EIR Economics

U.S. Savings League Annual Convention

Thrift institutions fight for their lives

by Kathy Burdman

The over 2,000 executives of the nation's savings and loan banks who gathered in San Francisco Nov. 16-20 for the U.S. League of Savings Association 1980 Annual Convention reflected with dead accuracy the mood of America. Fighting mad at the way Federal Reserve Board Chairman Paul Volcker's credit squeeze has throttled U.S. mortgage lending, U.S. League leaders in speech after speech rose to denounce Volcker.

The Fed chairman and his allies "should share early departure" from their jobs if Volcker continues to raise interest rates past reason, Leonard Shane, California president and regional director of the U.S. League told *EIR* in an interview. "I don't believe you're going to control inflation with interest rates. I don't see how Volcker can continue a policy that has failed."

S&L leaders, who do over 43 percent of America's residential mortgages, particularly attacked Volcker's enforced 25 percent drop in U.S. housing starts this year.

The nation's savings and loan institutions are in danger of walking right into a trap laid for them by Paul Volcker, Comptroller of the Currency John Heimann, and Federal Home Loan Bank Board Chairman Jay Janis.

They are about to adopt major portions of Volcker's mortgage policy: *mortgage indexation.*

The League is actively considering as inevitable the transformation of the U.S. banking and home lending system into the British and Canadian model of fully indexed mortgage markets now being urged by Volcker. As U.S. League Senior Counselor Norman Strunk stated in his convention speech, subtitled "Is There Life After Death?": "The S&L business in the form we have known it since World War II . . . is dead. It is time for a quiet burial of the long-term fixed rate mortgage . . . as is going on in Great Britain and Canada."

Strunk urged that the U.S. mortgage market be indexed, that all new mortgages be made at floating rates, whose interest payments will change as often as in the Variable Rate Mortgage (VRM)—every six months.

Only if U.S. S&Ls adapt to British indexation will they survive—although "transformed," Strunk said.

EIR does not believe there is such a "life after death" for America's savings and loan industry. As U.S. League Vice President Roy G. Green said, the general adoption of indexed mortgages will make housing in this country "unaffordable." British-style banking deregulation will shut down the U.S. home mortgage industry, and most S&Ls with it (see article page 37).

The U.S. League needs an alternative to Volcker's policy.

'Take to the streets'

On one level, the U.S. League is certainly aware that Volcker's banking deregulation under the March 1980 Depository Institutions Deregulation Act just doesn't work in any economic—or human—sense. "The people of our inner cities in the 1980s, given the total frustration over housing—unless we move to solve the real danger, they will take to the streets on the housing issue," Leonard Shane told *EIR*.

"Mortgage rates and interest rates are too high. Housing is in a slump. And we are moving into another earnings crunch," U.S. League outgoing President Edwin B. Brooks, Jr. said in his convention keynote. "It has been devastating to the housing industry and it has cost homebuyers millions of dollars in interest payments on their loans."

"I don't believe that housing should be made the scapegoat," Mr. Brooks told *EIR*. "I just don't believe that housing should have to compete with the casinos in Atlantic City, or with foreign countries, for credit. We've got to continue to house Americans, and we've got to build up our industry."

The Volcker Fed, Heimann's Comptroller's office, and allied regulatory agencies are now engaged in a virtual coup against Congress and other elected officials, League leaders further warned, taking over U.S. banking policy.

"Talking about Volcker at the Fed, the question is whether the direction of the nation's social and economic development is not being diverted," Mr. Shane told *EIR*. "This country is on the road to a major policy change, a long-range move away from our traditional commitment to housing, without any public debate.

"I don't want to use the word 'sneak,' but Volcker doesn't feel obliged to reach into the public arena for major decisions. I think it's horrible to put nonelected officials in a position to effect major shaping of national policy . . . not authorized by elected officials."

