

FEDERAL RESERVE BANK OF DALLAS
1988 ANNUAL REPORT



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Architectural designs of banks have changed as dramatically over the years as the services these institutions perform. Once, banks were built to resemble fortresses. Their exteriors provided the image of strength and stability. Their interiors exuded the image of security. Vaults were in the main lobby; tellers worked behind cages.

After World War II, the architectural trends in banking changed to reflect a friendlier, more customer-oriented approach. The architecture of financial institutions rapidly became less monumental in outward appearance and more operationally efficient and aesthetically inviting.

In the Eleventh Federal Reserve District, the diversity of cultures and people in Texas, Louisiana and New Mexico is reflected in the architecture. Our annual report salutes the design, history and innovation of financial institutions in this District.



M E S S A G E



Robert H. Boykin, (left); Adm. Bobby R. Inman, USN (Ret.)

For the states comprising the Eleventh Federal Reserve District—all of Texas and parts of Louisiana and New Mexico—the events during 1988 are viewed with guarded optimism in that there was renewed, though modest, economic strength. And in the year ahead, an acceleration of economic growth in the District is anticipated. This somewhat stronger regional economic outlook is likely to be led by a more broadly-based growth in manufacturing, particularly because of capacity constraints in other parts of the country.

Despite this limited economic optimism, solutions to the problems for financial institutions, both in this District and elsewhere in the country, have not, and will not, come easily. During 1988, more than 200 banks failed nationwide, more than 100 banks were closed in Texas alone, and 87 savings and loans were merged under the Southwest Plan. Moreover, the FDIC experienced the first loss in its 54-year history, and Congress continued to wrestle with the future of both the thrift industry and deposit insurance. In the year ahead, District financial institutions will remain troubled, and, without recapitalization, a turnaround in District banking conditions could lag the economic

recovery by at least two years.

¶ In our annual report this year, attention is focused on the changes to the banking structure over the past decade. One cannot separate the current events in the financial industry from the events in the District's economy within those last 10 years, particularly within the last four. Overbuilding and declining energy prices depressed both construction activity and real estate prices, causing severe economic problems in the District for both banks and thrifts. This situation was aggravated by problems associated, not only with energy and real estate loans, but also with loans to other businesses adversely affected by these factors. Much of what happened in 1988 and is likely to occur in 1989 is not rooted in the events of 1988 but rather in those of late 1985 and early 1986.

¶ Nevertheless, there is encouragement in the fact that the District's financial industry already is demonstrating capabilities to meet the needs of the future. At no time in this District's history have there been more changes occurring or more challenges to meet. Since the 1970s, the banking industry has had to face incredible change, competition and uncertainty. Although high risk is inherent in change, also inherent is the potential to break new

ground and redefine the direction of the future.

¶ The Federal Reserve has had changes too—changes from which a great deal has been learned. This knowledge has been applied to help the financial industry and the payments system operate more efficiently.

¶ In the area of financial services, Congress directed the Federal Reserve to implement a policy limiting the "holds" financial institutions can place on deposited funds and expediting the return of unpaid checks. In response, we implemented a new regulation, Regulation CC. This effort required more efficient and more technologically advanced processes and the cooperation and further education, not only of those of us in the Federal Reserve, but also of bankers and their customers. While continued adaptations will be required, this process was made less difficult in this District because of our earlier experience in expediting returns of checks in a pilot program for the Federal Reserve.

¶ The Federal Reserve also expanded its efforts to ensure the integrity and viability of its electronic services by enhancing and extending its existing disaster recovery program. Efforts in this area will ensure that transactions made electronically, not only are

the most efficient in the world, but are protected from unexpected events, whether natural or man-made.

¶ Throughout this year's annual report are photographs of financial institutions—past and present—from Texas, Louisiana and New Mexico. What is striking about the evolution in the banking industry is that, while the rules of operation and competition have changed along with the architectural style of the buildings, financial institutions still exist to serve individual customers and their communities. Those who continue to find this business important and interesting are to be commended, but still more commendable are those who make top priorities of commitments to personal attention to service, quality and innovation. The future of the financial industry lies with those who have the ability and the strength to maintain these commitments in the face of continuing change.



Bobby R. Inman
Chairman of the Board



Robert H. Boykin
President and Chief Executive Officer

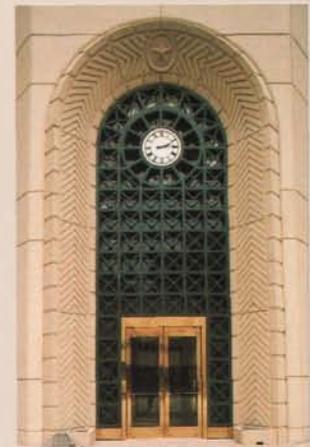
TEXAS

In Texas, banking got off to a slow start thanks to Sam Houston. Houston, a close friend of anti-banking advocate President Andrew Jackson, made sure that there was no provision for chartering banks in the Texas constitution of 1845. Out of necessity, merchants provided primitive banking services. Private, unregulated banks opened around the state.

With the passage of the National Banking Act in 1864, national banks were chartered in the state for the first time. Following the Civil War, the Texas constitution of 1869 contained no clause prohibiting state-chartered banks, and the state legislature assumed the authority to do so. Between 1870 and 1871, 30 banks were chartered by the state, but only eight opened. Branch banking was also allowed but did not occur.

In 1875, following a severe financial panic in 1873, the prohibition against state chartering of banks returned to the state constitution, leaving only private and national banks operating in the state.

Even with the prohibition of state banks, Texas was the first state to have a bankers association. The Texas Bankers Association was organized in Lampasas in 1885 to address the issue of state-chartered banks. At that time, Texas was the only state that prohibited state banks. In 1904, state chartering returned to Texas. But branch banking was prohibited. By 1910, only 14 of the 249 counties in Texas had no bank.



T H E S T R E N G T H T O C H A N G E

There have been few turning points in the history of the United States' banking industry. In fact, for the 50 years between 1930 and 1980, regulation of the banking industry remained essentially unchanged. But today the banking industry faces a serious turning point that has been preceded by more than a decade of deregulation and dramatic economic events. Currently, attention is focused on the role of deposit insurance, the viability of savings and loans, and expanded powers for commercial banking firms. As in the past, policy discussions will center on competitiveness, flexibility and stability. As we look back, the turning point the banking industry faces today will be as significant as any of the major turning points mentioned in this historical overview.

Historical Turning Points

In the early 19th century, commercial banks were licensed by individual states and their scope and authority were basically confined to the state granting their charters. There were two 20-year episodes (1791-1811 and 1816-36) when federally chartered institutions operated across the fledgling nation. These were the First Bank and the Second Bank of the United States. Each charter

was allowed to lapse because of political opposition to national banking institutions. In his veto of the recharter of the Second Bank, President Andrew Jackson decried the "exclusive privilege" and "monopoly" enjoyed by the Bank.

By the 1860s, two pieces of federal legislation—the National Currency Act (1863) and the National Banking Act (1864)—established a system of nationally chartered banks to be regulated by a newly created Office of the Comptroller of the Currency. There is no indication that Congress intended to prevent branching by the new national banks. Successive Comptrollers of the Currency, however, interpreted the acts as precluding branching by even national banks. The result was the establishment of the dual banking system we have today whereby a bank can choose its chartering agency and, thus, its regulatory structure.

The next major turning point was the creation of the Federal Reserve System in 1913 following several major financial panics. Congress set up the System to act as lender of last resort in order to ease the severity of financial panics and provide greater stability for both the banking system and the economy.

