01
Net income	1.18	1.15	1.08	.96
Dividends	.31	.35	.39	.38
Retained income	.87	.80	.69	.58
MEMO: Net interest margin, taxable equivalent	4.85	4.92	4.95	4.79

1. See notes to tables in the text.

A.2. Portfolio composition, interest rates, and income and expenses, insured commercial banks, 1980-83<sup>1</sup>-Continued

## C. Banks with \$100 million to \$1 billion in assets

Item	1980	1981	1982	1983
Balance sheet items as percent of average consolidated assets				
Interest-earning assets	87.2	88.0	89.0	89.4
Loans	55.4	54.1	53.4	52.7
Commercial and industrial	15.9	16.3	16.9	16.8
Real estate	20.5	20.0	19.4	18.9
Personal	15.4	14.0	13.2	12.9
Securities	25.2	25.7	25.3	26.5
U.S. Treasury	7.9	8.1	8.0	10.0
U.S. government agencies	4.4	5.0	5.5	5.4
State and local governments	12.3	11.9	11.1	10.3
Other bonds and stock	6	.7	.7	.9
Gross federal funds sold and securities purchased under resale agreement	5.4	5.5	5.9	5.6
Interest-bearing deposits	1.3	2.8	4.4	4.6
Deposit liabilities	84.0	83.2	82.9	84.3
In foreign offices	2	2	.2	.2
In domestic offices	83.8	83.0	82.7	84.2
Demand deposits	28.8	25.0	21.3	19.5
NOW accounts	1.5	3.6	5.2	4.9
Large time	14.4	15.0	15.4	13.0
Other deposits	39.1	39.4	40.8	46.8
Other selected financial liabilities	6.3	7.0	7.3	6.1
Gross federal funds purchased and securities sold under repurchase agreement	5.4	6.1	6.5	5.2
Other borrowings	.9	.9	.8	.9
MEMO: Managed liabilities	21.3	22.6	23.2	19.6
Effective interest rates (percent)				
<i>Rates earned</i>				
Securities	7.64	9.14	9.96	9.89
State and local governments	5.82	6.49	7.03	7.03
Loans, gross	12.79	15.23	14.68	12.78
Net of loan-loss provision	12.26	14.66	13.83	11.88
<i>Taxable equivalent</i>				
Securities	10.00	11.44	12.34	12.09
Securities and gross loans	11.91	13.99	13.92	12.55
<i>Rates paid</i>				
Time and savings deposits	9.05	11.46	10.67	8.82
Negotiable CDs	12.13	16.05	13.96	8.90
In foreign offices	12.99	15.84	14.44	9.23
Other deposits	8.06	9.99	9.69	8.81
All interest-bearing liabilities	9.50	11.97	10.89	8.79
Income and expenses as percent of average consolidated assets				
Gross interest income	9.47	11.25	11.05	9.85
Gross interest expense	5.62	7.39	7.13	6.00
Net interest margin	3.85	3.86	3.92	3.85
Noninterest income	.82	.87	.90	.94
Loan-loss provision	.26	.27	.40	.43
Other noninterest expense	3.20	3.34	3.42	3.38
Profits before tax	1.20	1.12	1.00	.98
Taxes	.22	.17	.12	.14
Other	-.03	-.05	-.04	-.01
Net income	.96	.91	.85	.84
Dividends	.36	.39	.40	.42
Retained income	.60	.52	.45	.42
MEMO: Net interest margin, taxable equivalent	4.40	4.40	4.47	4.37

1. See notes to tables in the text.

A.2. Portfolio composition, interest rates, and income and expenses, insured commercial banks, 1980-83<sup>1</sup>-Continued

## D. Thirteen money center banks

Item	1980	1981	1982	1983
Balance sheet items as percent of average consolidated assets				
Interest-earning assets	78.0	79.6	81.4	80.7
Loans	55.4	57.5	61.0	61.6
Commercial and industrial	29.9	31.2	33.6	33.5
Real estate	6.9	7.5	8.1	8.3
Personal	4.3	4.2	4.3	4.3
Securities	7.2	6.8	6.3	6.6
U.S. Treasury	2.2	2.0	1.7	1.9
U.S. government agencies	.9	.8	.7	.7
State and local governments	2.8	2.7	2.7	2.7
Other bonds and stock	1.4	1.3	1.2	1.3
Gross federal funds sold and securities purchased under resale agreement	1.6	2.1	2.4	2.5
Interest-bearing deposits	13.7	13.2	11.7	10.1
Deposit liabilities	75.3	74.2	72.5	71.2
In foreign offices	40.3	39.3	38.0	35.5
In domestic offices	35.0	34.9	34.5	35.7
Demand deposits	17.5	14.7	11.1	11.3
NOW accounts	.5	.7	.9	.8
Large time	11.1	13.5	15.7	13.3
Other deposits	5.9	6.0	6.8	10.3
Other selected financial liabilities	12.4	12.9	13.2	13.8
Gross federal funds purchased and securities sold under repurchase agreement	8.2	8.5	8.6	8.8
Other borrowings	4.2	4.4	4.6	5.0
MEMO: Managed liabilities	63.9	65.9	67.1	62.9
Effective interest rates (percent)				
<i>Rates earned</i>				
Securities	8.83	9.90	9.78	9.61
State and local governments	6.95	7.68	7.64	6.49
Loans, gross	14.95	17.63	15.65	12.62
Net of loan-loss provision	14.56	17.20	14.98	11.92
Taxable equivalent				
Securities	11.25	12.74	12.57	12.09
Securities and gross loans	14.52	17.10	15.35	12.57
<i>Rates paid</i>				
Time and savings deposits	12.98	16.02	13.67	9.77
Negotiable CDs	13.37	16.98	14.71	9.17
In foreign offices	13.94	17.17	14.88	10.72
Other deposits	8.29	9.40	8.79	8.19
All interest-bearing liabilities	13.07	16.20	13.65	10.22
Income and expenses as percent of average consolidated assets				
Gross interest income	10.40	12.58	11.50	9.26
Gross interest expense	8.40	10.69	9.40	7.09
Net interest margin	2.00	1.89	2.11	2.17
Noninterest income	.96	1.11	1.16	1.25
Loan-loss provision	.19	.21	.35	.39
Other noninterest expense	1.83	1.94	2.16	2.27
Profits before tax	.94	.86	.76	.76
Taxes	.36	.31	.24	.26
Other	-.01	-.02	-.03	.01
Net income	.56	.53	.50	.51
Dividends	.22	.21	.22	.27
Retained income	.34	.32	.27	.24
MEMO: Net interest margin, taxable equivalent	2.15	2.07	2.27	2.32

1 See notes to tables in the text.

A.2. Portfolio composition, interest rates, and income and expenses, insured commercial banks,  
 1980-83<sup>1</sup>-Continued

## E. Large banks other than money center banks

Item	1980	1981	1982	1983
Balance sheet items as percent of average consolidated assets				
Interest-earning assets	81.1	81.3	83.0	83.8
Loans	55.0	54.4	55.1	54.8
Commercial and industrial	20.8	20.7	21.8	21.5
Real estate	14.7	14.6	14.6	14.3
Personal	10.9	9.7	9.3	9.5
Securities	15.0	14.4	13.8	14.7
U.S. Treasury	4.5	4.2	4.1	5.3
U.S. government agencies	2.3	2.2	2.1	2.1
State and local governments	7.7	7.5	7.1	6.7
Other bonds and stock	.5	.5	.5	.6
Gross federal funds sold and securities purchased under resale agreement	3.6	3.9	4.3	4.4
Interest-bearing deposits	7.4	8.7	9.8	10.0
Deposit liabilities	75.8	75.0	74.1	74.3
In foreign offices	11.4	11.7	11.0	9.8
In domestic offices	64.4	63.3	63.1	64.5
Demand deposits	26.1	23.1	19.7	18.8
NOW accounts	1.2	2.5	3.2	3.1
Large time	15.7	16.8	17.7	15.2
Other deposits	21.4	20.9	22.5	27.4
Other selected financial liabilities	12.8	13.3	13.9	14.1
Gross federal funds purchased and securities sold under repurchase agreement	10.4	11.0	11.7	11.6
Other borrowings	2.4	2.3	2.2	2.5
MEMO: Managed liabilities	40.4	42.4	43.0	39.6
Effective interest rates (percent)				
<i>Rates earned</i>				
Securities	7.67	8.65	9.11	9.13
State and local governments	6.11	6.86	7.15	6.93
Loans, gross	13.85	16.62	14.98	12.29
Net of loan-loss provision	13.23	16.00	14.10	11.18
Taxable equivalent				
Securities	10.29	11.56	12.08	11.58
Securities and gross loans	13.08	15.53	14.38	12.14
<i>Rates paid</i>				
Time and savings deposits	10.64	13.49	11.75	8.77
Negotiable CDs	12.66	16.63	13.99	8.71
In foreign offices	14.37	17.94	14.83	9.23
Other deposits	7.72	9.55	9.33	8.69
All interest-bearing liabilities	11.36	14.11	11.85	8.91
Income and expenses as percent of average consolidated assets				
Gross interest income	9.71	11.60	10.72	8.99
Gross interest expense	6.76	8.64	7.68	5.98
Net interest margin	2.95	2.96	3.04	3.01
Noninterest income	1.01	1.13	1.22	1.30
Loan-loss provision	.30	.29	.42	.55
Other noninterest expense	2.76	2.92	3.07	3.09
Profits before tax	.90	.88	.77	.67
Taxes	.19	.15	.10	.12
Other	-.05	-.05	-.04	-.01
Net income	.66	.68	.63	.55
Dividends	.29	.31	.30	.29
Retained income	.37	.37	.33	.26
MEMO: Net interest margin, taxable equivalent	3.31	3.35	3.42	3.33

1. See notes to tables in the text.

## A.3. Income attributable to international business of U.S. commercial banks with foreign offices

Millions of dollars

Item	1982	1983
Pretax income attributable to foreign offices <sup>1</sup> . . . . .	3,037	3,200
Plus: Pretax income attributable to international business conducted in domestic offices . . . . .	953	1,092
Less: adjustment amount <sup>2</sup> . . . . .	160	174
Pretax income attributable to international business . . . . .	3,830	4,118
Less: All income taxes attributable to international business . . . . .	1,624	1,742
Net income attributable to international business . . . . .	2,206	2,376
<b>MEMO</b>		
Provision for possible loan losses attributable to international business . . . . .	1,029	1,688
<i>Noninterest income</i>		
Attributable to foreign offices <sup>1</sup> . . . . .	2,174	2,392
Attributable to international business . . . . .	2,844	3,164
<i>Noninterest expense</i>		
Attributable to foreign offices <sup>1</sup> . . . . .	3,634	4,440
Attributable to international business . . . . .	4,794	5,706
<i>Intracompany items attributable to international business</i>		
Interest income . . . . .	7,596	6,688
Interest expense . . . . .	10,147	9,349
Interest income of domestic offices from foreign-domiciled customers . . . . .	6,003	6,962
Fully consolidated		
Pretax income . . . . .	9,348	8,790
Total applicable taxes . . . . .	2,103	2,344
Net income <sup>3</sup> . . . . .	6,825	6,452
Average total assets . . . . .	1,249,052	1,305,614

1. Including Edge Act and Agreement subsidiaries.

2. Reflects the amount necessary to reconcile the preceding two amounts with pretax income attributable to international business.

For example, any net income of foreign offices from business with U.S.-domiciled customers is included here.

3. After gains and losses from securities transactions and extraordinary items.

# Staff Studies

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*The staffs of the Board of Governors of the Federal Reserve System and of the Federal Reserve Banks undertake studies that cover a wide range of economic and financial subjects. From time to time the results of studies that are of general interest to the professions and to others are summarized in the FEDERAL RESERVE BULLETIN.*

*The analyses and conclusions set forth are those of the authors and do not necessarily*

*indicate concurrence by the Board of Governors, by the Federal Reserve Banks, or by the members of their staffs.*

*Single copies of the full text of each of the studies or papers summarized in the BULLETIN are available without charge. The list of Federal Reserve Board publications at the back of each BULLETIN includes a separate section entitled "Staff Studies" that lists the studies that are currently available.*

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## STUDY SUMMARIES

### *GEOGRAPHIC MARKET DELINEATION: A REVIEW OF THE LITERATURE*

*John D. Wolken—Staff, Board of Governors*  
Prepared as a staff study in May 1983.

Following the Philadelphia National Bank decision (1963) and the revisions to the Bank Merger Act of 1966, the bank regulatory agencies were required to assess the potential competitive impact of bank mergers and decide in each case whether the merger would have significantly adverse effects on competition in "any line of commerce or any section of the country." As a result, the delineation of banking markets took on great importance.

This staff study critically reviews the theoretical and empirical literature dealing with geographic market determination. Emphasis is placed on the ability to define meaningful economic banking markets for the purpose of analyzing bank mergers and acquisitions in the context of current antitrust policy. Literature from disciplines other than banking is included. Following the review of the academic literature, the study evaluates the different approaches to geographic market determination used by the bank regulatory agencies and the approach recently

suggested in the merger guidelines issued by the Department of Justice.

The study finds that despite the extensive treatment of delineation of banking markets in the literature, the techniques used by researchers and regulators in banking have not changed much in the last decade. All of the current approaches rely in one way or another on evidence that indicates that for some bank customers the market is a relatively small geographic area.

Yet, during the past few years, the financial environment has changed markedly. And recent surveys indicate that nonlocal and nonbank firms are increasingly important to the traditional bank customer, though still to a limited extent. These facts raise questions regarding the relevance of the local geographic banking market and the approaches now used by the regulatory agencies.

The study concludes that these questions can be resolved only through additional research. The literature does not reveal any clearly superi-



or approach to geographic market definition, although it does illustrate well the tradeoffs between theoretical consistency and applicability. The recent empirical evidence on the extent of geographic banking markets is far from definitive. And in any event, financial markets are still

in transition, so that the applicability of the recent data is uncertain. Based on the review of the literature, the study concludes with suggestions regarding areas in which research would be profitable.

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### *A COMPARISON OF DIRECT DEPOSIT AND CHECK PAYMENT COSTS*

*William Dudley—Staff, Board of Governors*

Prepared as a staff study in the summer of 1984.

This paper presents the findings of a study of the relative cost of payment by direct deposit versus check. The study, which was requested by the Interagency Task Force on Electronic Fund Transfers, was undertaken to determine whether expansion of the direct deposit program would be in the public interest. The eight government agencies that make the majority of all recurring federal government benefit payments participated in the study, along with the U.S. Treasury (including the U.S. Secret Service), the Federal Reserve System, General Services Administration (for storage and retrieval of checks), and the depository institutions.