Kicking off the convention Nov. 17, Sen. Edwin "Jake" Garn of Utah, the Reagan Republican who will soon take the chairmanship of the Senate Banking Committee, similarly warned the convention that Volcker's Depository Institutions Deregulation Committee, which oversees the Deregulation Act, was acting to usurp congressional authority. The Committee "ignored the clear intent of Congress" in its actions allowing interest rates to soar this year, "and so its actions must be reviewed and corrected by the next Congress," Senator Garn said.

"Let Congress make the laws, not the regulatory agencies," Senator Garn told *EIR* in an exclusive interview following the convention, printed in full in our last week's issue. "Major national policy decisions should be made by Congress, and should not be drifted into by the regulatory agencies. I as chairman don't want things to just happen, to have the regulatory agencies sitting there making decisions involving our whole financial community."

Milton Feinerman, President of the Federal Home Loan Bank of San Francisco, warned in his convention speech that the Fed and the New York-led top 100 commercial banks are deliberately manipulating U.S. credit allocation so that "housing—because it is an outlawed priority, they say—must be scrapped."

In particular, Feinerman warned that the Fed is conducting banking deregulation in such a way as to raise S&Ls' costs and force them to cut back on housing credit. "Strong support, especially from the Federal Reserve and the commercial banks, has been given to the argument that scarce resources are most efficiently allocated in an economy free of regulatory impediments," Feinerman stated. "Make no mistake about it. The Federal Reserve and the commercial banks believe in the unification of our nation's financial system under the direct control of the Federal Reserve.

"I ask you to evaluate the danger and fallout from the possible misuse of such tremendous power vested in one agency."

Stiff upper lip

The U.S. League, however, has as yet come up with no real alternative to Volcker's deregulation. As a result, in practice the League has thrown all its political weight behind the one program which will ensure the extinction of the S&L industry: British-style mortgage indexation.

U.S. League Counselor Norman Strunk was clearly unhappy with the proposition in his speech, yet said that "realism" dictates that American S&Ls accept the British system. The Anglo-Canadian banks have already been deregulated and should be emulated, he said. "Much of what we are experiencing toward free market operations currently in this country is going on in Great Britain. Competition among institutions and open-market pricing are becoming very prevalent among the banks and building societies [British S&Ls] in Great Britain. In Canada for many years there has been a complete absence of governmental restrictions. Realism led in Canada ten years ago to the development of the roll-over mortgage and the virtual disappearance of the long-term fixed rate mortgage. As it happened in Canada, it is time for a quiet burial of that depression-era credit instrument. We are wisely taking a considerable step in their direction with our renegotiable rate mortgages."

Deregulation of the Anglo-Canadian banks' usury ceilings has meant they must pay sharply higher rates to their depositors, Mr. Strunk noted, raising their costs of doing business, especially as inflation brings deposit rates into double digits. Once these conditions were accepted, he said, British building societies could no longer afford to make long-term fixed-interest mortgages at 5 or 7 percent for 30 years without going bankrupt.

Instead, banks were "forced" to index mortgages, to let their rates float or be adjusted every six months to the same market interest rates they had to pay for deposits, into the double digits.

All this is true, but the effects of banking deregulation on the British economy should immediately alert S&Ls that something is horribly wrong there. During the period described by Mr. Strunk, since the advent of the Margaret Thatcher government in 1978, British housing construction has collapsed (while unemployment has skyrocketed to 8.6 percent, and industrial production has fallen by over 11 percent, worse than the 1929-30 Depression record).

Mr. Strunk, who was for many years the respected executive director of the U.S. League, now holds the position of secretary-general of the International Union of Building Societies and Savings Associations, the world organization of mortgage banks which is dominated by the British building societies. He is doubtless influenced by the British S&Ls and the dismal circumstances of the moribund British economy within which they operate.

