Address
Book

SDT Notes

on ~~THRIFTS~~

THRIFTS

MID-80's

a appraisal

B. Banking Industry

Book/Center

C - Credit Parameters/Compute

D. Deregulation

F-FSLIC

I. INSURANCE

L -LIABILITIES

N. Network

M. Market

P. PRODUCT (BANK)

PMI

Personnel

PRICING

R. Ready Credit

S. Salary Structure

T. TID BITS (FINANCIAL)

U - Underwriting Standards

W - WIVES

September 1, 1986

ADJUSTABLE RATE MORTGAGE CHEAPER/SAFER

July 86: 22% taking adjustables versus 78% fixed.

Fixed are priced at an average of 2 points higher.

Rates on conventional loans have become quite competitive with adjustable rates because there is a much bigger secondary market for conventional loans. Institutional investors also prefer to investments that have a fixed rate of return.

Lenders, who prefer to write adjustables for own portfolios, complain that they are a t a disadvantage because the secondary mortgage market is dominated by nonprofit, Govt.-backed corporations.

Low rate adjustables responsible for pulling housing market out of slump.

Better to have gone adjustable over last few years bec. rates have been trending down.

Goerens given choice between two mortgages> One was at 9% adjustable whose interest rate would be adjusted within a range of 2 percentage points, every three years. The other was a conventional 30 year mortgage with a 10 3/8% percent fixed rate.

if one assumes that rising rates would push the adjustable's rate up two points every three years, a borrower's monthly payments would be $70 less than the conventional mortgage in the first three years and $28 more than the payments for the conventional mortgage in the second three-year period. Thus, the adjustable mortgage payments would be slightly cheaper over the whole six years and the adjustable borrower would have saved $700 in fees.

Assume that the adjustable borrower put his savings, totaling $3200 in the first three years, in a bank account earning 5.5% interest. When the adjustable and conventional loans were again compared the adjustable was less expensive for just over eight years for borrowers in three tax brackets used, 25%, 33%, and 50%.

Adjustable loans are often easier to unload than conventional loans.

Economic VIEWPOINT

12/5

Kevin Villani: Institutional Credit Risk and the Appraisal Process

In early August. Equity Programs Investment Corporation (EPIC) failed to make a $1.5 million payment to owners of mortgage-backed securities (MBSs) issued by the firm. This began a chain of events that could culminate in EPIC's default on over $1.3 billion in MBSs. the collapse of a closely related savings and loan. and the failure of several major mortgage insurance companies.

The EPIC situation has created the most serious threat to the mortgage insurance industry since the Great Depression. Unlike the crisis of that era. however. the culprit in this instance is not the economy. but rather the institutional credit risk related to appraisal practices.

The EPIC Tale

EPIC began operations in 1975 by arranging limited partnerships to purchase model homes from developers and leftover homes that builders were unable to sell. The partnerships financed the homes by issuing mortgages which EPIC pooled and resold as mortgage-backed securities. The limited partners received tax benefits. the builders sold their models and leftovers for quick cash. and EPIC profited from the associated fees. In its first year. EPIC partnerships bought 68 homes: by 1984 the partnerships owned 20,000 homes worth about $1.5 billion.

Because house prices weakened. particularly in the Sun Belt where EPIC purchases were concentrated. EPIC found it difficult to resell the homes at the anticipated prices when the older partnerships matured. This increased EPIC's dependence on other sources of funds.

The rental income from the homes was typically insufficient to meet the payments on the mortgage-backed securities. so EPIC sought additional funds from various sources. including loans from EPIC's parent company. Community Savings and Loan. These financial supports had already weakened by this summer when Community was required to cut its ties to EPIC in order to qualify for FSLIC insurance. When it lost access to Community. a major source of additional funds. EPIC withheld payments on its mortgage-backed securities as it attempted to restructure its cash flow.

The Threat to MIs

The firms that insured mortgages on EPIC's properties fear that the values of the homes EPIC purchased were inflated and that a disproportionate share of the properties will end up in foreclosure proceedings. If this occurs. the insurers fear the sale of the properties will not generate sufficient income to cover EPIC's obligations to holders of its mortgage-backed securities. The insurers would have to make up any shortfall.

Faulty Appraisals

Appraisal procedures seem to be the root of this problem. The appraised value of owner-occupied. single-family homes is typically based on "comparables." Since the homes that EPIC purchased were either models or leftovers. this method may be inappropriate. Few if any comparables may be available for models since they are the first to be built. Leftovers are the homes that could not be sold at the asking price. Comparing them to homes sold at market prices overvalues them.

Using comparables presents another problem when builder or seller financing concessions are involved. Because a portion of the value of the financing is built into the house price. appraisals based on comparables overstate resale values without special financing.

The view that "owner-occupied" is synonymous with "single-family" and "rental" is synonymous with "multifamily" also contributed to the problem. While owner-occupied homes are appraised principally by using comparables. rental properties are appraised principally by discounting cash flows. Single-family homes rarely rent for enough to make them as attractive to investors. from a cash flow perspective. as they are to owner occupants. who look for both tax breaks and the American Dream. Although the EPIC properties were single-family. they were not owner-occupied. EPIC purchased the homes and leased them to builders or other tenants. The homes. therefore would have been overvalued if they were appraised as owner-occupied instead of rental properties.

In addition. the appraisals may not have been "arms-length" transactions. Links between EPIC and Continental Appraisal Group. which appraised a significant portion of the EPIC properties. suggest some bias in the appraisals. Also. the builders often gave EPIC substantial cash rebates. allegedly upwards of 25 percent of the purchase price.

For high loan-to-value ratio loans — as EPIC's typically were — on overvalued properties. the mortgage insurance claims are likely to exceed the property values. The losses to the mortgage insurers could be particularly high in this instance because the limited partners. unlike owner-occupants. have very little incentive to avoid default on the properties once they have reaped the benefits of the tax shelter. The results may be higher foreclosure rates and higher losses per foreclosure.

Kevin E Villani

Freddie Mac's Senior Vice President
– Financial and Economic Analysis

1. Can't use comparables method for new homes products. No benchmark
2. Ditto leftovers. Leftover because couldn't sell at asking price. ∴ Can't compare to "market."
3. Builder & Seller financing concessions
4. Rentals are valued on cash flow. less value than comparable

Appraisal

11/28: General concern inadequacy/loosely controlled. EPIC: 1/3 of 250M appraisers belong to association.

Should there be a national licensing scheme?

Doug Barnard Hearings: D-6A. Barnard has identified shoddy appraisals as one reason for thrift collapses. Certification exam? Like CPA?

Certification: Police by idj. group,
No huge reg. apparatus.

OR

Licensing cumbersome, but keeps bankers honest. Only way to eliminate fraud?

MEMORANDUM TO: Steve Taylor

FROM: Norman D. Wood

DATE: January 24, 1986

RE: Industry Appraisal Issues

As an output of the December Review, you asked that I fill you in on the issues concerning mortgage appraisals.

Fair Market Value does not accurately reflect the cash value of property

- Sales concessions, finance points and seller/builder contributions all play a role in inflating the appraised value. While this has always been a problem, the advent of low inflation rates and a flat or non-existent appreciation in some markets has again made it a major concern.

- FNMA has tightened underwriting standards (lower ratios, reduced seller contribtuions) to solve its appraiser "risks" on 91 plus LTV loans. Freddie Mac is looking to solve its 91 plus LTV "risks" through adoption of a cash equivalency appraisal approach. The definition of market value would be revised to require lenders, when ordering appraisals to provide the appraiser with all the financing data including special financing arrangements. Market value determinations would include payments "made in terms of cash or in terms of financial arrangements equivalent to cash". This would affect builders the most, due to their adding buydown and special financing arrangement costs into the sales price. Major objection to this approach is the appraisers' ability to adjust the value of comparable home sales, information is difficult to obtain and in some markets may not exist. The Federal Home Loan Bank Board is supporting this cash equivalency approach.

Every organization has its own appraisal "standard" form

The Veterans Administration (VA)and the Federal Housing Administration (FHA) plan to use a common two page appraisal form (sometime in 1986) in an attempt to bring standardization. Despite this, both FNMA and FHLMC each plan on using their own different form.

Currently there exists over 16 different organizations that designate appraisers.

Each of the organizations have a wide variety of standards. Some require up to 60 hours of classroom work and a qualifying exam, others a college degreee, in lieu of classroom training. Some will waive the qualifying exam for experience Standardization of both experience and educational requirements are a must if any type of consistency is to be achieved.

As long as a borrower's equity in a home plays a key role in whether a mortgage is likely to go bad, the appraiser's ability to determine a true market value will be critical. It seems to me FNMA/Citicorp have taken the only safe approach---limit 91 plus LTV loans.

It is a rare occasion to see an appraised value much below the sales price. A 5% "cushion" without a rapidly appreciating market is like making an unsecured loan at a discount.

xc C. Cooper

Retail Bank Developments

Booking Ctry

[illegible] aple –

– [illegible]
– [illegible]

703-821-3803 } VRN

Johnson

Kip – 617
729-2927

Memorandum

Gams ~~[illegible]~~
459 old Stamford Road
972-1690

– [illegible] Reviews

Dudley 713-891-2246

* Kip – ~~Reviews~~
  – Goals –
* Staff Meetings – Weekly –
*
  PLAN –
  Reagan Resume

この **Memorandum** は、情報化時代のポケットメモです。
ボールペン、万年筆で書きやすく、
裏抜けをふせいでおります。
やわらかく、かさばらないので、
ポケットにも気軽に入ります。
会議用、備忘用、連絡用などに、
ご活用下さい。

Seminary Meeting

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that
ue.

Issues FOR BANKS

FDIC wants to ↑ Capital to 9%.
Will count Subordinated debt.

- Death to smaller Banks
- Punish Better managed?
- Smaller banks already have higher % capitalization

- Tougher appraisal Requirements
- Tighter FNMA Guidelines
- Savings Banks aggressive competing for funds meaning higher than market deposit rates, forcing those banks into investments risky.
  Fed Home Loan Bank Bd. Sent out letter cautioning to lower deposit rates

---

- Trend in Home Values
  - Why did housing do well '70's?
    - Pop grew 11% 70's but households grew by 26%.
    - Baby Boom (1946-45) created boom in 1st time home purchase. Increase by 45%.
    - Boom spent by '80's
    - Other Reasons; Financial
      - Reg Q. - Can't get decent return on Savings, but easy to borrow save pain. Interest costs negative after tax and inflation, so house better investment than save.
      - ∴ Renters start buying
      - More money made available by mortg. bankers pooling securitys
      - Lax appraisals
      - Interest rate buydowns.

Environmental Changes affect [illegible]

1. Deregulation global
2. Technology
   - Cost Red'
   - & Mistake Cost Potential
3. Volitile Energy + Commodity Prices
4 Green Revolution

Now change:

→ . Demographics no longer there for HH formation

- Saver now gets real return

∴ Housing Spec down

- Renting now cheaper for some

Irony in nat'l Policy – We have tried to stimulate housing to achieve economic expansion even at expense of capital. Result New Homes old factories versus Japan Old Homes New factories W/O Jobs – No one can buy a house

In best interest for nation is program to down grade tax advant- for homes, and up grade tax incentives for capital projects that provide jobs. is best for econ

Hard to swallow, but true.