To aid in the analysis, the resource costs incurred in fiscal year 1981 by the participants in the study were calculated. In addition, the net budgetary cost to the federal government (including the cost of forgone check float) was determined. This computation relied on a Federal Reserve study of government check float completed in January 1984. The cost of enrolling a new claimant for either direct deposit or check

payment and the average cost for each form of payment once enrollment has been completed were ascertained. These two cost components were then combined in a present-value calculation to determine the relative costs of payment by direct deposit and check.

The study found that the average resource cost for the federal government and the depository institutions was significantly less for direct deposit than for check payment. For the government alone, the average direct deposit account generated an operational cost saving over its life with a present value of about five dollars. However, the findings indicated that the direct deposit program had a substantial negative impact on the federal government's budget. When the cost of forgone check float (which does not represent a resource cost to society as a whole) was included as a cost to the federal government of making a direct deposit payment, the cost of payment by direct deposit far exceeded the cost of payment by check. □

# Announcements

## *CHANGE IN SCHEDULE FOR THE FEDERAL RESERVE BULLETIN*

Beginning with this issue the FEDERAL RESERVE BULLETIN will be released the first of the month instead of during the last week.

To facilitate this changeover, this issue of the BULLETIN does not include the tables that regularly appear in the "Financial and Business Statistics" section. The data for the tables that would have been published in the November issue under the old schedule were not available in time for the November publication date. These data will be published in the December BULLETIN, and the tables will appear regularly in subsequent issues of the BULLETIN.

The reprint of the industrial production statistical release (G.12.3) for September will be pub-

lished in the December BULLETIN. The regular press release date for G.12.3 is not affected.

## *SYSTEM MEMBERSHIP: ADMISSION OF STATE BANKS*

The following banks were admitted to membership in the Federal Reserve System during the period September 11 through October 5, 1984:

### *Arizona*

Phoenix ..... Guardian Bank

### *California*

Red Bluff ..... Tehama County Bank

### *Florida*

Miami ..... Central Bank

Miami ..... Gulf Bank

# Record of Policy Actions of the Federal Open Market Committee

*MEETING HELD ON AUGUST 21, 1984*

## *1. Domestic Policy Directive*

The information reviewed at this meeting suggested that the expansion in economic activity was continuing at a relatively strong pace, though moderating from the annual rate of about 7½ percent recorded for the second quarter. Thus far in 1984, average prices, as measured by the fixed-weight price index for gross domestic business product, appeared to have risen more slowly than in 1983.

Industrial production rose 0.9 percent in July, the same as the increase in the preceding month, which had been revised upward. Production of durable consumer goods increased sharply, while output of nondurable goods rose little on balance. Output of business equipment remained sizable though somewhat below the advanced pace of other recent months. The rate of capacity utilization in manufacturing reached 82.6 percent in July, its highest level since early 1980.

Labor market reports for July gave mixed signals. Nonfarm payroll employment rose 300,000 further, just a little less than the average gain over the first six months of the year. However, the civilian unemployment rate, which had plunged to 7.1 percent in June, returned to its May level of 7.5 percent, as the survey of households showed a sharp drop in employment after two months of especially large increases. For the three-month period ending in July, both measures of employment reported a sizable increase of nearly 1 million jobs.

Retail sales fell 0.9 percent in July, after rising considerably in both the first and the second quarters of the year. Sales declines were reported at nearly all major types of stores but were especially pronounced at general merchandise, apparel, and furniture and appliance stores

where growth had been especially strong earlier. Sales of new domestic automobiles were a little above the annual rate of about 8¼ million units recorded for the first half of the year; but they dropped back to a rate of about 7½ million units in the first 10 days of August, in part because some popular models were in short supply.

Housing starts fell in July to a rate appreciably below the average in the second quarter. Starts of single-family units, declining for the third month in a row, were nearly 14 percent below the second-quarter average; multifamily starts, though edging down in July, remained above the average in the preceding quarter. Newly issued building permits declined almost 12 percent in July, with issuance down by comparable margins for both single-family and multifamily construction.

In contrast to the slowing in the consumer and housing sectors, business fixed investment continued to expand quite rapidly, and commitments for future spending remained high. Shipments of nondefense capital goods rose further in June and were up nearly 6 percent for the second quarter as a whole. New orders for such goods increased about 5 percent in the quarter and the backlog of outstanding orders continued to rise.

Incoming information on prices and wages indicated a continuation of recent favorable trends. The producer price index for finished goods increased 0.3 percent in July, after three months of virtually no change. Data on consumer prices in July were not yet available, but in June the consumer price index had risen 0.2 percent for the second consecutive month. Over the first seven months of 1984, producer prices increased at an annual rate of about 3 percent, and over the first half of the year, consumer prices and the index of average hourly earnings rose at annual rates of about 4 percent and 3½ percent respectively.

In the period following the July FOMC meeting, the foreign exchange value of the dollar against a trade-weighted average of major foreign currencies rose about 2 percent further to a new high in early August; subsequently the dollar's value fluctuated in a range a little below the peak. Over most of the intermeeting interval exchange markets were quite volatile, apparently reflecting changing perceptions among market participants about the outlook for interest rates, inflation, and economic activity in the United States. The merchandise trade deficit in June was somewhat above the May level, and for the second quarter as a whole the deficit was little changed from the high first-quarter rate.

At its meeting on July 16–17, 1984, the Committee had decided that open market operations in the period until this meeting should be directed initially toward maintaining existing pressures on reserve positions. That action was expected to be consistent with growth in M1, M2, and M3 at annual rates of around 5½, 7½, and 9 percent respectively during the period from June to September. The Committee also agreed that somewhat greater restraint would be acceptable in the event of more substantial growth of the monetary aggregates, while somewhat lesser restraint might be acceptable if growth of the monetary aggregates slowed significantly. Any such adjustment would be considered only in the context of appraisals of the continuing strength of the business expansion, inflationary pressures, financial market conditions, and the rate of credit growth. The intermeeting range for the federal funds rate, which provides a mechanism for initiating consultation of the Committee, was set at 8 to 12 percent.

M1 contracted at an annual rate of 1½ percent in July, after increasing at an average annual rate of about 12 percent in May and June. Data for early August, however, suggested some rebound in M1 growth. Growth in M2 was at an annual rate of about 5 percent in July, a relatively slow pace that was due in part to the sluggishness in M1, while expansion in M3 was relatively well maintained at an annual rate of a little below 9 percent. Despite the decline in M1 and comparatively slow growth in M2 in July, these aggregates remained well within the Committee's objectives for the year. From the fourth quarter of

1983 through July, M1 grew at a rate a bit above the midpoint of the Committee's range of 4 to 8 percent for 1984; M2 increased at a rate a little below the midpoint of its longer-run range of 6 to 9 percent. Over the same period, M3 expanded at a rate somewhat above the upper limit of its range of 6 to 9 percent.

Expansion of total domestic nonfinancial debt was estimated to have remained at an annual rate of around 13 percent in July, keeping growth thus far in 1984 at a pace above the Committee's monitoring range of 8 to 11 percent for the year. A pickup in growth of federal debt offset some slowing in expansion of private debt, as merger-related borrowing lessened. Total credit at U.S. commercial banks expanded at an estimated annual rate of 9¼ percent in July, after rising only slightly in June. The acceleration primarily reflected a shift from liquidation to accumulation in holdings of U.S. Treasury securities; growth in business and consumer loans showed little change from the pace in June.

Total reserves decreased in July at an annual rate of about 2 percent, after expanding rapidly over the two preceding months. The contraction reflected a marked deceleration in growth of required reserves, associated with weakness in transaction accounts as demand deposits fell following a sharp increase in June, and a reduction in excess reserves from the relatively high June level. In the two complete reserve maintenance periods since the July FOMC meeting, adjustment plus seasonal borrowing continued to average in the neighborhood of \$1 billion.

Despite little change in the average level of borrowing from the discount window, the federal funds rate tended to drift higher over the intermeeting period; recently funds traded in a range of 11½ to 11¾ percent, up from about 11¼ percent at the time of the Committee meeting in July, as banks seemed to be somewhat reluctant to borrow from the discount window and they bid more aggressively for funds in the market. Some other very short-term rates rose slightly over the intermeeting period but most short- and long-term rates declined, with yields on bonds falling about ⅝ to ¾ percentage point. Stock price indexes advanced 9 to 10 percent over the interval on record trading volume, as the market reacted positively to interpretations of the future

course of monetary policy in connection with the Federal Reserve's midyear report to the Congress, and to incoming data on economic activity, prices, and money supply growth.

The staff projections presented at this meeting continued to suggest that expansion in real GNP would moderate over the balance of the year and in 1985, a pattern of growth often characteristic of maturing business expansions and rising utilization of productive resources. The unemployment rate was projected to decline somewhat further over the period and, though current information on cost and price pressures remained quite favorable, the rate of price increase was expected to pick up a little from its recent pace.

In their discussion of the economic situation and outlook, Committee members generally agreed that the expansion in economic activity was continuing at a relatively strong pace, although they expected the rate of growth to slow appreciably over the next several quarters. They recognized, however, that the outlook for economic activity and for prices and wages remained subject to substantial uncertainties. These were especially pronounced because of the distortions created by unprecedented deficits in the federal budget and the balance of payments, the strength of the dollar, and the sensitive state of domestic and international financial markets.

A number of members pointed to indications—such as in housing, retail sales, and steel production—that the rate of expansion might be moderating appreciably, and some members commented on the emergence of more cautious attitudes among businessmen in many parts of the country. Members also referred to the cyclical tendency for expansions to lose momentum over time and to the risks inherent in the various imbalances and financial strains that were affecting the economy. Some members, however, continued to view the risks as mainly in the direction of more rapid expansion than was generally expected, given the economy's current momentum, the strength of business investment, and a highly stimulative fiscal policy. With regard to the nearer-term outlook, it was noted that a prolonged strike in the automobile industry could have a considerable impact, at least temporarily, in retarding the overall expansion.

The members expressed somewhat diverging views on the outlook for inflation. Some placed considerable stress on the prospect that price and wage pressures might increase as the economy's productive resources became more fully employed. An inflationary threat was also seen in the possibility of a sizable decline in the foreign exchange value of the dollar. Likewise, a number of members expressed concern that an excessive wage settlement in the automobile industry, if it were to occur, would tend to have an inflationary impact on other wage negotiations, with widespread consequences for wage-cost pressures in the economy.

Members who were relatively optimistic about the outlook for inflation stressed, among other factors, the prospects for continued good gains in productivity. They commented in particular about the renascent and apparently strong determination of businessmen to hold down their costs and to improve the efficiency of their operations. Moreover, the large investments in capital during recent quarters would, it was argued, help to enhance productivity over time. One member also observed that, while a sizable decline in the foreign exchange value of the dollar would tend to increase upward price pressures, such a result might well be more limited or delayed longer than usual in light of the relatively sluggish pace of economic activity abroad and consequent efforts by foreign competitors to retain recently enhanced U.S. market shares through aggressive pricing.

At its meeting in July, the Committee had reviewed and reaffirmed the basic policy objectives that it had established in January for growth of the monetary and credit aggregates in 1984 and had set tentative objectives for growth in 1985. For 1984 the policy objectives included growth of 4 to 8 percent for M1 and 6 to 9 percent for both M2 and M3 for the period from the fourth quarter of 1983 to the fourth quarter of 1984. The associated range for growth in total domestic nonfinancial debt was also reaffirmed at 8 to 11 percent for the year 1984. Given developments in the first half of the year, the Committee anticipated that M3 and particularly nonfinancial debt might increase at rates somewhat above the upper limits of their 1984 ranges. The tentative ranges established for 1985 included reductions of 1 and ½

percentage point from the upper limits of the 1984 ranges for M1 and M2 respectively, and no changes in the range for M3 and the associated range for total domestic nonfinancial debt.

In the Committee's discussion of policy implementation for the weeks immediately ahead, a majority of the members expressed a preference for continuing to maintain about the current degree of restraint on reserve positions. A number of members, while finding the current approach to policy implementation acceptable, nonetheless were prepared to look toward some slight easing of reserve conditions, either currently or soon should monetary growth fail to pick up from recent trends. They believed that such an approach would likely be consistent with attainment of the third-quarter objectives for monetary growth that had been set at the July meeting, given the shortfall in the aggregates since the meeting, and would also be consistent with signs of some weakening in the rate of economic growth relative to expectations. Moreover, in the view of at least some of these members, some lessening in the degree of reserve restraint would appropriately tend to offset the unusual pressures that had developed in the federal funds market during June and July. Those pressures were not associated with any change in the degree of reserve restraint, but they appeared to reflect the emergence of more conservative reserve management attitudes on the part of banks. Other members commented, however, that any active effort to ease reserve conditions would be undesirable at present, and could well be misinterpreted, unless clearly related to emerging weakness in monetary growth in the context of appreciably slower-than-expected expansion in economic activity.

One Committee member indicated a preference for somewhat tighter reserve conditions so as to help assure moderate rates of monetary expansion. In this view, the near-term pressure on interest rates that might result from such an approach to policy implementation could well preclude the need for greater, and more disruptive, rate increases later. On the other hand, other members commented that further restraint would be undesirable except in the context of rapid monetary growth against a background of greater strength in economic activity. It was

viewed that current reserve conditions had become restrictive enough, as pressures on financial institutions and borrowers had cumulated over a number of months, so that the risk of an unduly rapid spurt of money and credit growth was relatively low.

In discussing how operations might be adjusted during the intermeeting period if monetary growth should prove to be significantly faster or slower than targeted for the current quarter, most members felt that the implementation of open market operations should be sensitive to the potential desirability of somewhat lesser restraint over the weeks ahead, as well as to the possible need for some greater restraint should monetary growth resume at an excessive rate against a background of greater economic ebullience than seemed to be taking place currently. As compared with conditions at the time of the previous meeting, the monetary aggregates had weakened—with M1, for example, closer to the middle of its longer-run range—and there were more indications of a moderation in the expansion of economic activity. It was understood that any intermeeting adjustment in reserve pressures would not be made automatically in response to the behavior of the monetary aggregates, but would be undertaken only in the context of appraisals of the strength of economic activity and inflationary pressures, and evaluations of conditions in domestic and international financial and banking markets and the rate of credit growth.

