University of New Mexico
UNM Digital Repository

Economics ETDs | Electronic Theses and Dissertations

Spring 5-22-1959

A Historical Analysis of the Investment Policies of the Albuquerque National Bank

William G. Grady Jr.

Follow this and additional works at: https://digitalrepository.unm.edu/econ_etds

Part of the Economics Commons

Recommended Citation
Grady, William G. Jr.. "A Historical Analysis of the Investment Policies of the Albuquerque National Bank." (1959).
https://digitalrepository.unm.edu/econ_etds/62

This Thesis is brought to you for free and open access by the Electronic Theses and Dissertations at UNM Digital Repository. It has been accepted for inclusion in Economics ETDs by an authorized administrator of UNM Digital Repository. For more information, please contact disc@unm.edu.

378.789
Un3Ogr
1959
cop. 2

ALBUQUERQUE NATIONAL BANK - GRADY

THE LIBRARY
UNIVERSITY OF NEW MEXICO

Call No.

378.789
Un30gr
1959
cop.2

Accession Number

247475

A14405 423492

DATE DUE

NOV -2 '72 UNM
NOV -3 '72 UNM
MAY 16 2006
RECD UNM MAY 29'73
DEC -2 '84
RECD UNM DEC-7'84
AUG 1 1989
OCT-5'92
OCT 26 1992
OCT 21'92
MAY 17 2006
GAYLORD
PRINTED IN U.S.A.

UNIVERSITY OF NEW MEXICO LIBRARY

MANUSCRIPT THESES

Unpublished theses submitted for the Master's and Doctor's degrees and deposited in the University of New Mexico Library are open for inspection, but are to be used only with due regard to the rights of the authors. Bibliographical references may be noted, but passages may be copied only with the permission of the authors, and proper credit must be given in subsequent written or published work. Extensive copying or publication of the thesis in whole or in part requires also the consent of the Dean of the Graduate School of the University of New Mexico.

This thesis by .....William G. Grady, Jr.....
has been used by the following persons, whose signatures attest their acceptance of the above restrictions.

A Library which borrows this thesis for use by its patrons is expected to secure the signature of each user.

NAME AND ADDRESS	DATE
Lindy Miller Albuquerque NMex.	2-11-69

A HISTORICAL ANALYSIS OF THE INVESTMENT POLICIES OF THE ALBUQUERQUE NATIONAL BANK

By

William G. Grady, Jr.

A Thesis

Submitted in Partial Fulfillment of the

Requirements for the Degree of

Master of Arts in Economics

The University of New Mexico

1959

This thesis, directed and approved by the candidate's committee, has been accepted by the Graduate Committee of the University of New Mexico in partial fulfillment of the requirements for the degree of

MASTER OF ARTS

E. A. Castetter
DEAN

DATE May 22, 1959

Thesis committee

W. J. Parish
CHAIRMAN

David Hamilton

Julian S. Duncan

378.789
Un30gr
1959
cop. 2

PREFACE

This paper has been undertaken with the thought that the analysis of the investment policies of an individual commercial bank should have some worth in the economic scheme of things. The banking and monetary system of the United States is probably her first, and largest, economic institution. Decisions made by the individual bank comprises the policies of the banking system as a whole, and these policies affect every American in one way or another.

Another factor to be considered is the worth of the paper to other individuals who are called upon to make these bank investment decisions in their day to day lives. While the policies of one bank can hardly be expected to prevail as an ideal for all banks, and while the author certainly is not attempting to outline any sort of "proper" investment policies, still it is felt that the mere listing of investment decisions, and some of the factors which led to them, will undoubtedly be of some use to others faced with similar decisions.

The Albuquerque National Bank is the largest bank in the State of New Mexico, and the oldest in the city of Albuquerque. Its record over the past thirty-five years has been markedly successful. It is to be hoped that this narration of a portion of that record will be of some use to others

247475

traversing the same ground.

In addition to a narration, this paper will attempt to prove a thesis. The thesis is this: With proper supervision, the investment account of a commercial bank not only provides a bulwark against the depreciation of assets in a time of crisis, but more than that, the investment program with proper goals and methods implementing the historically defined and proven policies of an aware management, can be a completely flexible asset, available at all times for a variety of uses. It can be a needed source of revenue when loan demand falls (as in World War II). It can, if attention is devoted to the program, pay for the added costs of maintaining a well informed and well trained investment department, by making it simpler for management to move quickly in a given market situation. Added income is a poor reason for taking any added risks in a bond account. Still, the author believes that the risks of the bond account are necessarily reduced by the maintenance of a watchful investment department. The increased awareness alone should increase income sufficiently to pay for the department, merely as a by-product.

The author wishes to express his appreciation to Mr. Fred Luthy, President of the Albuquerque National Bank, for his time spent in helpful discussion, and for making available any and all of the records of the Bank, without which the paper could not have been written. To him, and to his life's work, The Albuquerque National Bank of Albuquerque, New

Mexico, this paper is respectfully dedicated.

For his help in pointing the way, for many helpful suggestions in the use of the material, and lastly for his patience, I would like to thank also, Dr. William J. Parish of the College of Business Administration, University of New Mexico.

TABLE OF CONTENTS

	Page
PREFACE	1
LIST OF FIGURES	v
CHAPTER	
I. THE EMPLOYMENT OF BANK FUNDS	1
II. A SOUND BANK	10
III. THE GREAT DEPRESSION	29
IV. MORE CRISES -- LOCAL AND WORLDWIDE	54
V. THE POSTWAR PERIOD - A PROBLEM OF GROWTH	75
VI. BANK INVESTMENT POLICY	94
EPILOGUE	110
APPENDIX	113
BIBLIOGRAPHY	133

LIST OF FIGURES

Figure		Page
1.	Assets of All Commercial Banks in the United States	6
2.	Illustration - "Scrip" Considered for Issue by Albuquerque National Bank During 1933 Banking Crisis	42
3.	Comparison of Book Value and Market Value, Albuquerque National Bank Bond Account, April 30,1934	50
4.	Bond Account of the Albuquerque National Bank, Selected Dates	57
5.	Bond Account of the Albuquerque National Bank, December 31, 1938	59
6.	Assets and Deposits, Albuquerque National Bank, The War Years	66
7.	Percentage of Securities Becoming Due Each Year, as of January 12, 1945	67
8.	Sample Investment Purchase During World War II	69
9.	Comparison of Albuquerque National Bank Bond Account Before and After World War II	70
10.	Total Loans and Investments of Member Banks - The War Years	72
11.	Direct Government Obligations Held by All Member Banks - Maturity Distribution	73
12.	Loans and Investments Compared in Postwar Period, Albuquerque National Bank and All Member Banks	78

LIST OF FIGURES (Cont'd)

Figure		Page
13.	Albuquerque National Bank Bond Account, as of December 31, 1952	88
14.	Albuquerque National Bank Bond Account, as of December 31, 1953	89
15.	Ratio Sheet for Albuquerque National Bank, and Various Averages, 1953	91
16.	Albuquerque National Bank Bond Account, as of December 31, 1950	92
17.	Charts:	
	I. Weekly Average Market Yields for Long Term U. S. Government Bonds and for Longest Treasury Bills, Latest Shown are for Week Ending, January 7, 1959	114
	II. Market Price (in Percentages of Par) of Two Long Term U. S. Treasury Bonds . .	114
18.	Seven Schedules	118

CHAPTER I

THE EMPLOYMENT OF BANK FUNDS

THE ART OF BANKING

> Modern commercial banking is an exacting business. . . . The rewards are modest; the penalties can be enormous.[1]

Taken as an integrated whole, America's banking system is the most important of its monetary institutions. Directing this system is no czar of the banks, no Commissar for the State Bank; for ours is a complex system of individual banks run by individual entrepreneurs. Though, as a system, the banks are subject to considerable influence from the federal government, still, in the last analysis, each bank must stand or fall on the strength of its own assets, upon the wise or foolish decisions of its own management. Each bank is managed separately, and what is good for the system as a whole may not be at all the same as that which is good for the individual bank. Each bank must preserve its own entity, and yet it must be able to produce enough earnings to justify its existence. Solving this basically conflicting requirement, that of maintaining solvency through safety, yet operating profitably, is the "Art of Banking."

---

[1] Roland I. Robinson, Management of Bank Funds, (New York: McGraw-Hill, 1951), p. 3.

It is not a science, for there are no clearly definable principles to be followed. There are no rules which can guarantee that the individual bank will always make a profit; there are no guide lines which can assure even that a bank will remain always solvent. However, since the bank which cannot remain solvent obviously cannot long remain a profitable operation, a definite priority is established: Standards of safety must be maintained. Once these standards have been met, then attention can be turned to making a profit for the stockholders. The simplest method available to a bank is to employ its funds so that standards of safety are maintained while a maximum return is yielded. This obviously oversimplifies the situation, for there are many alternative uses to which bank funds can be put.

In this paper we will examine how one bank has met this challenge. Granted that the principles which have proved workable for one bank will seldom, if ever, prove exactly the same for any other bank, still perhaps some principles can be found which will indicate at least some of the choices available. This is how one bank has attempted to master the art.

THE EMPLOYMENT OF BANK FUNDS

Four logical priorities for the employment of bank funds have been set out by Professor Roland I. Robinson, in one of the more recent books available on the subject.[1] These are as follows:

---

[1] Ibid., pp. 12-17.

The first, or highest, priority for bank funds belongs to its primary reserves. Banks have the legal obligation to pay out the majority of their assets upon demand, and in the form of cash. Cities served by a bank depend on it for cash requirements. Thus there is a steady and expected business in cash, which a bank must be ready to supply. Obviously, a bank will never be called upon to pay out all of its assets in cash, but a reserve must be maintained, and some of the reserve must be kept in cash to meet some deposit withdrawal claims. In addition, banks must meet the legal reserve standards set by the Federal Reserve System. These "legal reserves," members of the Federal Reserve System must keep in the form of deposits with the Federal Reserve Bank. Even cash in the vault does not count toward the fulfillment of the legal reserve requirement.

Yet, cash itself in the long run does not represent real safety, for idle cash earns nothing. It is usually best for a bank to keep as little actual cash on hand as possible, while keeping the balance of its funds earning some income.

The second priority, commonly called "secondary reserves," is aptly named by Professor Robinson, "Protective Investment." These funds must be kept in investments of such character as to guarantee their ready convertibility into cash without appreciable loss should an unusual demand for cash arise. They must be ready to be used to meet fluctuations in the cash needs of the community. These fluctuations are usually very likely, if not altogether expected, and normally will tend to have a

regular pattern. For example, seasonal variations in demand for cash are experienced in agricultural communities.

In addition, the secondary reserves must be kept at a level sufficient to meet other more remote but still possible demands for cash. These needs, caused by movements of the business cycle, local depressions, or perhaps a "run," can come quite suddenly; and the bank which is not adequately prepared for their coming can find itself in desperate straits with almost no warning.

Third in priority for the use of bank funds comes the need for which banks exist. Once a bank has made itself safe, it should devote itself to serving the community in which it is located. This is the business for which it is best fitted; making direct loans to its customers to fulfill their legitimate credit needs. Only after a bank has adequately filled this need, should it go on to the fourth stage of employing its funds, that of investment for income.

In this third stage of a bank's money operations exists the only justification for any large amount of risk-taking by a bank. The credit standards applied to direct loans need not be as high as those applied to a bank's open market investments. Banks are sometimes required to take rather substantial risks in their loan accounts, and should take them, when necessary. Banks are peculiarly fitted for lending, while they are not in a favorable position to deal in any but high grade, short term, fixed income securities. It might be noted in passing that other financial institutions, notably large insurance companies,

are in exactly the opposite position, since they are usually much closer to the open markets and removed from the local lending situations.

There is still another reason for banks to engage in as little open market operations as possible, particularly for income purposes. The modern securities markets reflect two great wars and a depression; obligations of the public debt dominate the market. Commercial banks are subject to strong influence of government, anyway (through the regulations of the Federal Reserve System and examinations by the office of the Comptroller of the Currency). The bank which leans heavily on the markets for income will tend to live on returns deemed adequate by the public authorities.

Few banks can find all the loans they would like to make, however, and in order to employ all their funds, banks must rely in part on Mr. Robinson's fourth and last priority, "Investment for Income."

HISTORICAL USES OF BANK FUNDS

It is the purpose of this paper to examine the investment assets of the Albuquerque National Bank, i.e., that portion of its assets which is given over to the purchase of investment securities. So we will be concerned primarily with the second and fourth of the priorities mentioned above. While these are secondary alternatives in both cases, nevertheless, they make up a very important section of a bank's balance sheet. Thousands of banks have failed in America for inadequate supervision of their investments in the securities markets. A large

share of the weaknesses which were revealed in the depression of the 'thirties, involved the investment portion of bank assets.

The accompanying chart (Figure 1), shows just how much of the assets of this country's banks are tied up in what can be termed investments of one sort or another.

FIGURE 1

ASSETS OF ALL COMMERCIAL BANKS IN THE UNITED STATES
(in millions of dollars)

	LOANS	INVESTMENTS	INVESTMENTS/ TOTAL ASSETS
6/30/1914	13,171	3,683	22%
6/29/1929	35,738	13,686	28
6/30/1933	16,349	14,008	46
6/30/1934	15,700	17,042	52
6/30/1935	14,909	19,679	57
6/30/1939	16,423	22,944	58
6/30/1949	41,025	72,748	64
12/31/1956	90,302	74,821	45

Source: Banking and Monetary Statistics, Table 3, Federal Reserve Bulletins, October, 1949 and June, 1957.

Many interesting inferences can be drawn from the table. Note the sudden and sharp fall in the total amount of loans outstanding from June, 1929 to June 1933 -- and the consequent fall in the total assets themselves. And yet, the dollar value of the investments increased somewhat over this same period. Loan demand was definitely off, but were banks perhaps pressuring their borrowers as well? The years 1933 to 1935 have been included because this was a turning point. In 1934, investments

assumed the major portion of total bank assets. The percentage given over to investments grew constantly up to the end of World War II. Since the war, loans have again taken the major share. However, investments have not receded to their pre-1920 levels, nor is there reason to expect them to do so. Naturally, one big reason for the switch was the large number of government securities which came onto the market during the 'thirties and early 'forties. But in addition to this, banks have learned that with proper supervision and planning, the high-grade bond markets, particularly U. S. Governments, can provide a good outlet for excess funds, as well as a haven for secondary reserve funds. The words "Protective Investment" have come to mean much more since banks have made widespread use of the government security markets.

The table also helps to highlight the extremes to which banks have employed their funds in securities. Prior to World War I, few banks bought many securities except those needed for circulation purposes. Partly because of slackened demand for loans and partly due to handsome returns available, they started making sizable investments in the 1920's. Without much experience or perspective, they entered the market when interest rates were higher than in the previous two generations (or since), and when an unusual volume of new issues was coming into the market. The general results were not good, and many banks suffered in the 'thirties for their short-sightedness in the 'twenties.

Depression experience reversed investment policies sharply.

Security affiliates were outlawed (those which had survived), and the character of investment by banks was put under direct regulation of the government in 1936 by the passage of the Banking Act of 1936.[1] A very conservative tradition grew up. Banks grew extraordinarily wary of long term issues. In the rush for short term securities, short term interest rates were driven almost to the vanishing point.

Then came World War II, and banks were asked to help finance the war. Bank investment portfolios, as shown by the figures in Figure 1, page 6, for June, 1949, reached new heights. Needless to say, this growth took place primarily, if not wholly, in the issues of the United States Government purchased by the banks. Since the war, we have had a decade or so of comparative peace. Banks have had to re-formulate an effective policy of "normal" peacetime investment while still safeguarding against the crises of the 'thirties and 'forties, depression and war.

In the thirty years or so since the banks began to purchase securities in substantially higher volumes, the investment picture has improved greatly. The banks themselves are much more experienced at meeting market problems, and the resources at their command, in the way of sources of information, etc., have become much more widespread and reliable. It is extremely doubtful that the United States will ever find itself again in the position of having its banking system close

---

[1] See discussion of this Act in final chapter.

up shop entirely, as it did in March, 1933. For one thing, the federal government is much stronger now, and of course would be a very powerful force in avoiding such a situation. But beyond this, and more important, the banks themselves have taken steps. They have fortified themselves against a recurrence, ever again, of such a debacle.

This, briefly, has been the general picture in bank investment for the past thirty years. The bank with which this study concerns itself has been in existence almost as long as this train of events has taken to occur. For a more specific view of this period in our banking history, let us turn to the particular viewpoint of one individual bank: The Albuquerque National Bank.

CHAPTER II

A SOUND BANK

. . . A sound bank must, and will be, maintained.[1]

BANKING IN THE STATE OF NEW MEXICO IN THE 'TWENTIES

Early in the 1920's, the United States experienced a short but major depression. Though not as widespread as the crisis of the following decade, to those sections affected, it was every bit as severe. Particularly was this true in agriculture, where serious losses occurred. The farmers and stockmen of America had been enjoying relative prosperity since the early days of World War I. For the five years prior to 1920, they had been able to sell all that they could produce, and at good prices. Not only our own army, but those of our allies, had to be maintained in the field by the bread and meat baskets of America.

And then the war ended. The demand for agricultural products shrank; in fact, huge surpluses soon appeared. Current production could find little or no market. Food prices reached their lowest levels since 1917. In the space of just fourteen months, from April, 1920 to June, 1921, the farm commodity

---

[1] George E. Breece, Chairman of the Board, Albuquerque National Bank, August 10, 1924.

price index fell from 243 to 114.[1]

New Mexico had been a state for only eight years in 1920. Its economy was almost wholly dependent on agriculture. Naturally, the effects of the fall in farm prices pervaded the entire economy of the state. Especially in the field of banking was the havoc great. Between 1920 and June, 1925, no fewer than 57 banks failed in the state. This was more than were to fail in the following fifteen years, including the "Great Depression" years.[2] It was the highest percentage (57 out of the 123 banks of 1920), of bank failures for any state in the union in this period.

Why was New Mexico's record so bleak? The reasons, now that we are blessed with hindsight, are fairly obvious. In New Mexico, most of the tangible wealth was farming property of some sort. The economy of the state as a whole was not diversified, and the assets of the banks reflected this. It has been estimated that the percentage of New Mexico's bank loans going to farmers in 1920 was on the average as high as 70 percent, and in some communities even as high as 90 percent.[3] A loan to a farmer, by its very nature, is rather risky. Farmers must borrow on the future. They borrow in the spring for the harvest in the fall. If the weather is unfavorable,

---

[1] Federal Reserve Chart Book on Financial and Business Statistics, Historical Supplement, September, 1957.

[2] Annual reports of the New Mexico State Bank Examiner.

[3] Thomas L. Popejoy, "Analysis of the Causes of Bank Failures in New Mexico, 1920 to 1925," New Mexico University Bulletin, (Vol. I, No. 1, 1931), p. 7.

and the harvest is poor, they must wait for a good year to repay the loan. When farm prices fall as drastically as they did in the early nineteen-twenties, farmers cannot repay their debts, even with a good crop. Their notes become almost uncollectable. With the major portion of their assets tied up in farm and ranch commodities, it is no wonder that so many New Mexico banks found themselves in dire straits.

There was another reason for the collapse of banking in the state. In 1920, New Mexico was served by 123 banks, spread throughout the state in communities of every size. Many of these communities were simply too small to support a bank, and several of them had more than one. As a whole, 123 banks were too many for a state with a total population of only 360,350.[1] A natural result of these numerous organizations being in existence was that many of them were seriously undercapitalized. With capital spread so thin, only a small percentage loss in the value of bank assets was enough to eat up the capital protection of the depositors.

Still another factor operating against the banks was the fact that loans themselves made up such a high percentage of their total assets. On the average, for all banks in the state on June 30, 1920, total loans were 8.3 times total investments.[2] There was not much "protective investment" being practiced. A curious factor, however, was the rather conservative

---

[1] U. S. Department of Commerce, 1956, Statistical Abstract of the United States.

[2] Report of the New Mexico State Bank Examiner, 1920.

investment policies that these banks did follow. In this same year, 1920, national banks in New Mexico had 81 percent of their total investments in U. S. Government Bonds, compared to a national average for all commercial banks of 45.7 percent.[1] This could have been a saving factor for New Mexico; many runs could have been averted had there been a ready market in which the banks could have sold their secondary reserves. The crisis could have been cushioned if there had been more of this sort of investment, and less of loaning to the general public. By June 30, 1929, the ratio of loans to investments was down to 1.7, which is quite a remarkable recovery; but, of course, there were only 52 banks left in the state. The weak had been weeded and the lesson learned, but the cost had been high.