Samuelson - GLOBAL DISINFLATION

Econ seems healthy, but

- Recovery stumbling
- Trade deficit
- farmer distress
- Internat'l debt crises
- Bank loan losses

⇓

Disinflation heavy cost

↓ spotty world growth ∴

— manu + farmers have weak export markets + surging imports

— trade deficit hurt our recovery + stimulate rest of world.

Reversing inflation Policy meant ↑ rates ∴ exported disinflation. Latin Am had higher loan rates and European nations raised their rates to avoid depreciation of their currencies.

Betters on inflation left in lurch

- farmers — heavy debt
- Latin nations expecting high export prices + low rates

Inflation bad:

- saps productive potential
- focuses attn on speculation

Banking Business Change

1. Direct access to public financing to most credit worthy borrowers. More risky now main source loan demand.

2. Dramatic change in spreads thru ↑ competition, deregulation, disintermed.

3. Change in focus from commercial bank to complex financial service company.

4. Technology impact.

In Sum
- More demanding riskier environment
- Shorter product life cycles.
- More complex product
- More diverse customer base.

Hypothesis
Private Deposit Insurance works better than banking regulation
- Some believe that banks inherently unstable.
- But like other industries ~~[illegible]~~ regulation creates inflexible environment that threatens that threatens overall idy stability.
- Regulation robs system of ability to innovate and adapt to changing conditions.

Myths:
1) • a run will create a contraction of ~~loans in~~ Money supply as loans are recalled — eg domino effect
- Not So. Loans can be sold off to other institutions.

(2) Myth - Customers can't judge institution quality ∴ must be regulated for their own protection.

No: Market discipline would create bank rating services + make customers more aware

Regulation makes them dumb and happy

Double Whammy -

- Lenders Won't allow assume loans
- Lendes charge prepayment ~~pole~~ penalty !

January 29 1986

Bankers Survey - Forecast '86. Survey by congressmen, regulators etc.

* 90% see major failure in 86

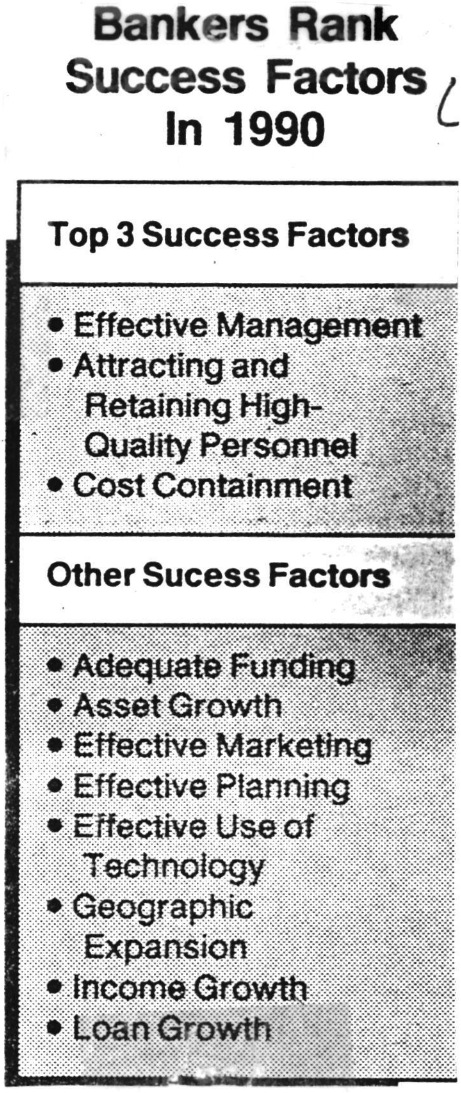
* Inside bet is Texas energy bank

* 81% believe thrifts will require major financial assistance

* 72% believe serious problems will arise in 1986 because of the banking industry's exposure to foreign loans.

* Mexico's ability to handle debt load will evaporate my mid-year. Such a development, the respondents indicated, would pose large questions about whether regional banks will continue to roll over their Third World loans and whether U.S. banks will respond to Treasury Secretary James Baker's request for a $20 billion increase lending to developing countries.

* Risk is that failure to address international debt situation could result in Congress considering a major restructuring of the financial institution industry in a crisis atmosphere.



Bankers Rank Success Factors In 1990

Top 3 Success Factors

- Effective Management
- Attracting and Retaining High-Quality Personnel
- Cost Containment

Other Sucess Factors

- Adequate Funding
- Asset Growth
- Effective Marketing
- Effective Planning
- Effective Use of Technology
- Geographic Expansion
- Income Growth
- Loan Growth

RETAIL BANKING DEVELOPMENTS

Retail Banking Developments:

Last 4 years (Braddock)

* ° Deregulation - changed the price value equation and forced banks to be smarter on price and cost.

° Coming of age of financial service business.

° Building of national banking infrastructure almost in anticipation of full interstate banking:

ATM sharing
Regional Compacts (with triggers)
Home banking
Cards (national)

° Beginning of Relationship management orientation:

Focus Relo
CMA

Next 4 Years

° Solution to geographic issue
° Industry consolidation
° How will integration fill out Sears, AMEX
° People (good) influx

Respect Regionals! They have the customers.

TAX Bill
* shift to secured
* Rise of auto captives

New Era in Bank Marketing

by
Richard S. Braddock
Sector Executive
Citibank/Citicorp

Richard S. Braddock
Sector Executive
Citibank Citicorp

at the
Bank Marketing Association Conference
Hawaii
November 11, 19[illegible]

New Era in Bank Marketing

As you know, I work for Citicorp. Though I'm described as banker, at heart I'm still a marketing person. So I can honestly say I'm glad to be here, and to have the chance to take part in this conference.

We're all aware of the major changes banking is going through, which may suggest a new era for bank marketing. Curiously, and in a round-about way, we seem to be getting back to the roots of modern banking. Historians trace the history of the industry back to the merchants of Renaissance Venice, who gradually left the life of trade for that of finance.

- In the United States, the first great bank was founded by the merchant Stephen Gerard.
- A group of merchants, led by Colonel Samuel Osgood, founded Citibank in 1812.
- The oldest U.S. investment bank, Alexander Brown and Sons, was started by a Baltimore trader.
- Even the stately house of J. P. Morgan began with a fortune earned in dry goods.
- The same pattern is true of many of the great houses of Europe. We can see this in the term "merchant bank," which is still used throughout the world to describe what we call an investment bank.

New Competitors

Today, while banks are confined just to banking—retailers and merchants, instead of leaving trade for finance, are free to combine the two. And many are doing just that:

- Retailers and oil companies have not only automated, but used their electronic systems to enter into new financial businesses.

You can get socks, stocks and a credit card called "Discover" at Sears; a six-pack of beer and CD at 7-Eleven, and gasoline and cash from an ATM at your local gasoline station.

- Retail stores account for 60 percent of all credit cards issued. They provide ongoing credit to 24 million more customers than do banks and oil companies *combined.*
- Over 40 million people have the Sears credit card. That's more domestic credit accounts than American Express or any individual issuer of MasterCard and Visa. And Sears Savings Bank has a real equity worth of six percent of total deposits, compared with an average for the savings and loan industry of slightly more than two percent.
- Bank of America has 2.1 percent of the almost $2 trillion U.S. consumer deposit base. But Merrill Lynch—with 1.8 percent—is catching up fast.
- General Motors Acceptance Corp. is the second-biggest mortgage banker in America. It has the largest share—3.7 percent—of the nation's $1.3 trillion market in consumer debt, which includes commercial paper operations.

In fact, more and more consumers are getting their credit and loans from non-banks. In 1964, banks held more than 57 percent of the nation's financial assets, according to the Federal Reserve. Non-banks—S&Ls, credit unions, insurance companies, finance companies and others—at that time held slightly less than 43 percent.

Today, the numbers have significantly shifted. As of June 30, 1985, according to the latest figures from the Fed, non-banks have 67 percent of the country's financial assets, banks 33 percent. And these figures tell only part of the story, since they don't include the financial activities of retailers, manufacturers, oil companies and other firms in non-financial industries.

As a banker and marketer, who sells financial services and products, my job at Citicorp is cut out for me—as is yours.

Was the past easier? We had fewer choices then. It wasn't too long ago that if we wanted a telephone, we called Ma Bell. After all, it was the only game in town. We bought American cars, and flew on any airline since the prices were all, more or less, the same. If we wanted to save money, we put it in a passbook savings account and got 5¼ percent at any bank anywhere in the United States. It was easy for the marketplace to act when the choices were limited.

But competition, inflation, the oil shocks of the 1970's and the new information technology changed all that. Deregulation of telecommunications combined with deregulation of banking, transportation and other industries is creating a new business environment. Many of the old rules are no longer working.

What is happening is that market identities are being redrawn along boundaries defined by distribution networks and technologies, rather than by traditional "functions."

What does all of this mean for us? I hope some of the messages are already evident:

- that we must think more and more like retailers as we approach our customers,
- our various strategic plans will literally bet our institutions and our careers, and
- the management of change will be our constant companion as we move into the future.

But beyond these broad messages, there is a new set of challenges—*driven by marketing*—which will separate the winners from the losers over time. I'd like to discuss several of these today.

New Product Development

The first is the increased importance of our role as new product developers. Up to now, the U.S. government has developed our products. It has done this by deregulating one product after another, often with unpredictable timing. In the future, now that much of the product-line deregulation is complete, we will have to replace the government, and build on our own new packages of products and services.

Deregulation, competition and technology have created a new consumer services industry, and with it a new set of opportunities. Citicorp, for example, is not just a bank. We see ourselves as a worldwide financial services organization, which wants to be allowed to compete freely with banks, brokers, insurance agents, real estate people and all the others who sell financial products and services.

Put simply, the new era of bank marketing must build on the momentum we already have but it must branch out. Basically, consumers still buy products one at a time, but many of them also tell us, for instance, that they are comfortable buying insurance—and stocks—from banks. They also tell us that they have major problems with *each* of the major players in the financial service industry today—banks, insurance companies, brokers. The door is open for an innovative solution to our customer's needs.

National Infrastructure

This leads directly to two more of our challenges:

1) the building of a national banking infra-structure, and

2) the introduction of a relationship management orientation.

First, we *are* developing a national banking infrastructure for the financial services industry. Federal laws, by and large, still don't allow banks to take deposits across the country. The inequality and inefficiency of this situation, as well as the banking needs of so large and diverse a nation, are finally being recognized.

In anticipation of a national banking system, we are seeing the growth of a support base to allow that to happen—and the beginning of an inevitable consolidation of the industry.

- So far, five states have opened their borders to banks from anywhere.
- 17 states have enacted laws allowing their banks to enter into regional compacts and another six are likely to do so this year.
- [illegible] states have regional banking with triggers that

allow nationwide banking in two to three years.

- Bank mergers across state lines are occurring practically every day. And many banks, including us, are quickly setting up shop in those states where we are allowed to do business.
- Thousands of banks, including us, have joined a variety of ATM sharing networks nationwide. These shared networks allow our customers to get cash in various parts of the country.
- Plastic cards already have a national as well as international customer base. The overwhelming majority of Citicorp's Bankcard, as well as its credit, private label, and travel and entertainment card customers are outside New York state.