At the conclusion of the discussion, all but one member indicated their acceptance of a directive specifying no change at this time in the degree of pressure on reserve positions, but calling for a response to any significant deviation in the aggregates from expectations against the background of economic and financial developments. The members anticipated that this approach to policy implementation would be consistent with growth of the various aggregates at rates for the quarter close to those specified at the previous meeting. Specifically, M1 was expected to grow at an annual rate of around 5 percent or slightly less for the period from June to September, a little less than expected at the previous meeting reflecting the contraction in M1 in July. The annual rates of growth for M2 and M3 in the third

quarter would continue to be 7½ and 9 percent respectively. The intermeeting range for the federal funds rate was left unchanged at 8 to 12 percent. It was also recognized that, within the context of this overall approach, operations might need to be modified if unusual financial strains appeared to be developing.

At the conclusion of the meeting the following domestic policy directive was issued to the Federal Reserve Bank of New York:

The information reviewed at this meeting suggests that the expansion in economic activity is continuing at a strong pace, but there are indications of a moderation in the rate of growth. In July, industrial production and nonfarm payroll employment rose further, but retail sales fell after rising considerably in earlier months and housing starts declined to a rate appreciably below the average in the second quarter. The civilian unemployment rate increased 0.4 percentage point to 7.5 percent. Information on outlays and spending plans continues to suggest strength in business fixed investment. Since the beginning of the year, average prices and the index of average hourly earnings have risen more slowly than in 1983.

In July, M1 declined after two months of rapid growth, though data for early August suggested some rebound, while M2 expanded at a relatively slow pace. M3 growth, however, remained comparatively sizable. From the fourth quarter of 1983 through July, M1 grew at a rate a bit above the midpoint of the Committee's range for 1984; M2 increased at a rate a little below the midpoint of its longer-run range, while M3 expanded at a rate above the upper limit of its range. Growth in total domestic nonfinancial debt appears to be continuing at a pace above the Committee's monitoring range for the year, reflecting very large government borrowing along with strong private credit growth. Most interest rates have fallen considerably since the July meeting of the Committee, with the largest declines generally in intermediate and long-term bond markets.

The foreign exchange value of the dollar against a trade-weighted average of major foreign currencies rose further to a new high in early August and since then has fluctuated in a range just below the peak. The merchandise trade deficit in June was somewhat above the May level, and for the second quarter as a whole the deficit was little changed from the high first-quarter rate.

The Federal Open Market Committee seeks to foster monetary and financial conditions that will help to reduce inflation further, promote growth in output on a sustainable basis, and contribute to an improved pattern of international transactions. In furtherance of these objectives the Committee agreed at the July meeting to reaffirm the ranges for monetary growth

that it had established in January: 4 to 8 percent for M1 and 6 to 9 percent for both M2 and M3 for the period from the fourth quarter of 1983 to the fourth quarter of 1984. The associated range for total domestic nonfinancial debt was also reaffirmed at 8 to 11 percent for the year 1984. It was anticipated that M3 and nonfinancial debt might increase at rates somewhat above the upper limits of their 1984 ranges, given developments in the first half of the year, but the Committee felt that higher target ranges would provide inappropriate benchmarks for evaluating longer-term trends in M3 and credit growth. For 1985 the Committee agreed on tentative ranges of monetary growth, measured from the fourth quarter of 1984 to the fourth quarter of 1985, of 4 to 7 percent for M1, 6 to 8½ percent for M2, and 6 to 9 percent for M3. The associated range for nonfinancial debt was set at 8 to 11 percent.

The Committee understood that policy implementation would require continuing appraisal of the relationships not only among the various measures of money and credit but also between those aggregates and nominal GNP, including evaluation of conditions in domestic credit and foreign exchange markets.

In the implementation of policy in the short run, the Committee seeks to maintain existing pressures on reserve positions. This action is expected to be consistent with growth in M1 at an annual rate of around 5 percent or slightly less, and in M2 and M3 at annual rates of around 7½ and 9 percent respectively during the period from June to September. Somewhat greater reserve restraint would be acceptable in the event of more substantial growth of the monetary aggregates, while somewhat lesser restraint would be acceptable in the event of significantly slower growth. In either case, such a change would be considered only in the context of appraisals of the continuing strength of the business expansion, inflationary pressures, financial market conditions, and the rate of credit growth. The Chairman may call for Committee consultation if it appears to the Manager for Domestic Operations that pursuit of the monetary objectives and related reserve paths during the period before the next meeting is likely to be associated with a federal funds rate persistently outside a range of 8 to 12 percent.

Votes for this action: Messrs. Volcker, Solomon, Boehne, Boykin, Corrigan, Gramley, Mrs. Horn, Messrs. Martin, Partee, Rice, and Ms. Seger. Vote against this action: Mr. Wallich.

Mr. Wallich dissented from this action because he preferred a directive calling for a somewhat greater degree of reserve restraint and marginally lower monetary growth in the third quarter. In his view such a directive was more likely to help avert more serious inflation and financial pressures later.

*2. Authorization for Domestic Open Market Operations*

At this meeting, the Committee approved a temporary increase from \$4 billion to \$6 billion in the limit on changes between Committee meetings in System Account holdings of U.S. government and federal agency securities specified in paragraph 1(a) of the authorization for domestic open market operations. The increase was effective for the intermeeting period ending with the close of business on October 2, 1984.

Votes for this action: Messrs. Volcker, Solomon, Boehne, Boykin, Corrigan, Gramley, Mrs. Horn,

Messrs. Martin, Partee, Rice, Ms. Seger, and Mr. Wallich. Votes against this action: None.

This action was taken on the recommendation of the Manager for Domestic Operations. The Manager had advised that projected increases in required reserves and currency might require net purchases of securities over the intermeeting interval in amounts close to the usual \$4 billion leeway. A likely rise in Treasury balances at Federal Reserve Banks would add to the need for System purchases of securities. Accordingly, the Manager requested the temporary increase in the limit to provide the necessary leeway for handling that contingency.



# Legal Developments

## *BANK HOLDING COMPANY, BANK MERGER, AND BANK SERVICE CORPORATION ORDERS ISSUED BY THE BOARD OF GOVERNORS*

### *Orders Issued Under Section 3 of Bank Holding Company Act*

#### **BankVermont Corporation Burlington, Vermont**

#### *Order Approving Registration of a Bank Holding Company*

BankVermont Corporation, Burlington, Vermont, has applied for the Board's approval under section 3(a)(1) of the Bank Holding Company Act ("Act") (12 U.S.C. § 1842(a)(1)) to register as a bank holding company as a result of its prior acquisition of the voting shares of Bank of Vermont, Burlington, Vermont ("Bank"). Applicant acquired Bank upon its conversion from an FDIC-insured state-chartered mutual savings bank to an FDIC-insured stock savings bank.<sup>1</sup>

Notice of this application, affording opportunity for interested persons to submit comments, has been given in accordance with section 3 of the Act. The time for filing comments has expired, and the Board has considered the application and all comments received in light of the factors set forth in section 3(c) of the Act (12 U.S.C. § 1842(c)).

The Board has previously determined that a state guaranty savings bank is a "bank" under section 2(c) of the Act if it accepts demand deposits (including NOW accounts), engages in the business of making commercial loans, and is not covered by the exemption created by the Garn-St Germain Depository Institutions Deregulation Act of 1982 for FSLIC insured thrift institutions.<sup>2</sup> Bank accepts demand deposits and NOW accounts and engages in the business of making

commercial loans. Its deposits are not insured by the FSLIC. Accordingly, the Board has determined that Bank is a "bank" for purposes of the BHC Act. The application has therefore been considered in light of the requirements of section 3 of the Act pertaining to the acquisition of banks.

Applicant was formed in 1983 to acquire the shares of Bank upon its conversion to a stock savings bank. Bank, which holds \$428 million in total domestic deposits, is the second largest depository institution in Vermont, controlling 10.6 percent of the total deposits in all depository institutions in the state.<sup>3</sup> Bank is the largest of nine depository institutions in the relevant banking market, holding 33.6 percent of the total deposits in all depository institutions in the banking market.<sup>4</sup> Applicant's prior acquisition of Bank represented a corporate reorganization and did not increase the concentration of banking resources in any relevant area. Neither Applicant nor any of its principals is affiliated with any other banking organization in any relevant banking market. Accordingly, the Board has concluded that approval of this application would not result in any adverse effects upon competition in any relevant area.

The financial and managerial resources of Applicant and Bank are regarded as generally satisfactory, and their prospects appear favorable, in light of certain commitments made by Applicant and Bank to improve Bank's capital. Although Applicant's prior acquisition of Bank did not result in any immediate changes in the services offered by Bank, considerations relating to convenience and needs of the community to be served are consistent with approval of the application. Accordingly, the Board has determined that Applicant's proposal to register as a bank holding company is in the public interest and that the application should be approved.

Based on the foregoing and other facts of record, the Board has determined that the application under section 3(a)(1) of the Act should be and hereby is approved.

1. On August 25, 1983, Applicant acquired 99.75 percent of the voting shares of Bank, then called The Burlington Savings Bank.

2. *The Frankford Corporation*, 70 FEDERAL RESERVE BULLETIN 654 (1984), *The One Bancorp*, 70 FEDERAL RESERVE BULLETIN 359 (1984); *Amoskeag Bank Shares, Inc.*, 69 FEDERAL RESERVE BULLETIN 860 (1983), *First NH Banks, Inc.*, 69 FEDERAL RESERVE BULLETIN 874 (1983).

3. Banking data are as of March 31, 1984.

4. Market data are as of June 30, 1983 for all depository institutions except credit unions. The relevant banking market is defined as the Burlington, Vermont banking market.

By order of the Board of Governors, effective September 24, 1984.

Voting for this action: Vice Chairman Martin and Governors Partee, Rice, Gramley, and Seger. Absent and not voting: Chairman Volcker and Governor Wallich.

JAMES MCAFEE  
[SEAL] Associate Secretary of the Board

FirstBank Holding Company of Colorado  
Lakewood, Colorado

FirstBank Holding Company  
Lakewood, Colorado

*Order Approving Acquisition of Bank*

FirstBank Holding Company of Colorado and its subsidiary, FirstBank Holding Company ("Applicants"), both of Lakewood, Colorado, and each a bank holding company within the meaning of the Bank Holding Company Act ("Act") (12 U.S.C. § 1841 *et seq.*), have applied for the Board's approval under section 3(a)(3) of the Act (12 U.S.C. § 1842(a)(3)) to acquire all of the voting stock of FirstBank at Broadway/County Line Road, N.A., Littleton, Colorado, a *de novo* bank ("Bank").

Notice of the applications, affording opportunity for interested persons to submit comments, has been given in accordance with section 3(b) of the Act. The time for filing comments has expired and the Board has considered the applications and all comments received in light of the factors set forth in section 3(c) of the Act (12 U.S.C. § 1842(c)).

Applicants' organization is the seventh largest commercial banking organization in Colorado, controlling 22 subsidiary banks with total deposits of \$452.6 million, representing 2.5 percent of total deposits in commercial banks in the state.<sup>1</sup> Since the bank to be acquired is a *de novo* bank, consummation of this proposal would not result in an increase in the concentration of banking resources in the state.

Bank is to be located in an unincorporated portion of Arapahoe County, Colorado, and will compete in the banking market approximated by the Denver, Colorado, Ranally Metro Area ("Denver RMA"). Applicants control 11 subsidiary banks in the market and currently rank as the sixth largest banking organization in the Denver RMA, controlling \$291.6 million in deposits, representing 2.7 percent of total deposits in the mar-

ket. As Bank is a *de novo* institution, consummation of the proposal will not have any significant adverse effects on either existing or potential competition in any relevant market.

The financial and managerial resources and future prospects of Applicants, their subsidiaries and Bank are considered to be generally satisfactory and consistent with approval.<sup>2</sup> Considerations relating to convenience and needs of the communities to be served are also consistent with approval of this application.

On the basis of the foregoing and all the facts of record, the Board has determined that the applications should be, and hereby are approved. The transaction shall not be consummated before the thirtieth calendar day following the effective date of this Order, or later than three months after the effective date of this Order, and FirstBank at Broadway/County Line Road shall be opened for business no later than six months after the effective date of this Order, unless such period is extended for good cause by the Board or the Federal Reserve Bank of Kansas City, acting pursuant to delegated authority.

By order of the Board of Governors, effective September 25, 1984.

Voting for this action: Vice Chairman Martin and Governors Partee, Rice, Gramley, and Seger. Absent and not voting: Chairman Volcker and Governor Wallich.

WILLIAM W. WILES  
[SEAL] Secretary of the Board

First Colonial Bankshares Corporation  
Chicago, Illinois

*Order Approving Acquisition of Bank*

First Colonial Bankshares Corporation, Chicago, Illinois, a bank holding company within the meaning of the Bank Holding Company Act ("Act") (12 U.S.C. § 1841 *et seq.*), has applied for the Board's approval under section 3(a)(3) of the Act (12 U.S.C. § 1842(a)(3)) to acquire all of the voting shares of

2. In several recent cases, the Board has noted its concerns regarding the capital adequacy of bank holding company applicants seeking to expand through sizeable acquisitions involving a significant level of intangible assets. *National City Corporation*, 70 FEDERAL RESERVE BULLETIN 743 (1984); and *Eagle Bancorporation*, 70 FEDERAL RESERVE BULLETIN 728 (1984). Although intangibles represent a substantial portion of Applicants' primary capital, the proposed acquisition of Bank, a *de novo* institution, would not result in any increase in Applicants' intangible assets, or any appreciable decline in Applicants' capital ratios. Virtually all of Applicants' intangible assets originated in 1981, when FirstBank Holding Company of Colorado acquired FirstBank Holding Company. Since that time, Applicants' ratio of intangibles to primary capital has decreased at a steady rate.

1. Banking data are as of December 31, 1983. Applicants also control an industrial bank, with deposits of \$1.3 million

Michigan Avenue National Bank of Chicago, Chicago, Illinois ("Bank").<sup>1</sup>

Notice of the application, affording opportunity for interested persons to submit comments, has been given in accordance with section 3(b) of the Act. The time for filing comments has expired, and the Board has considered the application and all comments received in light of the factors set forth in section 3(c) of the Act (12 U.S.C. § 1842(c)).

Applicant is the 30th largest commercial banking organization in Illinois, controlling three banks with total deposits of \$304.1 million, representing 0.3 percent of the total deposits in commercial banks in the state.<sup>2</sup> Bank is the 80th largest commercial bank in Illinois with total deposits of \$154.8 million, representing less than 0.2 percent of the total deposits in commercial banks in the state. Upon consummation of this proposal, Applicant would become the 14th largest commercial banking organization in the state, controlling total deposits of approximately \$458.9 million, representing approximately 0.4 percent of total deposits in the state. In the Board's view, consummation of this proposal will not result in any significant adverse effects on the concentration of banking resources in Illinois.