Also of note in this period is the fact that only five banks in the State of New Mexico were members of the Federal Reserve System, though the system was by now almost ten years old. The disadvantage of not being able to call on a strong central bank for support caused a critical shortage of funds. It took only a short run for most of New Mexico's banks to be depleted of cash for their customers. Correspondent banks were too far away to be of effective help in stemming the tide. Had some of the banks been able to discount some of their farm paper at the Federal Reserve Bank, they might have been able to emerge whole from the emergency. Unfortunately, this outlet

---

[1] Ibid., Federal Reserve Board of Governors, Banking and Monetary Statistics.

was not available to most of New Mexico's banks. Writing in 1931, Professor Thomas L. Popejoy of the University of New Mexico recommended as a must for the future of New Mexico banking, that more of her banks become members of the Federal Reserve System.[1]

THE SITUATION IN ALBUQUERQUE

The population of Albuquerque in 1920 was about 25,000.[2] The city was served by no less than five banks. These were the State National Bank and its affiliate, the State Savings Bank and Trust Company, the First National Bank and its affiliate, the First Savings Bank and Trust Company, and the Citizens National Bank.

Albuquerque was hit hard by the depression, and by January 1, 1924 only two of its banks were still in operation: the First National Bank and its affiliate. Five had been too many banks, even for the state's largest city.

But one bank was obviously not enough. The city, if it was to continue its growth, must have another bank. Led by Mr. George A. Kaseman, five businessmen of the city resolved to form a new bank to fill the gap. The new bank would have a beginning capitalization of $250,000.00 divided into 2,500 shares of common stock of $100.00 par value, all of which was to be issued. The five men subscribed to the stock as follows: Mr. Kaseman, 1,765 shares, Mr. William C. Reid, 25 shares,

---

[1] Popejoy, op. cit., p. 32.

[2] Bureau of the Census, Seventeenth Report, 1930.

Colonel George E. Breece, 500 shares, Mr. Owen M. Marron, 200 shares, and Mr. Joseph D. Waters, 10 shares.[1]

The new bank was not to be erected over any of the organizations which had passed on. In fact, it was made abundantly clear in the newspaper advertisements announcing the new establishment, that the new bank was to begin completely from scratch, and that its assets were to be totally separate from any of its predecessors.[2]

It is obvious from the distribution of the bank stock that Mr. Kaseman was the driving force behind the new bank, and he was chosen as its first president. Colonel Breece, who was in the lumber business locally, was elected Chairman of the Board of Directors, which was composed, quite naturally, of all five of the stockholders.

On January 18, 1924, the Albuquerque National Bank was granted its national charter, and on Monday, January 21, 1924, officially opened its doors for business. The quarters of the new bank were the former quarters of the defunct State National Bank, but as was reiterated time and again, this was a new bank.

There almost seems to be too much made of this fact (that it was a new bank) at the time. And yet, one can well imagine that it was not the best of atmospheres for the launching of such an enterprise. The citizens of Albuquerque had experienced

---

[1] Organization Agreement, as recorded in the minutes of the first meeting of the Board of Directors, January 14, 1924.

[2] Albuquerque Journal, various issues, January, 1924.

more than their share of the depression, and they could hardly be expected to be anything but wary of a new and untried institution, considering the fate of her predecessors. Both of the banks which had been closed were in the hands of federal receivers. An effort was being made to satisfactorily liquidate the assets of these banks at this very time. Many of Albuquerque's citizens had been depositors in these banks, and were understandably rather uncertain about the new organization.

The Albuquerque National Bank was determined to profit from the experience of the city's other banks, however, and from the beginning, the policies of the new bank were marked by concern for safety above all other considerations. The bank actually met a warm reception from the people of Albuquerque. Mr. Kaseman, born in Shamokin, Pennsylvania on July 5, 1868, had been a citizen of Albuquerque since 1891.[1] He was a well established member of the community, and the community felt justified in placing its confidence in him and in the bank which he was creating.

One of the first tasks faced by the Albuquerque National was to help the depositors and stockholders of the banks which had failed to find a satisfactory solution to their dilemma. The receivers of both banks came to the new bank for assistance.

At the suggestion of the receiver of the Citizens National Bank, Mr. David Cowan, a committee of the directors of the

---

[1] Eulogy to Mr. Kaseman, Board minutes for June 29, 1938.

Albuquerque National met with a stockholder's committee of the Citizens Bank. At the meeting, mediated by Mr. Cowan, it was proposed that the new bank take over the sound assets of the old. Many meetings followed in the next two weeks between these two groups, as they attempted to come to a conclusive agreement as to which assets were actually sound. The agreement was finally reached, however, and the Albuquerque National agreed to take over the assets so determined, and in exchange, pay the unsecured creditors of the Citizens National $0.70 on the dollar for their claims. This agreement was consummated on April 28, 1924.[1] The long expensive process by which a bank is ordinarily liquidated had been averted. In a little over three months from the date of its closing, the depositors of the Citizens National Bank had been repaid, probably at a higher percentage than they had expected.

Included in the agreement was a provision whereby the stockholders of the Citizens National agreed to purchase $50,000 worth of common stock in the Albuquerque National, which would increase its total capitalization thereby to $300,000. Two representatives of the stockholders of the Citizens Bank, in return, were to be elected to the Board of Directors of the Albuquerque National Bank. In addition, the Albuquerque National was to take over and occupy the quarters formerly occupied by the Citizens National Bank. The agreement was then approved by the Citizens' stockholders and the

---

[1]Board minutes, Albuquerque National Bank, April 28, 1924.

Comptroller of the Currency.

Representing the stockholders of the Citizens National in these negotiations were four men who were to play major roles in the operation of the Albuquerque National in the days to come. These four were Mr. Fred Luthy, who eventually became president of the Bank, Mr. John P. Simms, who was Chairman of the Board in the nineteen-forties, and Mr. D. A. Porterfield and A. L. Martin. Mr. Martin and Mr. Porterfield were the two men elected to the Board of the Albuquerque National to fulfill its part of the agreement.

At this same meeting, Chairman Breece stated that the policy of the new bank would continue to be one of restraint on loan volume. Prime consideration was to be given to making the Bank a sound financial institution. Only after this had been achieved, and the depositors assured of the safety of their funds, could attention be turned to accommodating their credit needs. Albuquerque would best be served, in the long run, by a bank which had made itself strong enough to withstand a repetition of the crisis, should it occur.

As a further "protective investment" the bank purchased an additional $100,000 worth of Liberty Loan bonds, using the funds made available by the merger.

On July 31, 1924, an examination of the assets of the State National Bank was begun, with an eye toward reaching the same sort of agreement that had been reached with Citizens National Bank. However, this project never reached fruition. One gathers from the newspaper reports of the day that a great deal

more controversy surrounded the closing of the State National than was true of the Citizens Bank. The stockholders and creditors of the State National were having a difficult time reaching any sort of agreement, and the Albuquerque National was understandably reluctant to involve itself in the dispute over the distribution of the State National assets.

On August 9, the stockholders' committee of the State National made public a letter to the Albuquerque National Board, asking that all action on the proposed assumption be deferred until the final report of the federal examiners was in the hands of the public. Colonel Breece, at the meeting of August 9, mentioned that rumors were in circulation in the city to the effect that the proposed assumption was being undertaken with the thought of forestalling a thorough investigation of the closed bank by the federal authorities. In order that the people should not get the wrong impression of the role being played by the Albuquerque National Bank in the liquidation, Colonel Breece made public a statement of policy on the matter. It ran, in part, as follows:

> The Albuquerque National Bank was organized to be as helpful as it could, consistent with sage banking practice, to relieve the condition created by the local bank situation. It was and is necessary to give to it, and maintain in it, the strength of a large, clear capital, unburdened and unimpaired by the conditions of the past three years. This status of a strong, safe, sound bank must, and will be, maintained.[1]

The Albuquerque National would not get involved in the

---

[1] Albuquerque Journal, August 10, 1924.

assuming of assets which had any taint of the conditions which had gone before. The assumption of the State National's assets is never again mentioned in the minutes of the Albuquerque National's board meetings. The subject was summarily dropped.

On September 25, 1924, Mr. Roy McDonald, who had been a Vice President and the Cashier of the Bank since its inception, announced his resignation, to assume a position in a California bank. Fred Luthy was appointed to take his place, with the same titles and duties. Then, on October 24, Owen M. Marron resigned from the Board of Directors, and at the stockholders' meeting of January 13, 1925, Mr. Luthy was elected to assume the vacancy on the board.

EARLY INVESTMENT POLICIES

The investment account of the Bank in its early days, in accordance with its announced conservative policies, was made up entirely of United States Government Bonds. The first purchase, reflected in the first Statement of Condition, on March 31, 1924, was of $200,000 worth of Liberty Loan Bonds. Though the actual acquisition cost is not available, all the Liberty Loan Bonds then outstanding were selling at a premium, the Third Liberty Loan 4½s, yielding about 3¾.[1]

As mentioned above, this investment was increased by $100,000 after the acquisition of the Citizens National's assets.

---

[1] C. F. Childs & Company, Concerning Government Securities (Chicago: Lakeside Press, 1947), p. 157.

In the country itself, money rates were low. Banking institutions were competing with strong corporations for the purchase of Governments, and both would have welcomed new issues on the part of the U. S. Treasury. But the Treasury was not in need of funds. In fact, it was the announced policy of the Secretary of the Treasury, Andrew Mellon, to reduce the federal debt as much as possible year by year. Public debt was too high, Mr. Mellon felt, and it should be reduced each year out of the surplus which the Treasury was accumulating out of current revenues.[1] In the fiscal year 1924, Mr. Mellon succeeded in reducing the gross federal debt by almost 2 billion dollars ($1,098,894,375.00, to be exact). Particularly, Mr. Mellon was interested in retiring those bonds which carried the circulation privilege. These were bonds which could be pledged by national banks to the Treasury against the issuance of national bank notes. By consolidating the issuance of currency in one federal agency, Mr. Mellon felt that the government would have much greater control over the amount of currency outstanding, and would be better able to restrict and expand the currency supply as the need should arise.

Many bankers criticized the purchases of Government Bonds in the open market by the Treasury and Federal Reserve System, at a time when money rates were low, and idle funds abundant in the country's banks.

On October 25, 1925, the Cashier of the Albuquerque

---

[1] Ibid., page 157.

National Bank was authorized to purchase $250,000 worth of circulation bonds and to deposit them with the Treasury Department. Thus, the bank would take its place among all national banks of any size, in having its own currency outstanding, signed by its own Cashier.

But if one believed the official voice of the federal government, in the person of the Secretary of the Treasury, the circulation privilege was in its dying days. Again, in his annual report for the year 1924, Secretary Mellon had recommended retiring all the national bank note currency then in circulation by the simple process of calling all the bonds which carried this privilege. This time, the Secretary gave some cogent reasons for this action, among them, bond secured currency was inelastic and unresponsive to the needs of business and commerce; national bank circulation was no longer necessary in view of the ability of the Federal Reserve to issue Federal Reserve Notes when needed; and lastly, the value of the circulation privilege to national banks was more sentimental than material.[1]

Despite the logic of the Secretary, it was almost a decade before the circulation privilege was taken from the national banks. The youngest national bank in New Mexico showed foresight by purchasing these bonds in the light of such a statement by the Secretary of the Treasury. Sentimental value it may have been, but it was not a very prestigious national

---

[1]Annual Report of the Secretary of the Treasury, 1924.

bank which did not have its own currency outstanding in the late 1920's.

This same month of October, 1925, the directors authorized the purchase of the banking quarters, which they had been leasing, at Second and Central. The Bank's headquarters have remained there, in downtown Albuquerque, ever since.

In September, 1925, the Bank had purchased $50,000 of Phillipine Islands 4's, for the purpose of securing Postal Savings deposits. This purchase was not disposed of for ten years, and served the same purpose until it was sold in December, 1935.

Up until 1926, the Bank's investments had been primarily applied to a given purpose, as above. In that year, the bond account began to be diversified a bit more and, for the first time, purchases of other types of investments than U. S. Governments began to appear in the statements. The Bank acquired, during the year, some $111,993 of "Other Bonds." These included $62,300 worth of City of Albuquerque bonds, along with other municipals, in addition to some public utilities (primarily railroads), and other corporates.[1]

For the first time, the percentage of Governments in the bond account fell below 100 percent. In the Statement of Condition issued for June 30, 1927, the Bank listed total investments of $1,081,358. Of this total, government issues amounted

---

[1]Statement of Condition, December 31, 1926.

to $898,066, or 83 percent.[1] The national average for the same call date was 40.5 percent.[2] Naturally, an incipient bank would be expected to possess a different composition of investments from the average of commercial banks nationally. Nationally, the tendency was to take advantage of the higher income rates available in corporates and municipals. This was the prosperous 'twenties and "normalcy" had returned to America. Permanent prosperity, it seemed, was just around the corner.

The government issues which had comprised the whole of the bond account for these first years had primarily been long term issues. Some Certificates of Indebtedness had been held, as well as some short term notes, but on the whole, these had been disposed of at maturity. On the call date in 1927, the Governments consisted entirely of Liberty Loan Bonds and other long term issues.

Through the late 1920's, the Bank's investment account shows a steadily decreasing percentage of U. S. Governments. Never did this percentage approach the national averages, however. (Only twice in the Bank's history have Governments made up less than 50 percent of the bond account. These were in June, 1931, and again in October, 1934. On this latter date, it reached the lowest percentage ever, 47.2, when the national

---

[1]This total does not include the $250,000 Consol 2's purchased to secure circulation.

[2]Board of Governors of the Federal Reserve System, 1941, Banking and Monetary Statistics.

averages were hovering between 40 and 43 percent).

Of course, there was a very pertinent reason why banks in general, and the Albuquerque National in particular, showed these decreases in government purchases. The federal government, under Secretary Mellon, was still pursuing its policy of reducing the national debt. Thus, each year, there were correspondingly fewer amounts of government securities outstanding and available for purchase. In 1927 alone, retirement of public debt made over a billion dollars available for investment in municipals and corporates.[1] Every type of investment bond other than federal governments had been increasing in amounts. Railroads, utilities, municipalities, and industrial corporations all were taking advantage of the large supply of loanable funds available.

In 1928, money rates reached the highest levels in seven years, and a new kind of loan began to take up a large portion of bank loan accounts: the "security" loan, or "loans to brokers." People were borrowing from banks to invest in the market, at what they hoped would be a higher rate of return than the interest they would have to pay the bank.

These bank customers were not the only ones trying to take advantage of the situation. In the annual report of the Federal Reserve Board of Governors for the year 1927, there appears some concern over the tendency of some banks to borrow from the System when it was not necessary for them to do so. The Board

---

[1]Childs & Company, op. cit., p. 171.

of Governors defined as a basic principle that Reserve Bank credit was not to be used for profit, and that continuous indebtedness to the Federal Reserve Banks was an abuse of Reserve Bank facilities. The country was riding the crest of the speculative wave. Even some banks had joined in the speculation in the stock market, if credence can be given to the warnings and apparent beliefs of the Board of Governors.[1]

A SOUND BANK EMERGES

Meanwhile, the Albuquerque Bank was consolidating itself as a permanent institution in the city of Albuquerque. In 1925, the Bank had applied for the powers of a fiduciary. These powers were granted by the Comptroller of the Currency, and in January, 1927, the Bank organized its Trust Department. The first Trust Officer was Fred Luthy, and his Assistant Trust Officer, Oscar M. Love. In October, 1928, the stockholders approved a change in the name of the Bank. In order that its added services should be better known to the public, it would henceforth be called the "Albuquerque National Trust and Savings Bank."

By December, 1929 the Bank had made sufficient purchases of other bonds to reduce the percentage of U. S. Governments to 64.7. Included in these purchases, in addition to U. S. municipals and corporates, were some $20,000 in the issues of foreign governments,[2] -- a class of securities that was to

---

[1] Annual Report of the Board of Governors of the Federal System, 1927, p. 67.

[2] Pertinent Statements of Condition, December 31, 1929.

suffer in the economic collapse of the 'thirties. The Albuquerque National, though it did make this investment and other small purchases of these securities from time to time, was indeed fortunate that it chose to keep this sort of investment to a negligible portion of its total investment account.

In early 1929, in response to demand from banks for additional issues of the federal government, a new type of government security was introduced. This was the Treasury Bill, a very short term issue designed to give banks another outlet for their secondary reserves. It was to mature in less than one year, but the Treasury Department quickly established the policy, still followed, of issuing them for ninety-one days. The Albuquerque National did not take advantage of this new security for some time, however, and remained primarily in the long term market.

For the 31st of December, 1929, the government bond account was equal to 32.1 percent of total deposits, while the total account was almost 50 percent of total deposits.

Thus, as the 1920's ended, and the 1930's began, the Bank found itself in a position of relative liquidity. This position was to stand it in good stead in the days to come. The circumstances which brought about the founding in one depression of the Albuquerque National Bank, were to have their brighter side in the much more devastating and widely felt collapse which befell the United States in the early 1930's. The Albuquerque National Bank had spent the six years prior to 1930 striving to avoid the faults which had been shown to exist among

New Mexico banks in the early 'twenties. When the more severe depression of the 'thirties came along, it found itself in a stronger position than the average bank.

It was as though the depression of the 1920's had served as a vaccine for the more serious illness which struck the national economy in the 1930's. The Albuquerque National Bank had been vaccinated.

CHAPTER III

THE GREAT DEPRESSION

> The weakest spots in our banking and business structure have been eliminated.
>
> Ogden L. Mills, April, 1932[1]

> The Administration has infected the Central Government with the fatal germ of financial socialism.
>
> Carter Glass, November, 1932[2]

In the year 1930, 1,345 banks suspended operations in the United States.[3] This was a record high, and included some very large banks which found themselves driven to the wall. Also in 1930, money rates reached their lowest levels since the end of the war in 1919. Short term rates fell to ½ of 1 percent, as banks and other corporations sought liquid securities in which to place their excess funds. Almost every bank in the country possessed excess reserves — indicating inactive demand for credit on the part of the public, and general lack of confidence of the banks in most investment securities.

---

[1] From an address by the Republican Secretary of the Treasury, April 25, 1932.

[2] From an address by the Democratic Senator from Virginia, November, 1932.

[3] Banking and Monetary Statistics.

The rate of interest paid on time deposits fell throughout the country, also due to the large supply of funds on hand in the banks.

The constriction of business activity also caused the first deficit in the U. S. Treasury budget since 1919. The Treasury found that it could issue new bonds at a rate of 3 percent; this was the lowest rate for a new offering since the Panama Canal 3's of 1911. Certificates of Indebtedness fell to 1-7/8 percent and then to 1-1/8 percent. This again would indicate that the banks preferred the short term issues as a measure for achieving liquidity.

So those banks still in operation were endeavoring to profit from the example of those banks which had failed to give liquidity prominence in their bond accounts — and there were plenty of examples to be seen. In the year 1931, 2,298 banks suspended operations, with total assets of $1,691 million; again a record number.[1]

What of Albuquerque and the Albuquerque National? With the crash of the stock market in October, 1929, and the events of the following months, it became increasingly clear that a major crisis was in the making. Every bank was doing its best not to become a statistic in the suspension column. All were striving to become as liquid as possible, and the Albuquerque National Bank was no exception.

In early December, 1932, the Bank was examined by the

---

[1] C. F. Childs & Company, op. cit., is the source for most of the statistics in this and the preceding paragraph.

federal bank examiners, and found to be in an adequate position of liquidity. The examiners had not required any charge-offs on the bond account. The board itself, however, was not satisfied. The investment policy of the 1920's, during which time the Bank had stayed primarily in long term issues, had caused some depreciation in the account as prices fell after 1929. The market value of the account was "considerably less than the book value," read the minutes. It was felt by the board that inasmuch as the bonds represented the secondary reserve of the Bank, some adjustment should be made to bring the book value more into line with market value. Since undivided profits at the time were not sufficient to cover the charge-off, President Kaseman offered a rather unique solution: He would give the Bank his personal note for the amount of the charge-off, thus permitting the face value of the more doubtful issues to be charged off completely. His offer was accepted, and the following issues were completely deleted from the Bank's investment account: $5,000 City of Buenos Aires 6½'s, $7,000 Chicago and Northwestern Railroad 4½'s, $7,000 German P. and C. 6½'s, $7,000 Missouri Pacific Railroad 5½'s, and $3,000 Susquehanna Silk Mills 5's. Mr. Kaseman's note was to be paid out of any recoveries on these charged-off assets.[1]

The Bank was fortunate that, faced with such a situation, there was available a man who was both financially able and

---

[1] Minutes of the Board of Directors' meeting, December 9, 1932.

willing to do this. Certainly, no one at the time could be sure that Mr. Kaseman would not have to pay this note out of his private assets. Railroad and foreign issues at the time were in particular disrepute; most of them having suspended interest payments entirely. Eventually, Mr. Kaseman was repaid in full out of the recoveries on the issues, and the matter turned out well for all concerned.