What's developing is a mixed distribution system for financial services. Such a system includes traditional elements like branches, as well as ATMs, telephone and mail. It's supported by a variety of plastic cards carrying a range of packaged products to build geographic reach. It will also have state of the art elements such as new types of terminals for home and office distribution. And it won't and can't be cut off by arbitrary laws or state lines.

It may be a smart tactic for some banks to fight rear guard regulatory actions in the face of these changes. But the marketing discipline should take change as a given, and figure how to cope, or even better, capitalize on new opportunities.

An interesting survey was just completed wherein customers voted 57 to 36 percent on favorable/unfavorable scale in support of unlimited interstate banking. If our job as marketers is satisfying customer's needs, isn't the long-term answer obvious?

Relationship Management

The second development, relationship management, is leading to a changing sales process. For the most part, banking is still a product-driven industry. Bankers wait for customers to come to them, and buy whatever is on their shelves. But we are seeing the emergence of a relationship management orientation. Packaged products and services—Merrill Lynch's Cash Management Account and our Focus Account, for example—are being sold.

In fact, the capability is here for banks to render a complete menu of financial services to any individual in the world. Phrases like "relationship banking" or "cross-selling" are shorthand for a wide variety of services that banks wish to offer their customers.

This relationship capability is putting added pressure on our outmoded regulatory system, driven in part by our customers who are becoming more informed, sophisticated and demanding with each day. In order to be financial services companies consumers want, banks are fighting hard to get into insurance, real estate and securities, while these firms are entering the banking business.

More Complexities in Marketing Responsibilities

But relationship sales are not easy, and they aren't coming quickly. Consumers resist putting all their eggs in one basket. The process of getting them there is iterative, and probably requires intense cross-selling over time. Moreover, it won't happen until we can master the complex, elusive sales process by putting clear, valid benefits on the table in the areas of price, superior information and service. And we'll have to learn to set our management language in a different context: not just profitability but also customer relationships, customer penetration and depth, and market and market segment shares.

Our sales orientation must be built around customers, not technology. While we may all love what technology can do for us, our customers may not share our enthusiasm.

Application of Technology

Technology—particularly, its use to help us further our goals—is my next challenge.

Once a technological breakthrough is known by people in search of applications, then a second creative process starts that will put the new discovery to work, to either solve an existing problem or accomplish a new thing that cannot now be done. Too often we forget these two development processes have separate time frames.

For example, the telephone was seen as a useless toy for many years. Its commercial application required a major educational effort on its benefits to the user.

The key message is that both of these processes—the invention and the search for its application—have to take place to make change a commercial reality.

As an industry, we have successfully put technology to work for our customers in many areas, but it is important we remind ourselves that technology by itself is clearly not the answer.

In our rush for new and better ways of doing things, let's not forget the many financial services "revolutions" that were just around the corner, but never quite lived up to our expectations.

You know them as well as I:

- The "cashless" and "checkless" societies have not arrived; in fact, check use is growing.
- ATMs have not replaced branch banking.
- The videotext explosion looks great on paper, but we are a long way from understanding how to make it meaningful for our customers.
- And even home banking is way behind "schedule".

All these supposed revolutions were perceived to be imminent. The main reason they haven't worked is that the customer decided our great idea wasn't so hot—at least not yet.

What we've learned at Citicorp is that technological change requires its own pace, its own rhythm, its own calendar. The consumer benefits must be proven every step of the way. It sometimes takes hundreds of tests and simulations to get the technology right, and most of the time "getting it right" means seeing how the customer interacts with the system, rather than just seeing if the system works.

In New York, we have a development lab, which allows us to test consumer responses to new products and services *before* we offer them to the public. The lab is equipped to deal with simulation, iterative product design, ergonomics—where we can test and refine the interaction between customers and employees.

This is not a panacea, but it serves us well. We brought 2300 consumers through this lab to help design our automatic teller machine program in New York. Today, some 70 to 80 percent of our customers use them, which is more than twice the national average.

We test about 20 new concepts every year. In today's environment, I believe it improves our chances of success, reduces our chances of failure and permits us to reach for a high standard for our new product offerings.

To us, the inherent value of technology is obvious. The banking business, while based on money, thrives on information. Our customers want information as well as cash, and technology allows us to dramatically increase our capability to provide that information in a reliable, timely fashion. But technology doesn't tell us how to do it right.

My next challenge gets closer to the core of what marketing is all about, because in today's media world, we face a communications challenge—namely, the problem of getting our message across. Can we penetrate the increasing competition in advertising messages? "Media-Trends" magazine reported this year that the average consumer is inundated with 230,000 commercial messages annually and hears 18,000 radio advertisements. From 1975 to 1985, the number of TV commercials increased 45 percent. Over 75 percent of these commercials have shifted from 60 to 30 second ads. And now the consumer is faced with an increasing number of split 30's. Today, prime-time advertising on television takes 14 to 15 minutes of each hour. Is it any wonder that only 20 percent of American consumers can remember the message in a TV ad the next day?

This new environment presents a clear challenge to us as marketers.

Corporate Image

And what about image? How well can we as marketers develop corporate identification as well as a coherent and effective company image through the major organizational changes, new acquisitions and opportunities for geographic expansion that are occurring within the industry?

American Express, Prudential, Sears, J.C. Penny and Merrill Lynch rank very high in public awareness. According to a recent study, over 85 percent of American consumers heard of these companies and the services they provide. However, relatively few say that they are familiar with the various commercial banks, particularly if they live more than a few miles from the banks' primary market.

The public must become familiar with our name and image if we are to succeed in selling them our services and products. It will be our job to better understand the characteristics of the image we want to project relative to the competition on such measures as familiarity, reputation, products and services offered, confidence, trust, and consumer relations.

Service

All this brings us to what the customer is really looking for—timely, reliable service. The role this should play in our strategies is my next challenge.

Can we sell service? Can we differentiate ourselves by the quality of our service, maintaining high standards in each and every customer transaction? For Citicorp, that means billions of individual transactions worldwide.

We all give lip service to maintaining the highest standards of accuracy, responsiveness and courtesy towards our customers. But recent studies have shown that banks are weak in these areas. For example, 73 percent of card-holding consumers say Sears does a better job than banks of handling card-related problems.

When you sell a financial service, you have to resell it every day by delivering good support services. In other words, it's a contractual obligation with your customer, not a unit sale—like going into the supermarket and buying Jello, for example. This financial obligation cuts a lot deeper than it does for a packaged goods manufacturer.

Also, money worries and frightens people. They're usually not relaxed when you deal with them, and this adds to our problems. While service is important in any industry, it's certainly more important in banking.

What counts is the quality of execution. Senior management must not only be committed to it, but must communicate that commitment through every level of the organization. And you have to give your employees the tools or capability to deliver the best possible service. Service is not delivered by miracles, but by lots of specific actions every day.

If this is done, service quality can be an offensive tool for banks. While I believe it's marketable, I also believe it won't be easy to accomplish.

Success will come to those companies which are able to provide the interface that reliably gives customers what they want, when they want, every day of the year and from any location. This is no small task. And the investment levels required for this are growing exponentially—for both the technology as well as for the effort to bring the consumer along every step of the way.

People

Let me turn to a last challenge—perhaps a threatening one—the upgrading of our people.

We have an attractive industry—$5.2 trillion in investments and outstanding balances, $150 billion in net customer revenue, and a revenue base that's doubling every ten years. And this industry compares favorably with any consumer business I'm aware of.

The chance to build a relatively new, successful and highly profitable business is drawing in more talented people than ever before. They are taking advantage of the opportunities not only to create new products and services, but to develop and deliver them as well.

Our industry will require bank marketers to take more and more responsibility. We are the focal points in a complex business process, since our programs inevitably impact such elements as customer service, credit losses, regulatory reactions and the processing of volume. To make matters even more difficult, we are working with customers who look at financial services with much anxiety.

These dynamics, coupled with the fact that often *retail* financial services for banks have traditionally been staffed with prototypical corporate bankers—no insult intended—make it certain that the industry will see a further inflow of talent in future years. We'll not only have to move over as they arrive but, in fact, we'll have to play a leadership role in attracting them. Our story, compared with other industries, is impressive—but only with the new people can our highest goal be attained.

I'm optimistic about the future. We've come a long way in a short time. We still have a long way to go. Though we continue to suffer setbacks in regulation, technology and service, I believe that eventually we will come forward with new innovations and solutions. The marketing discipline can and should provide the intellectual leadership needed in financial services.

Thank you.

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Two Citicorp senior executives have examined the LDC debt situation in recent speeches. Here is their assessment of it, and the road ahead.

Sheridan L. Steinberg
Director, Public Affairs

Copies!
Coleman
R.

Progress In LDC Debt

Reports By
Hans H. Angermueller
Vice Chairman

William R. Rhodes
Chairman, Restructuring Committee

The Baker Plan: A Commercial Banker's Perspective

Hans H. Angermueller
Vice Chairman
Citicorp Citibank

An address before
The Global Interdependence Center
Philadelphia
December 10, 1985

Two months ago Secretary Baker proposed a new approach to the debt crisis—that countries grow their way out of the debt problem rather than attempt to shrink their way out of it. It was the right message at the right time. After three years we are all—debtor countries, international institutions, creditor governments and commercial banks—suffering from "adjustment fatigue." Secretary Baker's proposal could give us all the second wind that we need in order to stay the course and bring countries with debt-servicing problems back to the voluntary capital market.

In talking about the debt crisis we all too frequently forget how much progress we have made since the crisis first erupted in 1982. Countries with debt-servicing problems have slashed their current account deficits from $66.7 billion in 1981 to $14.7 billion in 1984. In 1982 problem countries' real GDP shrank by 2 percent. Today, their GDPs are growing at a rate of about 4 percent, or about two-thirds of the rate of growth that obtained during the years 1967–1976, before the crisis began.

Accomplishing The Task Ahead

Since 1982 industrial nations have initiated a recovery from the worst recession since the 1930s. Growth is again positive and the demand for developing country exports is higher. Inflation is lower and so are nominal interest rates.

Since 1982 commercial banks, especially in the United States, have strengthened their capital. They are in a better position to extend credit to developing countries, should it be reasonable to do so.

Finally, since 1982 international institutions, especially the IMF, have become more flexible in their approach to solving the debt-servicing problems of developing countries.

In sum, we have made considerable progress toward resolving the international debt crisis. But much more remains to be done. And it is to Secretary Baker's credit that he has sketched out how we can accomplish the task ahead of us.

The key element in Secretary Baker's plan is *cooperation*—cooperation among the four principal players in the debt drama: the debtor-country governments, international institutions, creditor-country governments, and the commercial banks. Cooperation has brought us this far and cooperation is essential if we are to accomplish what remains to be done.

Each of the four players has a job to do. Debtor-country governments must adopt and maintain market-oriented economic policies. Specifically, this means they must maintain market-oriented exchange rates, interest rates, wages and prices; they must adopt sound monetary and fiscal policies; and they must promulgate growth-oriented structural reforms, such as "privatizing" nationalized industries and providing a better climate for increased investment, both domestic and foreign.