Bank operates in the Chicago, Illinois, banking market, where it is the 63rd largest of 389 commercial banking organizations in the market, controlling approximately 0.2 percent of the total deposits in commercial banks.<sup>3</sup> Applicant also competes in the Chicago, Illinois, banking market. Following consummation of this proposal, Applicant would be the 12th largest banking organization in the relevant market, with approximately 0.6 percent of the deposits in commercial banks in the market. Based on all the facts of record, the Board concludes that consummation of the proposed transaction would have no significant adverse effects on either existing or potential competition in any relevant market.

In evaluating this application, the Board also has considered the financial and managerial resources of Applicant and the effect on these resources of the proposed acquisition of Bank. The Board has stated

and continues to believe that capital adequacy is an especially important factor in the analysis of bank holding company proposals.<sup>4</sup>

In this case, Applicant's existing primary and total capital ratios are above the minimum levels specified in both the Board's current and proposed Capital Adequacy Guidelines.<sup>5</sup> Consummation of the proposal would not result in a decline in Applicant's primary or total capital ratios or in Applicant's tangible primary capital ratio. Although a portion of Applicant's primary capital consists of intangibles and the absolute amount of intangibles would increase following the proposed transaction, the ratio of intangibles to tangible primary capital would not increase. Moreover, although intangibles represent a portion of Applicant's pro forma capital structure, Applicant does not place excessive reliance on intangibles to meet the Board's Capital Adequacy Guidelines, and the Board does not believe that the amount of intangibles will affect Applicant's ability to serve as a source of strength to its banking subsidiaries.

Finally, the Board notes that the contracts for this transaction were completed and the application was accepted for processing before either the Board's proposed Capital Adequacy Guidelines or the *National City Corporation* decision were issued.

Based upon the above and other facts of record, the Board concludes that the financial and managerial resources and future prospects of Applicant, its subsidiaries, and Bank are generally satisfactory and consistent with approval.

Considerations relating to the convenience and needs of the communities to be served are also consistent with approval of this application.

On the basis of the record, the application is approved for the reasons summarized above. The transaction shall not be consummated before the thirtieth calendar day following the effective date of this Order, or later than three months after the effective date of this Order, unless such period is extended for good cause by the Board or the Federal Reserve Bank of Chicago, acting pursuant to delegated authority.

By order of the Board of Governors, effective September 25, 1984.

Voting for this action: Vice Chairman Martin and Governor Partee, Rice, Gramley, and Seger. Absent and not voting: Chairman Volcker and Governor Wallich.

JAMES MCAFFEE

[SEAL]

*Associate Secretary of the Board*

1. Applicant is currently a one-bank holding company, controlling First Colonial Bank and Trust Company, Chicago, Illinois. On February 23, 1984, Applicant received prior approval to acquire control of the Colonial Group, Inc., Chicago, Illinois, and, indirectly, its two subsidiary banks, Northwest Commerce Bank, Rosemont, Illinois, and All American Bank of Chicago, Chicago, Illinois. Although Applicant has not yet consummated this proposal, the data upon which the Board bases its analysis of the financial and competitive factors in this case reflect consummation of the proposal and financial and competitive factors in this case are analyzed as if this transaction had been consummated.

2. Banking data are as of December 31, 1983, and reflect bank holding company acquisitions approved as of July 31, 1984.

3. The Chicago, Illinois, banking market is approximated by Cook, DuPage, and Lake Counties, Illinois.

4. *National City Corporation*, 70 FEDERAL RESERVE BULLETIN 743 (1984).

5. Capital Adequacy Guidelines, 12 C.F.R., Part 225, Appendix A *Capital Adequacy Guidelines for Bank Holding Companies*, 49 *Federal Register* 30322 (July 30, 1984).

## First National Bankshares of Sheridan Sheridan, Wyoming

### *Order Approving Acquisition of Bank*

First National Bankshares of Sheridan, Sheridan, Wyoming, a bank holding company within the meaning of the Bank Holding Company Act ("Act"), 12 U.S.C. § 1841 *et seq.*, has applied for the Board's approval under section 3(a)(3) of the Act, 12 U.S.C. § 1842(a)(3), to acquire Ranchester State Bank ("Bank"), Ranchester, Wyoming.

Notice of the application, affording an opportunity for interested persons to submit comments, has been given in accordance with section 3(b) of the Act. The time for filing comments has expired, and the Board has considered the application and all comments received, including those of the Acting State Examiner of Banks for the State of Wyoming, in light of the factors set forth in section 3(c) of the Act, 12 U.S.C. § 1842(c).

Applicant is the 10th largest banking organization in Wyoming, controlling one subsidiary bank, the First National Bank of Sheridan ("FNBS"),<sup>1</sup> Sheridan, Wyoming, with total deposits of \$71.3 million, representing 1.9 percent of the total deposits in commercial banks in Wyoming.<sup>2</sup> Bank is the 81st largest banking organization in Wyoming, controlling deposits of \$9.6 million, representing 0.2 percent of the total deposits in commercial banks in the state. Upon consummation of this transaction, Applicant would become the 9th largest banking organization in Wyoming, controlling deposits of \$80.9 million, representing 2.1 percent of total deposits in commercial banks in the state. Accordingly, consummation of this proposal would not have any significant effects upon the concentration of banking resources in Wyoming.

Applicant and Bank both compete in the Sheridan County banking market.<sup>3</sup> Applicant's subsidiary bank, FNBS, is located in Sheridan, Wyoming, 13 miles from Bank, which is the only bank located in Ranchester, Wyoming. FNBS is the second largest of four commercial banks in the relevant banking market, and controls 34.9 percent of the total deposits in commercial banks in the market. Bank is the smallest commercial bank in the Sheridan County banking market, and controls 4.7 percent of the total deposits in commercial banks in that market. Upon consummation of this proposal, FNBS would remain the second largest

commercial bank in the Sheridan County market, and would control 39.5 percent of the total deposits in commercial banks in that market. Upon consummation of this proposal, the Herfindahl-Hirschman Index ("HHI") of 4003 would increase by 328 points to 4331.<sup>4</sup> The Sheridan County banking market is a highly concentrated market with the three largest commercial banks in the market holding 95.3 percent of the deposits. Upon consummation of this proposal, only three commercial banks would remain in the market; thus, the three largest commercial banks in the market would hold 100 percent of the market's deposits.

Even if competition from thrift institutions in the market were taken into consideration and 50 percent of the deposits held by thrift institutions were included in the calculation of market concentration, consummation of this proposal would increase the HHI in the Sheridan County market by 214 points to 3058 and FNBS would control 32 percent of the market's total deposits.<sup>5</sup> It would appear from these facts of record that consummation of this proposal would have substantially adverse effects on existing competition in the Sheridan County market.

The anticompetitive effects of this proposal are, however, mitigated by several factors. Currently, Bank is not a strong competitor in the market, and its effectiveness as a competitor has declined steadily since Bank's principals acquired control of Bank in 1979. The percentage of deposits in the market controlled by Bank was 5.5 percent in 1980, and had declined to 4.7 by year-end 1983. The ratio of Bank's loans to deposits was 62.5 percent in 1980, and had declined to 37.3 by mid-1984.

Section 3(c) of the Act provides that the Board may not approve an application under section 3 of the Act ". . . whose effect in any section of the country may be substantially to lessen competition, . . . unless it finds that the anticompetitive effects . . . are clearly outweighed in the public interest by the probable effect of the transaction in meeting the convenience and needs of the community to be served." 12 U.S.C. § 1842(c).

In assessing such considerations in light of the facts surrounding this proposal, the Board finds that the

4. Under the Justice Department Merger Guidelines, a market in which the post-merger HHI is above 1800 is considered highly concentrated. In such a market, the Justice Department is likely to challenge a merger that produces an increase in the HHI of 100 points or more.

5. Three thrift institutions in the market control deposits of \$97.3 million, representing 32.3 percent of the total deposits in commercial banks and thrift institutions in the Sheridan County banking market. The Board has previously determined that thrift institutions have become, or at least have the potential to become, major competitors of banks. *NCNB Corporation*, 70 FEDERAL RESERVE BULLETIN 225 (1984); *Sun Banks, Inc.*, 69 FEDERAL RESERVE BULLETIN 934 (1983); *Merchants Bancorp, Inc.*, 69 FEDERAL RESERVE BULLETIN 865 (1983); *Monmouth Financial Services, Inc.*, 69 FEDERAL RESERVE BULLETIN 867 (1983).

1. Applicant has one nonbank subsidiary, First Ag Corporation, Sheridan, Wyoming, which is an agricultural credit corporation.

2. Unless otherwise indicated, all commercial bank deposit data are as of December 31, 1983. All thrift deposit data are as of September 30, 1983.

3. The Sheridan County banking market is defined as Sheridan County, Wyoming.

anticompetitive effects are clearly outweighed in the public interest. The financial and managerial resources and future prospects of Applicant and its subsidiary are considered satisfactory and consistent with approval of this application. Bank's financial and managerial resources, absent consummation of the instant proposal, are less than satisfactory, and its future prospects are uncertain.

As noted above, Bank is the only bank located in the City of Ranchester. According to the facts of record, including reports of examination, it appears that Bank's overall financial condition has declined steadily since 1979. Accordingly, after reviewing these facts and taking into consideration the comments of the Acting State Examiner of Banks for the State of Wyoming, the Board has determined that consummation of this proposal would strengthen Bank and ensure that it continues to serve as a source of banking services for the residents of the City of Ranchester and Sheridan County, Wyoming.

Although the Board would prefer a less anticompetitive acquisition as a means for assuring the continuation of Bank as a vehicle for serving the convenience and needs of the public, it appears that such an alternative is not readily available.<sup>6</sup> Therefore, the Board views the improved financial prospects of Bank that would result from consummation of this proposal, and convenience and needs considerations as lending significant weight toward approval of the application and outweighing the anticompetitive effects that would result from consummation of the proposal. Accordingly, it is the Board's judgment that consummation of the proposal would be in the public interest and that the application should be approved.

On the basis of the record, the application is approved for the reasons summarized above. The acquisition shall not be consummated before the thirtieth calendar day following the effective date of this Order, or later than three months after the effective date of this Order, unless such period is extended for good cause by the Board or by the Federal Reserve Bank of Kansas City pursuant to delegated authority.

By order of the Board of Governors, effective September 28, 1984.

Voting for this action: Vice Chairman Martin and Governors Partee, Rice, Gramley, and Seger. Absent and not voting: Chairman Volcker and Governor Wallich.

JAMES MCAFEE

[SEAL]

*Associate Secretary of the Board*

6. Six financial organizations or investor groups, including Applicant, expressed an interest in purchasing Bank, but only Applicant offered to purchase Bank. Cf. *Van Buren Bancorporation*, 69 FEDERAL RESERVE BULLETIN 811 (1983); *National City Corporation*, 70 FEDERAL RESERVE BULLETIN 743 (1984).

First Taylor County Bancorporation, Inc.  
Bedford, Iowa

*Order Approving Formation of a Bank Holding Company*

First Taylor County Bancorporation, Inc., Bedford, Iowa, has applied for the Board's approval pursuant to section 3(a)(1) of the Bank Holding Company Act of 1956, as amended ("Act") (12 U.S.C. § 1842(a)(1)), to become a bank holding company by acquiring all of the voting shares of The Bedford National Bank, Bedford, Iowa ("Bank").

Notice of the application, affording interested persons an opportunity to submit comments, has been given in accordance with section 3(b) of the Act. The time for filing comments has expired, and the Board has considered the application and all comments received in light of the factors set forth in section 3(c) of the Act.

Applicant, a nonoperating corporation with no subsidiaries, was organized under the laws of Iowa for the purpose of becoming a bank holding company by acquiring Bank, which holds deposits of \$19.6 million.<sup>1</sup> Upon acquisition of Bank, Applicant would control the 355th largest of 643 banking organizations in Iowa, representing less than 0.1 percent of the total deposits in commercial banks in the state.

Within the relevant banking market,<sup>2</sup> Bank is the smallest of three commercial banking organizations and holds approximately 24 percent of the total deposits in commercial banks in the market. Neither Applicant nor any of its principals is associated with any other banking organization in the relevant market, and it appears that consummation of the proposal would not result in any adverse effects upon existing or potential competition or increase the concentration of banking resources in any relevant area.

The financial and managerial resources and future prospects of Applicant and Bank are regarded as consistent with approval, particularly in light of Applicant's commitment to provide additional capital to Bank. Applicant will incur debt, but it appears that Applicant is capable of servicing its debt while maintaining adequate capital at Bank. Accordingly, considerations relating to banking factors are consistent with approval. Considerations relating to the convenience and needs of the community to be served are also consistent with approval of the application.

Based on the foregoing and other facts of record, the Board has determined that consummation of the transaction would be in the public interest and that the

1. All banking data are as of June 30, 1984.

2. The relevant banking market is approximated by Taylor County, Iowa.

application should be approved. On the basis of the record, the application is approved for the reasons summarized above. The transaction shall not be consummated before the thirtieth calendar day following the effective date of this Order or later than three months after the effective date of this Order, unless such period is extended by the Board or by the Federal Reserve Bank of Chicago, acting pursuant to delegated authority.

By order of the Board of Governors, effective October 1, 1984.

Voting for this action: Chairman Volcker and Governors Martin, Wallich, Partee, Rice, Gramley, and Seger.

JAMES MCAFEE

[SEAL]

*Associate Secretary of the Board*

Fleet Financial Group, Inc.  
Providence, Rhode Island

#### *Order Approving Acquisition of Banks*

Fleet Financial Group, Inc., Providence, Rhode Island, a bank holding company within the meaning of the Bank Holding Company Act of 1956, as amended (12 U.S.C. § 1841 *et seq.*) ("Act"), has applied for the Board's approval under section 3(a)(3) of the Act (12 U.S.C. § 1842(a)(3)) to acquire all of the voting shares of Fleet National Bank of Boston, Boston, Massachusetts ("Fleet Boston"), and Fleet National Bank of Connecticut, Hartford, Connecticut ("Fleet Connecticut"), both proposed new banks.

Notice of the applications, affording opportunity for interested persons to submit comments, has been given in accordance with section 3(b) of the Act. The time for filing comments has expired, and the Board has considered the application and all comments received in light of the factors set forth in section 3(c) of the Act (12 U.S.C. § 1842(c)), including the comments of Citicorp, New York, New York, challenging the constitutionality of the Massachusetts and Connecticut statutes under which the proposed acquisitions are to be made.