This was the financial picture of 1931 and 1932. The future was uncertain, but indications were hardly favorable. The Albuquerque National, as this incident illustrates, was putting itself in a position where there could be no doubt of its ability to carry on operations should the national situation get any worse. And the national situation steadily got worse — much worse.

THE NATIONAL BANKING CRISIS

In the latter part of 1932, money rates reached lower levels than they had in the summer of 1931. The nation was deluged with credit while lacking the confidence to use it. This time, U. S. Government Bills went down to .09 percent. (On May 5, 1932, 60-day Bills were selling at a yield of .05 percent.)[1] Such was the demand for liquidity. To the banks, yields were of slight importance. Funds were virtually being warehoused, without charge or revenue, solely for protection and safety.

---

[1]Childs and Company, op. cit.

With the country showing such a lack of confidence in its banks, it is no wonder that bankers were worried. A crisis seemed almost inevitable. On February 13, 1932, President Hoover had appointed a new Secretary of the Treasury, Ogden L. Mills, in an attempt to restore confidence in the monetary system.[1] Mills had been Secretary for a year and a day, when the long-expected crisis began.

On February 14, 1933, all banks in the State of Michigan were ordered to close their doors. Using his executive powers, Governor William A. Comstock, in a completely unprecedented action, declared an eight day banking holiday for all banks in his state. The immediate effect was the paralysis of $1,500,000,000 of deposits in one of the country's most important industrial states.[2]

Such drastic action was quick to have its effect in other sections of the country. The securities markets were sharply depressed. Volume ran high in both stocks and bonds, and all averages were off. For the next two weeks, the government bond market fell one to two points per day, as banks, the principal sellers, raced to sell their prime securities to get cash to meet the demands of frightened depositors. The

---

[1]Andrew Mellon, whom Mills replaced, had been Secretary for eleven years, and had served under three Presidents. He was to be surpassed in longevity only by Henry Morgenthau, Jr.

[2]Most of this outline of the national banking crisis is taken from the account of C. C. Holt and N. Keith in their book, 28 Days, A History of the Banking Crisis. The authors, both writers for the Wall Street Journal at the time, have given a tense, on-the-scenes account.

public was shocked and frightened; confidence in the banking system was practically nil.

On February 24, the State of Maryland followed Michigan's example and declared a bank holiday. The same day in Ohio, several banks in Cleveland and Akron announced that withdrawals would be allowed on a restricted basis only. The rash of bank holidays spread; Indiana, Pennsylvania, Kentucky, and Tennessee all had full or partial bank closures by March 1. On March 2, eight more states took action. These included Oregon, Washington, Utah, Texas, Idaho, Wisconsin, and Georgia. The other state which suspended all banking operations on March 2, 1933, was New Mexico.

On March 3, New York and Illinois succumbed, and the country's financial centers, New York City and Chicago, were without banking facilities. The banking system of the United States had ground to a complete standstill.

THE NEW ADMINISTRATION

On Saturday, March 4, 1933, Franklin D. Roosevelt was inaugurated as President of the United States. On Sunday, in his first official act, he declared a nationwide banking holiday, to last from Monday through Thursday. The banking collapse was official and complete. In the intervening four days, legislation would have to be passed to relieve the situation. During those four days, the new Secretary of the Treasury, William H. Woodin, issued a series of regulations giving the public at least partial use of its banks. These allowed access to safe deposit boxes (Monday), the cashing of checks drawn on

the Treasurer of the United States (Tuesday), and on Wednesday, banks were allowed to make change, and to accept new deposits to be held in trust, separate from the impounded deposits. These were all rather limited operations, and for most of the country, it was a bankless week.

The issuance of scrip was considered, in some manner or other, by all cities of any size. Pressure was great to give the people some sort of medium by which normal exchange could be carried on. But heavy resistance to scrip was also felt. In Washington, arguments were being advanced pointing out that if scrip was issued in volume, it might drive out the regular currency. The drive against scrip was being waged by those who felt that what was needed was restoration of the potency of the check as medium of exchange, based upon re-establishment of confidence in the nation's banking system.

Scrip lost out in the end. Instead, banks were authorized on Thursday, to release cash in limited amounts to those whom the banks felt had a "legitimate need for currency." The result of this sort of rule was that depositors could, or could not, get cash, depending upon the individual bank's interpretation of the regulation. The government did not state what it considered a "legitimate need" to be.

On Thursday, the last day of the scheduled holiday, Congress met in emergency session and rushed through remedial legislation in an attempt to let the banks re-open on Friday, March 10.

Despite the speed of congressional action, the President

was forced to announce on Thursday night that the banks would remain closed for an indefinite period. The law provided that the procedures for re-opening the banks would be determined by the Secretary of the Treasury; and the Secretary must be allowed some time to lay down the procedure to be followed.

In the new banking law, President Roosevelt was given what amounted to dictatorial powers over the nation's banks. The emergency was likened to a wartime emergency, and the President was given wartime powers. As in World War I, the President was given authority over all credit, currency, and gold and silver transactions; and to restrict the banking business of Federal Reserve members in any way he chose. The Comptroller of the Currency was authorized to appoint a "conservator" for any national bank deemed insolvent and provisions were made for the reorganization of national banks.[1]

The law further gave the President power to expand the currency should the need arise, by providing that any Government bonds, deposited with the Federal Reserve System, should be exchangeable 100 percent for new currency, and that notes, drafts, bills of exchange, and banker's acceptances should be exchangeable for new currency at 90 percent of par. By new currency was meant the currency backed by the credit of the United States. It was no longer exchangeable for gold. The law prohibited the public from even holding gold.

The bill had passed the House of Representatives in less

---

[1]Note the word "conservator." It was coined in this law, to replace the harsher, more fearful word, receiver.

than an hour, and had been sent on to the Senate. The Senate took a little longer, but in only seven hours all told, the country had legislation which the lawmakers hoped would enable the banks to resume their normal functions.

On Monday, March 13, the banks began to be re-opened. The first to be allowed to open were national banks in the twelve Federal Reserve Bank cities. The next day, they were re-opened in those cities with an organized clearing house association; and by Thursday, March 16, 1933, any bank in the country, which could obtain its license from the Comptroller of the Currency (by showing that it was solvent), was allowed to open its doors.

The banking crisis was not over, and the depression had many dark days yet to come, but at least the banking system was functioning once more. The country slowly regained confidence in its banks, at least those which had been allowed to re-open.

Industry itself was stagnant in the country. It had been since the election of Roosevelt, as the country awaited his inauguration and his efforts to relieve the situation. In February, 1933, unemployment was estimated at 14 million, a new high. In the securities market, municipals were selling at their highest yields ever (or their lowest prices), and many cities had to default entirely, unable to meet their interest charges.[1]

---

[1] C. F. Childs and Company, op. cit., p. 214.

On June 16, 1933, the Congress passed the National Industrial Recovery Act, providing for the setting of prices and quotas for almost all industries, by the industries themselves. A quasi-socialistic revolution was being launched; the United States was to have a "New Deal," a planned economy.

It was a time of great change in the social patterns of the United States. No institution, however well established, was sacred in the attempt to end the business depression. Any solution was worthy of a try, and the nation's economy was subject to almost any experimentation.

NEW MEXICO

In New Mexico, as elsewhere, the banking crisis had hit hard. All banks in the state had been closed by executive order of Governor Arthur Seligman, on the second of March. On March 3, the New Mexico legislature passed Senate Bill S-40, approving the action of the Governor, and he then extended the holiday until March 7. By the time this second holiday had expired, the President had closed the banks.

As the Governor's proclamation was worded, banks in the state had the option of closing entirely, or remaining open but allowing only a 5 percent withdrawal of deposits. New Mexico banks were allowed to accept new deposits, in segregated trust accounts, at all times during the holiday. For the following two weeks, New Mexico bankers struggled with the task of re-opening the banks as soon as possible while doing all they could to serve the people without a banking structure.

On Friday, March 3, 1933, the Albuquerque National Bank received two wires from the State Bank Examiner in Santa Fe. In one, the bank was advised of the action of the legislature of that day, and of the extension of the holiday by the Governor. The text of this wire is worthy of recording, since it gives the reasons for the closing of New Mexico banks. It ran as follows:

> Governor Seligman issues proclamation mandatory order bank holiday March Third Fourth Sixth and Seventh STOP This step unavoidable since action of other states involving reserve centers STOP The financial condition in New Mexico is sound and there is every reason to believe the situation will be clarified in a few days.[1]
>
> John Bingham, State Bank Examiner

It indicates that when such a crisis hits the major financial centers of the country, that the banks in other, more remote areas, dependent on these centers for clearing operations and other functions, have little choice than to close up shop also. A flare-up such as occurred in Detroit, spreads rapidly, given the proper national state of mind, and it is not long until the entire country feels its ramifications. Certainly, a state such as New Mexico cannot long carry on normal banking without the services of the financial centers.

The second wire received that day by the Albuquerque National called a conference of all New Mexico bankers, in the capitol, for Sunday, March 5. Together, they would attempt to find a solution for the difficulty.

It was a time when normal communications would not suffice.

---

[1]Original in files of the Albuquerque National Bank.

Decisions by those in authority were being made not day by day, but hour by hour, and the wire or telephone call replaced the normal mails.

The Governor's conference in Santa Fe on Sunday resulted in a decision to attempt the re-opening of the banks, at least partially. Most banks would pay out some funds, to those whom it was felt had a "legitimate and immediate need for currency," and would continue to accept deposits on a trust basis. There was also much discussion about the advisability of issuing some sort of scrip, particularly in the larger cities, where many working people would be hurt by the cessation of their paychecks.

On this basis, the banks of New Mexico would re-open their doors Monday morning. Driving home from Santa Fe, the bankers of Albuquerque knew they had a long night ahead of them. Much work had piled up while the bank was closed. Thousands of checks drawn on banks, now closed, had been returned, and now had to be charged back to those who had deposited them. It would be necessary to work all night Sunday if the banks were to be re-opened Monday.

They were still working at the Albuquerque National at 4:09 A.M., when the Postal Telegraph Company delivered another wire from John Bingham.

The President had declared a national bank holiday, beginning with this Monday, March 6, through the following Thursday. To quote Mr. Bingham once more:

> . . . Follow instructions prepared by bankers committee Sunday afternoon except do not pay out any

currency until fully advised of text and meaning of President's proclamation.[1]

New Mexico's banks would not re-open that Monday morning.

Meanwhile, the business of the city of Albuquerque was at a standstill. Payrolls could not be met. Nobody could cash a check. Currency was driven from commerce, as people began to hoard it along with gold. No one could guess how long the present situation might last. What little cash people happened to have in their possession on Wednesday, March 1, might have to last for long weeks.

The need for a medium of exchange was thus felt in Albuquerque, as well as in the larger cities of the country. The bankers of the city began to petition the federal government for authority to issue scrip as soon as it began to appear that it might be ten or fifteen days before banking could be resumed. On Friday, March 10, following the President's announcement that the banks would be closed for an indefinite period, the Albuquerque National Bank and the First National Bank, in a joint wire to the Chief National Bank Examiner, asked permission to issue scrip in small denominations, up to $20.00. This was necessary, said the wire, for the protection of the little people of the city who depended on a weekly paycheck for their livelihood and who now faced a week without groceries, unless they could be given some method of paying for the necessities of life.

Another consideration made Albuquerque banks vitally

---

[1] From the original in the files of the Albuquerque National Bank.

FIGURE 2

$10.00 CLEARING CHECK $10.00

ALBUQUERQUE NATIONAL TRUST & SAVINGS BANK
Albuquerque, New Mexico

PAY---------- TEN DOLLARS ----------TO BEARER

Subject to the terms and conditions printed on the reverse hereof.

#0000

ALBUQUERQUE NATIONAL TRUST
& SAVINGS BANK

By_____
CASHIER

(Reverse side)

THE PRESIDENT OF THE UNITED STATES, having by proclamation, on March 6, 1933, called upon all national and other banks to prevent the hoarding of currency, this CLEARING CHECK is issued pursuant thereto by the within bank. It is designed to be used as a medium of exchange, and the faith and credit of the issuing bank is pledged for its redemption. It will be accepted at face value, without interest, in payment of any obligation of the holder to the bank which issued it, and may be deposited therein for the credit of the bearer, but will not be redeemed in currency until such time as the duly constituted authorities shall authorize and permit the same to be done, and then in conformity with such rules and regulations as may be made. It requires no endorsement, but passes by delivery only.[1]

Above is a facsimile of the scrip[1] which was considered by the Albuquerque National Trust and Savings Bank at the time of the banking crisis. It was never issued in Albuquerque, nor was any other scrip issued in the United States, by any bank, at this time.

---

[1]Taken from the draft copy prepared by the Albuquerque National Trust and Savings Bank. Original in bank files.

interested in some sort of scrip arrangement. Albuquerque was two days, at least, from a Federal Reserve Bank, and although ample currency was on hand to meet normal demand, a serious drain upon re-opening might prove embarrassing before new supplies of currency would be brought in. With the public in a doubtful state of mind, even a short delay would precipitate drastic and unnecessary results.

The request to issue the scrip (which was actually in the nature of a bank Cashier's Check) was never answered by the authorities. The President's announcement of Friday evening, that the banks would begin to re-open Monday morning, made the question of scrip academic and its issuance unnecessary.

On Wednesday, March 15, 1933, the Albuquerque National, having applied for and received a license from the Comptroller of the Currency, re-opened its doors. On the following Monday, March 20, the First National Bank of Albuquerque resumed operations and Albuquerque's banking facilities were back on a normal basis. The national banking crisis was over, and so, it seemed, was Albuquerque's,-- but the city's banking structure was not yet out of the woods.

CRISIS -- AGAIN

The First National Bank's affiliate, the First Savings Bank and Trust Company (a New Mexico State Bank), had been granted permission by the State Bank Examiner to re-open at the same time as the parent organization, and had done so. They

had been in operation for less than a month, when crisis returned to Albuquerque in a new form.

Mr. J. Ed Cox, Cashier of the First Savings Bank and Trust Company (and a Vice President of the First National Bank), was found dead in his home one morning. The next morning the State Banking Department announced that the First Savings Bank would suspend operations pending an examination by that office of the Bank's assets. A few days later, the same announcement was made for the First National Bank of Albuquerque. They, too, would close pending an examination by the federal authorities. It was subsequently announced that though discrepancies had been found in the books which had been Mr. Cox's responsibility, the total amount would not exceed his $100,000 banker's bond.

Eventually, the First National Bank was placed in the hands of a federal conservator, and was reorganized under the name of the First National Bank in Albuquerque.[1]

Thus, for six months in 1933, the city of Albuquerque had only one bank, the Albuquerque National Trust and Savings Bank. During this time, the Albuquerque National attempted to be of help in any way it could in reorganizing the closed bank, proposing a plan, at one time, to take over its assets. This offer, and others, were mostly of a temporary nature designed to get the closed bank back on its feet. The Albuquerque National recognized the fact that a city of Albuquerque's

---

[1] From the Albuquerque Journal, April, 1933, et seq.

size and potential needed at least two banks; after the crisis had passed, it would have been an easy task to raise funds for organizing another national bank in Albuquerque.

What of the Albuquerque National's liquidity position? On December 31, 1932, the Albuquerque National showed total securities held of $1,140,292.00, compared with deposits of $2,372,085.00 -- approximately 49 percent of deposits in investments. This was about average for the entire country, which had 48 percent deposits in investments. At the same time, the U. S. Government securities made up 42.1 percent of the total bond account, while the national average was also about 48 percent. The liquidity picture of the Albuquerque National was about average, neither abnormally liquid nor abnormally slow.

In six months, the picture changed completely. By the time of the next call on June 30, 1933 (the normal March call was not made in 1933), the investment account totaled $1,432,688.00 against deposits of $3,350,869.00, or about 43 percent. This figure was down some because of the sudden increase in deposits (a result of the fact that there was only one bank in the city at this time). But of this total investment account, $755,528 was now invested in U. S. Governments. This was 52.7 percent of the account, and was an increase of more than ten percentage points from the 42.1 of the December, 1932 report.

By the end of 1933, this percentage was up to 55, and it continued to rise thereafter. It should be mentioned

again that the percentage of U. S. Governments to total investments in December, 1932 was a record low for this ratio in the history of the Bank. Never had it been so low before, and it has never been so low since. In fact, in March, 1934, it reached a new high of 60.5 percent, and again in June, 1935, another new high of 75.0 percent.[1]

And so the year 1933 marked a turning point in the investment picture of the Albuquerque National Bank, as it did in investment thinking for all banks in the country. From then forward there would be more and more emphasis on liquidity in the bond account. The U. S. Government Bond would become the prime, and eventually, for the Albuquerque National, the sole outlet for investment funds. Of this more will be said in a later chapter.

AFTER EFFECTS

The multiple crises presented to the banking world in the spring of 1933 eventually passed. The problems which had created them, however, would take a much longer time to solve.

For one thing, the depression was still very much present. A lack of demand for funds had reached the point where almost every bank in the country had more cash on hand than it could use. At the end of the year 1934, the Albuquerque National Bank, for one, had almost exactly 50 percent of its deposits

---

[1]National figures from Banking and Monetary Statistics, Albuquerque National Bank figures from published Statements of Condition.

on hand in the form of cash and exchange due from other banks($2,699,283 Cash and Exchange to $5,389,615 in Deposits). It does not take a student of reserve banking to see that this was much more than would ever be needed to meet any sort of demand for cash. And yet, the investment outlets were not available.

Banks over the country were overflowing with unused funds, but private enterprise lacked the confidence and incentive to use them. The public was debt-shy, and not the least of the reasons for their uncertainty was the experimentation being carried on by the federal government.

Some of the solutions offered by the New Deal met with almost immediate public approval. The Federal Deposit Insurance Corporation, conceived in the emergency of March, 1933, was made a permanent organization in 1935. At first, all deposits in participating banks were insured up to $3,000. By stages this amount was raised to its present $10,000 level. All Federal Reserve members were required to join and subscribe to the premiums, and any other bank could join at its own option.

The New Deal is no longer with us in name, but the F.D.I.C. is only one of the New Deal's experiments which is now considered to have a permanent place in our economic institutions.[1]

---

[1] It is interesting to note that the F.D.I.C. has never paid out any funds whatsoever to any bank in the State of New Mexico, according to the F.D.I.C. Annual Report for 1957.

Another institution which served a very worthwhile purpose in these times was the Reconstruction Finance Corporation. This organization was conceived by President Hoover, and founded in early 1932. The Roosevelt Administration made it a prime instrument for preserving banks, as well as many industries in the country. The R.F.C. had been authorized by Congress to purchase preferred stock in national banks. By this method of equity financing, many banks in the country were able to obtain additional capital funds at a time when they would have perished without them, and when they were unavailable from any other source.[1]

In July, 1933, when it appeared for a time that the Albuquerque National might need additional capital funds in order to facilitate the assuming of the First National Bank's assets, the Albuquerque National considered taking advantage of the opportunity afforded by the R.F.C.

The issuance of $50,000 additional common stock and of $300,000 preferred stock was authorized by the Board of Directors. On July 15, 1933, formal application was made to the R.F.C. to buy this entire issue of preferred. Here a quirk of fate entered the picture.

This application was actually sent to the R.F.C. -- only to be returned. It had been made out on the wrong form. By the time the application was returned in August, there was

---

[1] See Jesse Jones, Fifty Billion Dollars, for an interesting history of the Reconstruction Finance Corporation.

no longer any need for the preferred stock. To quote the board minutes: "Now, in view of changing conditions, and questions and circumstances surrounding the reorganization of another national banking association in this community," the Bank's President, Mr. Kaseman, felt that it would be best to defer action on the application to the R.F.C.[1] Though the preferred was never issued, an additional $50,000 in common stock was issued in November, 1933.[2]

In July, 1933, Colonel George M. Breece, in order to devote more time to his lumber business, resigned as Chairman of the Board of Directors. In his place the stockholders chose Mr. Albert C. Simms of Albuquerque, and the Board named Mr. Simms the new Chairman.