As befits a general set of principles, they are necessarily vague. Obviously, the actual economic policies countries will adopt under the Baker initiative should be determined on a case-by-case basis. But one thing is clear: If countries are to grow, they must reward savings and capital. Savers, be they foreign or domestic, will only provide capital, be it equity or debt, if they have a reasonable prospect of receiving an adequate return. If countries are willing to reward capital, they can expect domestic savings to stay at home and foreign savings to flow in.

With this in mind, there are several other important steps—not specifically mentioned by Secretary Baker—that debtor countries should take if they are to attract development bank or commercial bank financing:

- These countries should commit themselves to making regular principal and interest payments on outstanding debt;
- Payment of existing obligations should in no way become subordinate to payment of interest or principal on new loans;

- No country should expect net new financing when it is unable or unwilling to meet its outstanding financial obligations.

All this may seem a tall order. And it is. But it is not beyond the capability of debtor countries and their governments. In fact, a switch toward market-oriented economic policies leads to a surprisingly fast and surprisingly significant improvement in a country's external accounts. Mexico found this in 1982–83, as did Brazil in 1982–84 and the Philippines in 1983–84. But countries have to stick with the market-oriented policies that bring about their improvement. As we have seen in Mexico and the Philippines the process works just as quickly, or perhaps even more quickly, in reverse. Deviation from market-oriented economic policies undermines the confidence of lenders and investors in a country. That deviation devalues the sacrifices that governments asked their people to undertake for it makes reasonable investors doubt that the government is able or willing to keep the promises that it makes. Thus, in working their way out of the debt crisis governments in developing countries should bear in mind that lenders and investors place a high premium on consistency. Countries that show consistent adherence to market principles can expect to receive the capital necessary to finance their growth; countries that do not adhere to those principles, or deviate from those principles, cannot expect foreign lenders, or even their own domestic citizens, to provide meaningful amounts of capital.

$20 Billion Needed in Next Three Years

If debtor countries have the courage to adopt and maintain these reforms, the other players have an obligation to support their efforts. Specifically, creditor-country governments should maintain non-inflationary growth. Lower inflation will bring about lower real interest rates and ease developing countries' debt service. Growth will increase demand for developing countries' exports and raise their ability to earn foreign exchange. Together, lower interest and higher exports spell lower debt service ratios and enhanced credit worthiness.

This, too, is a tall order, as anyone who has followed the debate on the U.S. budget can attest. But we owe it to ourselves, as well as to the debtor nations, to set an example in adopting sound macroeconomic policies and market-oriented tax and regulatory policies.

Needless to say, creditor-country governments should not offset the benefits of non-inflationary growth by resorting to protectionist measures that close industrial-country markets to exports from developing countries. Creditor countries cannot demand that debtor countries open their economies, if they are unwilling to open industrial markets to developing countries' exports. Nor can creditor-country governments expect banks to lend to debtor countries if regulators punish banks for making those loans through taxes, reserves or capital requirements.

International institutions must also support the developing countries that adopt and maintain market-oriented structural reforms. Specifically, multilateral development banks, such as the World Bank and the Interamerican Development Bank, must switch from exclusive reliance on making project finance loans as a preferred creditor to making structural adjustment loans as a general creditor. The recent joint statement of the World Bank and the IMF indicates that they are willing to move in this direction. In dollar terms, the multilateral development banks should increase their gross annual lending by 50 percent, so that their net credit outstanding to the fifteen Baker plan countries rises by $20 billion over the next three years.

Finally, commercial banks can and should extend a similar amount of new credit to these same countries, presuming that debtor countries, creditor governments and international institutions each do the job that they are supposed to do. If developing countries adopt sound policies, if creditor countries maintain non-inflationary growth and refrain from protection, and if international institutions also lend in support of developing countries' structural reforms, then the risk of loans to debtor countries will decline and it will be both profitable and prudent for banks to increase their exposure to these countries. Commercial banks are now working jointly and singly to figure out ways in which they can safely extend new credit to countries that take the steps needed to make themselves creditworthy again. But commercial banks are also working, and rightly so, to make sure that they do not extend new credit to countries that are not credit worthy.

In summary, the Baker proposals have been well received to date. All the players have basically said: "I'm willing, if you're willing." That's a good start.

Where do we go from here? Obviously, the first move is up to the debtor countries. For the Baker plan to succeed, debtor countries must be willing to take the necessary policy measures. Everything else depends on that. Fortunately, some countries are already moving in the right direction.

Debtors and Creditors Must Work Together

Ecuador has already taken many of the necessary measures, including the virtual elimination of its budget deficit, divestment of a number of state-owned enterprises, near-finalization of a multi-year restructuring, and near-finalization of a significant World Bank sectoral loan for agriculture.

Argentina has also started to make the necessary policy changes. This is enough to make even the most hardened skeptic take heart. A year ago no one thought that Argentina would take the steps that it did, and that it would be political suicide for any Argentine government to take those steps. But the fact is that even after imposing an almost unheard of austerity on the Argentine people, President Alfonsin retains his popularity. So much so that his Radical party was able to increase its Congressional margin in last month's elections.

Now it's true that not every political leader in the debtor countries is an Alfonsin. But it's also true that the Argentine president is not a global economist. What he is more than anything else is a politician, using the arts of politics to achieve what economists alone couldn't hope to accomplish.

The Austral plan, as it is called in Argentina, isn't a panacea for every country with debt problems. But some form of it, with local variations, could be. And with the right kind of politicians to push it through and make it stick, it opens up new hope for the people whose nations have been struggling and striving through nearly three years of loan restructuring and economic adjustment.

These hopes must not be dashed. All involved in the debt crisis—debtor nations, creditor nations, international institutions and commercial banks—must work together to put the developing countries with debt servicing problems back on the path to sustainable economic growth. And I believe that we will succeed for solving the debt problem is plainly in the self-interest of each of us. As Secretary Baker said in Seoul, "Fundamentally, there is no disparity of interest....We have a common interest in growth—sustained growth that rests on productivity, innovation and investment. Let us begin our efforts now."

LDC Debt: Outlook for 1986

by
William R. Rhodes
Chairman, Restructuring Committee
Citicorp/Citibank

Financial Times World Banking Conference
London
December 10, 1985

In 1985 we have seen a great deal of movement in the international debt crisis.

The current situation has attracted some glum assessments, as the press has reported. Patience with economic adjustment has worn thin, we read almost every day. Political factors in some countries have eroded adjustment programs, with disappointing results on inflation, deficit spending, and trade balances.

Looking back, there have been setbacks in some areas, both due to acts of God and acts of man. Last year's bright spots are, in some cases, this year's uncertainties.

Yet, I believe the overall situation is better than some have portrayed it to be. A number of the countries affected by the crisis are making an economic comeback. As a whole, countries with debt servicing problems are now growing at about 4 percent a year, or nearly three-fourths the rate from 1967 through 1976. Current account deficits are down to under 2 percent of GDP, which is better than in many countries whose credit worthiness has never been questioned.

The performance of the debtor countries adds up to an improvement, overall, since we met a year ago. I feel this establishes a reasonable basis for a few individual countries to begin preparing to return to the voluntary credit markets.

The Baker Initiative Is A Welcome One

Against this backdrop, we have seen an important new development, and a welcome one, in the form of the Baker Initiative. Introduced at the International Monetary Fund–World Bank meeting in Seoul in October, this proposal recognizes the need for the LDC's to grow their way out of their debt problems.

As we have emphasized from the beginning, adjustment is not an end in itself. It is only the means for countries to resume growth on a less-inflationary, more-sustainable basis than before the crisis began.

We are on the threshold of a new phase, a third phase, in our work with the debtor nations. This phase, like the first two, will be closely tied to individual country performance.

If only the reality of negotiation and economic performance were as neat as the description of the model. Economic adjustment is an intensely political process, and the speed with which countries advance depends in large part on their will to do so. We must never forget the political equation, particularly in Latin America. Many of these countries are undertaking adjustment in a period of one of the most significant political changes in generations, with widespread movement from military rule to democracy. From time to time, delays are inevitable.

To review briefly, the first phase began with emergency packages, rescheduling of maturing loans and some new lending. This served to tide the countries over as they began to adjust their economies, on the one hand, and to keep creditors in the market on the other.

Mexico was the first to adjust in this way. At the outset of the de la Madrid administration in December of 1982, Mexico introduced an adjustment program, which the following year allowed it to build reserves, cut inflation and resume growth.

On the other hand, Argentina embarked on such a program only last June.

Phase two is characterized by multiyear restructurings for those countries that made progress in adjusting their economies in phase one. A multi-year restructuring eases the burden of debt service in the short and medium term, postponing principal repayment until later in this decade and the next, when it will represent a smaller proportion of larger national economies.

On March 29, Mexico became the first nation to sign a multi-year restructuring, while Ecuador and Yugoslavia are both scheduled to sign by the end of this month. Venezuela, Uruguay and the Dominican Republic should do so at the beginning of next year.

The third phase is to promote a return to voluntary lending, or as some have called it, "voluntary lending with a push."

We do not see a return to the massive cross-border bank lending for government accounts that constituted such an historically large portion of LDC capital inflow in the 1970s. As we now know, much of those funds ended up financing balance-of-payments and budget deficits. Some short-term credit was also used to finance longer-term investment.

Instead, in the years ahead we hope to see the countries achieve a more balanced inflow of funds, predicated on the realities of the marketplace. Countries will re-enter the markets for project finance; co-financing by the commercial banks with the World Bank and regional development banks; bond issues, increasingly in currencies other than the dollar; and more trade finance.

The Baker Initiative is dedicated to making that possible. It doesn't replace the case-by-case approach of the last three years. Indeed, it explicitly recognizes the effectiveness of this method and seeks to help it move ahead.

Each Has A Role To Play

The four pillars of the initiative are the debtor countries, the multi-lateral development banks, or MDBs, commercial banks, and the governments of the industrialized countries. Each has its own role to play.

The debtor countries are asked to adopt comprehensive market-oriented structural policies to promote growth.

The MDB effort would include a continued key role for the IMF and increased and more effective structural and project lending amounting to $20 billion in net new money over the next three years.

The commercial banks are being asked to increase their net lending by $20 billion in support of these countries' adjustment programs over the same three years.

Implicit in the Initiative is a commitment by the industrial nations to adopt and maintain the same kind of market-oriented policies expected from the debtor countries.

Lower inflation, which would lead in time to lower interest rates, and sustained real growth, which would promote demand for LDC exports, are both vital. In addition, to preserve the market for those exports, protectionism must be resisted.

Contrary to certain news articles, I feel the proposal has been well received by the international banking community and I expect that the banks in general will endorse it as we proceed.

While the aims of the initiative were explicitly outlined in Seoul, the details are still being worked out.

On the commercial bank side, for example, there are national and international groups of banks working on the mechanics of the initiative.

For the time the Baker plan has been in front of us, I would say that the responses from the interested parties generally have been encouraging. Many questions remain unresolved, but I expect that they can be surmounted and that the first loans under the plan could come as early as the first semester of 1986.

As the case-by-case approach we have taken from the beginning indicates, these countries have their own strengths, their own weaknesses, and their own political agendas.