The fact is that indexed mortgages were the intent of the banking deregulators led by Paul Volcker, William Proxmire, and Henry Reuss in the first place. Close studies of the history of the 1980 deregulation act show that Volcker were not merely interested in "letting the S&Ls compete" for deposits by "freeing them" to pay more through phaseout of usury ceilings like Reg Q.

The reason given for the end to usury ceilings was itself that *mortgages were too cheap*, and they should be forced to be more expensive and less fixed, less predictable. "Ten years ago when depositors were very, very dumb and were willing to get a lousy 5 percent, what they did was subsidize the mortgage market in effect," a top Treasury official who worked on the deregulation act told *EIR*.

"The great unwashed masses of depositors got 5 percent, and so the S&Ls could afford to make mortgage loans at 7 percent to the smaller middle/upper-class few who could afford homes—this was an effective tax on the poor to subsidize housing for the rich.

"Mortgages were underpriced, period. These small-town fat S&L executives believed they had some kind of religious duty to keep making home mortgages at affordable rates, beyond all economic reason, at fairy-tale prices."

The deregulation act was rammed through explicitly to "raise mortgage prices," the official stated. "Mortgage rates have been raised, and they should be even higher than they are. Thrifts should be forced to price them not on their actual 8 percent costs of deposits, but on the interest rates they are foregoing by not investing in Treasury bonds at 12 percent and investing instead in mortgages."

Why in the world would the deregulators want to make mortgages more expensive, *EIR* asked.

"Because we have *too much housing in this country,*" came the answer. "Ten years ago when depositors were dumb and subsidizing mortgages, we went on a home-building spree, we built houses all over the country, contractors had a grand time. Gee, wasn't that fun, Ma? But now we have too many houses and scarce resources, especially scarce capital. We can't afford capital for housing.

"I think it's outrageous that the typical college graduate today expects automatically to be able to live in a 3-bedroom house with one and a half baths. He thinks it's his God-given right—that's asinine. He says it's the American dream—who says he's right? If he wants it he's going to have to pay more, a lot more, and then he'll see that he's going to have to be satisfied with a smaller, more efficient apartment."

It could not be clearer: one of the premises of the deregulation act is to destroy homebuilding. In particular, indexing mortgages will be one of the most efficient destructors. "Variable rate mortgages, renegotiable-rate mortgages, these are a god-send to us," said the Treasury official. "They make housing simply too expensive, and unplannable to boot."

U.S. League Vice President Roy G. Green told *EIR* in fact that the British-Canadian indexation system makes housing "simply unaffordable." Deregulation does not work because "I'm not sure that housing will ever be competitive at 15-18 percent interest rates. I don't think the consumer can afford such rates for any length of time," Mr. Green said.

American S&Ls cannot "accommodate" to the destruction of U.S. housing. The deregulation act is bad legislation and should never have been passed. The DIDC is unconstitutional, as the U.S. League charges in its current landmark suit against the Fed and the DIDC, and should be repealed.

But, as U.S. League President Rollin Barnard told *EIR*, "The suit against the DIDC is merely a defensive measure. What is really needed is to go on the *offensive,* to create the kind of banking structure that can build this nation." Mr. Barnard called for new legislation to accomplish this. The League has also established a Committee on Savings Industry Development, to be headed by Roy G. Green, to develop a legislative strategy.

EIR looks forward to covering their efforts.

President Barnard wants to take the offensive

EIR's banking columnist, Kathy Burdman, interviewed U.S. Savings League President Rolling D. Barnard last month.

EIR: What is your evaluation of Volcker's banking deregulation program?

Barnard: We oppose deregulation; we have a suit against the Depository Institutions Deregulation Committee

(DIDC) which charges that it is unconstitutional. We'll win this suit, but it's just a tactic on a narrow part of the S&Ls' narrow self-interest. It's just a cobblestone in the pavement, a defensive measure. What is really needed is to go on the *offensive,* to create the kind of banking structure that has built and can build this nation. What has to be done if we're a capitalistic nation is, let's start creating some capital here. We must revitalize the entire U.S. economy, reindustrialize it.