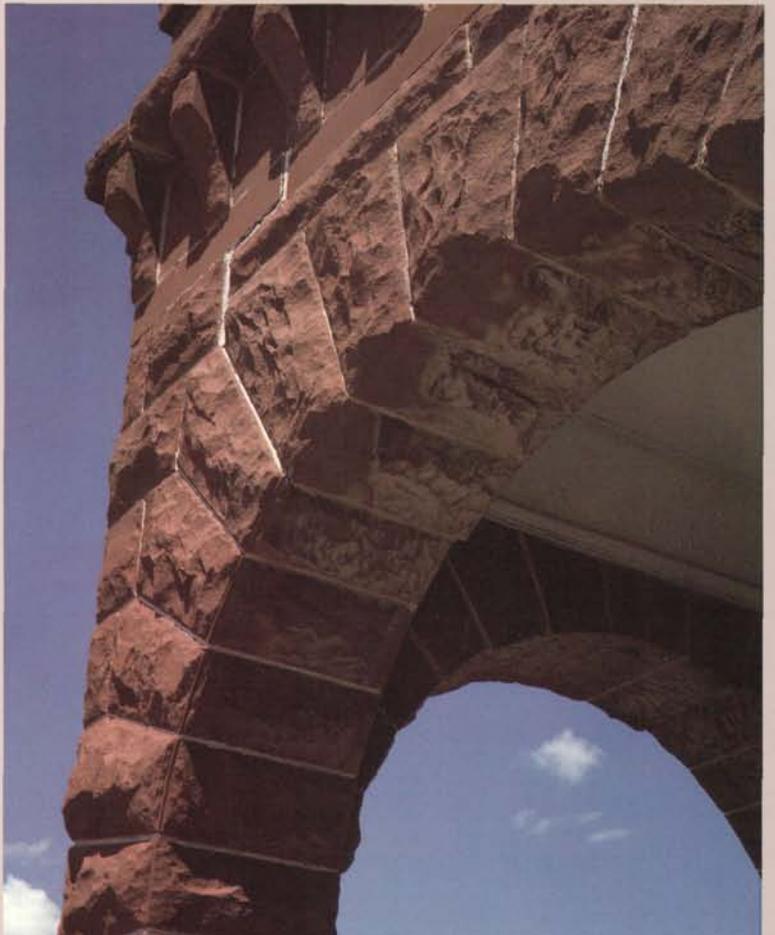
The newly created Federal Reserve System was unable to pre-

vent a rising tide of bank failures in the otherwise prosperous 1920s. To a large extent, these failures reflected distress in the agriculture sector. Farm prices were in decline and rural banks suffered. Approximately one out of six banks failed in the 1920s. Unfortunately, this was a record soon to be broken.

Perhaps the most important turning point occurred in 1933 when a steep decline in economic activity created a genuine crisis in the banking system. One of the first acts of newly elected President Franklin Roosevelt was to declare a "bank holiday" in March 1933 to stop widespread runs on banks and restore confidence in the banking system. Most banks reopened one week later and the runs were largely over. But Congress was convinced that major reform was needed and passed the Banking Act of 1933 a few months later.

The Banking Act redefined banking in the 1930s, and its effects are still prevalent. Among other things, the Act created the Federal Deposit Insurance Corporation (FDIC). In addition to providing an insurance fund, the FDIC also was given regulatory power over the institutions it insured. The Act also divorced commercial banking from investment banking by prohibiting banks from

As we look back, the turning point the banking industry faces today will be as significant as any of the major turning points mentioned in this historical overview.



T E X A S

Hard times hit both the Texas economy and the banking industry during the 1920s and lingered until World War II. The agricultural sector of the state was especially affected. After World War II, economic activity gradually improved. By the 1970s, growth in the oil industry contributed to economic prosperity in Texas. During the 1980s, the collapse of worldwide oil prices and a drop in real estate values seriously affected the economy and banking. As a result, in the late 1980s, the state legislature lifted restrictions on both branch banking and interstate bank acquisitions.

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underwriting most securities or dealing in them for their own accounts. Another significant provision of the Act prohibited all banks from paying interest on demand deposits and gave the Federal Reserve the power to set the rates for all other deposits. That led to the Fed's Regulation Q which, until 1986, governed rates paid on deposits.

☞ The 1930s also brought important turning points for savings and loan associations and credit unions. The Federal Home Loan Bank Board was established to oversee savings and loans. The Federal Savings and Loan Insurance Corporation (FSLIC), an insurance system similar to the FDIC, was established in 1934. A 1934 act permitted credit unions to be federally as well as state chartered.

☞ One issue left relatively untouched by the Banking Act of 1933 was the operation of bank holding companies. Charters of commercial banks specifically limited their activities and placed them under various types of regulatory control. However, bank owners could form bank holding companies which could operate other, nonfinancial subsidiaries. Permissible subsidiaries also included other banks, in the same or different states. Holding companies were the first break-

through in the interstate banking barrier. The Bank Holding Company Act of 1956 closed this avenue for most holding companies controlling two or more banks. This left one-bank holding companies outside the regulatory arena. As a result, they became attractive and grew rapidly in the 1960s. The Bank Holding Company Act Amendments of 1970 extended regulatory provisions to include one-bank holding companies.

☞ From the 1930s to the 1980s, regulation of the banking industry in the United States remained essentially unchanged. Each type of financial institution—banks, savings and loans, mutual savings banks, bank holding companies and credit unions—had fairly well-defined products, customers, interest rates and territories. Deregulation changed all that.

Deregulation

☞ By the late 1960s, federal banking regulators faced a difficult, and sometimes impossible, task in setting interest rate ceilings on deposits. Regulators soon realized that financial institutions—and commercial banks in particular—needed something to allow them to attract funds and avoid “disintermediation” of deposits. Disintermediation occurs

when investors withdraw funds from financial institutions and invest them directly in higher-yielding marketable securities.

☞ Two particular events led to major banking deregulation in the early 1980s. The first event was a 1970 ruling by the Federal Reserve that lifted interest rate ceilings on negotiable certificates of deposit (CDs). These CDs were large-denomination deposits (\$100,000 or more) designed to compete primarily with short-term, easily traded U.S. Treasury bills. As market rates on T-bills rose during the credit crunch of 1966, and again in the period from 1968-1970, investments in CDs declined significantly. As a result, in 1970, the Federal Reserve suspended interest rate ceilings on large negotiable CDs with maturities of 30 days or more. The availability of large, negotiable CDs paying market interest rates created a new money market instrument. But interest rates on retail deposits (less than \$100,000) continued to be capped. This situation resulted in the introduction of money market mutual funds by securities firms. Throughout the 1970s, and especially during times of high market interest rates, the number of these funds and their assets grew. In essence, market forces propelled the deregulation process.

☞ The second event leading to

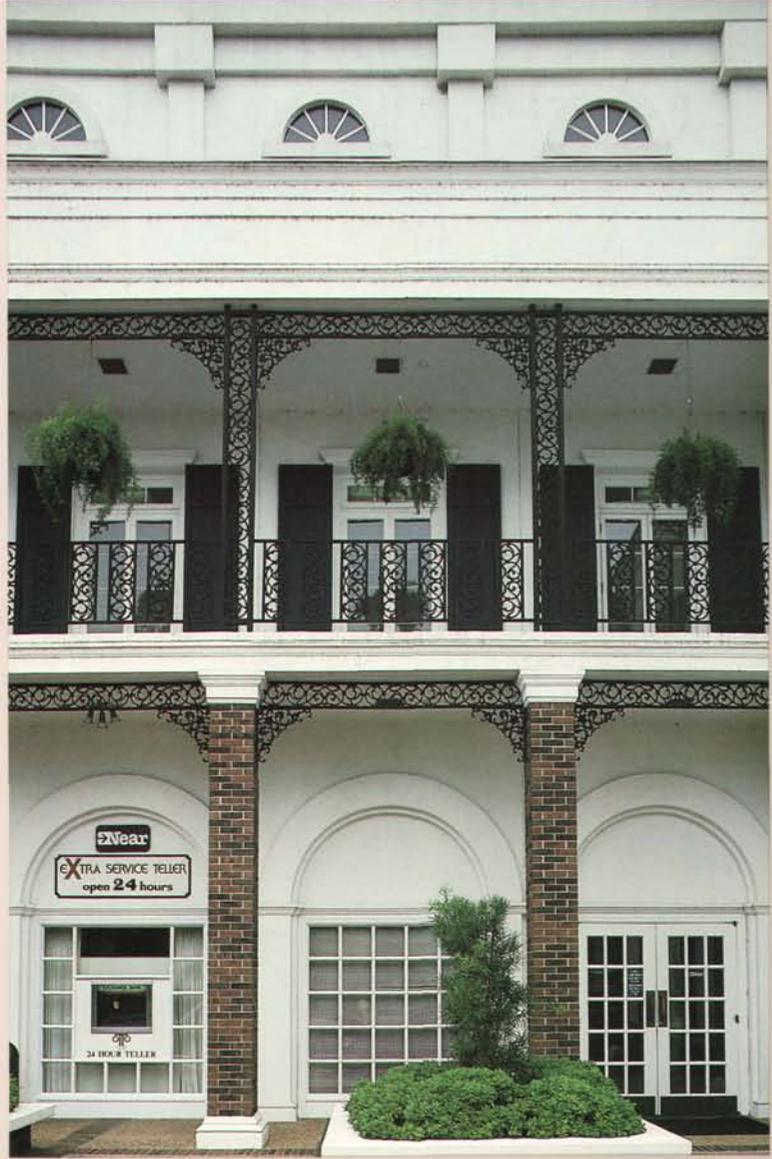
In essence, market forces propelled the deregulation process.