The Bank Advisory Committees, therefore, will remain the focal point of the banking community's effort, since they are the basis for the case-by-case approach.

Country-By-Country Status

Looking at the countries whose Advisory Committees I chair or co-chair, Brazil's external economy continues to perform well. November's trade surplus reached $1.105 billion, which suggests a 1986 total of $12.5 billion, close to last year's record of $13 billion. The current-account deficit, which originally was projected at $2 billion for this year, should be close to equilibrium. Foreign reserves are now in excess of $9 billion as against $7.5 billion at the end of 1984.

The internal economy is growing rapidly, with GDP expected to increase by seven to eight percent. Inflation, however, remains a problem, running at about the same level as last year, some 230 percent.

Brazil has indicated publicly that at this time it does not plan to reach a formal agreement with the IMF on an adjustment program. We will learn more about the government's plans for the economy and for the pending 1985-86 maturities at the end of this week when they meet with the bank advisory committee in New York.

In the meantime, we are working to complete the 140 day roll of trade and interbank facilities to January 17, 1986.

Mexico's disappointing economic performance in 1985 has been exacerbated by the devastation of the September earthquakes.

The trade surplus is expected to drop to $8 billion for 1985, compared to $13 billion in 1984.

The public-sector deficit this year is now likely to reach 9.6 percent of GDP, compared to 1984's 6.1 percent; and inflation should be about 60 to 65 percent, slightly higher than last year's 59 percent.

The new budget calls for a trade surplus of $7.5 to $8.5 billion, a cut in the public-sector deficit to 4.9 percent of GDP and an inflation target between 45 and 50 percent.

The bank advisory committee met with the government last week to review its economic projections. Mexico is already having general conversations with the Fund and negotiations are to begin in earnest when the budget is approved by Congress, which is expected before Christmas. Mexico estimates it will need $2.5 billion in net new money next year from commercial banks and has expressed an interest in the Baker Initiative.

Argentina has made significant progress this year after the introduction of its courageous Austral economic program this past June.

Argentine inflation, once among the highest in the world, has ranged between 1.9 percent and 2.4 percent in the last few months, compared to 31 percent in June, when the government began its adjustment program.

One of the challenges the government will face in the new year will be the phasing out of the wage-price controls that have been a key part of the Austral plan to date.

On November 26, the government paid approximately $340 million to its creditor banks, completely eliminating all public-sector interest arrearages for the first time in over three years.

The bank advisory committee expects to meet with the government in the next month or so to begin work on the bank portion of Argentina's financial plan for 1986 and some subsequent years.

Peru's arrearages to commercial banks on public sector indebtedness now stretch back over a year and have reached about $400 million, although the country's reserves stand at approximately $1 billion.

We meet with the government at every opportunity, either as a group or individually, and we continue to press for interest payments, trying to convince Peruvian officials that there is much to be said for cooperating with the international financial system.

Incidentally, Bolivia, one of Peru's neighbors, which suspended debt-service payments two years ago, has adopted a strong economic adjustment program. An IMF mission is now in Bolivia to negotiate a credit arrangement.

Uruguay is on the threshold of both phase two and phase three, having reached preliminary agreements with its advisory committee on a multiyear restructuring and the first voluntary loan by commercial banks to any Latin American country since the debt crisis began.

This loan, a $45 million co-financing with the World Bank for an energy project, will, when completed, be substantially over-subscribed. To illustrate its voluntary nature, there are some banks among the participants that have made no previous loans to Uruguay.

While this co-financing was in the works before the annual meeting in Seoul, it is consistent with the kind of loans we can expect to see under the Baker Initiative.

The special case of Colombia also gives us a preview of phase 3. Unlike many other LDCs involved in the debt crisis, Colombia has never missed an interest or principal payment. Nevertheless, it encountered the same reluctance in the marketplace as those nations that had. Now, with a unique monitoring arrangement with the IMF, Colombia has wrapped up a $1 billion syndication, mainly for export-related oil and coal projects. The signing of this loan is scheduled for a week from today.

Further loans of this kind will be linked to, and support, the structural adjustment many of us have been recommending, and which now has been given new impetus by the Baker Initiative.

Some early steps toward structural adjustment have already been taken. For example, Brazil has begun a program to sell shares in 17 state-owned companies, including Petrobras, the national oil company; Ecuador has divested itself of some state-owned companies; Mexico recently sold a major state-owned hotel chain and has applied for GATT membership as part of its new policy of liberalizing trade.

What Is Needed Now

I hope, however, that each country sees such measures as only the beginning. It will take bolder steps to reduce the pressures for capital flight, so that domestic savings will become a far greater source of development finance. I also hope that the countries will see their way clear to allowing more private direct investment from both domestic and foreign sources, which can be politically difficult in some cases, but which would help stimulate growth and reduce dependence on foreign borrowings.

Creditor governments also have a role to play as we move ahead. The LDC's will be expecting more multiyear restructurings from the Paris Club, when they negotiate such agreements with the commercial banks. I think they also have a right to expect that governments will maintain their export cover for developing nations that are making progress in their adjustment programs.

OECD nations must go further in resisting protectionist measures that threaten the ability of LDC's to export. It is important, too, that bank regulators in the creditor countries respond to improvements in asset quality with more prompt revision of country classifications.

For our part, we commercial banks are exploring new possibilities on a number of fronts.

One idea now under consideration is the creation of a trust or mutual fund, administered perhaps by the World Bank, with participation by the commercial banks, particularly those with smaller exposures, in amounts that meet their commitments to new financing. Drawdowns by the countries would be conditional upon their economic performance.

As usual, there are many potential problems as we move ahead. The direction of interest rates, oil prices, commodity prices and exchange rates are all large question marks, as is the threat of protectionism.

Finally, there still are occasional calls for non-market proposals such as capitalizing interest or limiting payments to fixed percentages of exports. These proposals, if adopted, would be counterproductive. Phase 1 was carefully designed to keep reluctant private institutions in the marketplace. Any such proposals could drive them out, depriving the LDC's of an important source of capital they will need to resume economic development. Sustained growth resulting from structural adjustment is the key for LDC's and growth will depend in large part on the markets for their exports in the developed world. According to Citibank's economists, the OECD growth rate will average a bit over three percent for 1986, with U.S. growth somewhat higher, which would maintain demand for LDC exports.

In sum, notwithstanding all the problems of the past year, I believe the countries have made real progress toward regaining their credit worthiness. I am confident that a year from now, when we look back at 1986, we will be able to report further progress.

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Customer Service

January 29, 1986

Bank Customer Service - NYBD Research

Heron: People wanted trouble-free checking, reduced line waits, quickly corrected mistakes, friendly, competent, well-trained staff, clearer, more easily understood statements.

Neubert: No home runs. Two and a half year, tob to bottom effort and inch by inch process. One customer says: tellers smile, loan officers rise to shake your hand. It's awesome.

Citibank uses video tapes, role-playing etc.

Deregulation
Depression

INTERSTATE BANKING

May 16, 1986

* Federal regulators want to win congressional support for interstate takeovers of failed and failing banks.

* Big agricultural and energy area banks weak.

* Regulators want to facilitate out of state bhc purchases of some of these banks go bust and hurt fdic.

* Financial markets too edgy about the banking system. Powers sought are precautionary.

* Garn: unclear whether he will move on regulator's bill on its own merits or try to combine it with a larger deregulation package.

* Garn: uncomfortable position of seeking to close "nonbank bank" loophole while Republican administration has begun vigorous lobbying to keep it open.

* Angermeuller wants to see full, in-state parity for an institution buying a failing bank in another site, and liberalized bidding procedures now designed to promote instate takeovers of troubled institutions.

ANGERMUELLER TESTIMONY May 16, 1986

May 7 testimony to house banking subcommittee:

* Interstate market for healthy banks now sellers market.

* Regulator's bill on emergency acquisitions should be changed so as to induce rather than deter out-of-state institutions in competitive budding.

* bill should permit out-of-state bhc bidder to expand within the state and region to the same extent as an inside bhc.

* permit non-binding discussions with potential out-of-state bhc bidders, but require prior notification to state regulators before entering into binding commitments.

* House Committee should also consider eliminating or simplifying emergency thrift and bank acquisition provisions in the Garn-St Germain Act which deal with multi-level bidding procedure priorities; (2) preferences for adjoining state bidders; and (3) limitations after acquisition on intra-state branching or principal office location.

* Perhaps attractiveness of making bid could be enhanced by permitting successful out-of state bidders to acquire a friendly bank for each bad bank purchased.

May 15, 1986

REGULATORS'S BILL

- Permit out-of-state bhc to acquire a commercial bank that is failing but not yet closed. Current law permits only if institution failed.

- Lower asset level from $500 million to $250 million.

State regulators contend that certain provisions of bill move closer to interstate banking:

1. Federal overrides of state regulator interests

2. Lowered threshold of eligibility.

3. Fed could block a state regulator's choice for an in-state buyer if it determines the acquiring bank lacks adequate financial resources.

State regulators are looking for compromise. Want veto power under FDIC emergency acquisition.

State regulator/Independent Banker's Association has recommended that Congress consider as an alternative retaining the $500 million threshold while also granting an exemption for the four largest banks in those states with fewer than four banks above $500 million in assets.

Garn may want to tie on even more fundamental legislation, which could make for difficult passage of the regulator's bill.

Risk of Depression

Now possible:

- * Am. bank portfolio includes $500B, third world and farm debt.

- * More bad debt as oil prices fall and affect companies and countries.

- * Banks must pay interest to depositors. So much bad debt will force a crack.

- * Gov't. insurance a fraud.

- * Lots of funny instruments people don't understand:

  - leveraged buyouts

  - bank bonds

  - bundled mortgages

- * U.S. now a debtor nation.

EXPANSION

Federal Law provision to allows ~~C.B.~~ Sick S+L's + Sick Banks to be acquired by BHC's and/or out of State S+L's. this was the act that provided exception proper for Interstate Banking.

Overview

- o Disadvantaged re other S/Ls (even non-Florida based)-S/Ls can branch state-wide without county restriction.

- o Since CSF is owned by a bank holding company, must comply with bank branching limits. So limited by FRB acquisition order and Garn Act.

- o General bank branching rule is that CSF (S+L owned by BHC's) can enter new county only by acquisition.

- o Additional key limitation is that acquisition must meet "public benefits" test as applied by FRB - usually requires that acquired S/L be bankrupt.

  - Community Federal
  - First Federal of the Florida Keys dog

- o Game Plan:

  - revisit legal issues to recertify and identify potential legal opportunities
  - coordinate with New York the assessment of regulatory environment, especially disposition of FRB.

- o Miscellaneous:

  - awareness of Community Reinvestment Act (CRA) issue 4(c)8

• Florida state Law calls for Commercial Banks to branch only within county of incorporation.