We intend to lay out a 60- to 120-day program when Congress reconvenes next year for a legislative review of this basic problem—the banking system as a whole is capital short. We need to renovate the banking system to provide capital for national industrial revitalization, to build the capital base to make all the wheels hum.

We have a national advertising campaign to defend the "American dream of home building" which will get off the ground in December, and we do want a broad expansion of capital for home building in America—but this is only the sounding bell. Housing won't get very far on its own, not if it's done at the expense of capital for farmers, or plant managers, or businessmen. This is not a war for the allocation of credit. We must expand capital for the entire economy, and we must have a banking system which can do this.

EIR: Do you have any specific legislation planned yet?
Barnard: Nothing specific yet I can cite; we are still formulating some programs in consultation with Capitol Hill. But we intend to move at the beginning of next year.

California official on Volcker credit policy

Leonard Shane, U.S. League California President, talked to EIR*'s Los Angeles bureau chief, Ted Andromidas:*

EIR: The U.S. League's Executive Director, William O'Connell, charged in a Sept. 22 speech that "it is legitimate to ask whether the Federal Reserve does not have too much power . . . This is an extraordinary and dangerous granting of power to a few unelected officials." What is your view?
Shane: I suscribe to that totally, and I go a few steps beyond. The problem with nonelected regulators is that . . . you elect governors, mayors, and city councilmen on the basis of what they stand for from an ideological and social standpoint. Who's got that opportunity with appointed officials? When we're talking about Volcker's leadership of the Fed, there's substantial question as to whether or not the direction of the nation's social and economic development is being diverted, in the face of what they see as the mechanical aspects of their policy. . . . I think it's a horrible effect to put nonelected officials in a position where they can shape national policy, particularly without public debate.

I think this country is on the road to a major policy change, a long-range move away from our traditional commitment to housing, without any public debate. We intend to force that debate, and one of the ways we feel we have is to persuade the Reagan administration to do a straight evaluative approach. We've been unsuccessful in getting the Carter administration to do that. The corollary is that what the Congress perceives in H.R. 4986 [the Depository Institutions Deregulation Act of 1980] and what Volcker perceives in H.R. 4986 are two different things, and the hearings demonstrate that. Hence the lawsuit, which is led by the U.S. League and others, against the DIDC for having acted outside the scope of legal authority. We're only a few weeks away from the decision at the lawsuit . . . certainly the judge at the hearing, I'm told really grasped the issue.

EIR: In terms of action, are you planning anything else beside the lawsuit?
Shane: We have formed a joint de facto Committee of the California Savings League, the California Realtors Association, and the Homebuilders are joining us, to try to deal with the situation. I don't want to use the word "sneak," perhaps the word subterfuge. But at the moment a lot of things are taking place that are just not being discussed in the public eye. Volcker does not feel obligated to reach into the public arena for his major far-reaching decisions.

EIR: Representative Ronald Mottl from Ohio indicated that if Volcker does not lower interest rates almost immediately, Carter or Reagan should fire him. Would the League propose anything like that?
Shane: I can't answer that question quite that way, but by indirection, I am concerned about Mr. Volcker and his associates, of high influence of like mind, and I'd suggest to you that there are going to be some people high in the Reagan administration like that; Charls Walker moves in the same ideological direction. My complaint is that what they are really doing is realigment of credit allocation in this country for purposes that they deem to be more proper. I'm not even sure they're wrong. I think they're wrong. But my concern is in dealing with your question "Should he be fired?" that there is a major directional change in this cliché of "reindustrialization," which I consider to be absurd nonsense. I could go on at great lengths as to what their scenario is, I think they have considered pursuing directions that are contrary to and not authorized by elected officials. And when that's the case, as with any appointed official, Mr. Volcker should share with many others an early departure, if they go contrary to the policies established by the elected

body politic. I am not willing to concede that the professional managers of our government should be making all the policies. . . . I do not believe in the omnipotence of public officials.