In April, 1934, the Comptroller of the Currency, in an effort to learn more of the financial status of the country's banks, asked for a report from all national banks as to the status of their bond accounts. In the report was to be outlined the book value of all investments made by the bank, and opposite this figure was to be entered the current market value of the investments. A copy of this report, as it was filed with the Comptroller by the Albuquerque National Bank, is reproduced on the following page.

---

[1] Minutes, Board of Directors Meeting, August 9, 1933.

[2] The Albuquerque National Bank has continued to have only the one issue, common stock, outstanding to this day.

FIGURE 3

COMPARISON OF BOOK VALUE AND MARKET VALUE, ALBUQUERQUE NATIONAL BANK BOND ACCOUNT

April 30, 1934

	BOOK VALUE	MARKET VALUE
U. S. Government Bonds	$ 863,603*	$ 880,933*
Home Owners Loan Corp.	67,215	68,032
Federal Land Banks	164,662	189,337
F.R.B. Stock	10,500	10,500
States, Counties, and Municipals	400,682	404,313
U. S. Territorial Possessions	50,000	49,000
Joint Stock Land Banks	995	710
Railroads	6,670	9,677
Public Utilities	27,390	25,902
Real Estate Corporations	990	50
Other Corporations	59,398	65,690
Foreign Governments	990	547
TOTAL OTHER BONDS	789,492	824,638
TOTAL SECURITIES HELD	$1,653,095	$1,705,571

*These figures include both types of U. S. Government Bonds which the bank was then carrying, U. S. Government Bonds, and U. S. Treasury Notes. A breakdown of these two was not required by the Comptroller.

SOURCE: Original of statement filed in records of Albuquerque National Bank.

The first obvious matter of significance in the table is that the Albuquerque National's bond account, in a time of falling investment values, had held its own. The very fact that market value exceeds book value for the total account proves a prudent investment program had been followed.

The second thing to be noticed is the high percentage of government bonds. They equal 52.3 percent of the total, and for the time represent a fairly conservative investment policy. Including in this total all of the issues guaranteed by the federal government, the "Governments" total reaches $1,096,475.00, or 66.3 percent of the total account. Thus was liquidity of the secondary reserves practically guaranteed.

Even in the portion invested in "Other Bonds," the Bank could by this time show a good position. Its investments in State, County, and Municipal bonds show a slight excess of market value over book value, and its corporates show an excess of $6,292. Even its railroad bonds were up to a point where market value was greater than book value.

Shortly after this report was received, the Comptroller instituted a new, more complete form for the quarterly call statements of national banks. Beginning with the October 17, 1934 report, the investment accounts of banks would be broken down, issue by issue, with the maturity dates of each included in the report.

In 1935, the last of the Consol 2's of 1930 and Panama Canal 2's of 1911 were retired by the Treasury. These were the last bonds outstanding which bore the circulation privilege,

and by August, 1935 no more National bank notes could be issued. These bonds were retired, ironically enough, out of the appreciation which accrued to the Treasury from the devaluation of gold.

On March 19, 1935, the Albuquerque National withdrew the last of its circulation bonds from the Treasury (where they had been held as security), and on April 9, 1935 they were redeemed by the Federal Reserve Bank. Thus, they do not appear in the foregoing report.

On February 4, 1935, another and new type of government bond appeared -- the Savings Bond. This bond was to be issued in small denominations -- as low as $25.00. They would be issued at a discount and would be redeemable at face value at maturity. The bonds were not to be negotiable, but were intended for purchase by the general public, an outlet for savings to be guaranteed by the government. Said Secretary Morgenthau, "We will democratize finance."[1]

THE CRISIS PASSES

And, so, the worst crisis in United States banking history was over. The Albuquerque National, with all the rest of the banks in the country, had learned what it meant to a bank to be in a liquid position in its primary and secondary reserves. Examples of what happened to a bank not so endowed, could be seen in every state in the Union, if not in every city.

---

[1] C. F. Childs and Company, op. cit., p. 231

What were the results? For one thing, the Federal Government received (or more accurately, took) a much stronger hand in the affairs of every bank in the country. The power of the government over the nation's banks became stronger than ever before, and probably would never be relinquished.

For another, the banks themselves attained a new perspective regarding the use of their investment accounts. Only the very largest of banks would henceforth engage in the active use of the securities markets as a source of income. Those banks which were large enough to have a well staffed and well informed investment department might continue to invest substantial sums in corporate or municipal bonds; but for most banks, it meant switching entirely to U. S. Government securities. Safety, not income, the goal of the Albuquerque National Bank in the 'twenties, became the goal of all banks in the 'thirties. Few banks, other than the largest, would bother henceforth to earn any substantial portion of their income from the market.

CHAPTER IV

MORE CRISES -- LOCAL AND WORLDWIDE

The years following the banking crisis were spent in consolidating the position of the Bank, and in preparing for the future. The assets of the Bank had been increasing each year, and additional facilities had become of pressing concern. In July, 1935, negotiations were begun which led to the purchase of the furniture and fixtures of the closed First State Bank and Trust Company.

By April, 1937, the physical plant having received attention, the Board undertook a review of the bond account. The total account at this time amounted to approximately $3,600,000. This was 67 percent of the total earning assets, and 48 percent of the total deposits. Viewed thusly, the account presented a good liquidity position. These investment reserves comprised $2,100,000 in Treasury Bills, about $300,000 in short term Treasury Bonds, and $300,000 in municipal securities -- primarily of local governments.[1]

The government bond market had suffered a sharp break in March, 1937.[2] With its investment account dominantly in high-

---

[1] Board minutes for April 6, 1937. Various percentages derived from Statement of Condition for March 31, 1937.

[2] Federal Reserve Chart Book on Financial and Business Statistics, Historical Supplement, September, 1957.

grade, short term securities, the decline in longer term paper made new purchases possible on a much better interest yield basis. The Bank, in carrying a large number of low yield, short term bonds, was in a position to increase its income by lengthening maturities somewhat. Given the recent decline in "Governments," consideration might be given to a program of staggered maturities.

One such program considered by the Board was to have approximately equal amounts of bonds due each year up to ten years, and possibly some in even longer maturities. By employing one million dollars in this way, Mr. Kaseman pointed out, revenue could be increased by ten to twenty thousand dollars per year. Mr. Kaseman went on to say that this policy, if adopted, might some day be regretted, but that on the whole, no bank can select the exact time for buying a bond, and over a five year period the additional revenue should more than offset the possible decline in prices.[1]

All this had taken place in the Spring of 1937. The plan had been tentatively adopted, and during July of that year, any available cash was invested under the new plan.

And then, in the latter part of 1937, Mussolini invaded Ethiopia. Europe was thrown into turmoil, and so was the U.S. Government Bond Market. The plan, though still considered worthwhile, was temporarily deferred, "in view of the foreign situation." For the Albuquerque National Bank, this represented

---

[1] Board minutes, May 20, 1937.

the end of the "Staggered Maturities Investment Plan," as such.

But an examination of the Statements of Condition for June, 1937 and December, 1937 shows that the plan, although short lived, had its effect. The bond account did shift into longer term bonds. On June 30, the account shows $2,193,543 in Treasury Bills, $75,000 in bonds maturing within twelve years, and $96,196 in bonds maturing after twelve years. By December, 1937, Treasury Bills were down to $1,342,534; Treasury Notes, with face value of $490,000, were due within five years, and long term bonds, maturing after ten years, totaled $645,000.

By March, 1938, however, the position of the bond account began to show evidences of abandonment of the plan. Bonds maturing after 1949 dropped back to $209,000 and this $400,000 shrinkage went into shorter term bonds. Treasury Bills (although still dropping percentagewise), were replaced now by comparatively short term Notes, rather than long term bonds.

The complete story is told by the accompanying table (Figure 4), which shows the bond account for the three call dates: June 30, 1937, December 31, 1937, and March 7, 1938.

FIGURE 4

BOND ACCOUNT OF THE ALBUQUERQUE NATIONAL BANK
SELECTED DATES

	6/30/37	12/31/37	3/7/38
Treasury Bonds Maturing before 12/31/49	$ 75,000.	None	435,003.
Treasury Bonds Maturing after 12/31/49	96,196.	645,921.	209,452.
Other U. S. Bonds (Savings Bonds)	15,000.	15,000.	22,500.
Treasury Notes	319,400.	490,350.	807,427.
Treasury Bills	2,193,543.	1,342,534.	759,793.
Federal Farm Mortgage Corp.	2,900.	2,900.	2,903.
Home Owners Loan Corp.	245,446.	120,122.	116,083.
TOTAL U. S. GOVERNMENTS	2,947,557.	2,616,828.	2,829,803.
Other Bonds	525,755.	377,626.	364,120.
TOTAL SECURITIES HELD	$3,473,312.	$2,994,454.	$3,202,469.

Source: Albuquerque National Bank Statements of Condition, selected dates, originals in bank files.

THE ABRUPT END OF AN ERA

And then, the event occurred which drove any thoughts of the new bond policy from the minds of all concerned.

On the evening of June 23, 1938, some ten or twelve men were gathered at an oil well in Lea County, outside the city of Hobbs, New Mexico. They were present to see the well "shot." Mr. Kaseman and Mr. Luthy were among those who had been invited to watch it "come in." Nitroglycerine, in large quantities, was to be used. Before they had actually reached the well, and while the men were fairly closely assembled, the

nitroglycerine exploded. The exact cause of the explosion has never been known.

Eight men were killed, among them, Mr. Kaseman. The others were all severely injured; and among these was Mr. Luthy, who was permanently blinded.

THE BEGINNING OF AN ERA

On July 25, 1938 the Board of Directors of the Albuquerque National Bank elected Mr. Fred Luthy as the new President of the Bank. Born in Albuquerque in March, 1894, Mr. Luthy received his A.B. degree in 1917 from Yale University, and after two years with the U.S. Army during World War I, he returned to Albuquerque. It has been his home ever since.[1]

The Bank itself, however, is a continuing organization. Its problems must be faced from day to day. On October 4, 1938, the new President made a report to the Board of Directors on the shift in the bond account. The shift, begun in the Spring of 1937, was about complete. In June, 1937, Government Bills alone represented 65% of the total investment account of the Bank. (See Figure 4, page 57.) By December, 1937, the bank held $645,000 -- over 20% of the account -- in bonds maturing after ten years, and Treasury Bills held but a 45% portion. Then gradual shift into a more middle-of-the-road position took place, resulting in a more even distribution of maturities throughout the account. The

---

[1] Taken from the biography of Fred Luthy in "Who's Who in America," 1957.

accompanying Figure 5 shows the position of the account after this final shift had taken place.

FIGURE 5

BOND ACCOUNT OF THE ALBUQUERQUE NATIONAL BANK
DECEMBER 31, 1938

U. S. Treasury Bills	$1,450,046	.38
U. S. Treasury Notes	954,632	.25
U. S. Bonds maturing in 5 years	None	
U. S. Bonds maturing in 5 to 10 years	669,935	.18
U. S. Bonds maturing in 10 to 20 years	231,955	.06
U. S. Bonds maturing after 20 years	16,300	.0075
Federal Farm Mortgage Corporation	2,900	.0007
Home Owners Loan Corporation	116,062	.03
Other bonds guaranteed by the U. S.	19,000	.005
TOTAL U. S. GOVERNMENT BONDS	$3,460,832	.9132
OTHER BONDS		
States, Counties, and Municipalities		
Maturing in 5 years	197,616	.05
Maturing after 5 years	120,840	.03
Federal Land Banks	4,060	.001
Railroads	2,516	.0006
Public Utilities	None	
Industrials	1,047	.0002
Stocks (including 13,950 stock in Federal Reserve Bank)	15,110	.005
TOTAL OTHER BONDS	$ 341,193	.0868
TOTAL SECURITIES HELD	$3,802,025	1.00
TOTAL DEPOSITS FOR THE BANK DATE	10,496,218	

Source: Statement of Condition of Albuquerque Nat'l Bank, original in files of the Bank.

Bills were down more than ever -- to 38% of the account; but Notes, which matured in less than five years, had risen to 25% of the account, while medium term bonds comprised 18%. The maturities had been spaced more evenly than before the 1937 shift. But as 1938 wore on, the situation in Europe looked increasingly dark. The actual plan of staggered maturities, according to a predetermined outline, was never again considered. Circumstances were to arise that would not permit it.

As the 'thirties closed, the Albuquerque National Bank, and all banks, found themselves faced with another completely new and different set of problems.

WAR IN EUROPE

In September, 1938, Prime Minister Chamberlain of Great Britain returned from the Munich Conference with Adolf Hitler's promise of "peace in our times." In September, 1939, full scale war broke out in Europe, as Hitler invaded Poland.

In America, at the end of 1938, bank reserves had reached record heights. The more conservative voices of American finance were beginning to criticize President Roosevelt's programs of industrial recovery in strident tones. Said an editorial writer for the Commercial and Financial Chronicle, "President Roosevelt's pump-priming continues despite ample evidence that it is ineffective in promoting sound and lasting economic improvement."[1]

---

[1] Commercial and Financial Chronicle, September, 1938.

When the war broke out in Europe, all fixed income securities on the American Exchanges broke sharply. By the end of 1939, however, they had climbed back to their previous record levels, and yields continued to decline. In June, 1939, Treasury Bonds sold at their lowest levels since January, 1932.

By the end of 1940, bank reserves totaled $14,000,000,000,[1] almost half of it in excess of legal requirements. Banks had more money available for loans and investments than ever before. Such a tremendous backlog of lending power was far beyond the Federal Reserve Board's power to control. The problem for the United States fiscal planners was about to shift from one of trying to instigate recovery, to one of trying to hold prices in line in the face of a potentially dangerous inflation.

In his annual report for the year 1940, Secretary of the Treasury, Henry Morgenthau, Jr., had this to say concerning bond yields and prices:

> In January, 1932, the yield on U. S. Government Bonds stood at the highest levels in the previous eight years. Since then a continuous decline of yields has taken place [a credit to Government anti-depression policy, was the inference]. This decline has been interrupted by five major upswings during this period: 1. March, 1933 - the banking holiday; 2. The end of 1933 - due to monetary uncertainty; 3. Mid-1934 - unsettled European conditions; 4. March, 1937 - announcement of the second increase in reserve requirements; and 5. September, 1939 - the outbreak of war.[2]

---

[1] Federal Reserve Board of Governors, Banking and Monetary Statistics.

[2] Annual Report of the Secretary of the Treasury, 1940.

Relative to long term yields, short term yields had declined sharply, and this, said the Secretary, was because of depression caused bank demand for liquidity. (This last claim none could dispute.)

In February, 1941, Congress passed the Public Debt Act of 1941. Henceforth, all new issues of the federal government would be fully taxable as to income.

After December 7, 1941, the price of long term governments fell, on the average, 2½ points. The Federal Reserve Board immediately began to support the market, at par. This action was undoubtedly reassuring to the institutional investor, who was thus not forced to sell at a loss. Hawaiian and Philippine securities fell sharply, from 10 to 20 points per issue. Municipal prices fell, and municipal yields rose approximately 31% in the one month of December, 1941.[1]

Suddenly, with the declaration of war, the whole fiscal and monetary system of the country had to be changed. It had been geared to the defense effort of a country at peace; this was found to be wholly inadequate for a country which now faced total war. The Federal Reserve System and the Treasury Department had to find adequate methods for diverting savings, taxation alone was not enough. Reserves, which were high, had to be pushed higher; for banks must be given sufficient funds and reserves to enable them to meet any and all demands made upon them by the Treasury.

---

[1] C. F. Childs and Company, op. cit., p. 281.

Legal reserves were reduced. The Federal Reserve Banks stood ready to buy all U. S. Bills at a 3/8% rate, thus pegging the market. Later, the Federal Reserve Banks offered the banks a re-purchase agreement at the same price.

The Federal Reserve Board, while supporting the program of the Treasury Department for raising funds for the war effort, was faced at the same time with the conflicting aim of holding down inflation. Banks, as they acquired more and more Federal bonds, had tremendous reserves and lending power. Price controls were established and put under the control of the Director of Economic Stabilization. The new long term issues of the Treasury were made ineligible for purchase by commercial banks.

It was the joint aim of the Treasury Department and the Federal Reserve Board, to maintain prices and yields of the bond market at existing levels for the duration of the war. In October, 1942, the Secretary of the Treasury announced his yield policy. Yields would fall along a rising trend pattern from 3/8% for Treasury Bills, to 2½% for long term bonds. Commercial banks would get a maximum average return of 2% on their government bond holdings. This pattern became fixed almost immediately, and a period of completely inflexible rate structures followed.

America was girding for an all out war effort. The problems of the depression seemed far behind.

WAR COMES TO THE ALBUQUERQUE NATIONAL

In April, 1941, business was going along pretty much as usual in Albuquerque, New Mexico. The Board of Directors of the Albuquerque National Bank considered, and decided to reject, a proposal to open "agencies" in first, Mountainair, a farming community to the southeast of Albuquerque, then in Socorro, 90 miles to the south, and later in Grants, 60 miles to the west. The proposal to open an agency in the eastern section of Albuquerque was also considered, and not rejected; but it was tabled for the time being.[1] The day would come when these sections would have to be served, but for now this capital investment would be delayed. There was a new need for capital funds arising.

For suddenly came the war, and business as usual became an entirely different matter.

Like all banks at the time, the Albuquerque National found itself with an excess of loanable funds. Once again, as in the early depression years, but for entirely different reasons, the income producing outlets for bank funds began to dry up. With the Federal Reserve trying to eliminate all unnecessary borrowing on the part of individuals (bank customers), and at the same time setting a limit on the return which a bank could earn on its investments, the Albuquerque National faced a drop in revenues.

---

[1] Ten years later, in October, 1951, the Bank opened its first branch, in the eastern section of Albuquerque.

In October, 1942, it was estimated that the year 1943 would find the Albuquerque National suffering a drop in revenue of about $84,000.[1] The reason, as Mr. Luthy explained to the Board, was the quite natural one that interest rates had fallen, and loan volume was decreasing steadily. The table on page 66 quite graphically shows the picture which Mr. Luthy was describing and as it eventually worked out through the war years.

Loans, the principal source of income for any commercial bank, were falling. With interest rates falling as well, earnings must face a sharp decline. To offset partially the deep fall in revenues experienced in 1942 and 1943, many bank services which previously had been provided to the public without charge, were now carrying a charge. These services were being made to bear at least some of the burden of their own cost. Service charges on checking accounts were increased slightly. Excessive withdrawals for savings accounts bore a small fee. The interest rate paid on time deposits was reduced to its lowest point ever -- one percent.

These new charges went into effect in October, 1942. Still the bank suffered a drop of over $66,000 in total revenue from 1941 to 1942, and a further drop of $8,000.00 in 1943.

At the beginning of the period shown in Figure 6, investments comprised 43% of the total assets. At its ending, they

---

[1] Board minutes, October 14, 1942.

FIGURE 6

ASSETS AND DEPOSITS
ALBUQUERQUE NATIONAL BANK
THE WAR YEARS

YEAR	LOANS	INVESTMENTS	CASH	DEPOSITS	GROSS EARNINGS
1940	4,274,952	3,847,945	3,454,471	11,143,176	165,608
1941	5,522,625	4,251,265	3,645,275	12,940,122	164,421
1942	5,007,717	5,013,346	6,087,757	15,569,830	98,073
1943	4,147,395	12,485,182	9,087,587	25,107,190	90,740
1944	4,902,300	16,639,703	8,459,105	29,219,663	138,471
1945	6,113,629	21,968,058	11,415,720	38,615,922	141,521
1946	12,924,979	23,782,003	11,158,157	46,639,078	422,994

Source: From a report prepared by Paul H. Barnes, Bank Auditor, in March, 1957, on file in Bank records.

made up 78% of the total. While the aggregate decline in loans was not too great, when it is viewed in the light of the large increase in deposits, the relative position of the loan account suffered an extensive decline.

The huge increases in deposits were, quite naturally, caused by the increase in government activity in and around Albuquerque. These increases were, in large part, public funds subject to withdrawal with practically no notice. Thus, these funds could not have been put to work in any long term risk outlets, even if such opportunities had been available. They were available in the securities markets, but as mentioned before, the Secretary of the Treasury had placed a strict limitation on the return a bank could obtain from its purchases of government securities.

At the end of 1942, Mr. Luthy reported that for 1943, the revenues obtained from loans could be expected to decrease by about $90,000. This would be partially offset, he expected, by the increase of bond holdings which the war was necessitating. Bond revenue, it was thought, would increase by about $50,000. Mr. Luthy observed that "we are following a very conservative policy in our bond portfolio,"[1] and gave the following percentages to illustrate his point:

FIGURE 7

PERCENTAGE OF SECURITIES BECOMING DUE EACH YEAR
As of January 12, 1943

1943	51.5
1944	6.0
1945	11.0
1946	8.0
1947	4.5
1948	6.0
	87.0 due in next six years
	8.5 due in 6 to 10 years
	4.5 due after 10 years

Source: Board of Directors minutes, January 12, 1943.