LOUISIANA

Banking history in Louisiana is tied to United States history, but also has roots in French laws and customs. In the 1800s, Louisiana's economy was based on agriculture and foreign trade. For instance, in 1834, exports handled by the port at New Orleans exceeded those at New York City. The cotton market in New Orleans was the second largest in the world.

Early in the 1800s, the organization of a bank required the state legislature's approval. By 1837, there were 16 banks, with main offices located in New Orleans and branch offices serving other cities. In 1837, the cotton market crashed, devastating cotton brokers, farmers and bankers.

In 1842, Louisiana passed the first state law that provided protection for depositors in case of bank failure. Based on French law, the act said that depositors would share equally with note holders in the case of liquidation.



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further deregulation was the introduction of negotiable order of withdrawal (NOW) accounts at mutual savings banks in Massachusetts. NOW accounts were revolutionary because they paid interest *and* allowed checks to be written against them—a combination that was not possible for banks. As a result of these events, two pieces of legislation were passed in the early 1980s to deal with the situation. With the passage of those acts, a new era in banking was born.

§ Money Market Mutual

Funds. Money market mutual funds (MMMFS) were introduced in 1973 and grew rapidly—especially by 1979 and into the early 1980s. MMMFS are financial intermediaries that allow small- and medium-sized investors to pool their funds and buy shares in a portfolio of short-term and large-denomination obligations of banks, large corporations and the federal government. In the early 1980s, yields on these types of accounts were higher than most investors could receive from financial institutions. Not only were shares easily redeemed, but most MMMFS provided check-like services. The popularity of these accounts rose dramatically and within a few years, investors had deposited more than \$200 billion in them. The popularity of

MMMFS posed a major competitive challenge to the banking industry. These funds were depleting the deposits placed in banks by offering flexibility and interest rates the banks could not. The introduction of MMMFS led bankers to recommend a “level playing field” among the participants in the financial marketplace.

§ **NOW Accounts.** Another revolution was occurring in Massachusetts about the same time. In the early 1970s, NOW accounts were authorized as an experiment for mutual savings banks. In 1973, Congress formally approved the new account for all financial institutions in the state. In 1976, a federal statute sanctioned their issuance throughout the New England states. Congress also approved NOW accounts for New York in 1978 and for New Jersey in 1979. These accounts were extremely popular and quickly spread throughout the New England states, New York and New Jersey. The success of NOW accounts led some to recommend them for the entire nation.

§ **Legislative Action.** In addition, a rapidly changing economic environment brought problems to the banking industry. Rising interest rates and inflation were the primary culprits. Bankers and consumers began recommending phasing out deposit rate ceilings,

permitting financial institutions to offer variable rate mortgages and generally easing other forms of regulation. In 1980, Congress passed the Depository Institutions Deregulation and Monetary Control Act. The Act made sweeping changes in banking. The principal components of the Act were:

- The Depository Institutions Deregulation Committee (DIDC) was established to oversee the orderly elimination of interest rate ceilings on all deposits by March 31, 1986.
- The Federal Reserve was given the power to set reserve requirements for all financial institutions that maintained certain types of transaction accounts.
- Banks and thrifts were allowed to offer NOW accounts.
- Federally chartered savings and loans were authorized to invest up to 20 percent of their assets in consumer loans and commercial paper.
- State usury laws were preempted for residential mortgages.

§ While the Monetary Control Act sent significant ripples throughout the banking industry, some fine tuning was necessary. Further steps toward that end were taken in 1982 with the Garn-St Germain Act. The principal components of the Garn-St Germain Act included:

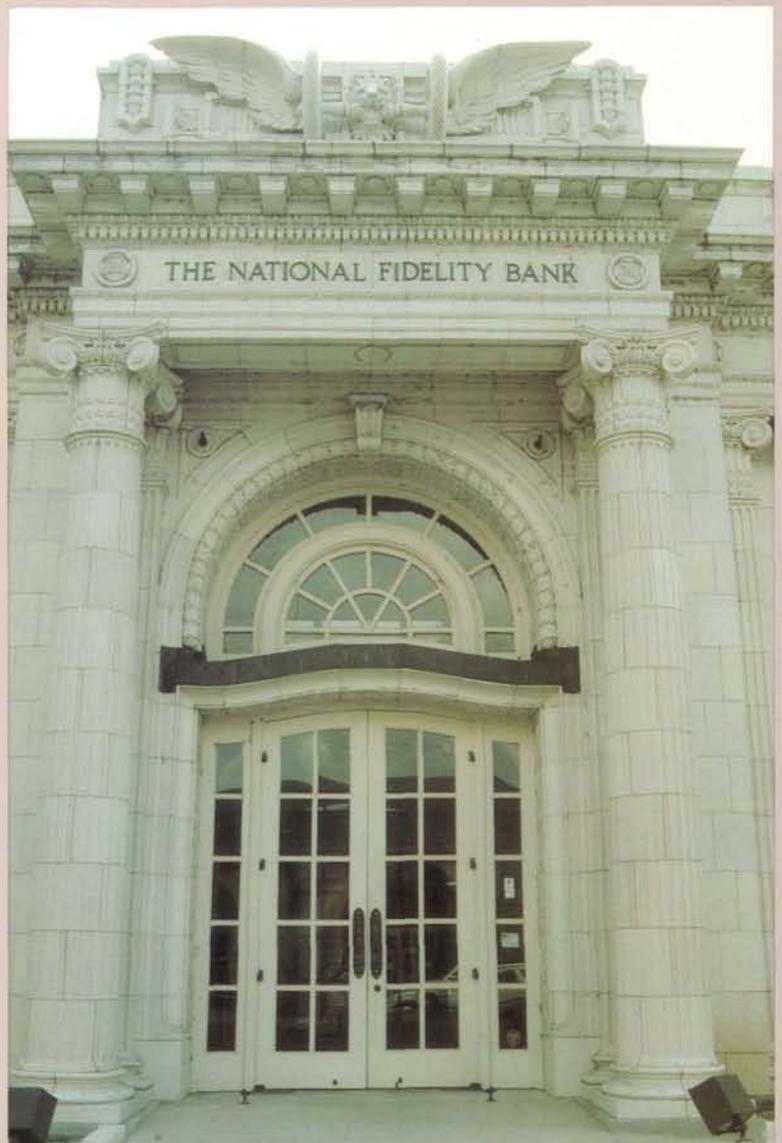
- The DIDC was instructed to authorize an account for banks that would compete directly with

A rapidly changing economic environment brought problems to the banking industry.

LOUISIANA

In the period prior to the Civil War, virtually all banks issued their own notes, most of which enjoyed only local circulation and were usually not accepted at face value. Citizens Bank was organized in 1833 to help finance the Lake Borgne Canal. Its \$10 notes were printed with the French word for 10, or *dix*. These notes became known as "dixies"—a term that eventually became the nickname for the South.

Throughout the decades, banking in Louisiana has been closely related to the agriculture, shipping and oil industries.



MMMFs.

- Federally chartered savings and loans were permitted to offer demand deposits for business loan relationships.
- Thrifts were allowed to invest 55 percent of their assets in various types of commercial loans and 30 percent in consumer loans.
- State chartered banks and thrifts were allowed to offer variable rate mortgages.
- Federal charters for new mutual savings banks were authorized.
- In instances involving a failing bank or thrift, federal regulatory agencies were authorized to allow mergers of banks with thrifts or mergers that crossed state lines.

☞ New merger guidelines as a result of the Garn-St Germain Act spurred regional reciprocal banking arrangements. Barriers to interstate banking have fallen quickly in the 1980s. In fact, as of January 1989, all but five states have passed some form of liberalized interstate banking law. By the early 1990s, we will see the full effects of the erosion of interstate barriers when many highly populated states drop their regional reciprocity provisions and open themselves to nationwide reciprocal banking.

Issues Affecting
the Current Turning Point

☞ Today, the issues affecting the current turning point in the banking industry are complex and far-reaching in their impact. Rapidly changing institutions and business strategies, spurred by technological advancement and financial innovation, have broken through the regulatory barriers to competition that were erected in the aftermath of the Great Depression. The financial services marketplace has continued to become increasingly sophisticated, integrated, international and competitive. These changes, coupled with the severe difficulties encountered by a large number of financial institutions, both in the Eleventh District and elsewhere in the country, have brought to a head the need for serious review of the U.S. regulatory structure. Calls are increasing for legislative and regulatory action to address three broad and interrelated points of change: the thrift crisis, deposit insurance reform, and the expansion of bank powers.