EIR: Do you have a dollars-and-cents estimate of the effect of Volcker's policies on housing?
Shane: It is inconceivable to me as practical and social phenomenon, that any force in the marketplace will force interest rates up to inordinately high levels and keep them there over any extended period of time, given the disaster that would represent, the damage, the destruction in the automobile industry that is struggling just to survive. I cannot imagine any responsible—or even irresponsible—leader saying that we are artificially going to sustain a prime that will not go below 18 percent let's say, for one year. Unthinkable.

There are economists, theoreticians, and academicians who are too theoretical. I don't believe you're going to control inflation with interest rates. It's a policy that has failed; I can't see how Volcker can continue a policy that has failed. Charls Walker said that from his position he did not believe in the special allocation, the special commitment, or funds to housing. I was surprised he got the applause he got. His speech was rather candid, it frightened me. There's a hopelessness that runs through the mechanical academician, the mechanical regulator. They don't seem to realize that out there there are millions of people whose lives they're ruining. . . .

Kathleen Connell recently said that she thinks that the people of the inner cities of the eighties—given the total frustration over housing—in the absence of our moving to solve the real danger, will take to the streets, on the housing issue. I believe that. The issue of the housing industry has to be a public discussion, so that some of the administrators don't run away with the policies.

Legislative strategist concerned about dereg

A special League Committee on Savings Industry Development will be headed by League Vice-President Roy G. Green, to "develop our strategy for working with the new administration in Washington." Mr. Green told EIR:

EIR: As chairman of the Committee on Savings Industry Development, how do you view the prospect of further banking deregulation in the U.S.?
Green: We are extremely concerned about the rush to deregulate banking which has developed in the U.S. The DIDC has rushed the phase-out of Regulation Q much faster than the intent of the legislation.

EIR: Beyond the Deregulation Act, U.S. League Senior Counselor Norman Strunk painted one totally deregulated future for the U.S. on the British-Canadian model, with fully indexed mortgages.
Green: If we are to be deregulated on one side of the balance sheet, with our deposits costs rising, then we must be fully deregulated on the other side, we must be able to lend at deregulated rates. We must go for fully Variable Rate Mortgages.

EIR: But is the entire process desirable?
Green: Our commitment is to housing in America first and foremost. If it can be proven that in a deregulated system, you can sucessfully channel money to housing, I would agree that deregulation works. However, up to now that's not been the case in the U.S., especially because of the way the DIDC rushed us to judgment.

And I'm not sure housing will ever be competitive at 15 to 18 percent mortgage rates under full deregulation. I don't think the consumer can afford such rates for any length of time. It's simply unaffordable.

EIR: What about interstate banking laws, such as the McFadden Act, which some regulators such as Fed Chairman Volcker seek to remove?
Green: While I'm for the free market, there are certain regulations needed in practice to protect the health of the banking system. Full interstate banking would not be beneficial. It would lead to banking consolidation in the hands of a few large banks, which would be bad both for consumers and for the economy, since it would mean reduced service to local communities.

EIR: Senator Banking Committee Chairman-designee Jake Garn told us that the regulators have been implementing many aspects of deregulation without congressional approval. In particular, the Fed's newly approved International Banking Facilities will have a very extensive Electronic Funds Transfer capability which Comptroller Heimann has said could make the McFadden Act obsolete.
Green: I agree with Senator Garn. With regard to interstate banking coming about by default, I was a member of the National Commission on Electronic Funds Transfer established in 1974, and in my comments at the time I expressed concern that EFT would lead directly to nationwide banking for those banks who could afford it on a national level. This, in turn, I warned would lead to the creation of a few "superbanks" which would dominate the system.

EIR: Does the Green Committee have any legislative plans?
Green: We have not developed any specific legislation. We will be studying all these issues in ongoing fashion.