• Acq of Banks in other counties is possible:

1. Acquiror/Acquiree were 18 mo old then merger.
2. But, FRB Bank Law also requires that when a bank owned S+L acquires another S+L (or merges) must meet Public Benefits test

TANDEM

- real estate brokerage services (but not for property owned by third parties)
- real estate development or subdivision
- acquiring improved real estate or manufactured housing for rental or resale
- interest rate futures transactions
- financial options trading
- income tax preparation
- insurance brokerage or agency for liability, casualty, auto, life health, accident or title insurance
- fiduciary services
- credit card operations
- data processing services
- investing in commercial paper and corporate debt securities

Activities Permitted S+L's by Garn Act

REGULATORY/LEGISLATIVE

Regulatory

- S/L is creature of statute
  - defines permissions
  - 1982 Garn Act increased powers
- Dual regulatory structure complicates operation of S/L
  - FRB: coordinated by NY Legal/authority to regulate as subsidiary of bank holding company,
  - FHLBB:
    - coordinated by CSF and NY Legal
    - role of Atlanta FHLB: ~~Sam Connelly~~/Debra Paradice
- Tandem / Affiliate rules regulate CSF interreaction with CSF affiliates
  - FRB: tandem rules contained in FRB acquisition order - requires that CSF operate as independent entity and not in tandem with other Citicorp subsidiaries
  - FHLBB: approval usually needed for sale or service transactions with affiliates to insure financial well-being of S/L
- Recent key regulatory issues
  - tandem relief* Janet Burak/Ellis Bradford Thompson/
  - treasury and sale of loans to affiliates application - FHLB/FRB FH Fuller NYCo
  - FBA complaint - PTP Enforcement
  - heavy volume of new regulations
  - status of FSLIC:

    406 corporation to purchase bad assets from troubled institutions

- tandem
- FBA complaint
- Pub Benefits Test
- *less Restric ~~on~~ at threshold
- lower entry

Activities permissible for federal savings and loan associations pursuant to the Garn-St Germain Act and the FHLBB's implementing regulations:

- equipment leasing
- purchase/sale of participations in loans
- commercial and standby letters of credit
- construction lending
- inventory and floorplan financing for dealers in consumer goods
- personal property leasing
- factoring
- reverse repurchase agreements
- suretyship agreements
- education loans
- investing in financial futures and option trading
- lock box services
- finance leasing/general leasing

*Caveat - 60% of assets must be in certain investments in order that Citicorp Savings remain classified as a domestic building and loan under the Internal Revenue Code.

Activities permissible for service corporation subsidiaries:

- real estate lending
- manufactured home lending
- home improvement loans
- educational loans
- consumer lending
- commercial lending
- services for financial institutions (including credit analysis; appraising; construction loan inspection; abstracting; investment, advisory and consulting services)
- maintaining and managing real estate
- relocation services

Bank S and L Buyouts 5/13/86

Gray: Government efforts to prop up ailing thrifts may be jeapardized by banks' plans to purchase healthy savings and loan associations.

The withdrawal of healthy savings and loans from the FSLIC would leave only the troubled institutions, taxing the agency's reserves and hampering a plan to re-strengthen the industry.

Local example:

Home Federal would change from a federally chartered to a state-chartered s and l to take advantage of a state law allowing and s and l to become a state-chartered bank.RATES
5/13/86

Mortgage rates continue decline but pace slows. Single digit for 5 weeks now.

Bank S and L Buyouts 5/13/86

Gray: Government efforts to prop up ailing thrifts may be jeapardized by banks' plans to purchase healthy savings and loan associations.

The withdrawal of healthy savings and loans from the FSLIC would leave only the troubled institutions, taxing the agency's reserves and hampering a plan to re-strengthen the industry.

Local example:

Home Federal would change from a federally chartered to a state-chartered s and l to take advantage of a state law allowing and s and l to become a state-chartered bank.Problem Banks
5/13/86

RATES 5/13/86

Mortgage rates continue decline but pace slows. Single digit for 5 weeks now.

Under deluge of refinancing requests, some lenders reluctant to cut rates further.

Some analysts believe bottom reached in late summer, dropping another 50 bp.

Average term mortgage loan down to 24.7 years in April from 25.3 years in March. Loans average 74% of purchase price. Average purchase price is 112,700.

Yeilds on 30 year treasuries, a bellweather of rates, fell to lowest levels since 1975 - 7.37%. May 7 Bond action sold record $27 billion in debt.

FSLIC 5/13/86

- Emergency plan to pump up to $25 billion into a federal fund to insure s and l deposits.

- self help plan analogous to the use of mortgage loan to buy a house.

- Due help to ailing thrifts of the early 80's, reserves only $6 billion to handle the 200 thrifts expected to fail over the next 3 years.

- GAO worst case cost scenario for thrift closure FSLIC obligation is $22 billion.

- The transaction: a financing corporation would be created to raise money for the FLSIC in a way that would shield the FHL banks and the FSLIC itself from any obligation to repay the initial $15 billion to be generated in the first three years.

  The 12 regional home loan banks, which are owned by member S and L's and regulated by the bank board, would contribute $3 billion in current and future profits to the new financing corporation, which the banks would own and operate.

  The corporation would use the $3 billion to buy zero-coupon Treasury bonds and then would use those bonds as collateral to raise the $15 billion by issuing regular bonds to investors in the open market.

  The corporation would use the $15 billion it will receive when the zero coupon bonds mature in the year 2020 to retire the $15 billion bond issue. The corporation would go out of business.

Bank S and L Buyouts
5/13/86

REGULATORY SUMMARY - EXPANSION AND TANDEM

Dual Regulatory Structure -

FEDERAL RESERVE BOARD (FRB) - Tandem rules contained in acquisition order. CSF must operate as independent entity and not in tandem with other Citi subs.

FEDERAL HOME LOAN BANK BOARD - Approval needed for sale or service transactions with affiliates.

EXPANSION

Typically S and L's can branch state wide (any state) sans county restrictions.

However, CSF is owned by a bank holding company and is therefore subject to FRB order and Garn act.

General FRB order: S and L owned by BHC can enter new county only by acquisition.

Additional limitation of Garn Bill and FRB: CSF acquisition must meet public needs test. Euphemism for bankrupt S and L acquisition?

Under public needs guideline, tried to buy Community Federal in Tampa. FRB (FHLBB?) said no, not unless also acquire First Federal of the Florida Keys (a bank in much poorer shape).

PROJECT

- Ideal branching hypothesis

- Acquisition screen to seek fit to branching hypothesis

Acquisiton analysis would focus on which bank's most closely fit strategic objectives established in ideal branching hypothesis, which are most likely to be available of the remaining candidates (which of these are closing in on neg net worth etc.).

- Delineation of obstacles (legal, willing seller etc.)

- Pro-active expansion project coordinating, legal, acquisition, public affairs, and legislative initiatives necessary to desired expansion.

- Evaluation of alternative legal constructs beyond current understanding.

Two Key Gain Goals:

1. Close NBB loophole
2. Reform Deposit Insurance Funds

Garn wants to tack on legislation that:

1. Banks can own discount brokerage
2. Underwrite commercial paper, municipal bonds, and mortgage backed securities.

In 1984 House (St. Germain), effectively killed legislation granting full interstate by 1990.

DEREGULATION

RATE DEREGULATION -

Reg Q:

- o Minimum balance
- o 5 1/4 % NOW Account
- o 5 1/2 % Passbook Account

PRODUCT DEREGULATION -

GEOGRAPHIC DEREGULATION -

Regional Compacts

IMPACT OF DEREGULATION

- Large bank consolidation

- Small bank specialization
  - S & L should do well because meet individual needs

- Large increase in user fees due to necessity to offer higher interest rates. Hurts small saver

- More products to consumer

NEW LEGISLATION

MARCH 31, 1986

GARN: Pessimistic on future deregulatory legislation

WHY?: House doesn't want GARN's comprehensive approach

SO: Garn has threatened to not consider House's piece meal approach

MOST RECENT PIECE MEAL:

o Financial Inst. Equity Act. of `85

o World outlaw non bank bank forward after May 9, 1984

o But Garn says stop gap. More hybrids would follow as this loophole closed.

GARN VIEW:

New regulation which would look at function rather than classification. Broad based change of regulatory structure.

HOUSE: Mood has shifted away from deregulation

HOUSE PRE-OCCUPATIONS:

o Consumer oriented legislation

o Rate cap on cards

St. Germaine wants to pressure GARN to change posture

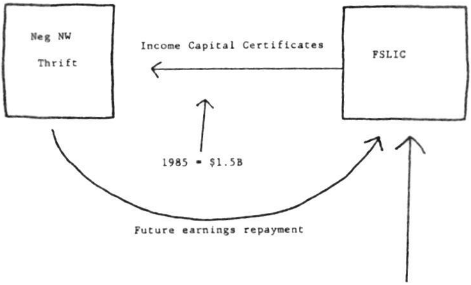
Lobby by:

Paul Volker
ABA
National Government Association

All of whom want NBB's loophole closed but not necessarily to do through comprehensive legislation

TREASURY: Shifted stance NBB's should operate

3/31/86



Neg NW Thrift

Income Capital Certificates

FSLIC

1985 = $1.5B

Future earnings repayment

Unobligated balance of
FSLIC Fund
1985 = $2.7B

TOTAL Fund = $6.1B

5 Year total bail out cost = $22.5B

460 insolvent thrifts

Deposit regulation
Post 1986

1. No interest on demand deposits

2. Only non-commercial customers eligible for NOW

3. Minimum withdrawal penalties on time deposits. Retain $150M ceiling on non-personal savings accounts.

4. Reg. D. : Maintain reserves equal to a percentage total transaction account and non-personal time and savings account deposits.

   Reserve requirements reduce the value of checking A/C balances to a bank and correspondingly will reduce the rate that a bank will pay on a deregulated checking account.

Deregulation

People who have stock in local banks will clean up.

Arizona 2.7 times book.

Issues

- regional compacts
- interstate banking triggers
- future of deposit insurance
- level of playing fields
- wider powers for banks and thrifts

GARN: Opposes national trigger

S & L Prospects?

Now have additional commercial and industrial lending powers; can be less dependent on housing.

'85 House (St. Germain) passing major legislation.

Why? Growing instability and shakiness of system.

Issues: 9% capital

By going for interstate privileges, have big bankers reduced ability to get add'l powers -- asking for too much? Need add'l powers given interest rate for deregulation.

Two tiered banking system. One group will not be allowed to fail.

S & L's only have 2% capital requirement. Playing field is not level.

Rudman: We must bring to order the regulatory process by establishing a spectrum of reserve and capital requirements that are determined by the make-up of the liabilities of the institution.

We must consider risk related deposit insurance premiums.

TRIGGER: undermines market for failing institutions.

Do expanded powers to compete with the Sears, but perhaps through independently capitalized subsidiaries.

Additional Powers:

- Real Estate
- Insurance
- Underwrite mortgage backed securities.

January 29, 1986

Rise in Regional Mergers Frustrates Big Banks - WSJ 1/20/86
Money Center banks kept out of the merger action in 1985 and probably also for 1986.

Supreme Court upheld right (in June 1985) of legislatures to establish merger compacts, in which states open their borders to one another while excluding banks from other regions, notably New York.

Trends:
* Super-regional banks are emerging as competitive threats

* Regulatory pressure on big banks to raise capital ratios, combined with surge in stock prices for regionals is making it unlikely that big banks could afford many sizable acquisitions even if they were allowed to pursue. Result: many banks are scaling back acquisition plans and focusing more on investment banking and on business closer to home.