Applicant, the largest banking organization in Rhode Island, has one banking subsidiary with total deposits of \$3.3 billion, representing 39.7 percent of the total deposits in commercial banks in Rhode Island.<sup>1</sup> Both Fleet Boston, which will compete in the

Boston banking market,<sup>2</sup> and Fleet Connecticut, which will compete in the Hartford banking market,<sup>3</sup> are proposed new banks. Applicant currently competes in neither the Boston nor the Hartford banking market. In light of the *de novo* nature of these proposals, consummation of the proposed transactions would have no adverse effects on competition or the concentration of banking resources in any relevant area.

The financial and managerial resources and future prospects of Applicant, Fleet Boston, and Fleet Connecticut are consistent with approval of the applications. As *de novo* institutions, the two proposed banks will provide additional full service banking facilities, and thus considerations relating to convenience and needs of the community to be served lend weight toward approval.

Section 3(d) of the Act prohibits the Board from approving any application by a bank holding company to acquire any bank located outside of the state in which the operations of the bank holding company's banking subsidiaries are principally conducted, unless such acquisition is "specifically authorized by the statute laws of the State in which such bank is located, by language to that effect and not merely by implication." (12 U.S.C. § 1842(d)). Based upon its review of the Massachusetts and Connecticut interstate banking statutes,<sup>4</sup> the Board concludes that Massachusetts and Connecticut have by statute expressly authorized, within the meaning of section 3(d) of the Act, a Rhode Island bank holding company, such as Applicant, to acquire a bank or bank holding company in the authorizing state.<sup>5</sup>

These applications raise a question under the United States Constitution concerning the constitutionality of provisions of the Massachusetts and Connecticut interstate banking statutes that bar bank holding companies located outside of New England from acquiring banks in Massachusetts or Connecticut.<sup>6</sup> The Board has addressed the constitutionality of the Connecticut and Massachusetts statutes in its Orders concerning three previous interstate acquisitions under these stat-

2 The Boston banking market includes all of Suffolk and Essex Counties, most of Middlesex, Norfolk, and Plymouth Counties, and part of Worcester and Bristol Counties, Massachusetts. It also includes 13 towns in southern New Hampshire.

3 The Hartford banking market is defined as Hartford County, Connecticut.

4 Mass. Ann. Laws Ch. 167A, § 2; 1983 Conn. Acts 411, § 2.

5 See *Hartford National Corporation*, 70 FEDERAL RESERVE BULLETIN 353, 354 (1984) (Massachusetts statute); *Bank of New England Corporation*, 70 FEDERAL RESERVE BULLETIN 374, 375 (1984) (Connecticut statute), and *Bank of Boston Corporation* (Colonial Bancorp, Inc.), 70 FEDERAL RESERVE BULLETIN 524, 525 (1984).

6 New England bank holding companies include those located in Connecticut, Maine, Massachusetts, New Hampshire, Rhode Island, and Vermont.

1. Banking data are as of March 31, 1984.

utes.<sup>7</sup> In its *Bank of New England Corporation Order*, the Board concluded that, while the issue was not free from doubt, there was no clear and unequivocal basis for a determination that the Connecticut statute is inconsistent with the Constitution.<sup>8</sup>

Subsequent to the Board's approval of the three prior applications under the Connecticut and Massachusetts interstate banking laws, protestants in each case sought judicial review of the Board's Orders on the sole ground that the Connecticut and Massachusetts interstate banking laws are unconstitutional. Following review of the issues, the United States Court of Appeals for the Second Circuit issued an opinion rejecting the petitioners' constitutional challenges to the New England statutes and affirming the Board's Orders.<sup>9</sup> The constitutional issues involved in Fleet's current applications are the same as those involved in the Second Circuit decision.

Based on the foregoing and other facts of record, the Board has determined that the applications should be and hereby are approved. The transactions shall not be consummated before the thirtieth day after the effective date of the Order, or later than three months after the effective date of this Order, and the banks to be acquired shall be opened for business not later than six months after the effective date of this Order, unless such latter periods are extended for good cause by the Board, or by the Federal Reserve Bank of Boston pursuant to delegated authority.

By order of the Board of Governors, effective October 4, 1984.

Voting for this action: Chairman Volcker and Governors Wallich, Partee, Rice, and Gramley. Abstaining from this action: Governor Martin. Absent and not voting: Governor Seger.

JAMES MCAFEE

[SEAL]

*Associate Secretary of the Board*

7. *Hartford National Corporation*, *supra*; *Bank of New England Corporation*, *supra*; and *Bank of Boston Corporation* (Colonial Bancorp, Inc.), *supra*.

8. *Bank of New England Corporation*, 70 FEDERAL RESERVE BULLETIN 376 (1984). It is the Board's policy that it will not hold a state law unconstitutional in the absence of clear and unequivocal evidence of the inconsistency of the state law with the United States Constitution. See *NCNB Corp.*, 68 FEDERAL RESERVE BULLETIN 54, 56 (1982). The Board repeated these constitutional findings with respect to the Massachusetts statute in *Hartford National Corporation*, 70 FEDERAL RESERVE BULLETIN 354 (1984), and with respect to the closely parallel Rhode Island statute in *Bank of Boston Corporation* (RIHT Financial Corporation), 70 FEDERAL RESERVE BULLETIN 737 (1984).

9. *Northeast Bancorp, Inc. v. Board of Governors of the Federal Reserve System*, Nos. 84-4047, 84-4051, 84-4053, and 84-4081 (2d Cir. Aug. 1, 1984), *petition for cert. filed*, 52 U.S.L.W. 3189 (U.S. Sept. 6, 1984) (No. 84-363).

### *Orders Issued Under Section 4 of Bank Holding Company Act*

Amsterdam-Rotterdam Bank, N.V.  
Amsterdam, The Netherlands

#### *Order Approving Application to Engage in Investment Advisory Activities*

Amsterdam-Rotterdam Bank, N.V., Amsterdam, The Netherlands, a foreign bank subject to certain provisions of the Bank Holding Company Act of 1956 ("Act"), has applied for the Board's approval, pursuant to section 4(c)(8) of the Act (12 U.S.C. § 1843(c)(8)) and section 225.21(a) of the Board's Regulation Y (12 C.F.R. § 225.21(a)), to acquire through its merchant bank subsidiary, Pierson Holding & Pierson, N.V. ("Pierson"), 50 percent of the voting shares of DP Asset Management, Inc., Wilmington, Delaware ("Company"), a *de novo* joint venture.<sup>1</sup> The remaining 50 percent of Company would be held by Delfi American Corporation, Wilmington, Delaware ("DAC").

Company proposes to engage in investment advisory and discretionary portfolio management activities for high net worth individuals, pension funds, trusts and other institutional clients. Company would serve primarily non-U.S. clients and would advise them with regard to investments in the U.S. securities markets. These activities have been determined by the Board to be closely related to banking and permissible for bank holding companies. (12 C.F.R. § 225.25(b)(4)).

Notice of the application, affording interested persons an opportunity to submit comments, has been duly published (49 *Federal Register* 21115 (1984)). The time for filing comments has expired, and the Board has considered the application and all comments received in light of the public interest factors set forth in section 4(c)(8) of the Act.

Applicant is the 43rd largest banking organization worldwide and the second largest in The Netherlands, controlling total consolidated assets of approximately U.S. \$40.0 billion.<sup>2</sup> In the United States, Applicant maintains a Federal branch in New York City and a representative office in San Francisco. Applicant engages in a wide range of retail and wholesale banking activities, as well as securities underwriting and brokerage activities outside the United States. Pierson, Applicant's wholly owned subsidiary, is the eighth largest bank in The Netherlands with total assets of

1. Applicant, a foreign bank operating a branch in New York, is subject to certain provisions of the Act by operation of section 8(a) of the International Banking Act of 1978 (12 U.S.C. § 3106 (1978)).

2. All banking data are as of December 31, 1983.

approximately U.S. \$2.1 billion. Pierson engages in merchant banking and securities activities. In the United States, Pierson maintains representative offices in New York City and San Francisco. DAC is a relatively small, privately-owned holding company for various subsidiaries principally engaged in the sponsorship, distribution and management of a group of nine mutual funds with net assets of approximately \$231.0 million.<sup>3</sup> DAC does not engage in securities underwriting.

Pierson and DAC would each own 50 percent of Company's shares and each would elect four directors to Company's eight-member board. DAC's directors would be eligible to sit on Company's board; however, Applicant has committed that none of DAC's other employees, including its officers, would serve concurrently as officers or employees of Company. Company would purchase a variety of services from DAC on a fee basis, including securities research and analysis, trading services, data processing, trust, and administrative services, and would lease office space from DAC.

In acting on Applicant's proposal to engage in investment advisory activities through the proposed joint venture, the Board must consider the standards enumerated in section 4(c)(8) of the Bank Holding Company Act. As noted above, the proposed activities are "closely related" to banking within the meaning of the Act. However, the Board must determine whether the performance of the proposed activities by Company can reasonably be expected to produce benefits to the public that outweigh possible adverse effects. 12 U.S.C. § 1843(c)(8).

Prior decisions of the Board in joint venture cases indicate a concern on the part of the Board that joint ventures not lead to a matrix of relationships between co-venturers that could break down the legally mandated separation of banking and commerce.<sup>4</sup> Joint ventures by banking organizations and commercial firms may also create the possibility of conflicts of interest and concentration of resources that the Act was designed to prevent, and impair or give the appearance of impairing the ability of the banking organization to function effectively as an independent and impartial provider of credit. Further, joint ventures must be carefully analyzed for any possible adverse effects on competition and on the financial condition of the banking organization involved in the proposal. The Board believes that these concerns are exacerbated where, as here, the joint venture involves a relationship between a banking organization and a securities firm that is more than a passive investor,

and thus the concomitant potential for the mingling of permissible and impermissible securities activities.<sup>5</sup>

In this instance, however, the Board notes that Company would not be engaged in impermissible activities, and that Applicant has offered various commitments to address the potential adverse effects described above, including the following:<sup>6</sup>

1. Applicant has committed to obtain the Board's prior approval to retain its interest in Company should DAC expand its business beyond its current mutual fund activities, and to divest its investment in Company should the Board so require;
2. Company's name would be distinct from DAC's and would not link Company with DAC;
3. None of Company's officers or employees would serve at the same time as officers or employees of DAC or any of its affiliates;
4. Although the offices of DAC and Company would be located in the same building, they would have separate entrances;
5. Applicant and its subsidiaries will not distribute prospectuses or sales literature for DAC's mutual funds or make any such literature available to the public at any of their offices;
6. Officers and employees of Applicant's bank subsidiaries will be instructed not to express any opinion concerning the advisability of purchasing the securities of any DAC mutual fund;
7. The names of Applicant's bank customers will not be furnished to DAC's mutual funds;
8. None of DAC's mutual funds will have offices in any building which is likely to be identified in the public's mind with Applicant or its subsidiaries;
9. Applicant and its subsidiaries will not act as registrar, transfer agent or custodian for any of DAC's mutual funds;
10. No officer, director or employee of DAC or its affiliates will serve as an officer, director or employee of Applicant or its affiliates, excluding Company;
11. Applicant and its subsidiaries will not engage, directly or indirectly, in the sale or distribution of

5. The proposed joint venture would not result in a violation of the Glass-Steagall Act, since it involves neither an affiliation nor management interlocks between Applicant and DAC. 12 U.S.C. §§ 78, 221a, 377. The joint ownership of a third entity, such as Company, is not prohibited under that Act.

The Board has approved only one previous joint venture application between a banking organization and a securities firm. *The Maybaco Company*, *supra*, note 4. In that case, however, the role of the securities firm was essentially that of a passive investor with little role in the management or operations of the joint venture.

6. Some of these commitments are required under the Board's Published Interpretation regarding investment advisory activities when advice is provided to an investment company by a bank holding company. 12 C.F.R. § 225.125. This application would not result in Applicant providing advice to an investment company, however, and Applicant has offered these commitments as a means of addressing the possible adverse effects of a joint venture between a bank holding company and a securities firm.

3. Data on DAC are as of September 30, 1983.

4. See, e.g., *The Maybaco Company and Equitable Bancorporation*, 69 FEDERAL RESERVE BULLETIN 375 (1983), and *Deutsche Bank AG*, 67 FEDERAL RESERVE BULLETIN 449 (1981).



any securities of DAC's mutual funds nor purchase for their own account any securities of any DAC mutual fund;

12. Applicant and its subsidiaries will not purchase in their sole discretion any securities of DAC's mutual funds in a fiduciary capacity, will not extend credit to any such mutual fund, or accept securities of any such mutual fund as collateral for a loan which is for the purpose of purchasing securities of any such fund;

13. Pierson will not make any investment in DAC or nominate any of its directors; and,

14. Applicant and its banking subsidiaries will not take into account the fact that a potential borrower competes with Company in determining whether to extend credit to that borrower.

With regard to competitive issues, DAC and Applicant do not currently compete with each other in the investment advisory area either in the United States or abroad. Accordingly, consummation of the proposed transaction would not eliminate any existing competition between Applicant and DAC.

With respect to potential competition, each joint venturer in this proposal offers a unique service or skill that the other needs and without which neither partner would be able to engage in Company's activities. Specifically, Pierson has indicated that its existing foreign customers desire access to the U.S. equity markets for small to mid-sized U.S. companies, an area in which Pierson lacks sufficient expertise and experience. DAC, on the other hand, would gain access to a foreign customer base through the joint venture that it might not otherwise be able to obtain. The Board believes that the unique needs of the two joint venturers in this case make it unlikely that either joint venturer would be able to enter the market independently. Accordingly, the Board concludes that consummation of the proposed transaction would not have a significant impact on potential competition in any relevant market. The relatively small absolute size and market share of DAC, when coupled with the small domestic presence of Applicant, also demonstrates that the proposal would be unlikely to result in an undue concentration of resources.<sup>7</sup>

There is no evidence in the record to indicate that consummation of the proposal would result in other adverse effects on the public interest. Moreover, the Board is satisfied that approval of this application does not inherently present the opportunity for unsound banking practices. In reaching this conclusion, the

Board has placed particular emphasis on the fact that DAC is not engaged in underwriting and dealing in securities.

The Board finds that consummation of this proposal may be expected to result in public benefits. In particular, Company is likely to increase the market for equities of small and medium-sized U.S. companies, as additional foreign investors begin to invest capital in the United States on the basis of advice obtained from Company. Further, the resources provided to Company by each joint venture partner should permit Company to be a viable and effective provider of investment advice regarding U.S. securities.