☞ The most pressing area of financial policy involves the future of the thrift industry and the FSLIC. As the financial industry continues to become more competitive and integrated, the differences between thrifts and banks

are eroding. At the same time, the recent huge losses incurred by U.S. thrifts and the resulting insolvency of the FSLIC are prompting serious attention on the part of policy makers. The exact details regarding how the regulatory structure will be changed remain unclear.

☞ In reaction to the thrift crisis, policy makers are focusing considerable attention on the federal deposit insurance system. Their concern has been magnified as the thrift crisis has brought to light some of the negative and unintended consequences of the deposit insurance system. While the system has served a stabilizing role in helping to prevent banking panics, it also has subsidized excessive risk taking by allowing institutions to pay fixed insurance premiums, regardless of the degree of risk in their loan portfolios. Moreover, those in charge of the deposit insurance system have allowed deeply troubled institutions to continue operating. Troubled institutions have offered premium rates to attract funds, thereby raising funding costs for their healthy competitors. In addition, depositors are often provided a perverse incentive to utilize the most risky financial institutions because of the generally more attractive interest rates offered by such institutions. The federal

The federal deposit insurance system obviously deserves serious attention as part of any regulatory reform package.



NEW MEXICO

New Mexico history is filled with tales of ambitious and enterprising people who came to the state to improve their economic condition. In the earliest days, merchants financed trade and commerce. These merchant-bankers provided most banking services. Given the special characteristics of the frontier, these "bankers" probably fulfilled banking needs effectively.

Their effectiveness may have actually delayed the coming of banks to New Mexico. Banking in New Mexico also was hampered by the state's sparse population, a shortage of currency, the agricultural basis of the economy, and the late arrival of railroads.

deposit insurance system obviously deserves serious attention as part of any regulatory reform package, especially in light of continued expansion in the range of activities allowed for financial institutions.

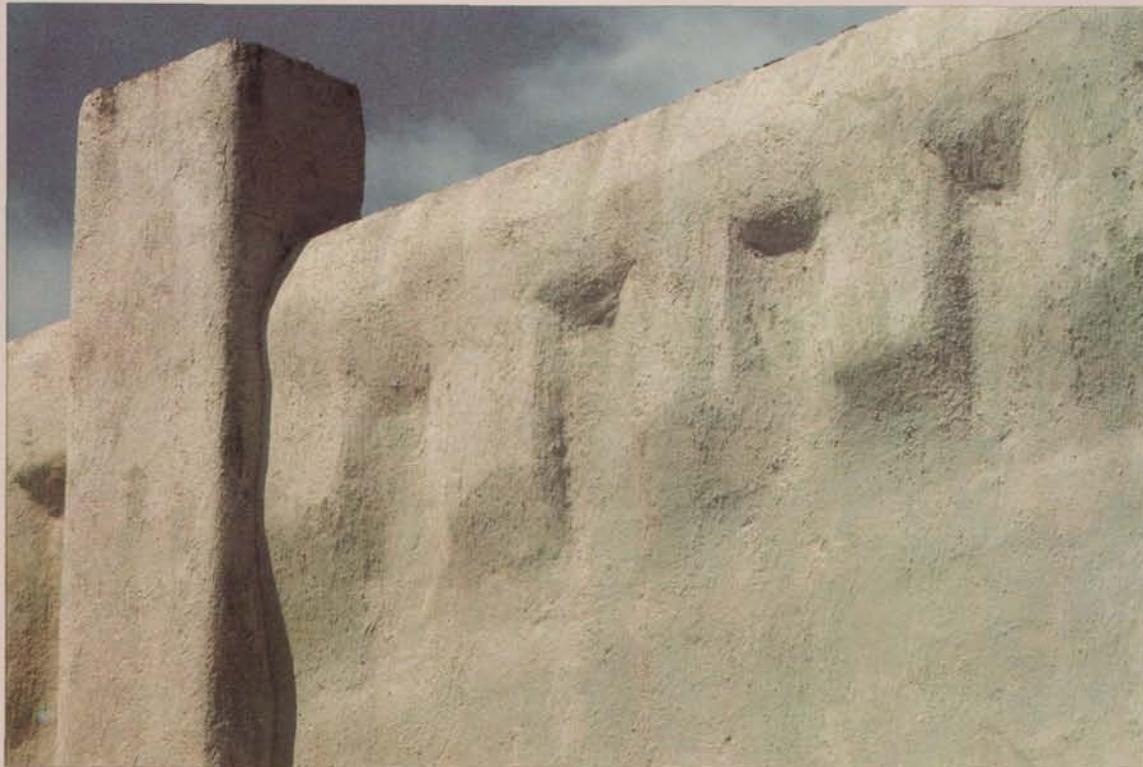
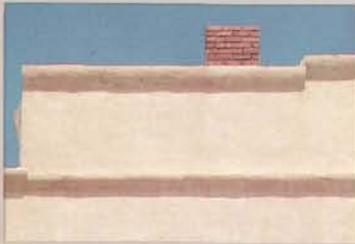
Despite the degree of deregulation that has already occurred, changing market conditions continue to underscore the need for some expansion of the powers financial institutions are allowed to exercise. Financial innovation continues to increase the gains from integrating a variety of financial services within a single firm, and banking organizations, now more than ever, require new powers to serve their customers. In response, recent Federal Reserve Board rulings allow bank holding companies additional leeway to raise money for corporations in the securities markets. Additional steps in this direction are likely to occur. Recognizing concerns that the new securities powers could lead to an excessive concentration of financial power among banks, the Fed's rulings require banking organizations to create "firewalls" designed to limit the flow of funds between the new securities affiliates and bank affiliates within the same holding company. This also limits the ability of holding companies to use bank deposits insured by the federal government

in financing their securities affiliates.

Summary

While the basic structure of the nation's present-day banking industry was determined in the 1930s, the rapidity of change in that structure has increased dramatically during the 1980s. This has made managing and regulating financial institutions an increasingly complex task. Strict definitions of permissible lines of commerce and structure are becoming less practical. For financial institutions, the changing environment means new challenges and opportunities. As the complexity of the financial marketplace increases, so should the flexibility with which financial institutions operate. For regulators and legislators, managing the direction of financial innovation is paramount. Together with the Congress, financial institutions and their regulators must resolve the issues of the thrift crisis, deposit insurance reform, and the expansion of bank powers. The strength of our nation's banking industry has always been in the hands of those who have had the ability to innovate and the strength to change.

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NEW MEXICO

It was not until the completion of rail lines and the rise of agricultural prices at the turn of the century that the New Mexico banking industry experienced significant growth. In 1900, only 26 banks existed in New Mexico. By the time the territory became a state in 1912, at least 122 banks had been established in the area.

Initially, banking in New Mexico was closely tied to the agriculture sector. As agricultural prices rose and fell, so did bank profits. This relationship continued throughout the first half of the 20th century. As the state's development of mineral, defense, and oil and gas industries increased, so did the number of banking firms in larger cities.

The post-World-War-II expansion of banking in New Mexico occurred during the greatest period of economic growth in the state's history. The increase in economic activity had the greatest effect on banking in larger cities.



Y E A R I N R E V I E W

As banking becomes more nationwide and worldwide in its scope, we look every day for ways to increase the speed and reliability of our services in a complex environment. During 1988, operations were highlighted by changes in check processing that resulted from federal legislation during the prior year; efforts to protect our electronic transactions from all types of disasters; reductions in paper-based services; and efforts to increase the number of service options available electronically. In addition, our supervision staff faced an unusual and challenging year in monitoring the performance of banks in this District.

Disaster Recovery

Because most of the dollar volume of transactions in the United States takes place electronically using computers and data communications equipment, financial institutions and their customers could be seriously affected by a major outage at the Dallas Fed. The reliability and availability of our computer system is crucial to smooth financial service operations. As a result of the potentially serious consequences of failures of computers and communications equipment, the Dallas Fed, and the entire Federal Reserve System, have made

disaster recovery a high priority.

To meet this priority, a disaster recovery plan was initiated for the Eleventh Federal Reserve District to ensure that services continue in the face of a traumatic computer or communications disruption. The recovery plan is designed for two types of disasters—one in which the data services operations are inoperable and one in which the entire Dallas Fed is inoperable. The plan covers the most critical electronic services—transfers of funds, automated clearinghouse, transfers of securities and accounting services.