The propriety of such a policy can hardly be questioned, given the uncertain circumstances of the time.

For the duration of the war, normal bank investment problems became entirely different. It was no longer a case of looking for the best possible place for bank funds. Only one

[1] Board minutes, January 12, 1943.

outlet was really available, the government bond market. And investing in governments became a relatively unchanging affair, as far as income was concerned, since yields on government securities had become a fixed and inflexible matter. The only question remaining was the maturities of the bonds to be purchased; and since the Treasury Department was financing the war mainly through the issuance of short term securities, even this became a relative problem. The Albuquerque National Bank, with all other banks, was bidding each week for its allocation of government Bills. For the Albuquerque National, this amounted to $100,000 to $200,000 worth of Bills each week.[1]

For the Treasury, the problem of course, was one of excess purchasing power. As much of the financing of the war as possible had to be done by borrowing from non-bank sources. For this reason, the War Loan Drives came into being. American citizens were urged by their bankers, their entertainers, and by professional salesmen, to purchase more and more War Savings Bonds.

The Fifth War Loan Drive, in 1944, proved one of the most successful of the drives. It was floated in its entirety to non-bank investors, albeit over one-third of the purchases had been financed by temporary bank credit. After it had been completed, the Treasury Department thanked the banking system for its support in the Drive.[2]

---

[1] Board minutes, May 12, 1942.

[2] C. F. Childs and Company, op. cit., p. 314.

For the Sixth War Loan Drive, held in late 1944, banks were forbidden to purchase any of the new offering, until after it had been completely sold out. The banks were then allowed to purchase the bonds on the open market, if they chose. To purchase them on the open market, of course, the banks had to pay a premium; for all government issues were selling at premiums on the market, in keeping with the Federal Reserve's policy of keeping yields fixed. A sample of the prices which banks had to pay for their investments during the war is shown by the following purchase, made by the Albuquerque National Bank on May 20, 1943:

FIGURE 8

SAMPLE INVESTMENT PURCHASE
DURING WORLD WAR II

BOUGHT:

$300,000	2½s Treasury Bonds due 1948-51	@	107-2/32
300,000	2-7/8s " " " 1955-60	@	110-61/64
500,000	⅞s " " " 1945-47	@	104-12/32
300,000	3-1/8s " " " 1946-49	@	106-13/32
250,000	2½s " " " 1949-53	@	106-61/64
250,000	2½s " " " 1951-54	@	109-25/64

Source: Board minutes, Albuquerque National Bank, May 20, 1943.

Every purchase had to be made at a premium. Was it wise? The Board wondered, and considerable discussion of the problem took place; but the bank really had little choice. The bond market was the only outlet available, and the funds had to be put to work some place, if only from a purely selfish motive.

But above this motive the Government had to finance the war, and banks, including the Albuquerque National, had to support the war effort. The war had to be won before any of the old problems would seem very important again.

The end of the war found the Bank's bond account in about the same middle-of-the-road position it had been in at the start of the war. By this time, of course, the overwhelming percentage of the account was in U. S. Governments. Very few other securities had been issued during the war, and the Albuquerque National had ceased purchases of other bonds years before the war began. For all practical purposes, the account was now a U. S. Government Bond account. It was composed as follows on June 30, 1945:

FIGURE 9
COMPARISON OF ALBUQUERQUE NATIONAL BANK BOND ACCOUNT BEFORE AND AFTER WORLD WAR II

	6-30-45	6-30-45		12-31-38	
U. S. Treasury Bills	None	None		.38	
U. S. Treasury Certificates of Indebt.	6,638,000	.30		None	
U. S. Treasury Notes	5,122,098	.23		.23	
U. S. Savings Bonds	237,300	.01			
Other U. S. Bonds					
Maturing within 5 years	3,035,107	.14		None	
Maturing from 5 to 10 yrs	6,430,591	.29		.18	
Maturing in 10 to 20 yrs	399,307	.02		.06	
Maturing after 20 years	16,300	.0007		.0075	
Other Bonds guaranteed by U. S.	None	None		.005	
			.9935		.9132
TOTAL U. S. GOVERNMENT BONDS	21,851,704				
OTHER BONDS					
States and Political Subdivisions	116,354	.005			
Others	1,297	.0005			
Federal Reserve Bank Stock	24,000	.001	.0065		.0868
			1.00		1.00
TOTAL SECURITIES HELD	21,993,355				
TOTAL DEPOSITS	38,615,922				

Looking back to Figure 5 on page 59, showing the same figures for the year 1938, one can see that the relative position of each type of maturity had not changed a great deal. The Treasury Bills of 1938 had been replaced by the Certificates of Indebtedness of 1945, still in approximately the same relative amounts. The middle term bond, maturing in 5 to 10 years, had dropped as a percentage, from 29% to 18%, but the slack had been taken up by short term bonds maturing in less than five years, 14% as against none in 1938. This had come about quite naturally, since the Treasury Department had been issuing mostly short term bonds throughout the war, and many long term bonds were ineligible for bank purchase. Other bonds, making up almost 9% in 1938, had all but disappeared by 1945.

The greatest difference to be seen, of course, is the large aggregate growth, both of total deposits and of total investments over this seven year period. Total securities had increased from $3,800,000 to $21,800,000, or nearly seven times. Total deposits had increased a little less than three times, from $10,498,000 to $38,615,922. Investments grew to 56.9% of deposits, whereas in 1938 they had been only 36%.

A comparison of this picture with the national averages shows that the Albuquerque National Bank was part of a larger picture. Every bank in the country held a similar portfolio of investment securities. With the outbreak of the war, holdings of government securities increased by leaps and bounds, and constituted a very large percentage of earning

assets by 1945. This becomes apparent from the accompanying Figure 10.

FIGURE 10

TOTAL LOANS AND INVESTMENTS OF MEMBER BANKS
- THE WAR YEARS -
(in millions of dollars)

	TOTAL LOANS AND INVESTMENTS	TOTAL LOANS	INVESTMENTS		
			Total	U.S.Govts.	Other
12/31/40	$ 37,126	$15,321	$21,805	$15,823	$5,982
12/31/45	107,183	22,775	84,408	78,338	6,070
12/31/46	96,362	26,696	69,666	63,042	6,624

Source: Federal Reserve Bulletins, Selected dates.

On December 31, 1940, the volume of loans of all member banks aggregated $15,321 million. At the same time, total investments amounted to $21,805 million. The proportion of investments to total earning assets was 59%. On December 31, 1945, loans of all member banks aggregated $22,775 million, while investments amounted to $84,408 million. The percentage of investments to total assets had increased to 79 percent. Of the total investments, 93 percent consisted of government securities. Thus, during the war, government obligations became the principal earning asset of the commercial banks. The banks further relied primarily on short term government securities as their principal source of liquidity. This becomes apparent from Figure 11, following:

FIGURE 11

DIRECT GOVERNMENT OBLIGATIONS
HELD BY ALL MEMBER BANKS
- MATURITY DISTRIBUTION -

	TREASURY BILLS	TREASURY CERTIFICATES	TREASURY NOTES	1-5 YEARS	5-10 YEARS	10-20 YEARS	OVER 20 YEARS
12/31/35	1,192	-	5,403	*	*	*	*
12/31/40	652	-	2,594	1,367	2,886	4,345	493
12/31/45	2,275	16,895	14,271	7,897	28,656	5,357	2,152
12/31/46	1,167	10,043	5,602	10,939	26,334	5,853	2,368

*Not reported separately prior to December 31, 1938.

Source: Federal Reserve Bulletins, Selected dates.

What did the future hold? Government securities had earned a permanent and substantial place in the investment portfolios of all commercial banks. While it was expected that the Federal Government would begin to decrease the number and amounts of federal securities outstanding, and that banks would be forced to turn more and more to the municipal and other securities markets for investment outlets, the U. S. Government security has shown its worth as a source of liquidity. For many banks it would continue to be the only reasonable location for excess funds, as well as for secondary reserves.

Another factor which would tend to decrease the total holdings of securities by commercial banks was the pent up propensity to consume which the war had forced the American public to hold in check. Said one commercial banking publication, of this tendency: "It is quite possible that the volume of loans made by the commercial banks will increase (in this post-war period) so that investments may in the future become a much

less important source of revenue than was the case before."[1]

This was the picture as the war ended. The Albuquerque National Bank, placed in a city which had only begun to grow when the war came along, and whose potentialities had been greatly increased by local Federal investment during the war, seemed ideally located for a tremendous growth in the years which were to follow. The future looked bright for the State of New Mexico, for its largest city, and for its largest bank.

---

[1] American Banking Association, Present Day Banking, 1947-1948, p. 208.

CHAPTER V

THE POSTWAR PERIOD - A PROBLEM OF GROWTH

The postwar period has been characterized in Albuquerque, New Mexico by one overriding problem: that of creating adequate financial capacity in the face of tremendous growth. This growth has not been a steady thing. It has been growth that has come in spurts, thereby compounding the problem. From the day the war ended, Albuquerque began to have what are commonly termed "growing pains." The city had a population of about 50,000 at the end of 1945. Today the metropolitan area exceeds the 200,000 mark. Scarcely a year has gone by, in the dozen or so since the end of the war, that new construction for homes and businesses has not set a new record. This rapidly expanding population has demanded, and received, substantially expanded but lagged services.

Keeping up with this growth has been the prime problem of all Albuquerque business concerns, including its banks. The banks of the city have been called upon for more and more credit to finance this growth. In addition, their deposit totals have spurted to new levels almost every year.

On February 13, 1946, the total assets of the Albuquerque National Bank reached a new high of $49,366,802. The Bank was 351st in size in the nation. Only a year before, its

position had been 405th.[1]

Growth had created other problems as well. The physical plant of the Bank had to be improved. Spreading in all directions, the city was badly in need of additional banking facilities in the new and growing areas. Particularly was this true of the burgeoning eastern section. Plans had to be made to open branches, and the funds had to be found for a large investment in physical plant and equipment. The minutes of the meetings of the Board of Directors in the year 1946 begin to focus on this problem of providing new and additional physical facilities, and of improving existing facilities. The new population had to be served.

In April, 1946, Mr. Luthy reported to the Board that the bond account now totaled $27,235,000. Of this total, $6,700,000 would come due in the current year, 1946. Less than two million dollars of the total account would not be due for five years or more. Faced with what most economists predicted would be a cut back in production and a decline in Gross National Product, the bank was in a position to move quickly and take advantage of almost any investment opportunity which might present itself.[2]

At this same meeting in April, 1946, the Board voted to

---

[1] Annual Report of the Federal Deposit Insurance Corporation, 1946.

[2] In one of the more glaring errors of recent times on the part of most professional economists, the economy did not cut back appreciably following the war. Instead, the problem continued to be one of holding down inflationary pressures in the face of a continuing wage and price spiral.

begin remodeling the Bank. One floor would be added to the present structure, and excavation for a complete basement would be started. But this was to be only temporary, for plans were begun to build a complete new building within the next five years. A number of circumstances were to occur which would delay this proposed new building, but it is significant that as early as 1946, the Bank recognized that its present quarters were simply inadequate to serve the future needs of the city.

At a Board meeting in October, 1946, called for the purpose of meeting with the National Bank Examiners, who had just completed a month's audit of the Bank, the Bank's board was told by the Examiner that the "immediate future was liable to test the financial and credit fibres of this country, particularly the Southwest."[1]

Another problem for the Albuquerque National (and for all banks faced with a growth situation), also began to receive attention in late 1946. This was the problem of keeping Capital Structure in line with added responsibilities caused by the increase in deposits.

In 1946, earnings of the bank amounted to almost three times those of 1945. The reason: pent up demand for loans was finally released and once more the Bank could earn some return on its funds. As stated above, loans as a percentage of total assets regained their previous levels, and investments (still bearing the 2% limit) went down. (See Figure 12

---

[1]Board minutes, October 4, 1946.

below:

FIGURE 12

LOANS AND INVESTMENTS COMPARED
IN POSTWAR PERIOD
ALBUQUERQUE NATIONAL BANK
(In thousands of dollars)

	LOANS	INVESTMENTS	TOTAL EARNING ASSETS	INVESTMENTS/ TOTAL ASSETS
6/30/45	6,113	21,968	28,081	.78
6/30/46	12,924	23,782	36,706	.64
6/30/49	19,924	16,293	36,218	.44
6/30/51	21,694	18,770	40,483	.46
6/30/52	22,443	29,452	51,896	.57
6/30/54	27,413	32,237	59,651	.54
6/30/55	34,016	33,412	67,428	.49
6/30/56	46,745	26,743	73,488	.36

ALL MEMBER BANKS OF FEDERAL RESERVE SYSTEM
(in millions of dollars)

12/30/45	22,775	84,408	107,183	.77
12/31/49	36,230	65,297	101,528	.64
12/31/51	49,561	62,687	112,247	.56
6/30/52	50,526	62,976	113,502	.55
12/31/54	60,250	71,352	131,602	.54
6/30/55	64,315	80,080	130,788	.61
6/30/56	74,783	59,645	134,428	.45

Sources: Statements of Condition, Albuquerque National Bank and Federal Reserve Bulletins, Selected dates.

Note:

The pressure of credit expansion in the postwar period caused a decline in investments as a percentage of total assets throughout the country. After rising until the early 'fifties, the percentage seems to be falling quite markedly again, showing new demand for credit today.

Another factor of note was that recoveries began to exceed charge offs in 1946, thus reversing the trend of the war years when charge offs exceeded recoveries every year from 1941 to

1945. This was a natural result of the return to Albuquerque of many former bank customers and borrowers whose notes had had to be charged off during the war.

In February, 1947, the bank disposed of its property at Sixth and Central in downtown Albuquerque, which it had been holding with an eye toward moving its new headquarters building west of the present site. This sale made possible the addition of $150,000 to the Surplus account, and brought total Capital Structure to $1,800,000. By the end of 1947, capital accounts had reached almost two million dollars, at $1,918,258. Still this represented only 4.7% of total deposits (down to $40,397,407, by the end of 1947), and this was still considered inadequate by the Board of Directors. In its meeting of October 31, 1947, the Board expressed the feeling that the capital structure should be increased by about $250,000 per year, and that, together with the elimination of the least desirable loans, this would bring about the desired improvement in the capital position.

Actually, the capital structure was increased by $500,000 in 1947 and by about $414,000 in 1948. So the Board was doing all in its power to improve the capital situation. However, deposits were growing at such a rate that it was next to impossible to keep up with them.

In December, 1948, the Board reached the decision that capital structure could not be kept in the position which they felt was necessary simply by additions from earnings. In that month, the bank issued a $400,000 stock dividend, which

immediately transferred $400,000 from Undivided Profits to the Capital Stock account, bringing the Capital Stock account to an even $1,000,000. While this by itself did not increase the Capital Structure, it did increase the Capital Stock and insure that the $400,000 could no longer be available for dividends, thus would become a permanent part of the Capital Structure.

As 1950 approached it became apparent that the proposed branch for the eastern section of Albuquerque could not be delayed much longer. The Bank had purchased some property on East Central Avenue for the proposed branch, and in March, 1950, the Board made formal application to the Comptroller of the Currency for the building and establishment of an East Central Branch. The property was located at the corner of Bryn Mawr and Central, one block east of the head office of Albuquerque's newest bank, the Bank of New Mexico, which had been formed in 1941. Because of this proximity, the Comptroller's office felt that the new branch should not be constructed on this particular property, and in May, 1950 the Albuquerque National's application was rejected.

The year 1950 also found the bank still trying to solve its problems with capital. In December, 1950, another capital stock dividend, of $200,000 this time, was declared, increasing capital stock account to $1,200,000. At the same time the bank undertook the sale (which was quickly consummated) of an additional $300,000 in common stock to the public. This stock, still at a $100 par value, quickly sold at

a price of $250 per share. Capital stock now reached the total of $1,500,000, the largest capital stock total for any bank in the history of the State of New Mexico.

Along with these capital structure changes, the Board chose to increase its membership from six to nine members. The three new members were to be elected from among those stockholders who were not primarily banking people. The three new Directors elected by the stockholders, were Ellis A. Hall, of the oil and mining industry; J. L. York, a prominent New Mexico stockman; and Mr. Thomas M. Cabeen.

In 1953, Mr. Hall was killed in an airplane accident and Mr. Pete Mattcucci, Albuquerque merchant, was named to the Board. These nine people (including Mrs. George A. Kaseman) still serve as Board members today.

The newly constituted Board still faced the problem of an East Central Branch, and while they felt that the Bryn Mawr location was the best place for the branch, they also felt that building this branch was so imperative that it should be opened anywhere it was possible. Another application was made to the Comptroller of the Currency. This time the application was approved, and on July 14, 1951, the Albuquerque National Bank opened its first branch office. It was in a rented building at 4021 East Central Avenue, about eight blocks east of the originally planned site. Named to manage the new branch was Mr. Robert L. Fripp.

THE NATIONAL POSTWAR PICTURE[1]

In March, 1948, the Federal Reserve Board restated its policy of support for the Government Bond market. The Open Market Committee announced that its policy of supporting Government Bond prices at par or slight premiums would continue. Rumors of impending changes in the rate structure, particularly in short terms, kept investors uneasy, however. The general trend of the market was lower, with heavy support purchases by the Federal Reserve in order to keep the price up. In August, 1948, Secretary of the Treasury Snyder announced that as an anti-inflationary measure, short term rates would be reduced (confirming the rumors), but the continuance of the long term peg at 2½% was assured, said he. In November, President Truman was re-elected, and the bond market moved up. All issues sold above their pegged levels, probably because of the removal of the election uncertainty. Soon after this, a report of the Committee for Economic Development called for modification of the government's policy of maintaining bond prices above par. Said the Committee report: "the policy is inflationary and makes for multiple expansion of bank credit." Still the pegging continued.

In June, 1950, the United Nations accused the Soviet-dominated government of North Korea of having broken the peace by attacking South Korea. United States air and ground forces,

---

[1] Most of the statistics and statements contained in the following national section are taken from C. E. Childs and Company's Circular #237 of August, 1950. The Circular is a complete resume, year by year, of activity connected in any way with the U. S. government bond market.

ordered into Korea by President Truman, gave the South Koreans "cover and support" and opposed the Communist invasion. The decision in Korea did not alter the program of support buying by the Federal Reserve Board, but shortly afterward, in July, a wide rift between the Treasury Department and the Federal Reserve Board broke into the open.

The Treasury Department announced a vast offering of Treasury Notes; two series of 13-month 1½% Notes, in exchange for four series of maturing securities totaling $13,750 million -- this being the largest refunding operation in the history of the Treasury Department. The decision to offer 1½% Notes shocked both the Government Bond market and the Reserve Board; for the presently outstanding 1½% Notes had been tremendously unpopular, and the Board had had to support the market for them by buying heavily. In a bluntly worded statement released after the Secretary's announcement, the Federal Reserve Board and its Open Market Committee declared, "we are prepared to use all the means at our command to restrain further expansion of bank credit consistent with the policy of maintaining orderly conditions in the government security market." This statement was construed as notice by the Central Bank to the Secretary of the Treasury that it would support his cheap money policy this time, but never again.

Inflation was the problem faced by the national economy; this was a recognized fact. The best method of meeting the problem was a subject for disagreement.

From this day forward, the Federal Reserve's support of

the Government Bond market became an issue of doubt. It seemed only a question of time until the peg would be removed, when the Treasury once more would be put on its own to borrow at whatever rate it could obtain in the market.

In March, 1951, the Treasury Department and the Federal Reserve Board issued a joint statement announcing the reaching of complete accord between the two with respect to debt management and monetary policies to be pursued in furthering their common purpose: "to assure the successful financing of the Government's requirements and minimize monetization of the debt."

On the fifteenth of March, Chairman McCabe of the Federal Reserve Board announced his resignation and Assistant Secretary of the Treasury William McChesney Martin was appointed his successor. (The feud was apparently not quite over.) On March 8, Secretary Snyder had announced (simultaneously with the announcement of the Accord), a new issue of long term non-marketable, non-redeemable 2½% bonds. With this announcement, the bond market broke downward, with no official support visible for any issue. Newspapers reported a free market in Government issues for the first time since before the war, and stated that the Federal Reserve System would no longer support the market but would simply maintain "orderly market conditions." On March 13, long term governments broke below par for the first time since 1939.