Based on the foregoing facts of record, the Board has determined that the balance of the public interest factors it is required to consider under section 4(c)(8) of the Act is favorable. Accordingly, the application should be and hereby is approved. In approving this application, the Board has relied on all the commitments offered by Applicant, including the commitment to secure the Board's prior approval to retain its interest in Company if DAC expands its operations beyond its current mutual fund activities. This determination is subject to all the conditions set forth in the Board's Regulation Y, including those in sections 225.4(d) and 225.23(b), and to the Board's authority to require such modification or termination of the activities of a bank holding company or any of its subsidiaries as the Board finds necessary to assure compliance with the provisions and purposes of the Act and the Board's regulations and orders issued thereunder, or to prevent evasion thereof.

The proposed activity shall be commenced not later than three months after the effective date of this Order, unless such period is extended for good cause by the Board or by the Federal Reserve Bank of New York, acting pursuant to delegated authority.

By order of the Board of Governors, effective October 1, 1984.

Voting for this action: Chairman Volcker and Governors Martin, Wallich, Partee, and Seger. Voting against this action: Governor Rice. Absent and not voting: Governor Gramley.

JAMES MCAFEE  
[SEAL] Associate Secretary of the Board

#### *Dissenting Statement of Governor Rice*

I would deny this application because I believe that approval of this proposal would serve to erode the Glass-Steagall Act's fundamental objective of drawing a dividing line between the banking and securities industries. Further, approval of this application would establish an adverse precedent that would encourage other banking organizations to join together with secu-

7. The Board notes, in addition, that Company's proposed investment advisory activities are relatively limited in scope. Accordingly, this proposal does not pose the same potential for conflicts of interest or other adverse effects that arose in *Deutsche Bank*, *supra* note 4, where the joint venturers had applied to engage in a broad range of activities.

rities firms in similar joint venture relationships involving additional securities- and non securities-related activities.

Moreover, in my opinion, the only public benefit to be gained by approval of this proposal would be a small inflow of foreign dollars into the U.S. securities markets. I believe that this one public benefit is not sufficient to outweigh the potential adverse effects that could result from approval of a joint venture that contemplates such a significant level of involvement between a banking organization and a securities firm.

Accordingly, I dissent from the Board's decision to approve this application.

October 1, 1984

*Orders Issued Under Section 5 of Bank Service Corporation Act*

Spencer County Bank  
Santa Claus, Indiana

Christmas Lake Agency, Inc.  
Dale, Indiana

*Order Approving Investment in a Bank Service Corporation*

Spencer County Bank, Santa Claus, Indiana ("Bank"), an insured state nonmember bank, has applied for the Board's approval under section 5(b) of the Bank Service Corporation Act, as amended ("BSCA") (12 U.S.C. § 1861 *et seq.*), to acquire all of the voting shares of Christmas Lake Agency, Inc., Dale, Indiana ("Agency"), a general insurance agency which proposes to become a bank service corporation subject to the BSCA.<sup>1</sup>

Bank intends to acquire all of the outstanding shares of Agency from its owners (two of whom are principals of Bank and collectively control 50 percent of Agency's voting shares) and move the operations of Agency into the facilities of Bank, which is located in a community with population not exceeding 5,000. In connection with this proposal, Agency has applied under section 5(b) of the BSCA to engage as a bank service corporation in general insurance agency activities in an area approximated by Spencer County, Indiana, the service area in which both Bank and Agency currently operate.

Section 4(f) of the BSCA, 12 U.S.C. § 1864(f), provides that a bank service corporation may perform

1. Agency currently engages principally in the sale of casualty and credit life insurance, but expects to expand its activities in the future to encompass a full line of general insurance agency business, including fire, casualty, life and health insurance.

at any geographic location any service, other than deposit taking, that the Board has determined, by regulation, to be permissible for a bank holding company under section 4(c)(8) of the Bank Holding Company Act.<sup>2</sup> Agency proposes to engage in general insurance agency activities to the extent those activities are generally permissible for bank holding companies under the Board's Regulation Y, 12 C.F.R. § 225.25(b)(8)(ii).

Section 5(b) of the BSCA, 12 U.S.C. § 1865(b), requires prior Board approval of any investment by an insured bank (as defined)<sup>3</sup> in the capital stock of a bank service corporation that performs any service under authority of section 4(f) of the BSCA. Section 5(b) of the BSCA also requires a Company that becomes a bank service corporation under the BSCA to obtain the Board's approval before providing a service under authority of section 4(f) of the Act.

Section 5(c) of the BSCA, 12 U.S.C. § 1865(c), authorizes the Board, in acting upon applications to invest in bank service corporations, to consider the financial and managerial resources of the institutions involved, their prospects, and possible adverse effects, such as undue concentration of resources, unfair or decreased competition, conflicts of interests, or unsafe or unsound banking practices. The Board finds that considerations relating to these factors are consistent with approval and that there is no evidence of adverse effects.

Accordingly, on the basis of the record, the application is approved for the reasons summarized above. This determination is subject to the Board's authority to require such modification or termination of the activities of a bank service corporation as the Board finds necessary to assure compliance with the BSCA or to prevent evasions thereof. The transactions shall be consummated within three months after the date of this Order, unless such period is extended for good cause by the Board or the Federal Reserve Bank of St. Louis.

By order of the Board of Governors, effective October 2, 1984.

Voting for this action: Chairman Volcker and Governors Martin, Partee, Rice, Gramley, and Seger. Abstaining from this action: Governor Wallich.

JAMES MCAFEE  
[SEAL] *Associate Secretary of the Board*

2. Under section 4(c)(8) of the Bank Holding Company Act, a bank holding company may engage in activities determined by the Board to be closely related to banking and a proper incident thereto.

3. Under section 1(b)(5) of the BSCA (12 U.S.C. § 1861(b)(5)), the term "insured bank" has the meaning provided in section 3(h) of the Federal Deposit Insurance Act (12 U.S.C. § 1813(h)) and encompasses banks insured by the Federal Deposit Insurance Corporation ("FDIC"). Spencer County Bank is an FDIC-insured, state nonmember bank.

## ORDERS APPROVED UNDER BANK HOLDING COMPANY ACT

*By Federal Reserve Banks*

Recent applications have been approved by the Federal Reserve Banks as listed below. Copies of the orders are available upon request to the Reserve Banks.

## Section 3

Applicant	Bank(s)	Reserve Bank	Effective date
Ambanc Financial Services, Inc., Beaver Dam, Wisconsin	The American National Bank of Beaver Dam, Beaver Dam, Wisconsin	Chicago	October 2, 1984
American State Bancorp, Sheridan, Indiana	American State Bank of Sheri- dan, Sheridan, Indiana	Chicago	September 28, 1984
B. B. Financial Corporation, Boca Raton, Florida	Boca Bank, Boca Raton, Florida	Atlanta	October 3, 1984
Broadway Bancshares Inc., San Antonio, Texas	Broadway National Bank-West- Plex, Bexar County, Texas	Dallas	September 19, 1984
Camden National Corporation, Camden, Maine	Camden National Bank, Camden, Maine	Boston	September 19, 1984
Cape Coral Financial Corpora- tion, Cape Coral, Florida	Community National Bank, Cape Coral, Florida	Atlanta	October 2, 1984
Citizens Bancshares, Inc., Salineville, Ohio	The Union Commercial Savings Bank, Palestine, Ohio	Cleveland	September 21, 1984
CNB Financial Corporation, San Saba, Texas	The City National Bank of San Saba, San Saba, Texas	Dallas	September 28, 1984
Commonwealth Trust Bancorp, Inc. Covington, Kentucky	Peoples Deposit Bank, Burlington, Kentucky	Cleveland	September 21, 1984
Community Banks of Florida, Inc., Mims, Florida	Community National Bank, Mims, Florida	Atlanta	September 19, 1984
Cylinder Bancorporation, Cylinder, Iowa	Cylinder State Bank, Cylinder, Iowa	Chicago	October 4, 1984
DeMotte Bancorp, DeMotte, Indiana	DeMotte State Bank, DeMotte, Indiana	Chicago	October 2, 1984
Drummond Bancshares, Inc., Drummond, Wisconsin	State Bank of Drummond, Drummond, Wisconsin	Minneapolis	October 2, 1984
Eagle Financial Corp., Cedar Falls, Iowa	Aredale State Bank, Aredale, Iowa	Chicago	October 2, 1984
FBL Bancshares, Inc., Liberty, Illinois	The Farmers Bank of Liberty, Liberty, Illinois	St. Louis	October 1, 1984
Farmers National Bancshares, Inc., Opelika, Alabama	The Farmers National Bank of Opelika, Opelika, Alabama	Atlanta	September 22, 1984
Financial BancCorp, Inc., Trinidad, Colorado	Trinidad National Bank, Trinidad, Colorado	Kansas City	September 24, 1984

## Section 3—Continued

Applicant	Bank(s)	Reserve Bank	Effective date
First Delta Financial Corporation, Dermott, Arkansas	First State Bank of Dermott, Dermott, Arkansas	St. Louis	September 27, 1984
First Kentucky National Corporation, Louisville, Kentucky	The Third National Bank of Ashland, Ashland, Kentucky	St. Louis	October 1, 1984
Georgia Community Bancorp, Inc., Reynolds, Georgia	Bank of Terrell, Dawson, Georgia Commercial State Bank, Donalsonville, Georgia The Citizens State Bank of Reynolds, Reynolds, Georgia	Atlanta	September 28, 1984
Grant County Bancorp, Inc., Williamstown, Kentucky	Grant County Deposit Bank, Williamstown, Kentucky	Cleveland	September 21, 1984
Holdco of Pinellas County, Inc., St. Petersburg, Florida	First Bank of Pinellas County, Treasure Island, Florida	Atlanta	September 21, 1984
Jackson County Bancshares, Inc., Scottsboro, Alabama	The Jackson County Bank, Scottsboro, Alabama	Atlanta	October 2, 1984
Liberty Shares, Inc., Hinesville, Georgia	The Hinesville Bank, Hinesville, Georgia	Atlanta	September 21, 1984
Lismore Financial Services, Inc., Lismore, Minnesota	State Bank of Lismore, Lismore, Minnesota	Minneapolis	September 19, 1984
Menomonie Financial Services, Inc., Manomonic, Wisconsin	First Bank and Trust, Menomonie, Wisconsin	Minneapolis	September 28, 1984
NCNB Corporation, Charlotte, North Carolina	NCNB National Bank, Fairfax County, Virginia	Richmond	October 2, 1984
Northeast Bancorp, Inc., New Haven, Connecticut	Citizens National Bank of South- ington, Plantsville, Connecticut	New York	September 28, 1984
Northern Neck Bankshares Cor- poration, Warsaw, Virginia	Northern Neck State Bank, Warsaw, Virginia	Richmond	October 2, 1984
Panhandle Aviation, Inc., Clarinda, Iowa	Oakland State Bank, Oakland, Iowa	Chicago	September 7, 1984
Prattville Financial Services Corporation, Prattville, Alabama	Bank of Prattville, Prattville, Alabama	Atlanta	September 21, 1984
RBDC Corporation, Chicago, Illinois	Republic Bancorp, Co., Chicago, Illinois	Chicago	October 1, 1984
St. James Bancorp, Inc., St. James, Minnesota	Jackson State Bank, Jackson, Minnesota	Minneapolis	October 2, 1984
Seneca Bancshares, Inc., Fairlea, West Virginia	The Ronceverte National Bank, Fairlea, West Virginia	Richmond	October 3, 1984
Siloam Springs Bancshares, Inc., Bentonville, Arkansas	First National Bank, Siloam Springs, Arkansas	St. Louis	September 27, 1984

## Section 3—Continued

Applicant	Bank(s)	Reserve Bank	Effective date
The Sumitomo Bank, Ltd., Osaka, Japan	CPB, Inc., Honolulu, Hawaii	San Francisco	September 27, 1984
Tate Financial Corporation, Coldwater, Mississippi	Citizens Bank, Coldwater, Mississippi	St. Louis	October 2, 1984
Trust Company of Georgia, Atlanta, Georgia	First Thomson Bancorp, Inc., Thomson, Georgia	Atlanta	September 20, 1984
Tyler Bancshares, Inc., Tyler, Texas	Tyler National Bank, Tyler, Texas	Dallas	October 4, 1984
WNB Resources, Inc., Kerrville, Texas	First National Bank of Kerrville, Kerrville, Texas	Dallas	October 2, 1984

## Section 4

Applicant	Nonbanking company	Reserve Bank	Effective date
Maryland National Corporation, Baltimore, Maryland	Summit Industrial Bank, Lakewood, Colorado	Richmond	September 21, 1984
Security Pacific Corporation, Los Angeles, California	Clifford Drake & Company, Inc., New York, New York	San Francisco	September 26, 1984
Society Corporation, Cleveland, Ohio	BancSystems Association, Westlake, Ohio	Cleveland	September 27, 1984

*PENDING CASES INVOLVING THE BOARD OF GOVERNORS*

*This list of pending cases does not include suits against the Federal Reserve Banks in which the Board of Governors is not named a party.*

- Seattle Bancorporation v. Board of Governors*, No. 84-7535 (9th Cir., filed Aug. 15, 1984).
- Old Stone Corp. v. Board of Governors*, No. 84-1498 (1st Cir., filed June 20, 1984).
- Citicorp v. Board of Governors*, No. 84-4081 (2d Cir., filed May 22, 1984).
- Lamb v. Pioneer First Federal Savings and Loan Association*, No. C84-702 (D. Wash., filed May 8, 1984).
- Girard Bank v. Board of Governors*, No. 84-3262 (3rd Cir., filed May 2, 1984).
- Melcher v. Federal Open Market Committee*, No. 84-1335 (D.D.C., filed, Apr. 30, 1984).
- Florida Bankers Association v. Board of Governors*, No. 84-3269 and No. 84-3270 (11th Cir., filed Apr. 20, 1984).
- Northeast Bancorp, Inc. v. Board of Governors*, No. 84-4047, No. 84-4051, No. 84-4053 (2d Cir., filed Mar. 27, 1984).
- Huston v. Board of Governors*, No. 84-1361 (8th Cir., filed Mar. 20, 1984); and No. 84-1084 (8th Cir. filed Jan. 17, 1984).
- De Young v. Owens*, No. SC 9782-20-6 (Iowa Dist. Ct., filed Mar. 8, 1984).
- First Tennessee National Corp. v. Board of Governors*, No. 84-3201 (6th Cir., filed Mar. 6, 1984).
- State of Ohio v. Board of Governors*, No. 84-1270 (10th Cir., filed Jan. 30, 1984).
- Ohio Deposit Guarantee Fund v. Board of Governors*, No. 84-1257 (10th Cir., filed Jan. 28, 1984).
- Colorado Industrial Bankers Association v. Board of Governors*, No. 84-1122 (10th Cir., filed Jan. 27, 1984).
- Financial Institutions Assurance Corp. v. Board of Governors*, No. 84-1101 (4th Cir., filed Jan. 27, 1984).
- First Bancorporation v. Board of Governors*, No. 84-1011 (10th Cir., filed Jan. 5, 1984).