Central to the Dallas Fed's disaster recovery plan is a building in Culpeper, Virginia. This building, located about 60 miles outside Washington, D.C., is equipped with the latest in large-scale computers and communications systems. Because of its capabilities, the Culpeper center has been chosen to serve as an alternate processing site for the Eleventh Federal Reserve District. If a severe disaster occurs at the Dallas Fed, records are reconstructed at Culpeper and operating capability is restored within the shortest possible time.

The first major test of the plan came in June 1988 when a simulated disaster forced the closing of the Dallas Fed and its transfer of funds system. Using

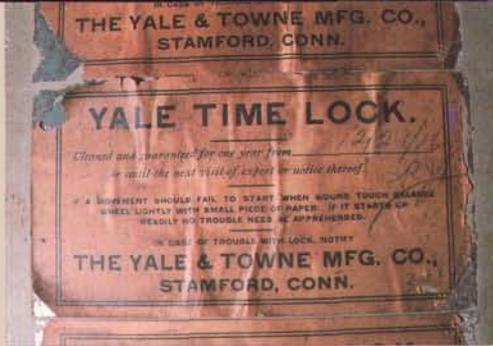
back-up copies of our software and transaction records, our data services staff and the staff at Culpeper were able to restore and verify our operating systems in under 12 hours. This simulation makes us the first Federal Reserve Bank to simulate a disaster and transfer processing to Culpeper in under 12 hours.

While the amount of time required to re-create our operations was extremely good, the Dallas Fed has plans to significantly reduce that time during 1989. Because each Federal Reserve Bank must "revalidate" its disaster recovery plans twice each year, plans are already under way to decrease the amount of time necessary to be back in business. Our goal is to make sure that, in case of a disaster, all information is recovered and all electronic services are restored quickly with a minimum of disruption to the financial marketplace.

Check Services

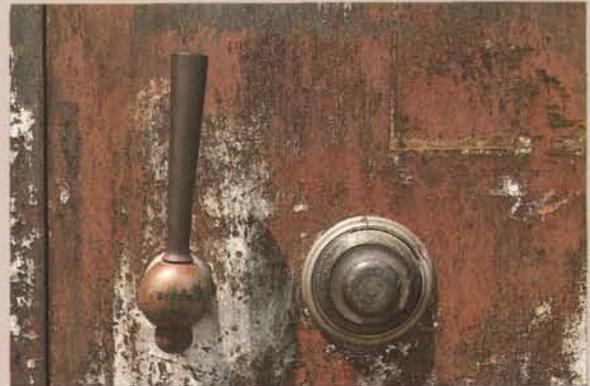
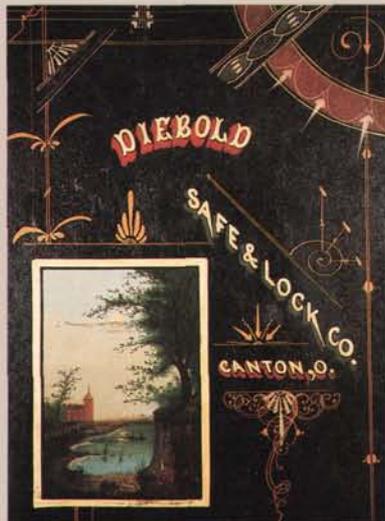
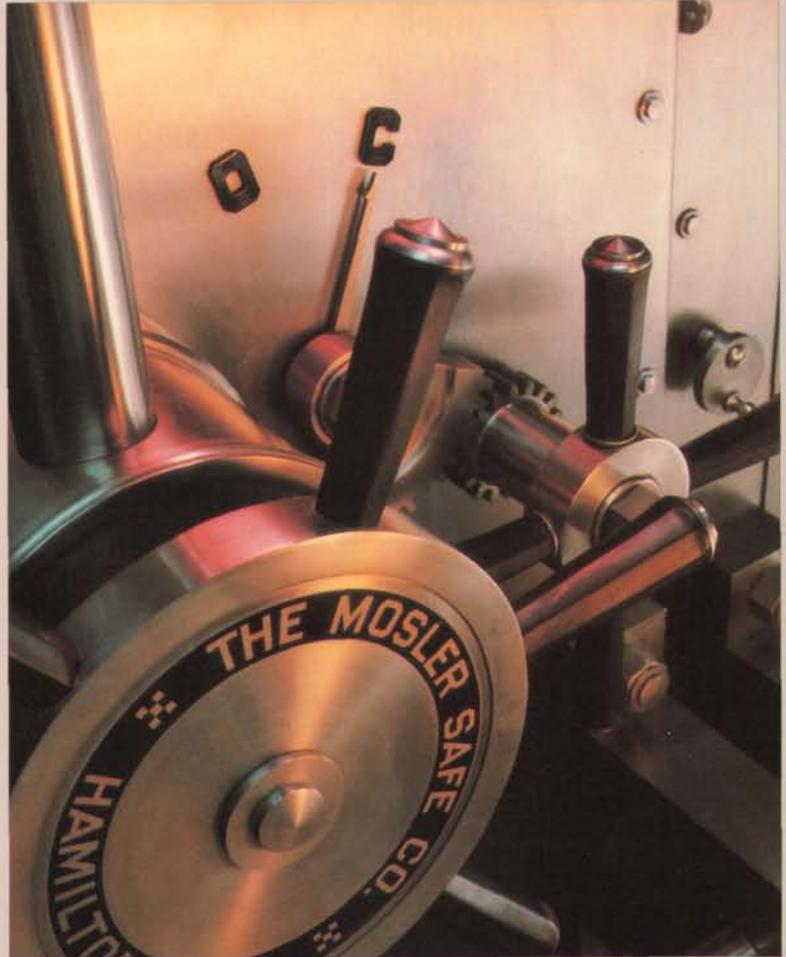
This year was one in which we implemented a major change in the direction of the nation's payments system. The Expedited Funds Availability Act (and the subsequent Federal Reserve Regulation CC) caused ripples throughout the financial industry. As mandated by the Act, our efforts, and

The Expedited Funds Availability Act caused ripples throughout the financial industry.



Historically vaults have been a central element in bank design. Once prominently located in the main lobby, vaults now are usually located underground. Vaults have evolved from highly decorated and ornamental safes to massive blocks of steel.

The three vaults that have spanned the history of the Federal Reserve Bank of Dallas were made by the Mosler Safe Company of Hamilton, Ohio. In 1959, Edwin H. Mosler, Jr.—then president of the company—spoke to a group of businessmen about vault design. “We keep up constantly with the ways burglars find that what man makes, man can break. And they find ways; and we find ways to stop them.”



those of financial institutions nationwide, centered around shortening the time necessary to collect and return a check. Two series of seminars designed to educate bankers in this District and help them prepare for the coming changes were held.

☞ The events of this year are merely the first step in a new era in check processing. Starting in the late 1950s, technology to imprint magnetic ink on the bottom of checks to make sorting faster was developed. Approximately 10 years later, the Federal Reserve announced that it would no longer handle checks that did not have this magnetic—MICR—encoding. That announcement spurred the industry into the standardization of check processing we have today. Regulation CC takes this evolutionary process one step further toward automation and standardization of returned checks—not just those in the forward presentment process.

☞ This legislation touches virtually every financial institution and consumer in the nation and will be the springboard for future improvements in the collection and return of checks.

Electronic Services

☞ As the 1980s come to a conclusion, probably the most signifi-

cant story in financial services revolves around the evolution of electronic services. As the volume of transactions grows and the speed necessary to get those transactions across the nation or around the world increases, our attention to the advancement of electronic services will continue to be among our top priorities. Since the early 1980s when the Federal Reserve's communications network was expanded, we have implemented programs to keep ahead of the game with innovations that will transfer funds and information quickly and accurately.

☞ As part of this goal, we continue to develop and expand services offered over the RESPONSE network—our electronic link to financial institutions in this District. In addition to the services currently offered, the Federal Reserve System is continuing its efforts to plan for electronic service needs of the future. Due to the explosive growth in both volume and dollar values carried over electronic networks, the System developed a list of goals for the service through the mid-1990s including virtually 100 percent reliability, faster throughput and more flexible service options. Financial institutions nationwide were asked to complete a survey on the list, and face-to-face interviews with leading

funds authorities were conducted. The results will guide us in the right direction in offering the kinds of electronic services necessary to manage the financial marketplace of the future.