* Major banks view acquisitions of troubled thrifts as main hope for expanding across state lines in near future.

Fastest Growing Super-regionals:
* Wachovia/First Atlanta - 16.7 billion
* NCNB/Georgia, SC, and Fla acquisitions - $20.7 billion

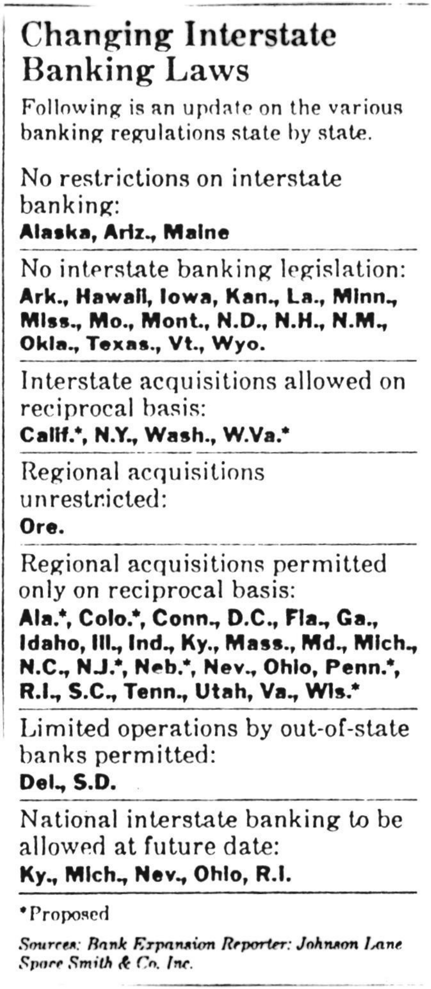
Therefore:
We'll have more large banks with money centers less of a meaningful, separate group.

Some support for Regionals to include NY
Pa and Nj where smaller banks don't want to be passed up in getting premiums for acquisitions.

Regulatory restrictions prohibit Citicorp from combining thrifts with other operations.

Run-up in stock prices could slow up interstate mergers.

More small banks will push for triggers. If you're a bank that has decided your not going to be a survivor, why would you want to restrict the sale of your franchise only to banks within the region?



Changing Interstate Banking Laws

Following is an update on the various banking regulations state by state.

No restrictions on interstate banking:
Alaska, Ariz., Maine

No interstate banking legislation:
Ark., Hawaii, Iowa, Kan., La., Minn., Miss., Mo., Mont., N.D., N.H., N.M., Okla., Texas., Vt., Wyo.

Interstate acquisitions allowed on reciprocal basis:
Calif.*, N.Y., Wash., W.Va.*

Regional acquisitions unrestricted:
Ore.

Regional acquisitions permitted only on reciprocal basis:
Ala.*, Colo.*, Conn., D.C., Fla., Ga., Idaho, Ill., Ind., Ky., Mass., Md., Mich., N.C., N.J.*, Neb.*, Nev., Ohio, Penn.*, R.I., S.C., Tenn., Utah, Va., Wis.*

Limited operations by out-of-state banks permitted:
Del., S.D.

National interstate banking to be allowed at future date:
Ky., Mich., Nev., Ohio, R.I.

*Proposed

Sources: Bank Expansion Reporter; Johnson Lane Space Smith & Co. Inc.

EPIC
EXPENSE
ECONOMY

The Research Institute

Executive Wealth Advisory

Section Two

January 20, 1986

SPECIAL REPORT

Title page

The 1986 Economic Outlook: A Guide for the Investor

The domestic and international economic scene has seldom inspired such a paradoxical mixture of hope and apprehension as it does today. On the one hand, a soaring U.S. stock market, declining interest rates, low rates of inflation, a weaker dollar, and a continuing—although sluggish—recovery tend to inspire confidence. On the other hand, an imposing array of unresolved economic issues and problems, ranging from the huge debt burden of the Third World to the Federal budget deficit, awaken deep misgivings. In plotting their course for 1986, investors must keep both these factors—the short-run positive signs and the major long-run uncertainties—in mind. Whether you are by temperament an optimist or a pessimist, caution and vigilance are more than ever the order of the day. Here is how RIA economists size up the outlook for the economy in 1986:

► ***The business cycle.*** When the economy's real GNP growth rate slowed to an annual rate of about 1.1% in the first half of 1985, it seemed that the economic recovery that began late in 1982 had finally run its course. But statistics for August and September showed that it was getting a second wind: factory output, housing starts, car sales, durable goods orders and retail sales were all climbing. Despite subsequent faltering, more recent signs suggest that this trend is continuing. In November, for example, the operating rates at American factories, mines and utilities edged up a bit after two consecutive monthly declines. And, although new housing starts had a sharp decline, a number of industry pros think there will be a rebound as mortgage rates continue to fall, attracting new home buyers. We estimate that the overall real GNP growth rate for 1985 was 2.5%, with the fourth quarter rate growing at nearly 4%.

We project that the economy will continue to grow at a very moderate rate well into 1986. Service industries will lead the way, but many other sectors of the economy should also enjoy some growth. Trade sensitive industries, however, face hard times. And by the end of the year a general recession is a distinct possibility. It's important to remember that the current recovery had its third birthday in November and is well past its prime. Consumers are deeply in debt, and now likely to spend with restraint. And continuing pressure on prices from foreign competition will limit increases in aftertax corporate profits. The economy is still growing, yes, but it has lost much of its impetus.

► ***Major uncertainties.*** Here are some of the key problems and issues that could take a decisive turn next year and which—if not resolved—will continue to cast a shadow over trade, industry, and investment:

• ***The Federal budget deficit:*** Currently running at over $200 billion, the deficit could double in 4 or 5 years at its present rate of growth. Interest on the national debt is rising even faster than the GNP. True, Congress has recently mandated automatic spending cuts if the deficit does not shrink to zero by 1991. Yet aside from this desperate measure, which may, in any case, be overturned in court or changed by Congress itself, there has been no substantial action to close the gap by cutting expenditures or raising taxes.

• ***The trade deficit:*** Although the decline in the value of the dollar in 1985 may begin to turn the tide by making U.S. exports more competitive, and foreign imports more expensive, the trade deficit seems headed toward another record in 1985. In the third quarter, the current account—the broadest yardstick of trade in goods and services—increased to $30.45 billion. Even if the trade deficit begins to improve next year, and the dollar remains where it is or declines, the flood of foreign imports will subside, and our exports increase, only slowly. And there is a danger that a rise in the cost of imports could spark a resurgence of domestic inflation.

• ***The dollar.*** The future movement of the dollar in international currency markets depends on a wide variety of factors, including the course of U.S. interest rates. Declining rates tend to weaken it; and a rise in rates strengthens it.

• ***Tax reform.*** A tax revision plan that would make the most sweeping changes in the tax code in over 40 years has finally passed the House. It differs in many ways from the bill the Administration proposed, and is likely to be changed dramatically in the Senate. Debate on the bill could last all year. Meanwhile, uncertainty about its ultimate provisions may inhibit business decisions throughout the economy.

• ***Third World debt.*** The Reagan Administration's new initiative to ease the debt crisis may relieve the problem, at least for a while, but it remains to be seen whether it can really contribute to a long-range solution.

▶ ***Outlook for key industries.*** Here is a rundown of the 1986 outlook for particular industries that may offer investment opportunities.

• ***Service industries:*** Service industries have been top performers in recent years, creating almost nine of every ten new jobs since the 1981-82 recession. This sector will continue to outpace the economy as a whole, but its growth won't seem impressive by its own past standards.

... *Advertising.* Because corporate profits will be modest, the growth in advertising spending in 1986 is likely to fall below the double digit mark for the first time in this decade, and may not return to a 10%-plus rate until 1988.

... *Banking and finance.* While the turmoil of this industry may calm down a bit in 1986, it is far from over. So selectivity remains crucial for investors. Some of the problems that have plagued commercial banks—causing 90 bank failures in the first three quarters of 1985—should ease up next year. The industrial recovery in the Midwest will improve the financial condition of that region's banks. The money-center banks that have made large loans to developing nations should benefit from a softer dollar and lower energy prices, which have taken some of the financial pressure off the less developed countries. But there is little relief in sight for banks that specialize in farm loans. Among commercial banks, the trend toward mergers and regional banking will continue. There may also be some more liquidations. We estimate that commercial bank assets grew 6% in 1985 and will repeat that performance this year.

Many thrifts are still severely undercapitalized and plagued by problem loans. Mergers and liquidations will continue to thin their ranks. Still, the industry as a whole should enjoy moderate growth in assets and capital position in 1986, provided interest rates don't rebound to double digit levels.

... *Financial service companies.* Mutual funds, consumer and commercial lending institutions, and brokerage firms will continue to give banks stiff competition. Unhampered by

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government regulations, they can more easily adapt to market changes than banks, and can also enjoy a wider "spread" between loan rates and interest paid for funds.

... *Health care*. The trend to watch is cost containment. A "get tough" attitude on the part of both the federal government and health insurers, as well as the development of new alternatives such as outpatient surgery and home care, have helped to curb hospital costs. Thus the growth rate of health care costs has been slowing since 1980. In that environment, both drug and hospital-management companies should do fairly well, but hospital supply companies—particularly those that make sophisticated equipment—may face a profit squeeze.

... *Insurance*. Like the banks and financial services companies, the insurers have their share of problems. Although life insurers have adapted readily to a changing economic environment in the last ten years by offering interest-sensitive policies, such as universal and variable life, we expect a slowdown in the industry's growth rate over the next several years. The growth rate of insurance in force should fall well below the "normal" pace of about 11% per year.

Property/casualty insurers are just beginning to emerge from one of the most serious cyclical setbacks in recent years. The industry should make money this year. We project that total pretax income for these insurers should be about $2 billion in 1986, compared to an estimated loss of $2.5 billion in 1985. This more optimistic outlook, however, applies only to strong companies.

... *Entertainment*. This industry has benefited in recent years from 10% average annual increases in recreational spending. But after an estimated increase of about 10% in 1985, we project a sharp downturn to 5% in 1986. The reason: disposable personal income will probably level off. Which segments of the industry will suffer most? Which may surge ahead? This is hard to predict because of the impact of "the fad factor" on consumer spending patterns. Witness the recent rise and decline of video games and home computers. We figure that box office receipts of the motion picture industry backed off in 1985 because of a lack of blockbuster movies. Some recovery may be expected in 1986.

We have more confidence in our prediction that TV ad revenue will grow at a respectable rate, although not as fast as in previous years.

... *Printing and publishing*. We project that the book boom will continue for the duration of the 1980s. But a slower economy will reduce the growth rate.

▶ ***Motor vehicles.*** This industry has made an impressive comeback through cost reduction, and can now operate profitably on smaller volume. But the industry will continue to lose market share to foreign companies until American manufacturers offer more competitive prices and convince consumers that American cars compare in quality to imported ones. The boom in car sales last August and September, due to cut-rate financing and end-of-year discounts, did not decrease sales of foreign cars. It simply brought new buyers into the market. The late-'85 boom will probably mean reduced initial sales of 1986 models. In fact, the period of expanding sales that started in 1982 may be at an end. We project a 2% decline in total value of shipments this year from 1985 levels. The truck segment, however, will probably continue to grow next year.