On April 10, 1951, the Federal Reserve Board officially announced the removal of its support of the market. There be-

gan a steep decline in the market, as Governments began to seek a non-artificial level.

What was the result? Fred Futny announced to the Board of Directors of the Albuquerque National Bank on March 13, that for the first time in over ten years, the Bank showed a loss in its bond account. The reason: the upheaval in the bond market. The sudden price drop had caused paper losses for more than one bank. However, now that the support situation had finally been clarified, the Albuquerque National, and all banks, could now begin to make plans for their bond portfolios, secure in the knowledge that the prices at which they would be buying and selling would once more be determined by free market conditions. While these conditions were by no means fully predictable, still they were easier to foresee than the decisions of a government department that could not see eye to eye with the Federal Reserve Governors on the best approach to the problems of the economy.

MORE EXPANSION -- AND MORE

Still the physical problems of growth remained uppermost in the minds of the management of the Albuquerque National Bank. In December, 1951, the Comptroller of the Currency turned down the Bank's application for another branch in the northern section of Albuquerque. The reason: the Comptroller's office felt that the community could not support another branch in that section of town, and that (in the Comptroller's opinion) profitable operation of such a branch would not be possible at

that time.

Four months later, in April, 1952, the Bank re-applied for the North Fourth Street Office charter and the Comptroller had changed his mind. The application was quickly approved. Real estate on North Fourth Street did not present as much of a problem as that on East Central Avenue and, as a result, the Bank was able to secure suitable property. The Bank constructed a completely new building for the North Fourth Office, which was opened on June 1, 1953 with Mr. Robert J. Hall as its manager.

In October, 1952, the highly successful East Central Office had to be enlarged, to twice its original size. Recognizing that this branch could not long continue to operate in a rented building that constricted its operations, the Board began to plan for the construction of a new permanent East Central Office Building.

On June 11, 1953, the Bank opened a drive-in and walk-up facility next to its main office to try to relieve some of the pressure in the lobby of the main office.

Plans were still progressing on the proposed new building for the Main Office. It was decided about this time to tear down the old main office building (which the Bank had been occupying since 1925), and to erect a completely new and expanded building in its place.

In June, 1954, the Bank opened a branch office in downtown Albuquerque's newest skyscraper, the Simms Building.

The new Main Office building was completed and officially

opened in March, 1957. This beautiful building possesses three stories and a full basement. The expansion room built into it should contain enough space to fill the Bank's head office needs for a long time to come.

The new building for the East Central Office was opened officially in January,1959, and almost simultaneously the Bank opened its seventh separate banking facility, the East Mensaul Boulevard Office in the still booming northeastern section of the city.

Will there be more branches? Very probably. Where will the next branch office be? It is difficult to say. The city undoubtedly has not finished growing, and the next office will be located wherever the demand warrants it.

THE BOND ACCOUNT

Now let us go back and pick up the picture of the bond account. After the break in the bond market of March 1951, the Bank moved into short terms, primarily, from a fairly heavy mid-term position. The call statement for June, 1951 shows $10 million in Treasury Notes out of a total account of not quite $19 million (or over 50% in Notes), with less than a million in Treasury Bills. The most likely reason for the shift into short terms (evidenced by $16 million in Bills and Certificates out of a total account of $27 million on December 31, 1951, while Notes dropped to $7 million) seems to have been a justifiable attitude of wariness, while waiting to see just what the exact outcome of the Treasury-Federal Reserve squabble would be, and where it would leave

the bond market.

This short term position was maintained throughout 1952, but as 1953 came into view Mr. Luthy felt that a slight shift into longer term bonds was called for. On April 16, 1953, Mr. Luthy reported this fact to the Board of Directors and asked that consideration be given to investing in longer term bonds.

To back up his position, Mr. Luthy cited a study of the Bond account which the Wells Fargo Bank of San Francisco had just completed. This investigation had been commissioned by the Bank with the idea of obtaining the opinions of an informed, yet disinterested, third party in regard to shifting the account into longer term maturities.

The investment portfolio of the Bank, before this study was undertaken, stood as follows:

FIGURE 13

ALBUQUERQUE NATIONAL BANK BOND ACCOUNT
(as of 12/31/52)

Treasury Bills	$12,550,383
Treasury Certificates of Indebtedness	6,562,000
Treasury Notes	11,948,332
U. S. Savings Bonds	724,600
Other Government Bonds Maturing Within 5 Years	2,121,900
" " " " 5 to 10 Years	1,325,708
Other Government Bonds Maturing Within 10 to 20 Years	66,403
Other Government Bonds Maturing After 20 Years	None
TOTAL SECURITIES HELD	$33,321,827

Source: Statement of Condition in files of Albuquerque National Bank.

The Wells Fargo Bank recommended a moderate lengthening of maturities. Since this finding concurred with the recommendation of the management of the Bank, the Board authorized a policy of slightly extending the maturities of the bond account. Accordingly, the shift took place, and on December 31, 1953, a year later, this was the position of the account:

FIGURE 14

ALBUQUERQUE NATIONAL BANK BOND ACCOUNT
(as of 12/31/53)

Treasury Bills	$ 3,984,950
Treasury Certificates of Indebtedness	7,671,062
Treasury Notes	10,945,832
U. S. Savings Bonds	574,600
Other Government Bonds Maturing Within 5 Years	6,979,901
Other Government Bonds Maturing within 5 to 10 Years	864,157
Other Government Bonds Maturing within 10 to 20 Years	66,392
Other Government Bonds Maturing After 20 Years	140,000
TOTAL SECURITIES HELD	$31,226,897

Source: Statement of Condition, Albuquerque National Bank.

The Wells Fargo Bank had recommended selling approximately $1,300,000 of Treasury Bills and re-employment of these funds in a selection of bonds of a three to nine year maturity range. This $1,300,000 represented only about 3½% of the total account, and only 1.6% of total deposits as of the study date, April 20, 1953.

For this relocation of funds, the Bank would receive a net gain of approximately .61% in income, or about $7,960 annually. This appreciation in income was small, but there

would be other desirable results of a shift to longer terms. The Bank was quite strong in its holdings in the near term area, and thus amply hedged against the possibility of a sharp rise in interest rates. (This was the "tight money" period, and it turned out that this position was well taken, since interest rates continued to rise over the next two years.)

But such a short term position does not take into account a possible reversal of the trend, with interest rates turning around and moving lower. Of course, if this should happen, it would be desirable to have some investments in somewhat longer term bonds, which would, of course, appreciate in value as interest rates moved lower.

The accompanying sheet of ratios, prepared for this audit by the Wells Fargo Bank, shows the position of the Albuquerque National Bank relative to other banks in New Mexico and in the country.

One problem with which the bank had been concerned, and which the Report analyzed, was proper capital structure ratio. This seemed to have been solved when viewed in the light of the ratios of other banks. The capital ratios, in every case, are in a comparable position with other banks in the state and nation.

FIGURE 15

RATIO SHEET

	Alb. Nat'l as of 4/20/53	All insured Commercial Banks in the U.S. as of 12/31/52	All insured Commercial Banks in New Mexico as of 6/30/52
RATIOS BEARING UPON LIQUIDITY			
1. Cash to Deposits	22.8%	25.9%	28.9%
2. Cash and One-year Governments to Deposits	59.7	57.0	-
3. Loans to Deposits	32.7	37.2	34.2
CAPITAL RATIOS			
1. Total Capital Funds* to Deposits	6.2	7.3	5.9
2. Total Capital Funds* to Loans	19.0	19.7	17.2
3. Surplus and Undivided Profits to Loans	12.8	13.6	10.3
4. Total Capital Funds* to "Other Bonds"	-	90.7	170.9
5. Surplus and Undivided Profits to "Other Bonds"	-	62.8	102.3
6. Total Capital Funds* to Total Assets, Less Cash and Governments	18.4	15.7	15.2
GENERAL RATIOS			
1. Other Bonds to Total Bond Account	-	18.2	8.2
2. Fixed Assets** to Total Capital Funds	14.2	11.2	17.7
3. Fixed Assets** to Capital Stock	44.6	36.5	44.0
4. Fixed Assets** to Total Deposits	.9	.8	1.0
5. Deposits as of date indicated are	6.7 times 12/30/39 deposits	3.1 times 12/30/39 deposits	6.0 times 12/30/39 deposits

*Includes Reserves.

**Fixed Assets include Bank Premises, Furniture and Fixtures, and other Real Estate.

Source: Albuquerque National Bank: Wells Fargo Study, of 4/20/53. All commercial banks: Federal Reserve Bulletins, June, 1953. New Mexico Banks: Report of the State Bank Examiner, 1953.

THE PRESENT POSITION

The bond account of today for the Albuquerque National resembles closely this account of December, 1953. It has increased in aggregate value naturally (on the call statement for June 23, 1958, the Albuquerque National Bank became the first bank in the history of the State of New Mexico to pass the $100 million mark in total deposits), but its percentage breakdown is about the same.

FIGURE 16

ALBUQUERQUE NATIONAL BANK BOND ACCOUNT
(as of 12/31/58)

Treasury Bills	$ 3,398,928
Treasury Certificates of Indebtedness	5,826,000
Treasury Notes	7,218,956
U. S. Savings Bonds	99,900
Other Government Bonds Maturing Within 5 Years	8,916,879
Other Government Bonds Maturing Within 5 to 10 Years	5,850,927
Other Government Bonds Maturing Within 10 to 20 Years	None
Other Government Bonds Maturing After 20 Years	365,102
TOTAL SECURITIES HELD	$31,676,693

It is a good, middle-of-the-road position, which takes into account the risks faced by a bank in investing its secondary reserves (outlined in Chapter I). It is a short enough position to take advantage of rising interest rates, and still sufficiently long in maturities to be a hedge against any decline in interest rates. It is this sort of ready-for-anything account which best suits the bank investor -- whose aim must always be primarily liquidity and unimpeachable

solvency.

After a long upward climb from 1954 through to the end of 1957, short term interest rates fell sharply with the recession in the fall of 1957, to a low about May, 1958. Since then they have begun to climb again, and though they have still not reached their 1957 high, the trend once more seems to be upward. Long term rates have been fairly stable throughout this period of time, with a slight break to about 3% in the recession, and now back almost to 4%.[1]

So the interest rate, once more back on a free and uncontrolled basis, will fluctuate up and then down, according to the dictates of the supply of, and demand for, loanable funds. Any bank must be prepared for these fluctuations, in either direction. The Albuquerque National Bank is so prepared.

---

[1] Federal Reserve Bulletin Chart, January, 1959.

CHAPTER VI

BANK INVESTMENT POLICY

A GOAL

As in every investment program, whether it be for an individual with $1,000 to invest, or for an institution with $1,000,000, there must be a definite goal for the bank investment program. The selection of this goal involves consideration of many factors. Primary among these factors, and in the order of their importance to a bank, are liquidity, income and flexibility.

For a bank of any size, where more than one person will have a voice in the making of investment decisions, it is usually a good idea to have this goal clearly stated and defined, for the guidance of all. Usually the goal will be incorporated within a written statement of the broad investment policies of the institution.

The bank which has a satisfactory income without its income from investments, has the potential of a much more flexible position, that of being able to take advantage of opportunities as they arise. And this matter of timing, for banks, as for any investor, can be very important. It can mean the difference between a "good" investment and a "bad" investment, though the investment itself may involve the same security.

REGULATION OF COMMERCIAL BANK INVESTMENTS

By the passage of the Banking Act of 1936, as amended in 1938, there were certain limitations placed upon banks in the choosing of investment outlets for their funds. Before examining what bank investments should be, let us see what, by the limitations of the law, they can or cannot be.

There are three major provisions of this act which deal with bank investments. They apply, incidentally, only to member banks of the Federal Reserve System.

1. The Ten Percent Rule. A bank cannot invest more than ten percent of its total capital in the securities of any one issue. Par value, and not market value, is the determinant measure. This rule does not apply to the obligations of the Federal Government, nor to those of any State, County, or Municipality.

2. Stocks. Members of the Federal Reserve System are required to purchase stock in their local Federal Reserve Bank. Other than this, a bank can own stock only in subsidiaries established for specified purposes, such as owning and maintaining the bank building, operating a safe deposit business, or for carrying on foreign business.

Any stocks acquired through default must be disposed of "within a reasonable time."

3. Bonds. The only restriction here is that a bank is forbidden to buy bonds which are "strictly speculative." The Comptroller of the Currency relies on the various rating agencies (Moody's, Standard and Poor's, etc.) for what is

speculative and what is not. However, banks can buy bonds which are not rated in these, provided they apply the same type of tests. Thus, any bond which a bank can show to be non-speculative may be of bank investment quality. One further provision is that any premiums paid must be amortized over the life of the bond.

These restrictions are really not very restrictive. They do not approach the limitations which a well informed, normally prudent banker would consider justifiable.

QUALITY

By quality is meant the degree of risk of nonpayment of the investment obligation. It is commonly called the "credit risk" in most investment manuals. For a bank, this risk must be considerably less in its investments than in its loans. It cannot be overemphasized that the primary business of banking is the lending of direct loans to customers. To the extent that a bank must assume any credit risk at all, it should be assumed in its loan account and not in its investments.

Another reason why banks must keep this credit risk at a minimum is that, unlike most businesses, the proportion of funds supplied by the owners of banks (Capital Funds) is small in relation to the amount supplied by the creditors (or depositors). Currently, this ratio is $13 supplied by depositors for every $1 invested by the owners (for member banks of the Federal Reserve System).[1]

---

[1] Federal Reserve Bulletin, January, 1959.

Thus, the margin for risk taking is small for a bank. The risks taken by one investing his own money will generally be greater than those taken by one who is acting as a quasi-trustee for another's funds.

Under the general heading of quality comes another factor which is of extreme importance to the bank investor. This is marketability.

Banks must face their severe demands for liquidity under the most trying of circumstances. That is, an unusual demand for cash on the part of depositors will not usually take place, unless first the price of securities in the markets has been seriously depressed. This is why secondary reserves are normally defined in terms of their ready convertibility into cash, without appreciable loss.

The bank which has made adequate provisions for liquidity, through protective investment in short term securities, need not usually resort to its long term holdings to meet its cash needs. This is of course relatively true, depending on the severity of the drain upon the bank's funds.

The test of quality, or the "credit risk," does not apply to any investments in the securities of the Federal Government. As long as the national government is a sovereign body, with the power of monetary expansion, their obligations will be met. Inflation may be the social cost of this, but in a narrow, financial sense, these securities are wholly safe, quality-wise.

The vast expansion of the federal debt has made it

unnecessary for many banks to depend on any other outlet for their investable funds. This brings up the thought: should banks buy anything other than "Governments?" Because of the emphasis which banks must place on liquidity and the avoidance of credit risk, only two other investment outlets are really available for serious consideration by a bank. These are the issues of political subdivisions, such as states, counties, and municipalities (commonly referred to as the municipal market), and the high grade bond issues of corporations. We will look more closely at these two markets later in this chapter.

DIVERSIFICATION

The next test to be applied to the analysis of a bank portfolio is that of diversification. For a bank, this means primarily: do the loan account and the investment account, when combined, give a reasonable balance. This usually means that a bank should not invest in open market securities of a nearby industry, even though the banker may be well able to judge their intrinsic value.

Again, this point is not applicable to the securities of the Federal Government. An investment account consisting of all federal government issues will, generally, more than balance the risks of a primarily local loan account.

MATURITY SPREAD — OR LIQUIDITY

This last of the tests of a bank's investment portfolio becomes very important, since it is the only one which applies

to Federal Bonds. The other risks can be effectively hedged by investing in "Governments." This last must be seriously considered in setting up such a bank portfolio.

First, however, it should be said that in considering maturity spread, only the highest quality of investments should be included. Inferior investments, in fact any issue where there is a question of credit risk, cannot be considered when planning a maturity spread. Inferior investments may not be paid at all.

Allied closely to maturity dates is the problem of the changing money rates, or changing yields, on given types of securities.

The longer the maturity, the greater the influence of changes in yield. Many investors need not worry about this problem, since they can always hold to maturity. For example, insurance companies almost never meet any cash demands which might strain their liquidity. This is true of almost all institutional investors other than banks.

The rates and yields of short term securities tend to fluctuate more than for the long term issues. Conversely, long term prices fluctuate more. Short terms are usually so close to maturity that the principal value remains very stable.

Inasmuch as short term rates fluctuate more widely than long term, they tend to be lower than long term when rates are low, and to be higher when rates are high. Past history shows that time has been divided about equally between periods

when short term rates were higher, and periods when short term rates have been lower. As contrasted with the forty years or more of high short term rates prior to 1930, the past thirty years have shown a strong bias to lower short term rates.[1]

Because of their need for liquidity, banks have tended to dominate the short term market for government issues, while other institutional investors, notably the insurance companies, have tended to dominate the long term markets. For this reason also, and the experience of the past three decades, the question arises: should banks buy any long term bonds?

The obvious advantage, given these years of higher long term rates, is an increase in income resulting from the lengthening of maturities. Assuming that a bank has made adequate provisions for liquidity, the problem becomes one of employing bank funds effectively in the light of (1) the tendency of the public to save more with banks, and (2) the existence of a huge public debt.

THE POSSIBILITY OF A DECLINE IN DEMAND DEPOSITS

A decline in demand deposits would require disposing of any long terms held against these deposits. Liquidity requires the holding of investments which are readily salable, and salable at any time, without appreciable loss. This objective cannot be fulfilled by long terms, even though a complete absence of credit risk exists. Some liquidity can be

---

[1] See A. H. Goldenweiser, Monetary Management (New York: McGraw-Hill, 1949), p. 67.

sacrificed, however, for the sake of holding long term bonds. Exactly how much depends primarily on factors having to do with the growth of time deposits, and the flow of savings.

The growth of time deposits. In 1949, time deposits (outside central reserve cities and exclusive of government and inter-bank accounts) made up about 33% of total deposits, while demand deposits averaged about 67%. Before the war, these two figures were much closer -- about 45% in time deposits and 55% in demand deposits. This relationship may be reached again with the slow but steady increase banks have been experiencing in mass savings. In large part, savings are increased at the expense of demand deposits. (For example, consider the man who cashes his paycheck at the bank, depositing part of it to his savings account.)

The flow of savings. The recent flow of savings has not decreased demand deposits, however, because banks, insurance companies, and other recipients of people's savings have poured the money back into the demand deposit pool by making new loans and investments. The time may come, though, when new debt will absorb a smaller and smaller percentage of savings without an increasing balance being placed in old debt. Particularly, is this true in the case of government debt. With no great rise in government debt, and a slackening of demand for funds by corporations, municipalities, etc., segments of the public debt, now monetized in the banking system might be transferred to individuals and to the institutions where they place their savings. This would be counter-inflationary,

but would be decreased in effect by forces acting to increase new investments. Among these forces would be recurring government deficits, further encouragement of home mortgage and consumer credit, renewed demand for corporate expansion funds, and institutional purchases of equity securities. Given these forces, in many and all combinations, no decline in bank deposits or assets need be expected.

No really embarrassing decline in demand deposits is likely to be permitted. What is significant, is that time deposits may become more important, rather than less so, in the national financial economy.

What does all this mean to the individual bank investment policy? The implication is that a bank able to attract a relatively high proportion of savings money might be well advised to expand its long term holdings. It could also imply a system of staggered maturities for the investment of savings deposits.

The question of liquidity also enters in. To how great a risk may bank deposits and bank capital be properly exposed? There is a fairly well-developed attitude that banks with more extensive loan and mortgage portfolios are better advised not to extend risks further by owning long term bonds, even where the credit risk of such bonds is negligible. In an article written for the Harvard Business Review, John J. Moynihan, at the time Senior Bank Examiner for the New York

State Banking Department, questions this attitude.[1]

Mr. Moynihan questions this approach on the grounds that two distinct types of risk are assumed, while in reality these two types of risk are complementary rather than supplementary. His belief rests on the hypothesis that in the natural order of "things economic," money rates will ease in a period of poor business, and stiffen when times are good. For example, assume a bank holds a diversified loan portfolio as well as long term bonds. If, under expanding business conditions, interest rates rise, the bonds will depreciate, and a paper loss will be inevitable. However, if the capital cushion is of sufficient proportions to guard against such a contingency, no great harm will have been done. Moreover, losses normally expected in loans will probably not appear during the upturn. But, given the same portfolio in a down turn, the bank with longer term investments will be better prepared to face a long slide. As Mr. Moynihan points out, many banks in the 'thirties were happy to offset losses on loans and mortgages, and to preserve adequate capital ratios through profits on long term bonds.