☞ In order to achieve a more efficient electronic service network, progress must be made toward eliminating paper-based automated clearinghouse (ACH) and transfer of funds transactions. Progress on that goal was made during 1988 in the Eleventh District. Offices in this District reduced paper commercial ACH return items and notification of change volume by more than 25 percent largely based on the success of CATIE. CATIE—the Customer Assistance Touch-Tone Information Express—was introduced in 1987 initially to provide direct access to reserve and clearing account balances. In 1988, services were expanded over CATIE enabling financial institutions to return ACH items over the telephone as well. For transfer of funds, the volume of those made nonelectronically was reduced 15 percent versus those made in 1987.

☞ In addition, this Bank offered financial institutions more options for returning ACH items than any other Federal Reserve Bank. Institutions can return ACH items through a personal computer, dedicated computer link or

The events of this year are merely the first step in a new era in check processing.



Two thousand years ago, Roman architect Marcus Pollio wrote that an architect's duty is to provide constructive strength, practical utility and aesthetic effect. These goals have not changed, although buildings have.



over the telephone by using CATIE.

Customer Assistance Services

While we see and encourage trends toward more electronic services, we also realize the importance of the human element in service. Our Customer Assistance Division—still the only formal such group in the Federal Reserve System—worked with the District’s financial institutions in solving problems. Representatives handled almost 80,000 calls and 60,000 letters from District institutions. This year, our customers helped evaluate the quality of services provided in this area and it was gratifying to learn that our customers view the competency of our staff as highly as we do.

Cash and Securities Services

During 1988, a new 24-hour electronic service for ordering currency and coin went online. Called ACCENT, the system serves institutions in the Dallas, Houston and San Antonio offices. The system enables financial institutions to place cash transactions directly, select the amount of cash to be delivered, and receive early credit for currency and coin shipped to the Dallas Fed. ACCENT minimizes the possibility of error and eliminates the need for possi-

ble reverification.

Rising interest rates have caused a dramatic increase in the volume of securities transactions. Purchasing securities through the Treasury Direct program is one of our fastest growing services because of rates paid and the ease of participation.

The offices of the Dallas Fed also became more involved in issuing Savings Bonds for corporate customers utilizing the payroll savings plan. The Treasury Department has encouraged our participation in this area to help corporate customers efficiently distribute Savings Bonds. Also in an effort to increase the efficiency of Savings Bond handling, we participated in a nationwide program known as E-Z Clear. Under this program, Savings Bonds are encoded with the redemption value, sent to the Fed with check shipments, and processed on the high-speed equipment used to handle checks. This program eliminates exception item handling and is much more efficient for Savings Bond issuers.

Supervision and Regulation Activities

The economic climate in 1988 had a significant impact on the supervision of banks and bank holding companies in the Eleventh

District. The state of the banking industry in this District, and in Texas especially, was well publicized. Of the more than 200 banks closed nationwide, 113 were closed in Texas and four in the Eleventh District’s portion of Louisiana. However, no banks were closed in our portion of New Mexico. That and related problems required our efforts to be focused on meeting the normal mandates imposed upon us as supervisors, while at the same time dealing with area troubled banks and bank holding companies in an unusual and difficult time.

Our staff and resources were strained as we sent examiners out to review financially strained institutions. In addition, in order to administer borrowing effectively, considerable resources were expended in obtaining, evaluating and overseeing collateral that had been pledged against loans at the discount window.

During 1988, court and administrative rulings paved the way for statewide branching within Texas. First Interstate Bank of Texas became the first financial institution in the District to convert its offices to branches statewide, although several smaller institutions preceded that bank in establishing branches across county lines.

While we encourage trends toward more electronic services, we also realize the importance of the human element in service.



The physical structures of banks in the Eleventh Federal Reserve District are comprised of everything from Roman columns to modern art. Bank buildings in this District are especially influenced by Spanish, French and German architecture. While a building can be appreciated for its design, its details give it character.

B O A R D O F D I R E C T O R S



Head Office

Seated (from left): Robert L. Pflugger, Rancher, San Angelo, Texas; Adm. Bobby R. Inman, USN (Ret.), (Chairman), Chairman of the Board and Chief Executive Officer, Westmark Systems Inc., Austin, Texas; T.C. Frost, Chairman of the Board, Frost National Bank, San Antonio, Texas. During most of 1988, Mr. Frost was the Dallas Fed's representative to the Federal Advisory Council.

Standing (from left): Robert Ted Enloe, III, President, Lomas & Nettleton Financial Corporation, Dallas, Texas; Leo E. Linbeck, Jr., Chairman of the Board and Chief Executive Officer, Linbeck Construction Corporation, Houston, Texas; Charles T. Doyle, Chairman of the Board and Chief Executive Officer, Gulf National Bank, Texas City, Texas; Maj. Gen. Hugh G. Robinson (Ret.), (Deputy Chairman), Chief Executive Officer, Tetra Group, Dallas, Texas; Gary E. Wood, President, Texas Research League, Austin, Texas; Robert G. Greer, Chairman of the Board, Tanglewood Bank, N.A., Houston, Texas.



El Paso Branch

Seated (from left): David L. Stone, President, The Portales National Bank, Portales, New Mexico; Humberto F. Sambrano, President, SamCorp General Contractors, El Paso, Texas.

Standing (from left): Diana S. Natalicio, President, The University of Texas at El Paso, El Paso, Texas; Henry B. Ellis, President and Chief Credit Officer, MBank El Paso, N.A., El Paso, Texas; Peyton Yates, (Chairman), President, Yates Drilling Company, Artesia, New Mexico; Elbel Olson, Owner, NAMBE of Ruidoso, Ruidoso, New Mexico.

Not pictured: John R. Sibley, (Chairman Pro Tem), President, Tri-Mountain Enterprises, Carlsbad, New Mexico. Mr. Sibley resigned effective September 15, 1988.

The revolution in bank architecture occurred primarily in bank lobbies. Originally, interiors of banks were rather cramped and tellers stayed inside wooden "cages." Business transactions were conducted through steel bars or voice tubes. Following World War II, a new lobby concept developed. Facilities became better lit, more open, and more inviting to customers.



B O A R D O F D I R E C T O R S



Houston Branch

Seated (from left): Jeff Austin, Jr., President, First National Bank of Jacksonville, Jacksonville, Texas; Gilbert D. Gaedcke, Chairman of the Board and Chief Executive Officer, Gaedcke Equipment Company, Houston, Texas; David E. Sheffield, Vice Chairman, Texas National Bank, Victoria, Texas.

Standing (from left): Jenard M. Gross, President, Gross Builders, Inc., Houston, Texas; Clive Runnells, President and Director, Mid-Coast Cable Television, Inc., El Campo, Texas, and President and Director, Runnells Cattle Company, Bay City, Texas.

Not pictured: Walter M. Mischer, Jr., (Chairman), President and Chief Operating Officer, The Mischer Corporation, Houston, Texas; and Andrew L. Jefferson, Jr., (Chairman Pro Tem), Attorney, Jefferson and Mims, Houston, Texas.