*Dimension Financial Corporation v. Board of Governors*, No. 83-2696 (10th Cir., filed Dec. 30, 1983).

*Oklahoma Bankers Association v. Federal Reserve Board*, No. 83-2591 (10th Cir., filed Dec. 13, 1983).

*The Committee for Monetary Reform v. Board of Governors*, No. 84-5067 (D.C. Cir., filed June 16, 1983).

*Association of Data Processing Service Organizations v. Board of Governors*, No. 82-1910 (D.C. Cir., filed Aug. 16, 1982); and No. 82-2108 (D.C. Cir., filed Aug. 16, 1982).

*First Bancorporation v. Board of Governors*, No. 82-1401 (10th Cir., filed Apr. 9, 1982).

*Wolfson v. Board of Governors*, No. 83-3570 (11th Cir., filed Sept. 28, 1981).

*First Bank & Trust Company v. Board of Governors*, No. 81-38 (E.D. Ky., filed Feb. 24, 1981).

*9 to 5 Organization for Women Office Workers v. Board of Governors*, No. 83-1171 (1st Cir., filed Dec. 30, 1980).

*Securities Industry Association v. Board of Governors*, No. 80-2614 (D.C. Cir., filed Oct. 24, 1980), and No. 80-2730 (D.C. Cir., filed Oct. 24, 1980).

*A. G. Becker, Inc. v. Board of Governors*, No. 80-2614 (D.C. Cir., filed Oct. 14, 1980), and No. 80-2730 (D.C. Cir., filed Oct. 14, 1980).

*A. G. Becker, Inc. v. Board of Governors*, No. 81-1493 (D.C. Cir., filed Aug. 25, 1980).

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# Financial and Business Statistics

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*NOTE. The statistical tables that usually appear in this section could not be published in this BULLETIN because new data had not become available since the publication of those tables at the end of October in the October BULLETIN. The*

*regular series of tables for domestic financial, domestic nonfinancial, and international statistics will be published in the BULLETIN for December 1984, which will be issued in the first week of December.*

# Guide to Tabular Presentation, Statistical Releases, and Special Tables

## GUIDE TO TABULAR PRESENTATION

### Symbols and Abbreviations

c	Corrected	0	Calculated to be zero
e	Estimated	n.a.	Not available
p	Preliminary	n.e.c.	Not elsewhere classified
r	Revised (Notation appears on column heading when about half of the figures in that column are changed.)	IPCs	Individuals, partnerships, and corporations
*	Amounts insignificant in terms of the last decimal place shown in the table (for example, less than 500,000 when the smallest unit given is millions)	REITs	Real estate investment trusts
		RPs	Repurchase agreements
		SMSAs	Standard metropolitan statistical areas
		. . . .	Cell not applicable

### General Information

Minus signs are used to indicate (1) a decrease, (2) a negative figure, or (3) an outflow.

"U.S. government securities" may include guaranteed issues of U.S. government agencies (the flow of funds figures also include not fully guaranteed issues) as well as direct

obligations of the Treasury. "State and local government" also includes municipalities, special districts, and other political subdivisions.

In some of the tables details do not add to totals because of rounding.

## STATISTICAL RELEASES

### List Published Semiannually, with Latest Bulletin Reference

Anticipated schedule of release dates for periodic releases. . . . .	<i>Issue</i>	<i>Page</i>
	June 1984	A83

## SPECIAL TABLES

### Published Irregularly, with Latest Bulletin Reference

Assets and liabilities of commercial banks, March 31, 1983.....	August 1983	A70
Assets and liabilities of commercial banks, June 30, 1983.....	December 1983	A68
Assets and liabilities of commercial banks, September 30, 1983.....	March 1984	A68
Assets and liabilities of commercial banks, December 31, 1983.....	June 1984	A66
Assets and liabilities of U.S. branches and agencies of foreign banks, June 30, 1983.....	December 1983	A74
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# A4 Special Tables □ November 1984

## 4.30 ASSETS AND LIABILITIES of U.S. Branches and Agencies of Foreign Banks, March 31, 1984<sup>1</sup>

Millions of dollars

Item	All states <sup>2</sup>			New York		California, total <sup>4</sup>	Illinois, branches	Other states <sup>2</sup>	
	Total	Branches <sup>3</sup>	Agencies	Branches <sup>3</sup>	Agencies			Branches	Agencies
<b>1 Total assets<sup>5</sup></b>	<b>238,100</b>	<b>186,559</b>	<b>51,541</b>	<b>166,580</b>	<b>6,075</b>	<b>41,970</b>	<b>10,833</b>	<b>6,364</b>	<b>6,228</b>
2 Cash and due from depository institutions	46,132	42,091	4,042	39,383	478	3,805	1,890	286	289
3 Currency and coin (U.S. and foreign)	22	19	3	15	1	2	2	1	1
4 Balances with Federal Reserve Banks	812	748	64	649	14	45	23	65	15
5 Balances with other central banks	20	20	0	19	0	0	1	0	0
6 Demand balances with commercial banks in United States	1,284	1,103	181	1,029	64	84	48	20	40
7 All other balances with depository institutions in United States and with banks in foreign countries	43,786	40,017	3,769	37,498	398	3,652	1,810	198	230
8 Time and savings balances with commercial banks in United States	22,571	20,465	2,107	19,058	313	1,829	1,064	175	132
9 Balances with other depository institutions in United States	239	226	13	226	0	13	0	0	0
10 Balances with banks in foreign countries	20,976	19,326	1,650	18,214	86	1,811	765	22	97
11 Foreign branches of U.S. banks	1,185	1,109	75	1,046	20	46	63	0	9
12 Other banks in foreign countries	29,791	18,217	1,574	17,168	66	1,765	683	22	88
13 Cash items in process of collection	209	184	25	173	1	22	7	3	4
<b>14 Total securities, loans, and lease financing receivables</b>	<b>142,077</b>	<b>108,844</b>	<b>33,233</b>	<b>95,371</b>	<b>4,302</b>	<b>25,942</b>	<b>8,135</b>	<b>3,463</b>	<b>4,864</b>
15 Total securities, book value	9,208	8,479	729	8,020	72	634	338	27	117
16 U.S. Treasury	5,077	4,886	191	4,632	58	56	210	20	100
17 Obligations of other U.S. government agencies and corporations	539	519	19	516	0	16	0	2	5
18 Obligations of states and political subdivisions in United States	67	57	10	42	0	1	14	1	9
19 Other bonds, notes, debentures, and corporate stock	3,526	3,017	509	2,830	14	562	114	3	3
20 Federal funds sold and securities purchased under agreements to resell	7,905	6,847	1,058	6,472	544	465	322	39	63
<i>By holder</i>									
21 Commercial banks in United States	6,849	6,055	794	5,690	305	440	312	39	63
22 Others	1,056	792	265	782	240	25	10	0	0
<i>By type</i>									
23 One-day maturity or continuing contract	7,664	6,605	1,058	6,230	544	465	322	39	63
24 Securities purchased under agreements to resell	343	213	130	212	113	10	0	0	9
25 Other	7,320	6,392	928	6,019	431	456	322	39	54
26 Other securities purchased under agreements to resell	241	241	0	241	0	0	0	0	0
27 Total loans, gross	133,143	100,588	32,555	87,564	4,236	25,353	7,804	3,439	4,747
28 Less: Unearned income on loans	274	223	51	213	6	45	7	3	0
29 <b>EQUALS Loans, net</b>	<b>132,869</b>	<b>100,364</b>	<b>32,504</b>	<b>87,351</b>	<b>4,231</b>	<b>25,307</b>	<b>7,797</b>	<b>3,436</b>	<b>4,746</b>
<i>Total loans, gross, by category</i>									
30 Real estate loans	5,142	2,150	2,992	1,509	12	2,126	207	285	1,003
31 Loans to financial institutions	51,675	40,353	11,322	36,632	872	10,061	2,836	441	834
32 Commercial banks in United States	28,417	22,062	6,355	19,984	245	6,346	1,430	302	110
33 U.S. branches and agencies of other foreign banks	24,574	18,491	6,083	16,789	196	6,144	1,096	284	67
34 Other commercial banks	3,843	3,571	272	3,195	49	203	334	19	43
35 Banks in foreign countries	21,224	16,528	4,696	15,210	573	3,515	1,089	137	701
36 Foreign branches of U.S. banks	674	544	130	511	0	128	15	10	9
37 Other	20,551	15,985	4,566	14,700	573	3,387	1,074	127	691
38 Other financial institutions	2,033	1,762	271	1,437	54	200	317	2	23
39 Loans for purchasing or carrying securities	1,281	1,250	31	1,169	0	111	0	1	0
40 Commercial and industrial loans	59,226	45,074	14,152	37,388	1,852	11,078	4,147	2,530	2,231
41 U.S. addressees (domicile)	35,119	25,933	9,185	19,713	255	8,073	3,568	1,796	1,714
42 Non-U.S. addressees (domicile)	24,107	19,140	4,967	17,675	1,597	3,005	579	734	516
43 Loans to individuals for household, family, and other personal expenditures	212	185	27	139	2	25	9	28	9
44 All other loans	15,607	11,577	4,031	10,728	1,499	1,951	605	154	670
45 Loans to foreign governments and official institutions	14,814	10,889	3,925	10,145	1,481	1,883	559	106	639
46 Other	794	688	106	583	17	68	46	48	31
47 Lease financing receivables	0	0	0	0	0	0	0	0	0
48 All other assets	41,985	28,778	13,207	25,354	749	11,757	536	2,576	1,012
49 Customers' liability on acceptances outstanding	13,977	10,994	2,983	10,519	134	2,778	296	162	88
50 U.S. addressees (domicile)	8,375	5,972	2,404	5,656	3	2,395	268	34	20
51 Non-U.S. addressees (domicile)	5,602	5,023	579	4,863	132	384	27	127	69
52 Net due from related banking institutions <sup>6</sup>	21,867	12,863	9,004	10,333	435	8,050	0	2,319	730
53 Other	6,142	4,921	1,220	4,503	180	929	240	96	194

## 4.30 Continued

Item	All states <sup>2</sup>			New York		California, total <sup>4</sup>	Illinois, branches	Other states <sup>7</sup>	
	Total	Branches <sup>3</sup>	Agencies	Branches <sup>3</sup>	Agencies			Branches	Agencies
<b>54 Total liabilities<sup>5</sup></b>	<b>238,100</b>	<b>186,559</b>	<b>51,541</b>	<b>166,580</b>	<b>6,075</b>	<b>41,970</b>	<b>10,883</b>	<b>6,364</b>	<b>6,228</b>
55 Total deposits and credit balances	120,622	105,540	15,082	97,243	1,966	12,456	3,159	3,562	2,236
56 Individuals, partnerships, and corporations	37,376	34,525	2,851	29,745	141	1,514	900	3,204	1,872
57 U.S. addressees (domicile)	20,884	20,797	88	16,535	19	409	762	3,132	28
58 Non-U.S. addressees (domicile)	16,492	13,729	2,763	13,210	122	1,105	138	72	1,845
59 U.S. government, states, and political subdivisions in United States	57	57	0	16	0	5	0	35	0
60 All other	83,189	70,958	12,231	67,482	1,825	10,937	2,258	324	464
61 Foreign governments and official institutions	4,351	4,090	261	3,988	81	155	14	25	87
62 Commercial banks in United States	33,543	27,035	6,508	25,429	844	5,933	1,041	136	159
63 U.S. branches and agencies of other foreign banks	22,922	18,072	4,849	17,021	328	4,903	572	70	28
64 Other commercial banks in United States	10,621	8,961	1,658	8,409	517	1,030	468	66	131
65 Banks in foreign countries	44,800	39,403	5,397	37,659	882	4,809	1,188	157	105
66 Foreign branches of U.S. banks	6,721	5,505	1,215	5,211	222	983	266	20	19
67 Other banks in foreign countries	38,079	33,898	4,181	32,448	660	3,826	922	137	86
68 Certified and officers' checks, travelers checks, and letters of credit sold for cash	496	430	66	406	17	40	16	5	12
69 Demand deposits	3,250	3,096	245	2,724	61	101	139	107	119
70 Individuals, partnerships, and corporations	1,706	1,595	111	1,374	0	53	118	75	86
71 U.S. addressees (domicile)	995	995	0	791	0	21	114	69	0
72 Non-U.S. addressees (domicile)	711	600	111	583	0	32	4	5	86
73 U.S. government, states, and political subdivisions in United States	11	11	0	10	0	0	0	0	0
74 All other	1,534	1,400	134	1,341	61	47	21	32	33
75 Foreign governments and official institutions	305	302	3	275	0	2	2	25	1
76 Commercial banks in United States	132	110	22	108	18	1	0	1	4
77 U.S. branches and agencies of other foreign banks	26	18	8	18	8	0	0	0	0
78 Other commercial banks in United States	106	92	14	90	10	1	0	1	4
79 Banks in foreign countries	601	558	43	552	26	5	3	1	15
80 Certified and officers' checks, travelers checks, and letters of credit sold for cash	496	430	66	406	17	40	16	5	12
81 Time deposits	116,155	101,643	14,511	93,814	1,724	12,243	2,946	3,381	2,047
82 Individuals, partnerships, and corporations	34,669	32,184	2,484	27,812	24	1,350	709	3,054	1,719
83 U.S. addressees (domicile)	19,293	19,293	0	15,402	0	321	578	2,992	0
84 Non-U.S. addressees (domicile)	15,375	12,891	2,484	12,410	24	1,030	130	62	1,719
85 U.S. government, states, and political subdivisions in United States	46	46	0	6	0	5	0	35	0
86 All other	81,440	69,413	12,027	65,997	1,700	10,887	2,238	291	328
87 Foreign governments and official institutions	4,012	3,775	237	3,699	62	153	12	0	85
88 Commercial banks in United States	33,365	26,892	6,472	25,289	814	5,941	1,041	135	155
89 U.S. branches and agencies of other foreign banks	22,883	18,041	4,841	16,990	320	4,903	572	70	28
90 Other commercial banks in United States	10,482	8,851	1,631	8,300	495	1,028	468	65	126
91 Banks in foreign countries	44,064	38,746	5,318	37,008	824	4,804	1,185	156	88
92 Savings deposits	702	635	67	449	0	66	73	74	39
93 Individuals, partnerships, and corporations	701	634	67	449	0	66	73	74	39
94 U.S. addressees (domicile)	435	435	0	270	0	26	70	69	0
95 Non-U.S. addressees (domicile)	266	199	67	178	0	40	3	5	39
96 U.S. government, states, and political subdivisions in United States	0	0	0	0	0	0	0	0	0
97 All other	1	1	0	1	0	0	0	0	0
98 Credit balances	516	257	259	255	181	47	0	1	32
99 Individuals, partnerships, and corporations	301	112	189	111	117	44	0	1	28
100 U.S. addressees (domicile)	161	74	88	72	19	32	0	1	28
101 Non-U.S. addressees (domicile)	140	39	101	39	98	2	0	0	1
102 U.S. government, states, and political subdivisions in United States	0	0	0	0	0	0	0	0	0
103 All other	214	144	70	144	64	3	0	0	3
104 Foreign governments and official institutions	34	13	21	13	20	1	0	0	0
105 Commercial banks in United States	46	33	13	33	12	1	0	0	0
106 U.S. branches and agencies of other foreign banks	13	13	0	13	0	0	0	0	0
107 Other commercial banks in United States	33	20	13	20	12	1	0	0	0
108 Banks in foreign countries	134	98	36	98	33	0	0	0	3