So given, first of all, adequate capital, and adequate secondary reserves in the form of short term bonds, there does seem to be some justification, other than more income considerations, for the holding of long term bonds by a bank. Exactly the proportions to be held, and the exact maturity

---

[1] John J. Moynihan, "Should Banks Buy Long Term Bonds?" Harvard Business Review, November, 1950.

spread, is, of course, a matter to be decided upon by the individual bank, in relation to its capital, its secondary reserves, and its proportions of time deposits.

One other facet of investing in long term bonds should be mentioned. This is the significance of the interest yield curve and its implications to bank investors. The market for government securities has always been a specialized one. Insurance companies buy "long." Commercial banks buy "short." With the great need of the commercial bank for liquidity, it would be a dubious practice for the commercial bank to attempt to "play the pattern" (as it is called) of yield curves. But the growing bank, with ever more funds to invest in securities, need not completely ignore the possibility either.

When short term rates are above long terms, the yield curve will slope downward; conversely, when the slope of the curve is upward, long term rates are above short term. Again, history shows that time has been about equally divided between the upsweeping curve and the downward curve. Again, also, the past three decades have been periods of constantly upswinging curves. These patterns have two implications: the possibility of "playing the pattern -- or investing and withdrawing at different levels, and the use of the shape of the curve as a guide to investment policy.

"Playing the pattern" can be illustrated quite simply: Suppose an investor buys a 20-year security with a 2½ percent coupon at par. The yield on this security to maturity will be 2½ percent -- if held to maturity. However, if an upsweeping

yield curve prevails, the implication is that the market yield of the security will go down with time. Let us assume that the 15-year-to-maturity yield is 2 percent. This means that after 5 years the security will sell for $106.45 for each $100 or par. If the investor elects to sell, he has collected coupons at the rate of 2½ percent each year, and he has a capital gain of $6.45, or not quite 6½ percent. The effective yield for the five years from the twentieth year to the fifteenth from maturity is roughly 3¾ percent.

The investor who is not concerned with liquidity and can sell off securities before maturity, can take advantage of this opportunity (and insurance companies do, to a large extent), but to what extent is it appropriate for commercial banks? At best, it would be dubious practice, but certainly it can be used as one guide to investment policies. A bank fortunate enough to have a man or department expert in these matters would be well advised to use these talents, if for no other purpose than additional information for forming its investment policies. The bank with growing amounts of funds available for investment, could even employ a very small portion of its new funds in such a program. The additions to income might be surprisingly significant.

OTHER INVESTMENT OUTLETS

Let us turn now to the other investment outlets available to banks, besides government bonds.

Municipals. With the gradual redemption of the outstanding Federal, partially tax exempt issues taking place, the

major attraction of municipals, i.e., State, County and Municipal bond issues, is their tax exemption feature. Income from any of these issues is fully exempt from taxation by the Federal Government.

Most other institutional investors, such as mutual insurance companies, Savings and Loan Associations, and mutual investment funds, are generally exempt from federal taxes anyway. So banks share this market largely with high income individuals.

Computation of the tax benefit on these issues is direct. If a bank is in the 38% income tax bracket, this means that 62% of its income is tax free. Therefore, multiplying the yield of a fully taxable issue by .62 would give a direct comparison with the yield of a fully tax exempt issue.

States, Counties and Municipalities do not have the power of monetary expansion. So their issues do carry some degree of credit risk. Thus, they must be examined carefully for credit risk before the purchase can be made safely. For this reason, too, it seems unreasonable to include these investments in the protective investment portion of a bank's portfolio. It would be more conservative, and therefore more desirable from the bank's viewpoint, to employ in this manner only a part of those funds in excess of secondary reserve requirements. (The fourth and last of Mr. Robinson's priorities mentioned in Chapter I.)

There are three types of these bonds: the General Obligation Bond, the Revenue Bond, and the Housing Authority Bond.

The General Obligation Bond. This bond is secured by the full faith and credit of the issuing political subdivision, and is payable from taxes which may be levied on all of its taxable property. It constitutes a first lien against the property taxed. Some are limited tax obligations; others are unlimited.

The Revenue Bond. This type was developed because of the need of public bodies to find more ways of raising money. Revenues from a particular project are used for payment, instead of dependence on any taxing power. They are issued in connection with projects such as toll roads, electric power facilities, and water works, which receive revenues for their services.

The Housing Authority Bond. This is the newest type of municipal bond. Local housing authorities in various localities are empowered to issue their own bonds. They have no taxing power and their income is derived solely from housing projects. These bonds have come to be regarded among the highest grade of municipals because of the pledge of faith of the United States, through the Public Housing Administration, of annual contributions to the local housing authority.

Municipal bonds are always offered with a legal opinion of a recognized municipal bond attorney as to the legality of the issue. Since the opinion is necessary to constitute good delivery of the bonds, it must be kept with the bonds in the event they are to be re-sold.

The following represents a partial list of factors to

be considered before a municipal bond is purchased:[1]

Reputation and size of the community
Population
Growth of industry
Tax collection history
Purpose of the issue
Tax sources for payment of bonds and interest
Local economic and political conditions and prospects for area improvement
Reputation of the dealer offering the bonds
Record of payment of obligations
Ratings, when available
Comparison with other similar issues

From all of this, it is apparent that investing in municipals is an art in itself which would require much training and extensive investigation to master. For this reason, the bank which does not have its own investment department, with a portion of the department given over exclusively to the investigation of municipal investment opportunities, would be well advised to concentrate on the issues of the federal government. The income foregone, is probably not enough to offset the additional costs, and, of course, the additional risks inherent in the municipal market.

CORPORATES

Should the small or medium sized bank purchase any corporate bonds? The answer must generally be no. The art of

---

[1]Check List for Municipals, from a speech by Durwood C. Dubois, Vice-President, Ohio Citizens Trust Company, Toledo; reprinted in Banking, Journal of the American Banking Association, March, 1959.

investing in corporates, like municipals, has attracted many fine minds and much literature has been written on the subject. In spite of these advantages, however, investment operations have not been reduced to the point where losses can be kept within "small and actuarially predictable" amounts. It is a difficult market, and a dangerous one. Small banks must rely on the advise of salesmen and dealers, and their big city correspondents. As in the case of municipals, though, the amount of income to be foregone is relatively small. The differential between high grade corporates and Governments has seldom been more than ½ of 1 percent, and is even smaller for those short term corporates which are suitable for bank investment. The risks foregone, however, can be quite large, and since they are unpredictable, it would seem unreasonable to take them.

EPILOGUE

The Albuquerque National Bank of Albuquerque, New Mexico has now been in existence for over thirty-five years. During that period of time it has faced, and solved, the day-to-day problems of the bank investor. It has withstood well two of the greatest periods of upheaval in the history of American finance -- the "Great Depression," and World War II. Its investment policies have been proven.

Since World War II, a new problem has come forward of prime importance to the bank, both in its investments and in its general operations. This is the problem of unprecedented growth. The Albuquerque National Bank is no longer a small, nor even a medium sized institution. With total assets, at the latest count, of well over 120 million dollars, it is now a large bank.

Plans for the future must take this fact into consideration. In the years ahead, the Bank will undoubtedly be investing more funds in more securities than ever before. The officers of the Bank are going to be called upon to make investment decisions much more frequently. The time is undoubtedly coming when at least one officer of the Bank will devote his full time to these decisions, and to the developing of the information necessary to enable the management to make them. Developing this information and keeping it current, through

constant analysis of the Bank's investment account, will soon require the establishment of an investment department within the Bank. Perhaps the cost of such a department can be shared, in part, by the demands of the personal trust department, or a future common trust division. Very probably, this department will come from what is now the Trust Department, since this department already has the market experience.

One thing which can be said for certain is that with the growth of the Bank, the amount of funds which must be kept employed, both for protective investment purposes and for income purposes, will continue to grow steadily.

Correlative with the establishment of this department, and the transfer of these responsibilities to more people, there should be set forth a complete, written statement of investment policies and goals. The policies and goals themselves, their worth already proven, will not necessarily have to be revised, but they will have to be communicated to more and more people.

Federal defense policies at present make any decrease in the amount of federal obligations available for investment seem unlikely in the near future. However, with the growth of the Bank's investable funds, attention will probably have to be given once more to the possibilities of investing in municipals, and perhaps even in corporates. This too, would require a capable investment staff in order for the Bank to keep informed of developments in these markets.

The management of the Bank realizes all this, of course,

and such a department is included in its plans for the future.[1] This would seem to be the only major change to be expected in the investment policies of the Albuquerque National.

It should be reiterated, that over the past thirty-five years, the management of the Albuquerque National Bank has proved its ability to meet all the problems which its investments have posed. This ability, and these policies, can be expected to continue to do as well in the days to come.

---

[1] Interview with Mr. Fred Luthy, February 6, 1959.

APPENDIX

AN ANALYSIS OF ALBUQUERQUE NATIONAL BANK BOND ACCOUNT ON MARCH 12, 1959

To begin the analysis, the following charts will help to illustrate the movements of prices and yields in the Government securities markets over the past few years. This will give us some idea of the market background in which the Albuquerque National Bank has been operating in its bond account transactions.

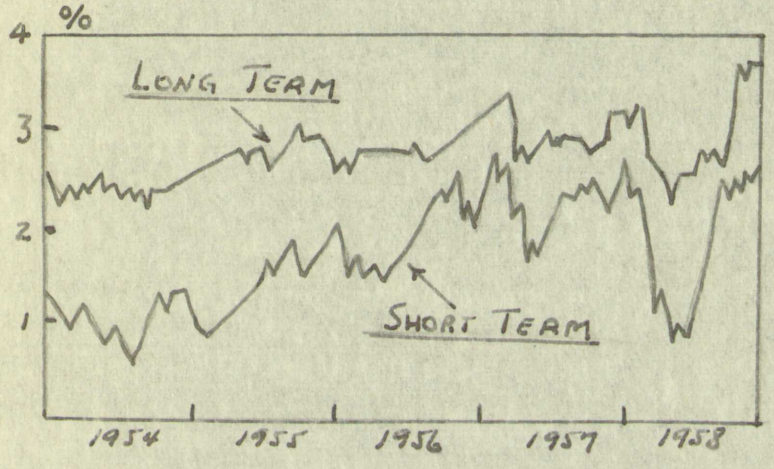
The first thing apparent in Chart I is the point, mentioned before, that short term rates fluctuate more widely than long term rates. For any given change in interest rate, the dollar price change will be less in short bonds than in long ones. Even if the yield of short bonds should rise more than that of long bonds, the dollar price decline of the former would likely still be less. This tends to prove one of banking's investment precepts -- that short term bonds are substantially less subject to the risk of wide market fluctuation than longer issues. The wide fluctuation of prices of long bonds, shown in Chart 2, also indicates why long term bonds of any kind are unsuitable for bank investment until liquidity requirements have been fully satisfied.

Both the graphs show, also, the spectacular decline which occurred in long term issues in 1958. This decline has had

FIGURE 17

CHART I

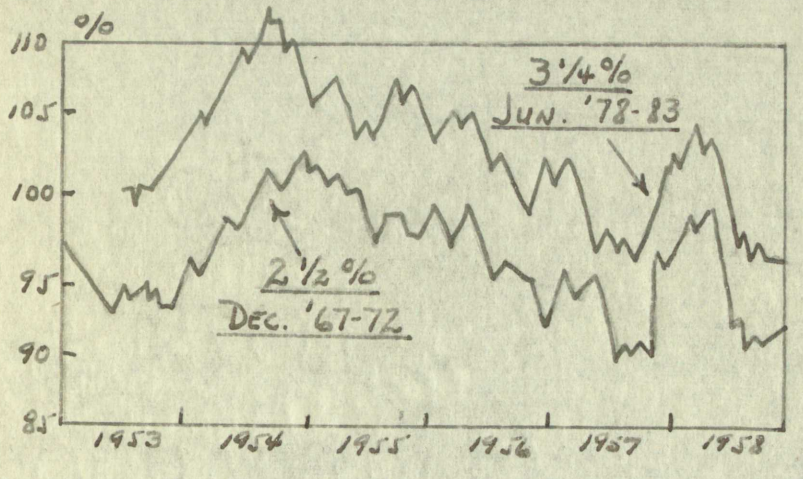
WEEKLY AVERAGE MARKET YIELDS FOR LONG TERM U. S. GOVERNMENT BONDS AND FOR LONGEST TREASURY BILLS. LATEST SHOWN ARE FOR WEEK ENDING JANUARY 7, 1959



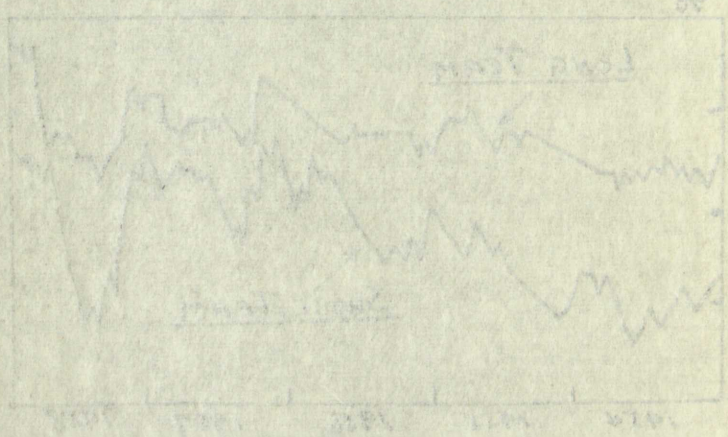
Source: Federal Reserve Bulletin, January, 1959.

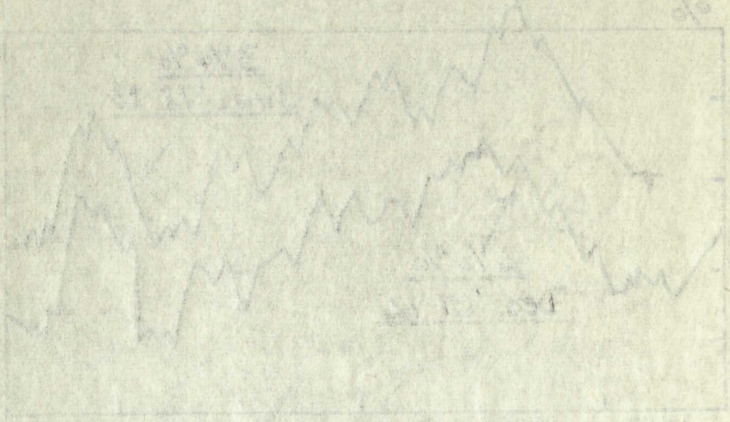
CHART II

MARKET PRICE (IN PERCENTAGES OF PAR) OF TWO LONG TERM U. S. TREASURY BONDS



Source: Prepared by the First National City Bank of New York, and reprinted in Burroughs Clearing House, January, 1959.





the result of causing paper losses in the bond accounts of almost every bank in the country. The Burroughs Clearing House article, from which the second graph is taken, was written about this subject and entitled "1959 - A Bond Loss Work-Out Year for Banks." At the end of 1958, seven big New York banks, alone, showed losses on paper of around $200 million. On the basis of proportionate holdings of U. S. securities, this means that United States banks were carrying on their books at year end, securities at a value between $500 million and $600 million more than they were worth in the marketplace. This paper loss is, of course, not particularly serious. A bank which owns a billion or more of Government securities, can roll up millions in dollar depreciation rapidly when Treasury securities decline even a small percentage in price. For the New York banks the depreciation in book value ranged all the way from 1½ to 4½ percent of total book value.[1] For the Albuquerque National Bank, with total book values of $39 million plus, the depreciation as of December 31, 1958 amounted to about $746,000, or only 2.4 percent of total book value.[2]

This is some indication of the market for U. S. Government securities during the winter of 1958-59 -- the period which this analysis covers.

Another background factor to be considered before examining

---

[1] "1959 - A Bond Loss Work-Out Year for Banks," Burroughs Clearing House, January, 1959.

[2] This compares favorably with the same ratio on March 12, 1959, when the loss was down to only 1.6% of a total account of $39 million, plus.

the analysis, is the particular stage in the Bank's development at which the analysis is made. The last two years have been years when the bank has been expanding its physical capacities. A new head office building was completed in early 1957. In January, 1959, the East Central Office moved into a completely new building,- and one week later the bank opened another completely new branch office in northeastern Albuquerque.

This vast expansion of plant (detailed in Chapter V) in such a short period of time, has resulted in the Bank's fixed asset totals reaching higher levels than ever before. As a percentage of capital structure, too, the Bank's physical plant represents a larger investment than ever before. The Bank's first responsibility is to its customers and depositors, and they have created the demand which has made these investments necessary.

Despite these large fixed asset investments, the Bank's capital position, as we shall see, continues strong. The only deviation from the average bank which will be seen, is the ratio of fixed assets to Total Capital Funds, which was 25.7 for the Albuquerque National, while the national average was 13.6. Needless to say, the "average" American bank has not been engaged in the Albuquerque National's building program.

So the date of the analysis, March 12, 1959, finds the Albuquerque National in a temporary position of working out paper losses in its bond account (as are all banks this year),

and with a larger than average investment in fixed assets.

One further comment is necessary before the analysis. It should be said that the "average" figures for "all banks" are in no way presented as an "ideal" for the Albuquerque National Bank or any individual bank, but rather with the thought that they serve a useful purpose in pointing out wide deviations in the individual situation for further study.

The Schedules shown on the next seven pages are modeled primarily after the schedules prepared by the Wells-Fargo Bank for its analysis of the account in 1953. Taken together, they present, I think, a fairly complete, and graphic, insight into the investment portfolio of the Albuquerque National Bank.

FIGURE 18

SCHEDULES 1 THROUGH 7

SCHEDULE 1

CURRENT MARKET APPRAISAL
ALBUQUERQUE NATIONAL BANK

Par Value	Issue	Rate	Maturity	Approximate Market Dollar Price	Approximate Market Value
$ 2,600,000	U.S. Treasury Bills		Various dates		$2,578,085
3,540,000	U.S. Treasury Certificates of Indebtedness	1-1/2	3-24-59	99-29/32	3,536,681
2,000,000	U.S. Treasury Bills		5-15-59	2.70 yield	1,989,200
1,010,000	U.S. Treasury Certificates of Indebtedness		5-15-59	99-21/32	1,006,528
2,400,000	U.S. Treasury Bills		6-22-59	2.80 yield	2,379,466
660,000	U.S. Treasury Certificates of Indebtedness	1-5/8	8-1-59	99-13/32	656,081
300,000	U.S. Treasury Bills		9-21-59	3.10 yield	294,878
700,000	U.S. Treasury Notes	3-1/2	11-5-59	100-5/32	701,093
3,616,000	U.S. Treasury Certificates of Indebtedness	3-3/4	2-15-60	100-8/32	3,625,040
2,000,000	U.S. Treasury Notes	3-1/4	5-15-60	99-30/32	1,998,750
400,000	U.S. Treasury Bonds	2-1/8	11-15-60	97-25/32	391,125
560,000	U.S. Treasury Bonds	2-3/4	9-15-61	97-14/32	545,650
4,090,000	U.S. Treasury Bonds	2-1/2	11-15-61	96-18/32	3,949,406
2,000,000	U.S. Treasury Notes	4	2-15-62	100-24/32	2,015,000
1,500,000	U.S. Treasury Notes	2-5/8	2-15-63	95-20/32	1,434,375

SCHEDULE 1 (Cont'd)

5,000,000	U.S. Treasury Bonds	2-1/2	8-15/63	94-20/32	4,731,250
1,500,000	U.S. Treasury Bonds	3	2-15-64	96-12/32	1,445,625
4,000,000	U.S. Treasury Bonds	2-5/8	2-15-65	93-6/32	3,727,500
500,000	U.S. Treasury Bonds	3	8-15-66	94-22/32	473,437
50,000	U.S. Treasury Bonds	2-1/2	6-15-62/67	86-22/32	43,343
140,000	U.S. Treasury Bonds	3-1/4	6-15-78/83	89-30/32	125,912
500,000	U.S. Treasury Bonds	4	2-15-80	99-24/32	498,750
224,000	U.S. Treasury Bonds	3-1/4	5-15-85	89-20/32	200,760
135,000	U.S. Savings Bonds Series "P"		7-1-60	Redemption Value	125,415
$39,425,000					

TOTAL BOOK VALUE: $39,120,045
TOTAL MARKET VALUE: 38,473,354

EXCESS OF BOOK VALUE OVER MARKET VALUE:
$646,690 (Equal to 1.6% of Book Value)

March 12, 1959

RATIO SHEET

	Alb. Nat'l Bank 3/12/59	All U.S. Insured Com'c'l Banks 6/25/58	All N.M. Insured Commerc'l Banks 12/31/57
RATIOS BEARING UPON LIQUIDITY			
1. Cash to Deposits	20.7%	21.2%	25.9%
2. Cash and one-year Gov'ts to Deposits	35.1	25.3*	—
3. Loans to Deposits	42.8	46.8	39.1
CAPITAL RATIOS			
1. Total Capital Funds to Deposits	7.0	8.7	6.1
2. Total Capital Funds to Loans	16.1	18.7	15.6
3. Surplus and Undivided Profits to Loans	12.0	—	—
4. Total Capital Funds to "Other Bonds"	272.0	90.3	120.8
5. Surplus and Undivided Profits to "Other Bonds"	202.6	—	—
6. Total Capital Funds to Total Assets Less Cash and Gov'ts	13.4	14.8	13.3
GENERAL RATIOS			
1. "Other Bonds" to Total Bond Account	.7	23.0	—
2. Fixed Assets to Total Capital Funds	25.7	13.6**	26.5
3. Fixed Assets to Deposits	1.8	1.2**	1.6
4. Time Deposits to Total Deposits		30.2	22.1

*Includes all Bills and Certificates of Indebtedness held, but no notes or bonds.