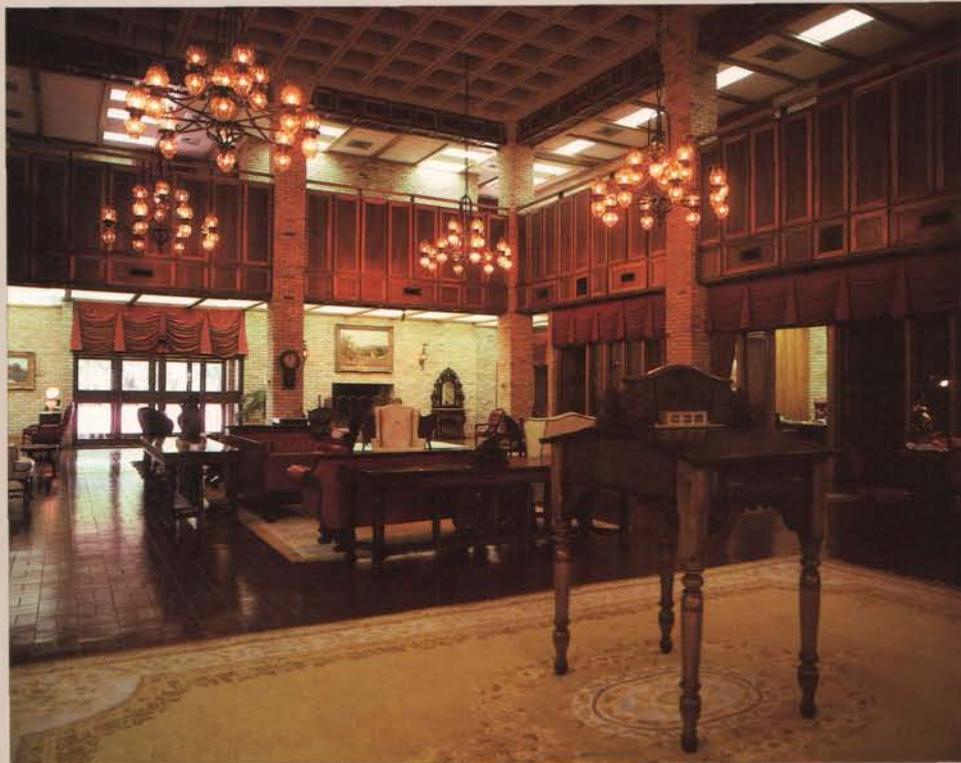
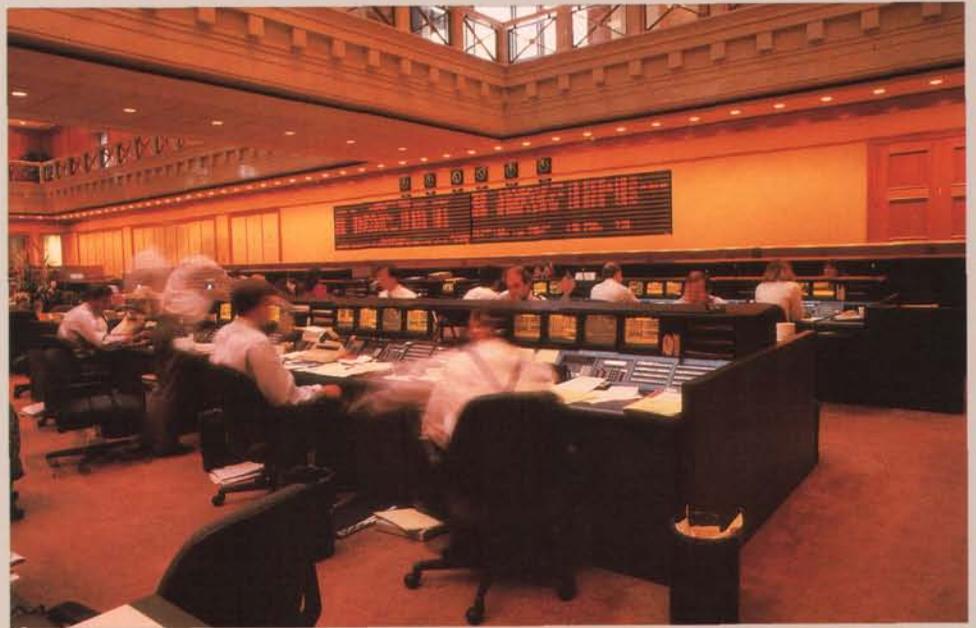
San Antonio Branch

Seated (from left): C. Ivan Wilson, Chairman of the Board and Chief Executive Officer, First City Bank of Corpus Christi, Corpus Christi, Texas; Sam R. Sparks, President, Sam R. Sparks, Inc., Progreso, Texas; Robert T. Rork, Regional Chairman, NCNB Texas, Dallas, Texas.

Standing (from left): Robert F. McDermott, (Chairman), Chairman of the Board and President, United Services Automobile Association, San Antonio, Texas; Jane Flato Smith, Investments and Ranching, San Antonio, Texas; Lawrence E. Jenkins, (Chairman Pro Tem), Vice President (Retired), Lockheed Missiles & Space Company, Inc., Austin, Texas.

Not pictured: Ruben M. Garcia, Chief Executive Officer, Modern Machine Shop, Inc., Laredo, Texas.

The evolution of bank interior design has been influenced by customers' changing needs and banks' abilities to provide new services. Bank vaults, once a prominent design feature of the lobby, have been removed from their costly central locations and are now usually located off to one side or in a basement. The focus is on more personal contact and financial service innovation.



M A N A G E M E N T T E A M



Robert H. Boykin, President and Chief Executive Officer, (left); and William H. Wallace, First Vice President and Chief Operating Officer



Seated (from left): Millard E. Sweatt, Senior Vice President, General Counsel, and Secretary; Jay K. Mast, Senior Vice President; Robert Smith, III, Senior Vice President in Charge of the Houston Branch; Thomas H. Robertson, Vice President in Charge of the San Antonio Branch; Harvey Rosenblum, Senior Vice President and Director of Research.

Standing (from left): Tony J. Salvasaggio, Senior Vice President; James L. Stull, Senior Vice President; George C. Cochran, III, Senior Vice President; Sammie C. Clay, Vice President in Charge of the El Paso Branch; W. Arthur Tribble, Vice President.

Not pictured: Robert F. Langlinais, Vice President and General Auditor.



Banks originally were designed to resemble fortresses. Heavy ornamentation and rich use of mahogany and marble projected an aura of solidity, security and success. When FDIC insurance became a reality in the 1930s, this fortress-like appearance was no longer necessary. The days of Roman columns and stone structures gave way to more modern architectural forms.



A D V I S O R Y C O U N C I L S

Advisory Council of Financial Institutions

JOHN H. DALTON
*Council Chairman
Chairman and
Chief Executive Officer
Freedom Capital Corporation
San Antonio, Texas*

JAMES A. ALTICK
*President and Chief Executive Officer
Central Bank
Monroe, Louisiana*

WILLIAM E. BRADY
*Chairman of the Board
and President
Denton Savings Association
Denton, Texas*

KENNETH L. BURGESS
*President
Security State Bank
Abilene, Texas*

H.O. BURSUM, III
*President,
Chief Executive Officer, and Cashier
First State Bank
Socorro, New Mexico*

WALTER E. JOHNSON
*President
First Interstate Bank of Texas, N.A.
Houston, Texas*

BEN LAND
*President
Family Federal Savings and Loan
Association
Shreveport, Louisiana*

DELTON P. MOORE*
*Chairman
Texas Credit Union League
Manager
Texaco PAW
Employees Federal Credit Union
Port Arthur, Texas*

GARRY OWEN
*President and Chief Executive Officer
First Federal Savings Bank
of New Mexico
Roswell, New Mexico*

BOOKMAN PETERS
*Chairman of the Board
and Chief Executive Officer
First City National Bank of Bryan
Bryan, Texas*

A.W. RITER, JR.
*Senior Chairman of the Board
NCNB Texas—Tyler
Tyler, Texas*

LOWELL SMITH, JR.
*Chairman of the Board
and President
First State Bank
Rio Vista, Texas*

*Mr. Moore was appointed to the council to fill the position left by Clyde N. Choate, President, Enserch Federal Credit Union, Dallas, Texas.

Advisory Council of Small Business and Agriculture

CAROLYN DRAPER
*Council Chairman
President
3-D Distribution Systems, Inc.
Dallas, Texas*

J. WAYLAND BENNETT
*Charles C. Thompson Professor of
Agricultural Finance
and Associate Dean
College of Agricultural Sciences
Texas Tech University
Lubbock, Texas*

ROBERT M. CARTER
*Farmer
Plainview, Texas*

JOHN O. CHAPMAN
*Rancher
Chapman Ranch, Texas*

LLOYD E. CLINE
*President
Lloyd Cline Farms, Inc.
Lamesa, Texas*

J.B. COOPER, JR.
*Farmer
Roscoe, Texas*

SHARON JOBE
*Chief Financial Officer
TCP Industries, Inc.
Dallas, Texas*

ROBERT W. PHILIP
*Partner
Arthur Andersen & Company
Dallas, Texas*

DAN PUSTEJOVSKY
*Chairman of the Board
G. & P. Seed Company, Inc.
Aquilla, Texas*

WILLIAM P. STEPHENS
*Executive Director
Farm and Ranch Heritage Institute
Las Cruces, New Mexico*

J. ALFRED WASHINGTON
*Publisher/Owner
Dallas Weekly
Dallas, Texas*

CARLOS A. ZUNIGA
*Vice President
Zuniga Freight Services, Inc.
Laredo, Texas*



Architectural designs of financial institutions play an important role in their image. A financial institution's facilities affect its ability to deliver services, its image in the marketplace, its ability to respond to growth and change, and the philosophy of its management.