For notes see end of table

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4.30 Continued

Item	All states <sup>2</sup>			New York		Calif.- total <sup>4</sup>	Illnois, branches	Other states <sup>2</sup>	
	Total	Branches <sup>3</sup>	Agencies	Branches <sup>3</sup>	Agencies			Branches	Agencies
109 Federal funds purchased and securities sold under agreements to repurchase	21,196	15,479	5,716	14,226	680	5,026	840	279	146
<i>By holder</i>									
110 Commercial banks in United States	17,532	12,271	5,260	11,155	346	4,893	718	279	141
111 Others	3,664	3,208	456	3,071	334	132	121	0	5
<i>By type</i>									
112 One-day maturity or continuing contract	20,245	14,660	5,586	13,468	570	5,006	778	279	146
113 Securities sold under agreements to repurchase	1,865	1,836	30	1,826	12	9	10	0	9
114 Other	18,380	12,824	5,556	11,642	558	4,996	769	279	137
115 Other securities sold under agreements to repurchase	950	820	130	758	110	20	62	0	0
116 Other liabilities for borrowed money	46,851	27,597	19,254	26,026	2,130	16,768	760	498	670
117 Owed to banks	43,412	24,750	18,662	23,230	2,060	16,216	750	486	670
118 U.S. addressees (domicile)	41,207	22,744	18,463	21,285	1,995	16,182	733	445	569
119 Non-U.S. addressees (domicile)	2,205	2,006	199	1,945	65	35	17	41	101
120 Owed to others	3,439	2,847	592	2,796	70	552	10	12	0
121 U.S. addressees (domicile)	3,063	2,621	442	2,574	6	462	10	12	0
122 Non-U.S. addressees (domicile)	376	227	150	222	64	90	0	0	0
123 All other liabilities	49,430	37,942	11,488	29,085	1,299	7,719	6,125	2,026	3,176
124 Acceptances executed and outstanding	15,679	12,354	3,326	11,863	178	3,075	302	169	91
125 Net due to related banking institutions <sup>6</sup>	29,800	22,194	7,606	14,086	1,016	4,214	5,723	1,741	3,020
126 Other	3,951	3,394	557	3,136	105	430	100	115	65
MEMO									
127 Time deposits of \$100,000 or more	86,794	74,423	12,371	67,193	217	11,861	2,561	3,232	1,730
128 Certificates of deposit (CDs) in denominations of \$100,000 or more	29,277	27,464	1,812	22,826	1	1,125	1,073	3,121	1,130
129 Other	57,518	46,959	10,559	44,367	216	10,736	1,488	111	599
130 Savings deposits authorized for automatic transfer and NOW accounts	55	31	25	11	0	12	7	9	16
131 Money market time certificates of \$10,000 and less than \$100,000 with original maturities of 26 weeks	0	0	0	0	0	0	0	0	0
132 Time certificates of deposit in denominations of \$100,000 or more with remaining maturity of more than 12 months	8,855	8,835	20	7,737	1	172	204	731	10
133 Acceptances refinanced with a U.S.-chartered bank	3,998	2,873	1,125	2,584	100	1,026	61	226	1
134 Statutory or regulatory asset pledge requirement	60,705	60,166	539	52,707	429	115	7,376	16	63
135 Statutory or regulatory asset maintenance requirement	8,776	8,331	444	5,606	0	478	379	1,873	440
136 Commercial letters of credit	7,976	5,323	2,653	4,782	181	2,321	242	252	199
137 Standby letters of credit, total	15,937	13,328	2,608	11,483	87	1,914	944	513	996
138 U.S. addressees (domicile)	13,183	10,868	2,315	9,310	7	1,713	756	475	921
139 Non-U.S. addressees (domicile)	2,754	2,460	293	2,173	81	201	188	37	75
140 Standby letters of credit conveyed to others through participations (included in total standby letters of credit)	1,638	1,501	137	1,312	0	132	55	44	96
141 Holdings of commercial paper included in total gross loans	891	556	335	517	6	317	39	1	13
142 Holdings of acceptances included in total commercial and industrial loans	5,344	3,893	1,451	3,610	71	1,427	76	141	18
143 Immediately available funds with a maturity greater than one day (included in other liabilities for borrowed money)	31,374	17,038	14,336	15,933	1,640	12,654	609	246	293
144 Gross due from related banking institutions <sup>6</sup>	87,860	69,850	18,010	64,018	1,300	15,528	1,891	3,446	1,676
145 U.S. addressees (domicile)	22,938	15,165	7,772	11,807	101	7,144	198	2,939	748
146 Branches and agencies in the United States	22,400	14,908	7,492	11,554	101	6,865	194	2,938	746
147 In the same state as reporter	1,147	650	497	588	3	447	10	19	79
148 In other states	21,253	14,258	6,995	10,966	98	6,419	184	2,919	668
149 U.S. banking subsidiaries <sup>7</sup>	537	257	280	253	0	279	3	0	2
150 Non-U.S. addressees (domicile)	64,923	54,685	10,238	52,211	1,199	8,383	1,694	508	928
151 Head office and non-U.S. branches and agencies	62,634	52,662	9,972	50,208	1,198	8,208	1,684	498	840
152 Non-U.S. banking companies and offices	2,288	2,023	265	2,003	1	176	10	10	89
153 Gross due to related banking institutions <sup>6</sup>	95,794	79,182	16,612	67,771	1,882	11,692	7,614	2,869	3,966
154 U.S. addressees (domicile)	22,652	16,599	6,053	9,880	304	3,181	3,874	2,357	3,055
155 Branches and agencies in the United States	22,387	16,385	6,002	9,767	304	3,152	3,794	2,345	3,024
156 In the same state as reporter	952	470	482	409	23	444	10	17	49
157 In other states	21,434	15,915	5,519	9,358	281	2,708	3,794	2,328	2,975
158 U.S. banking subsidiaries <sup>7</sup>	265	214	52	113	0	29	80	12	31
159 Non-U.S. addressees (domicile)	73,142	62,583	10,558	57,891	1,577	8,511	3,740	511	911
160 Head office and non-U.S. branches and agencies	71,240	60,792	10,448	56,125	1,573	8,426	3,725	511	880
161 Non-U.S. banking companies and offices	1,902	1,792	110	1,766	4	85	15	1	31

## 4.30 Continued

Item	All states <sup>2</sup>			New York		Calif- ornia, total <sup>4</sup>	Illinois, branches	Other states <sup>1</sup>	
	Total	Branches <sup>3</sup>	Agencies	Branches <sup>3</sup>	Agencies			Branches	Agencies
<i>Average for 30 calendar days (or calendar month) ending with report date</i>									
162 Total assets	237,079	184,475	52,604	165,129	6,446	42,637	10,120	6,641	6,107
163 Cash and due from depository institutions	41,565	37,782	3,784	35,273	457	3,500	1,785	295	256
164 Federal funds sold and securities purchased under agreements to resell	6,813	5,727	1,086	5,518	510	522	114	73	76
165 Total loans	128,685	96,538	32,147	84,064	4,080	25,076	7,386	3,442	4,637
166 Loans to banks in foreign countries	21,894	16,935	4,958	15,489	577	3,954	1,042	112	720
167 Total deposits and credit balances	115,709	100,671	15,037	92,461	1,992	12,397	3,016	3,743	2,099
168 Time CDs in denominations of \$100,000 or more	28,217	26,467	1,750	21,662	11	1,103	1,027	3,343	1,071
169 Federal funds purchased and securities sold under agreements to repurchase	20,582	15,057	5,525	13,873	609	4,994	610	343	153
170 Other liabilities for borrowed money	44,211	24,789	19,422	23,341	2,232	16,904	705	472	557
171 Number of reports filed <sup>8</sup>	444	268	176	173	31	115	43	32	50

<sup>1</sup> Data are aggregates of categories reported on the quarterly form FT-11-C '002, "Report of Assets and Liabilities of U.S. Branches and Agencies of Foreign Banks." This form was first used for reporting data as of June 30, 1980. From November 1972 through May 1980, U.S. branches and agencies of foreign banks had filed a monthly FR 886a report. Aggregate data from that report were available through the Federal Reserve statistical release G-11, last issued on July 10, 1980. Data in this table and in the G-11 tables are not strictly comparable because of differences in reporting panels and in definitions of balance sheet items.

<sup>2</sup> Includes the District of Columbia.

<sup>3</sup> Includes all offices that have the power to accept deposits from U.S. residents, including any such offices that are considered agencies under state law.

<sup>4</sup> Agencies account for virtually all of the assets and liabilities reported in California.

<sup>5</sup> Total assets and total liabilities include *net* balances, if any, due from or due to related banking institutions in the United States and in foreign countries (see

footnote 6). On the former monthly branch and agency report, available through the G-11 statistical release, *gross* balances were included in total assets and total liabilities. Therefore, total asset and total liability figures in this table are not comparable to those in the G-11 tables.

<sup>6</sup> "Related banking institutions" includes the foreign head office and other U.S. and foreign branches and agencies of the bank, the bank's parent holding company, and majority-owned banking subsidiaries of the bank and of its parent holding company (including subsidiaries owned both directly and indirectly). *Gross amounts due from and due to related banking institutions* are shown as memo items.

<sup>7</sup> "U.S. banking subsidiaries" refers to U.S. banking subsidiaries majority-owned by the foreign bank and by related foreign banks and includes U.S. offices of U.S.-chartered commercial banks, of Edge Act and Agreement corporations, and of New York State (Article XII) investment companies.

<sup>8</sup> In some cases two or more offices of a foreign bank within the same metropolitan area file a consolidated report.

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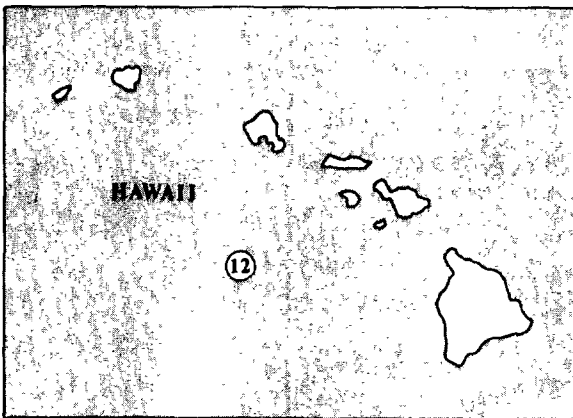
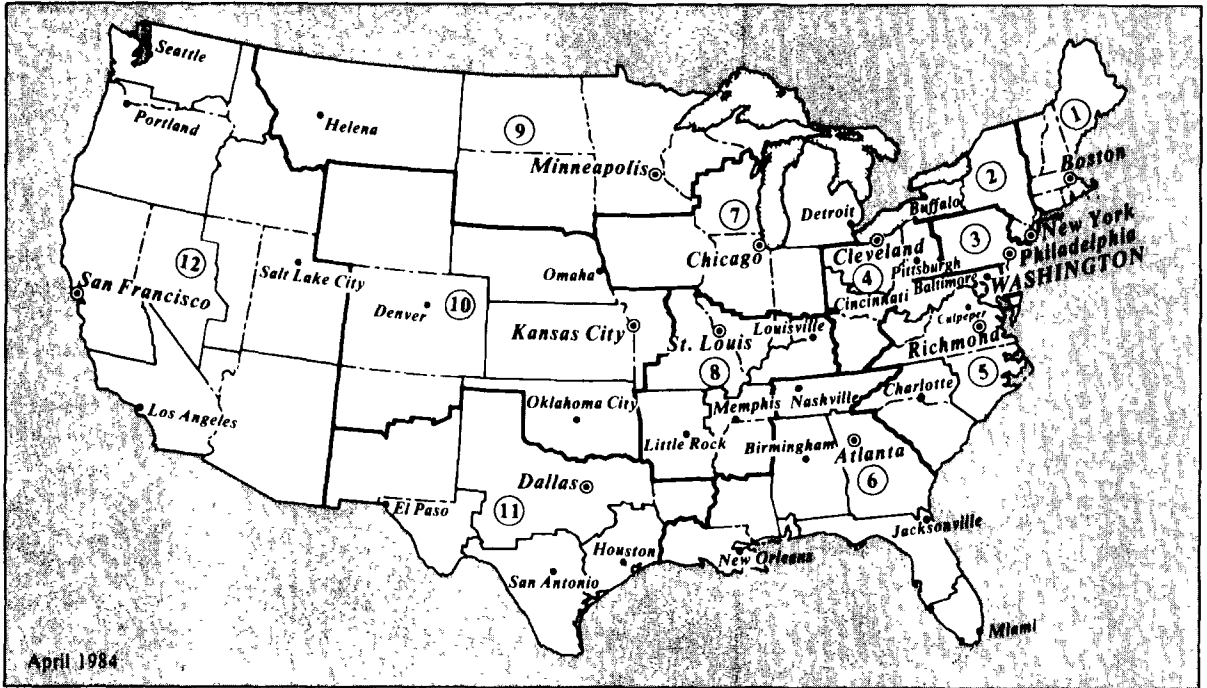
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- Boundaries of Federal Reserve Branch Territories
- ★ Board of Governors of the Federal Reserve System
- ⊙ Federal Reserve Bank Cities
- Federal Reserve Branch Cities
- Federal Reserve Bank Facility