**As of 12/31/57. Latest figures available.

Sources: Albuquerque National Bank Statement of Condition, March 12, 1959; Federal Reserve Bulletin, January, 1959, national averages; FDIC Report No. 48 of December 31, 1957, New Mexico averages.

SCHEDULE 3

ASSET RISK IN RELATION TO CAPITAL POSITION

There are a number of ratios frequently used by bank supervisory authorities and others as measures of the risk element in a bank's assets relative to the size of its capital accounts. In many of these ratios it is assumed that U. S. Treasury securities are risk-less regardless of their maturity. The author is not in accord with this view as he believes there is a risk of interest rate changes with attendant fluctuations in government security prices, which fluctuations will vary in degree depending upon the maturity of the issues involved. To take into account this market risk in bonds and the credit risk in both loans and in bonds other than governments, we will use the following ratio which relates so-called "free capital" of a bank to an estimate of the risk in the assets. The percentage of risk assigned to each asset category is necessarily arbitrary, and others might assign different percentages to the different groups. Nonetheless, it is believed that the risk percentages chosen are reasonable in themselves, and in any case, the final ratio, prepared on the same basis for all banks, has a certain validity for purposes of comparison. The calculation of the estimated risk in the Albuquerque National Bank's assets is shown below with the final ratio derived by dividing the figure for total risk into the amount of "free capital." "Free capital" is computed by deducting from total capital funds such more or less fixed assets as bank building, furniture and fixtures, other real estate, etc. The final ratio in a measure indicates the protection the capital accounts afford depositors against the estimated risk in the assets of the bank.

On the following page is another ratio commonly used to determine what percentage of its assets a bank can afford to employ in long term bonds.

Asset	Albuquerque Nat'l Bank Totals	Arbitrary Assumption Percentage Risk	Estimated Amount of Risk
Loans	$50,815,642	10%	$5,081,564
U.S. Savings Bonds	99,900	0	—
0-1 Year U.S. Securities	16,734,592	0	—
1-5 Year "	16,875,012	3	506,250
5-10 Year "	4,550,871	7.5	341,315
Over 10 Year U.S. Securities	859,867	10	85,987
"Other Bonds"	302,250	10	30,225
		TOTAL	$6,045,341
Capital Accounts	$8,224,033		
Less fixed assets	2,114,474		
Free Capital	$6,109,559		

Ratio of "Free Capital" to Estimated Risk

Alb. Nat'l Bank: 101.0%

All insured commercial banks in U. S., as of 12/31/57: 100.5%

SCHEDULE 4
FORMULA FOR ALLOWABLE AMOUNT OF LONG TERM INVESTMENTS

This is another ratio commonly used by bank supervisory authorities to determine the amount of a bank's funds which might safely be placed in long term employment. Again, the final figure is not presented as an ideal, but merely as an indicator. From the final figure, deducting the actual amount of long term investment would give an indication of the margin of safety which a bank would enjoy in its investment account. The formula follows:

> From Capital Funds, deduct Fixed Assets, Federal Reserve Stock, and Other Real Estate. From this total, deduct ten percent of the Risk Assets (Loans and Investments other than U. S. Governments) and add two thirds of Total Time Deposits. This will give the final figure for funds which might safely be employed in long term investments.

For the Albuquerque National Bank on December 31, 1958, it runs as follows:

Capital Funds		$ 5,624,212	
Less			
	Fixed Assets	2,036,556	
	Federal Reserve Stock	138,000	
			3,449,656
Less			
	10% of Loans	6,373,308	
	10% of Other Bonds	30,225	-2,953,877
Add			
	2/3 Time Deposits	17,921,020	14,967,143 Total allowable

Deducting from this final figure the actual amount of long term investment by the bank on this date of $6,216,029, gives the Albuquerque National Bank a margin of safety of $8,751,114.

This particular analysis was done as of December 31, 1958 in order to be as conservative as possible. Loans on this date amounted to over 50% of deposits for the first time in many years, and, of course, fixed assets were also high. Granting these temporary situations (loans were down to 42.6% of deposits by March 12, 1959), the margin of safety is even more impressive.

SCHEDULE 5

LIQUIDITY POSITION, REVERSE BREAKDOWN OF STATEMENT OF CONDITION

LIABILITIES		RESOURCES	
SECTION NO. 1			
Capital Accounts	$ 8,224,033	Banking House, Furniture and Fixtures	$ 2,114,474
Other Liabilities	—	Federal Reserve Stock	138,000
		Loans (to balance)	5,971,559
TOTAL SECTION NO. 1	8,224,033		8,224,033
SECTION NO. 2			
Implied "Working" of Basic Deposits (54% of Total Deposits)	63,333,838	Cash (20%)	12,776,767
		Loans (Remainder)	44,844,083
		Long Gov'ts (over 5 years)	5,410,738
		Other Bonds	302,250
TOTAL SECTION NO. 2	63,333,838		63,333,838
SECTION NO. 3			
Implied Potentially Vulnerable" Deposits (20% of Total Deposits)	23,218,640	Cash (20%)	6,243,728
		U.S. Gov'ts (due in one to 5 years)	16,875,015
		U.S. Savings Bonds	99,900
TOTAL SECTION NO. 3	23,218,643		23,218,643
SECTION NO. 4			
Implied "Seasonal and Volatile" Deposits (26% of Total Deposits)	29,635,070	Cash (Remainder)	5,104,230
		Federal Funds Sold	8,000,000
		U.S. Gov'ts (due in one Year or Less)	16,530,840*
	29,635,070		29,635,070
TOTAL LIABILITIES	$124,513,360	TOTAL ASSETS	$124,513,360

*$101,776 deducted from one-year governments, and from deposits to bring statement of 3/12/59 into accordance with bond list of 3/4/59.

Date of Statement: 3/12/59
Date of Bond List: 3/4/59
Date of Analysis: 4/15/59

SCHEDULE 6

SEASONAL FLOW OF FUNDS
(000 omitted)

FIRST HALF OF YEAR

Spring Inflow and Outflow

First Six Months	Change in Deposits	Change in Loans	Total Outflow	Total Inflow
1951	+ 573	+ 962	389	
1952	+ 211	+2484	2273	
1953	- 562	+1858	2420	
1954	-3604	+2696	6300	
1955	+2527	+5808	3281	
1956	-7838	-4369	3469	
1957	+2083	+ 126	2209	
1958	+8966	-6715		2251

LAST HALF OF YEAR

Fall Inflow and Outflow

Last Six Months	Change in Deposits	Change in Loans	Total Outflow	Total Inflow
1951	+7139	-1735		8874
1952	+8363	+ 961		7402
1953	+5809	- 545		6354
1954	+8078	+ 795		7283
1955	+5960	+8674	2714	
1956	+9172	+1672		7500
1957	+2191	+7068	4877	
1958	+8094	+16491	8397	

SCHEDULE 7

MATURITIES
(Par Value)

YEAR	U.S. GOVERNMENT OBLIGATIONS	PERCENT OF TOTAL DUE EACH 5-YEAR PERIOD	PERCENT OF TOTAL CUMULATIVE FOR 5-YEAR PERIODS
1959	$13,210,000		
1960	6,151,000		
1961	4,650,000		
1962	2,000,000	82.5	82.5
1963	6,500,000		
1964	1,500,000		
1965	4,000,000		
1966	500,000		
1967	50,000	15.3	97.8
1968			
1969			
1970			
1971			
1972			
1973			
1974			
1975			
1976			
1977			
1978			
1979			
1980	500,000	1.3	99.1
1981			
1982		.3	
1983	140,000	.3	99.4
1984			
1985	224,000	.6	100.0
TOTAL	$39,425,000		

The first factor to be considered is the relationship of capital accounts to bondholdings and other risk assets. My conclusion is that the Bank's capital position continues strong. This is evident from the various capital ratios in Schedule 2 and Schedule 3. The ratio of Capital Funds to Total Assets less Cash and Governments is 13.4, compared to a national average of 14.8. Particularly significant,also, is the ratio of "Free Capital" to Estimated Risk -- 101% for the Albuquerque National, compared to a national average of 100.5%. The maintenance of these ratios at these favorable levels, while in the process of great expansion of plant, speaks well for the Albuquerque National.

The next factor concerns the character of changes in loans and deposits. When loans increase, there should, by the logic of money and banking, be an equal increase in deposits. An increase in deposits, less than that shown by loans, or a decrease in deposits while loans are increasing, would represent a net outflow of funds from the Bank. The reverse situation would indicate a net inflow. These flows for the Albuquerque National Bank over the past decade are shown in Schedule 6. As evidenced by Schedule 6, 1957 and 1958 (in addition to being expansion years) have been years in which the normal flow of funds into and out of the Bank just about reversed itself from the trend of the past. For the first time during the nine year period shown in the chart, there was a net inflow of funds in 1958 during the first half of a calendar year. During the last half of the

year, when there used to be an inflow of funds, three of the last four years have shown a net outflow. Demand for loans during the last half of 1958 was particularly heavy, and on December 31, 1958, the statement of condition showed loans of over 50% of deposits for the first time since the earliest years of the Bank's history.[1] Perhaps the seasonal flow of funds in Albuquerque has changed permanently. Future years will tell for certain, but the chart indicates at least the beginning of a change in trend.

Another important aspect of the account is liquidity. In this regard, the ratio of Cash and One-year Governments to Deposits in Schedule 2 is particularly significant. For the Albuquerque National Bank on the date of the analysis it is 35%, compared to a national average of 25.3%.

Schedule 5, the Reverse Breakdown of Statement of Condition, is very pertinent to the liquidity factor. It attempts to show how the assets of the Bank are being used to support the different deposit categories of liabilities. Basic to the analysis of Schedule 5 is the fact that short term bonds of high credit rating are substantially less subject to the risk of wide market fluctuations (discussed above). Accordingly, as a secondary reserve for liquidity purposes, i.e., to achieve maximum marketability at a minimum risk of loss, short terms seem the only outlet suitable. For the purposes of Schedule 5, bonds have been classified into the three categories shown below. Opposite these are indicated

---

[1] This ratio was back to 42.8 by March 12, 1959 (See Schedule 2).

the type of deposits that most probably can be properly employed in issues in these maturity categories.

Maturity Range	Type of Deposit
Governments due or callable beyond five years Other bonds due beyond three years	"working" or basic deposits
Governments due or callable beyond one year but not exceeding five years High grade other bonds due up to three years	Deposits that are potentially, but probably not immediately, vulnerable to withdrawal
Governments of maturity up to one year Finance company and commercial paper, call loans, bank acceptances, etc.	Deposits that are seasonal and especially vulnerable to immediate withdrawal

A brief explanation of the deposit categories may be in order.

By "working" or basic deposits is meant the portion of the bank's deposit liability which is likely to remain with the bank under virtually any conditions, i.e., even through a period of severely depressed economic conditions.

By potentially vulnerable deposits is meant deposits that might flow out, not during the period immediately ahead for seasonal or other reasons, but over a period of years in response to changing economic conditions in the country or in the bank's locality or by reason of changes in competitive conditions.

Seasonal and especially volatile deposits is a self-

explanatory caption referring to the movements over the next year that the bank may expect.

By "Reverse" Breakdown is meant that this statement was prepared in the reverse manner. It can be prepared by the individual bank by analysis of its deposits to determine exactly what percentage of deposits fall into the three categories. This would give a direct answer to how much in asset funds should be employed in the various maturity ranges. In reverse, the statement is prepared from the asset side. The assets are broken down and from that breakdown, the implied percentages of deposits are derived. Thus, if it is felt by the bank that the percentage of deposits implied in Section No. 4 is smaller than the actual percentage of volatile deposits, some shortening of maturities would probably be indicated. If the percentage in Section No. 4 is larger than the actual case, then some lengthening of maturities might be considered.

The management of the Albuquerque National has felt that in view of the heavy dependence of Albuquerque's economy on various governmental enterprises connected with the atomic energy program, the Albuquerque banks probably have higher percentages of fairly volatile deposits than most banks in the country. Thus, Section No. 4 of the Schedule shows the Albuquerque National prepared to support fully 26% of its deposits by these short term funds.

The bank's strong liquidity position cannot be questioned.

There is a long used formula for determining what portion

of a bank's funds can properly be employed in long term securities, which runs as follows: Beginning with the Capital Funds available, the Fixed Assets are deducted, and then ten percent of the Risk Assets (Loans and Investments other than Governments) are deducted; to this is added two thirds of Time Deposits (excepting public funds). This figure should approximate the amount which might be properly used for long term investment.[1]

Using this formula, as shown in Schedule 4, and the figures of December 31, 1958 Statement of Condition, the Albuquerque National Bank comes up with a total of $14,967,143 allowable for long term investment. At the time, actual long term investment totaled $6,216,029, leaving the bank with a margin of safety of $8,751,114.

It is evident that the liquidity position of the bank is strong. It is also fairly evident from these figures, and from the percentage figures in Schedule 7, that the bank's secondary reserve position is adequate. Bondholdings, as shown in Schedule 7, are mainly in the short and intermediate term areas.

The most obvious move indicated by these analyses, would be a moderate lengthening move by the bank in its bond account. Taken by themselves, the figures indicate that such a move could easily be made without endangering either the capital position or the liquidity position of the bank. On

---

[1]Reprinted in Banking, Journal of the American Bankers Association, March, 1959.

the other hand, however, there are certain market circumstances to be considered.

During the month of February, 1959, the prices of government securities improved in all maturity ranges. This seemed to indicate at least the beginning of what might be "easier money" policies on the part of monetary authorities. But on March 2, the Reserve Banks in New York, Chicago, Philadelphia, and Dallas raised the rediscount rate from 2½% to 3%. This would seem to indicate that the monetary authorities had no present intention of easing the credit situation. Furthermore, the Federal Reserve Board made a review of the intentions of consumers, which resulted in the conclusion that there would be no let up in consumer purchases. All indications are that 1959 will continue to be a year of recovery and that demand for new loans will tend to increase rather than decrease.[1]

In Albuquerque, the effects of the 1957-58 national recession were negligible. New construction and other data continue to indicate that 1959 will be an even bigger year in Albuquerque than in other parts of the country.[2] Demand for loans, so markedly high in 1958, will probably be even greater as 1959 moves on.

---

[1] Banking, Journal of the American Banking Association, March, 1959. Various articles relating to the outlook for 1959.

[2] Albuquerque Progress, published by the Albuquerque National Bank in January 1959, showing the results statistically in 1958 and outlook for 1959 in Albuquerque.

For these reasons, I believe that the Albuquerque National Bank would probably do better to continue its policy of staying primarily in the short and intermediate areas, thereby leaving the margin noted above available to meet the pressure of these loan demands. Again, this is the prime function of any bank, and it is here that risks must be taken which should not be taken in the bond account. Serving Albuquerque always has been the bank's prime objective. The small increase in income that would come from lengthened maturities would be insignificant relative to the bank's responsibilities in a growing metropolis.

The only major risk faced by a bank with a bond account of longer average maturities is that of a rising interest rate which depreciates the value of the bond account. As we have seen, as of December, 1958, when the market for Governments was extremely weak, the total depreciation of the Albuquerque National's bond account amounted to only 2.4% of the total. This type of loss need be realized voluntarily only to establish tax losses, etc. If the secondary reserve is maintained properly, this risk can be effectively hedged by simply not selling the bonds when the price is not right. Only when a bank is forced to sell and sustain losses, does this risk become serious.

BIBLIOGRAPHY

PRIMARY SOURCES

1. Minutes of the meetings of the Board of Directors of the Albuquerque National Bank, 1924 through 1959.

2. Albuquerque National Bank Statements of Condition, 1924 through 1959.

3. Reports prepared by various officers of the Albuquerque National Bank, relative to Assets, Deposits, Earnings, Capital, etc.

4. Correspondence files of the Albuquerque National Bank, relative particularly to the 1933 banking crisis.

5. Reports by the Office of the Comptroller of the Currency and the National Bank Examiners, relative to examinations of the Albuquerque National Bank, 1924 through 1959.

6. Report on the Bondholdings of the Albuquerque National Bank, prepared by the Wells Fargo Bank and Union Trust Company of San Francisco, 1953.

7. Interviews with President Luthy and other senior officers of the Bank.

SECONDARY SOURCES

Government Publications

1. Board of Governors of the Federal Reserve System, Banking and Monetary Statistics, (National Capital Press, Washington, 1943).

2. U. S. Department of Commerce, Statistical Abstract of the United States, (U. S. Government Printing Office, Washington, annually).

3. U. S. Bureau of the Census, Seventeenth Report, (U. S. Government Printing Office, Washington, 1931).

4. U. S. Department of the Treasury, Report of the Secretary of the Treasury, (U. S. Government Printing Office, Washington, annually).

Government Publications (Cont'd)

5. Board of Governors of the Federal Reserve System, Report of the Board of Governors, (National Capital Press, Washington, annually).

6. U. S. Department of the Treasury, Report of the Federal Deposit Insurance Corporation, (U. S. Government Printing Office, Washington, annually).

7. Board of Governors of the Federal Reserve System, Federal Reserve Chart Book on Financial and Business Statistics, (U. S. Government Printing Office, Washington, monthly), and Historical Supplement, (annually).

8. Board of Governors of the Federal Reserve System, Federal Reserve Bulletin, (Washington, monthly).

9. Board of Governors of the Federal Reserve System, Banking Studies,(Washington, 1952).

10. New Mexico State Banking Department, Report of the State Bank Examiner, (Santa Fe, annually).

Periodicals and Journals

1. "1959 - A Bond Loss Work-Out Year for Banks," Burroughs Clearing House, January, 1959.

2. Albuquerque Progress, Albuquerque National Bank Publication, January, 1959.

3. Albuquerque Journal, Albuquerque Publishing Company, various issues, 1924 and 1933.

4. Herbert Bratter, "We Need More Facts to Judge Municipals," Banking Journal of the American Bankers Association, March,

5. Thomas L. Popejoy, "Analysis of the Causes of Bank Failures in New Mexico, 1920 to 1925," Thesis for degree of Master of Arts (New Mexico University Press, Albuquerque, 1931).

6. John J. Moynihan, "Should Banks Buy Long Term Bonds," Harvard Business Review, November, 1950.

Books

1. Robinson, Roland I., The Management of Bank Funds, (New York: McGraw-Hill, 1951).

Books (Cont'd)

2. C. F. Childs and Company, Concerning Government Securities, (Chicago: Lakeside Press, 1947).

3. Goldenweiser, A. E., Monetary Management, (New York: McGraw-Hill, 1949).

4. Kent, Raymond P., Money and Banking, (New York: Rhinehart and Company, Inc., 1948).

5. James, Marquis and Bessie Rowland, Biography of a Bank - The Story of the Bank of America N. T. & S. A., (New York: Harper Bros., 1954).

6. Holt, C. C. and Keith, N., 28 Days - A History of the Banking Crisis, (Binghamton, N. Y.: Greenberg Publishers, Inc., 1933).

7. Westerfield, R. B., Money, Credit, and Banking, (New York: Ronald and Company, 1938).

8. Jones, Jesse H., Fifty Billion Dollars, (New York: MacMillan Company, 1951).

IMPORTANT!

Special care should be taken to prevent loss or damage of this volume. If lost or damaged, it must be paid for at the current rate of typing.