O F F I C E R S

Head Office

ROBERT H. BOYKIN
President and Chief Executive Officer

WILLIAM H. WALLACE
*First Vice President
and Chief Operating Officer*

GEORGE C. COCHRAN, III
Senior Vice President

JAY K. MAST
Senior Vice President

HARVEY ROSENBLUM
*Senior Vice President
and Director of Research*

TONY J. SALVAGGIO
Senior Vice President

JAMES L. STULL
Senior Vice President

MILLARD E. SWEATT
*Senior Vice President,
General Counsel and Secretary*

LYNE H. CARTER
Vice President

JACK A. CLYMER
Vice President

W. MICHAEL COX
Vice President and Economic Advisor

BILLY J. DUSEK
Vice President

ROBERT D. HANKINS
Vice President

HELEN E. HOLCOMB
Vice President

JOEL L. KOONCE, JR.
Vice President

ROBERT F. LANGLINAIS
Vice President and General Auditor

El Paso Branch

SAMMIE C. CLAY
Vice President in Charge

ROBERT W. SCHULTZ
Assistant Vice President

JAVIER R. JIMENEZ
Operations Officer

Effective January 1, 1989

REBECCA W. MEINZER
Vice President

GERALD P. O'DRISCOLL, JR.
*Vice President
and Associate Director of Research*

LARRY J. RECK
Vice President

JESSE D. SANDERS
Vice President

EUGENIE D. SHORT
Vice President

LARRY M. SNELL
Vice President

W. ARTHUR TRIBBLE
Vice President

UZZIAH ANDERSON
Assistant Vice President

BASIL J. ASARO
Assistant Vice President

TERRY B. CAMPBELL
Assistant Vice President

M. DON DORSEY
Assistant Vice President

BILLY D. FULLER
Assistant Vice President

JOSEPH T. GHOLSON
Assistant Vice President

JERRY L. HEDRICK
Assistant Vice President

ANDREW W. HOGWOOD, JR.
Assistant Vice President

RICHARD D. INGRAM
*Assistant Vice President
and Assistant Secretary*

ALBERT J. JARAMILLO
Assistant Vice President

Houston Branch

ROBERT SMITH, III
Senior Vice President in Charge

VERNON L. BARTEE
Vice President

RENE G. GONZALES
Assistant Vice President

LUTHER E. RICHARDS
Assistant Vice President

JOHNNY L. JOHNSON
Assistant Vice President

C. LaVOR LYM
Assistant Vice President

JAMES R. McCULLIN
Assistant Vice President

DEAN A. PANKONIEN
*Assistant General Counsel
and Assistant Secretary*

JOHN R. PHILLIPS
Assistant Vice President

LARRY C. RIPLEY
Assistant Vice President

MARY M. ROSAS
Assistant Vice President

ROBERT J. ROSSATO
Assistant General Auditor

THOMAS H. RUST
Assistant Vice President

PHILIP R. SPEAR
Assistant Vice President

MICHAEL N. TURNER
Assistant Vice President

STEPHEN M. WELCH
Assistant Vice President

ROBERT L. WHITMAN
Assistant Vice President

EMILIE S. WORTHY
Assistant Vice President

RICHARD J. BURDA
Examining Officer

MARVIN C. McCOY
Examining Officer

San Antonio Branch

THOMAS H. ROBERTSON
Vice President in Charge

TAYLOR H. BARBEE
Assistant Vice President

JOHN A. BULLOCK
Assistant Vice President

THOMAS C. COLE
Assistant Vice President

S T A T E M E N T O F C O N D I T I O N

	December 31, 1988	December 31, 1987
ASSETS	(Thousands)*	
Gold certificate account ¹	\$ 676,000	\$ 669,000
Special drawing rights certificate account ²	307,000	307,000
Coin	27,877	28,955
Loans to depository institutions	687,785	416,225
Securities:		
Federal agency obligations	390,710	448,081
U.S. government securities	13,104,763	12,986,405
Total securities	\$13,495,473	\$13,434,486
Items in process of collection	695,590	574,682
Bank premises (net)	22,498	20,336
Other assets	2,084,434	917,611
Interdistrict settlement account	(2,812,546)	5,028
TOTAL ASSETS	\$15,184,111	\$16,373,322
LIABILITIES		
Federal Reserve notes	\$11,663,736	\$12,312,019
Deposits:		
Depository institutions	2,401,129	2,985,403
Foreign	12,900	12,750
Other	840	55,876
Total deposits	\$ 2,414,869	\$ 3,054,028
Deferred credit items	616,195	499,129
Other liabilities	173,249	157,496
TOTAL LIABILITIES	\$14,868,049	\$16,022,672
CAPITAL ACCOUNTS		
Capital paid in	\$ 158,031	\$ 175,325
Surplus	158,031	175,325
TOTAL CAPITAL ACCOUNTS	\$ 316,062	\$ 350,650
TOTAL LIABILITIES AND CAPITAL ACCOUNTS	\$15,184,111	\$16,373,322

*Detail figures may not balance to totals because of rounding.

¹This Bank's share of gold certificates deposited by the U.S. Treasury with the Federal Reserve System.

²This Bank's share of special drawing rights certificates deposited by the U.S. Treasury with the Federal Reserve Bank of New York.

I N C O M E A N D E X P E N S E S

For the year ended December 31	1988	(Thousands)*	1987
CURRENT INCOME			
Interest on loans	\$ 152,867		\$ 16,924
Interest on government securities	1,030,436		980,240
Income on foreign currency	25,762		29,246
Income from priced services	48,081		46,023
Other income	930		1,020
Total current income	\$1,258,076		\$1,073,454
CURRENT EXPENSES			
Current operating expenses	\$ 81,159		\$ 76,490
Less expenses reimbursed	5,070		4,763
Current net operating expenses	\$ 76,089		\$ 71,727
Cost of earnings credits	6,332		4,969
Current net expenses	\$ 82,421		\$ 76,696
CURRENT NET INCOME	\$1,175,655		\$ 996,759
PROFIT AND LOSS			
Additions to current net income:			
Profit on sales of government securities (net)	\$ 1,358		\$ 2,488
Profit on foreign exchange transactions (net)	0		153,364
Other additions	11		70
Total additions	\$ 1,369		\$ 155,922
Deductions from current net income:			
Loss on foreign exchange transactions (net)	\$ 43,936		\$ 0
Other deductions	23		20
Total deductions	\$ 43,959		\$ 20
Net additions (deductions)	\$ (42,590)		\$ 155,902
Cost of unreimbursed Treasury services	\$ 1,888		\$ 2,504
Assessment by Board of Governors:			
Expenditures	\$ 7,387		\$ 6,877
Federal Reserve currency costs	9,541		9,830
NET INCOME AVAILABLE FOR DISTRIBUTION	\$1,114,249		\$1,133,450
DISTRIBUTION OF NET INCOME			
Dividends paid	\$ 10,516		\$ 9,863
Payments to the U.S. Treasury	1,121,027		1,105,796
Transferred to Surplus	\$ (17,294)		\$ 17,791
Surplus, January 1	175,325		157,534
Surplus, December 31	\$ 158,031		\$ 175,325

*Detail figures may not balance to totals because of rounding.

V O L U M E O F O P E R A T I O N S

HEAD OFFICE AND BRANCHES COMBINED

	Number of Pieces Handled		Dollar Amount (Thousands)	
	1988	1987	1988	1987
Currency received and counted	964,414,800	883,620,250	12,131,634	11,533,427
Coin received and counted	2,031,387,000	1,975,981,000	333,233	309,804
Food stamps redeemed	226,475,250	206,636,225	1,111,041	1,028,646
Transfers of funds	6,382,598	6,287,618	9,030,389,655	9,018,968,357
CHECKS HANDLED				
U.S. government checks	34,423,947	34,940,896	48,691,642	47,492,216
Fine sort	271,931,207	260,093,356	72,410,327	72,845,488
All other ¹	1,103,220,490	1,011,009,063	582,703,122	548,771,257
ACH ITEMS HANDLED				
Commercial	61,653,567	47,860,311	306,570,875	326,210,299
Government	29,240,042	27,018,829	21,672,430	16,778,829
COLLECTION ITEMS HANDLED				
U.S. government coupons paid	24,693	28,086	19,276	27,422
All other	227,721	227,245	424,929	679,324
ISSUES, REDEMPTIONS, EXCHANGES OF U.S. GOVERNMENT SECURITIES				
Definitive and book-entry	8,542,845	9,340,164	493,948,487	994,215,840
LOANS				
Advances made	3,556	2,761	459,853,173	59,760,201

¹Exclusive of checks drawn on the Federal Reserve Banks.



FEDERAL RESERVE BANK OF DALLAS
400 South Akard Street
Dallas, Texas 75202
(214) 651-6111

EL PASO BRANCH
301 East Main Street
El Paso, Texas 79901
(915) 544-4730

HOUSTON BRANCH
1701 San Jacinto Street
Houston, Texas 77002
(713) 659-4433

SAN ANTONIO BRANCH
126 East Nueva Street
San Antonio, Texas 78204
(512) 224-2141