▶ ***Aerospace.*** Revenues should increase steadily over the next few years for the main sectors of this industry. The domestic airlines are enlarging their fleets. And because of unspent defense appropriations, military aerospace shipments will grow in 1986 and beyond—regardless of the economy's performance.

Be wary, however, of the general aviation industry, which makes private plans for corporations and individuals. It will remain severely depressed in 1986.

▶ ***Personal consumer durables.*** The recent sharp increase in consumer debt could hurt this market in 1986. Overall growth in the toy industry—with no hot new items comparable to Cabbage Patch Dolls in sight—will be a moderate 9%, well below its level in the 1984 boom. We estimate that photographic equipment sales may have declined a bit in 1985, and will fall a bit more in 1986. Overall growth of sporting goods will not be extraordinary—about 10%—but there will be boom items, particularly in exercise equipment. Foreign competition will continue to hurt sales of most types of domestic sporting goods.

▶ ***Drugs and cosmetics.*** Over the long run, the aging of the U.S. population (by the year 2000 the number of people over 65 will increase by 26%) will boost demand for prescription and over-the-counter drugs, and for cosmetics such as skin moisturizers and hair colorings. Growth of sales and profits in the drug industry will be stronger than in many others, probably 10% annually for the next few years. But growth won't be as fast as in the past and will reflect primarily price rather than volume increases.

▶ ***Information processing.*** For mainframe computers, 1985 was a big year. And we project that shipments of computers of all kinds and peripherals will continue to increase in 1986.

As in telecommunications (see discussion below), there will probably be consolidation. Two distinct types of suppliers will succeed: major, full-range suppliers of computer/telecommunications equipment and smaller companies functioning as niche marketers.

Personal computers, which had a tremendous boom from 1981 to 1984, will grow much more slowly in the future. Consumers are now in love with VCRs.

• ***Consumer electronics.*** The current stars are the compact-disc (CD) player and the video-cassette recorder (VCR). According to some analysts, 25% of U.S. homes now own a VCR and demand is still growing.

The trends toward slow growth of one-brand component stereo systems (or "rack systems") and declining sales of portable compact stereo systems should continue in 1986.

Look for the emergence of 8-millimeter "camcorders" (combined camera/sound recording devices) in 1986 and for two or three years beyond. They will compete with the existing VHS camcorders.

But investors should always keep in mind that pricing and technology can change rapidly in this industry.

▶ ***Telecommunications.*** The two sides of this industry—products and services—face very different prospects and trends in 1986. In services, an overcrowded slate of companies in the long distance area is likely to experience a shakeout during the next few years, which will affect smaller firms more than the giants. The little guys will be forced to consolidate or find new market niches. One contest to watch: the increasing convergence of data processing and telecommunications has led to a head-on collision between two primary players—IBM (which linked its SBS/Skyline service with MCI in 1985) and AT&T, which has expanded rapidly into the office systems field.

On the product side, foreign competition is a major problem. In fact, the U.S. has had a trade deficit in telecom products since 1984. This has hit the high-tech end of the market especially hard, eroding our lead in PBX's and digital switching equipment. Nevertheless, these will be the primary growth areas in telecom products. Fiber optics and microwaves will also do well. Cellular mobile service will continue to grow, but not as fast as in the past. New applications of cellular technology and satellite service will become greater factors over the next 5 to 10 years.

▶ ***Food and beverages:*** Changing lifestyles are having a major impact on this industry. Many old standbys, such as red meats, canned fruits and vegetables, breads, pastries and distilled liquors, are losing market share. By contrast, processed frozen dinners, poultry products, whole-grain and high-fiber cereals, diet soft drinks, crackers, cookies and candy are thriving. The investor's task is to pick the winners in the fierce competition now raging in each of these areas. The introduction of new products and novel and jazzy packaging by innovative companies will help them gain a competitive edge.

THE KIPLINGER WASHINGTON LETTER

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THE KIPLINGER WASHINGTON EDITORS

1729 H St., N.W., Washington, D.C. 20006 Tel: 202-887-6400

Cable Address: Kiplinger Washington D C

Dear Client: Washington, Dec. 13, 1985.

Business prospects for 1986 look good.

The economy isn't about to run out of gas, as some seem to think. After three years of expansion, jitters are not surprising at this stage. But upon rechecking...and weighing the risks that must be monitored... we've concluded that '86 probably will be a little better than this year.

We expect growth of 3% to 3½% as measured by gross nat'l product, total output of goods & services. Compares with about 2½% for this year. GNP is picking up now and we think this strength will carry through '86. Slightly slower in the first half, a little faster next summer and fall.

Inflation will quicken somewhat...consumer prices climbing 4½%, only 3½% this year. Nudged up as the dollar slips and business expands.

Profit gains will be modest...nothing spectacular, but improving from this year's slump. Tight management and cost-cutting will pay off. And imports won't be quite as competitive, allowing wider profit margins.

Unemployment won't change much...will hold at 7% or a hair less.

Lower interest rates will play a big part in sustaining business. They'll slip a bit more from present levels...then inch up after midyear as business strengthens. Prime down to 8½% by spring, then rising to 9%. Home mortgages will fall to 11% or even less, settling there for a time. T-bills, down to 6½%, then up to 7%. T-bonds, hovering at 9% to 9½%.

Exports should boost the economy also...a significant turnaround. With a softer dollar, U.S. farms and factories will be more competitive both here and abroad...giving a real lift to their sales and production. Evidence of a shrinking export-import gap will be clear by next summer.

Lean inventories will be a plus...they'll require replenishing.

Retail sales will be so-so, gaining around 3% after inflation... exclusive of autos, which will be down. Consumers are loaded with debt, will pull back some to work down the burden...loosen up after mid-1986.

Merchants will counter with lots of sales...price cuts the rule. They will make sure inventories don't pile up...order at the last minute. And delay paying bills as long as they can, putting a squeeze on vendors.

Home building will remain healthy...number of new units started will nearly match the '85 total. Most emphasis on single-family homes. Too much multifamily housing in many cities, so builders will ease up.

Gov't buying will spur business too, despite the deficit-cutting.

Plant & equipment spending will add less oomph than this year. Companies are worried about taxes. And have ample production capacity.

Agriculture, a very weak spot, with little improvement in sight. Another year, maybe two, before farm economy and land prices hit bottom.

On balance, the favorable factors have a slight edge for 1986. A year for strengthening your firm's financial base...and tight managing.

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Car sales will drop next year after a boomy '85...to 10½ million from nearly 11 million. Domestics will bear the loss, imports will gain.

More imports are coming from more countries in next few years.

Korea, Brazil, Mexico, Taiwan and Spain will add to domination of small-car market by foreigners. Over 40% of ALL sales will be taken by imports in 1990...up from 25% today. Means fewer manufacturing jobs for Americans, although Japanese and Koreans will build some plants here.

Cars will be more expensive to fix...costly diagnostic equipment becoming a necessity to repair late models. Some parts are hard to reach because of down-sizing, so more time has to be spent getting at problems.

But routine maintenance will be easier in future cars...filters, spark plugs, etc., simpler to replace. Good news for do-it-yourselfers.

Superchargers will be making a comeback in a few sporty cars. Ford will have one in two years. Fast power, but drain on the gas tank.

Risks of doing business overseas will shift to new areas in '86.

Potential trouble spots include South Korea, Turkey and Egypt... so say experts who study these things. Oil glut hits OPEC big spenders like Saudi Arabia, which also must worry about religious fundamentalism.

Ongoing trouble in the Philippines, but a united opposition slate has a chance to end Marcos' rule...presses him for reforms in any case. Still, there'll be no easy fix. Major U.S. bases will remain vulnerable.

Brazil, Argentina and Venezuela look better...greater stability.

Iran-Iraq war won't be settled anytime soon. Few countries care about the conflict, and those that do would just as soon see it continue. Fighting one another keeps the two from troubling their other neighbors, cuts competitive oil production and provides markets for arms merchants.

New rules coming from health agencies...Food and Drug Adm., Consumer Product Safety Commission, Occupational Safety & Health Adm.

Will reduce the use of a common solvent...methylene chloride. A possible carcinogen, will be taken out of hair and paint sprays... used less in paint strippers. But still a trace in decaffeinated coffee.

Stiffer regulation of asbestos & ethylene dibromide from OSHA. Aim is to cut chances of workers getting cancers from too much exposure. Separate standards on asbestos for construction and industrial workers.

Employers are stressing health more too...to keep workers fit and productive. Plenty of money being spent on health clubs & equipment.

Big benefits need not cost a bundle. They can come from programs to help workers stop smoking and control drinking, more healthful foods in company cafeterias and mandatory seat-belt use in company vehicles.

No speedy sale of Conrail next year. Congress will drag it out.

Increases chances for a public sale, which Conrail would prefer. That would avoid antitrust problems posed by a sale to another railroad. Much depends on Conrail profits and its ability to repay federal loans.

Reagan effort to curb steel imports is a flop. Lax enforcement and loopholes mean foreign steel will grab 23% of our market next year. That's nearly 5% higher than the White House promised over a year ago. Europe and third world producers have hiked exports, not Japan this time.

Congress will squawk, but even U.S. steelmakers aren't agreeing on what should be done. Doesn't help the chances for import legislation.

Federal Trade Comm. has had it with gypsters who merely pay fines after losing FTC cases...then start over with phony new consumer frauds. So the agency will ask for jail terms when it files future fraud charges. Should reduce scams involving jewelry, diamonds, oil & gas leases, etc.

Simpler arbitration rules for warranties are on tap at the FTC. Few firms now agree to such a solution because procedures are cumbersome. FTC will call a conference to draft guidelines for more workable rules... hopes arbitration will be used more widely to settle consumer complaints.

And the agency will try to make ATTEMPTED price-fixing a crime... even if the would-be fixer fails to persuade his competitors to go along.

Credit unions will keep on growing strongly...adding new members, expanding through mergers to get benefits of modern banking technology.

Competing with banks...credit and debit cards, automated tellers, NOW accounts, discount stockbrokering, mortgage loans and other services beyond their traditional personal loans, auto loans and savings accounts.

Many pay high rates on savings, charge low rates on credit cards.

They're in good financial shape...with a healthy insurance fund. But they face competition from retail giants invading financial services.

New devices to help the handicapped will soon reach the market:

Robotic arm, near $10,000, ready in '86. Can be used for eating, turning pages, picking up a phone...activated by fingers or a chin lever. Future models will be able to do more, even responding to voice commands.

For some persons who can't walk...electrodes to stimulate muscles in paralyzed legs so they can take steps. Controlled by a belt computer. On the market in a year or two. Later, electrodes for paralyzed hands.

For the deaf, implants to pick up words...not muffled sounds.

And for the blind, radio pathfinder systems being investigated.

Major medical advances using laser surgery. Experiments going on with "photoradiation" to treat some large cancers that are easy to reach. Chemical helps laser zero in on cancer cells...leaves normal cells alone.

Also lasers to weld tissues...blood vessels, nerves and tendons. Lasers for cosmetic surgery becoming common...to remove birthmarks, etc.

The in-shape look will triumph. No fun for the flabby.

That's the fashion news for '86. You decide if it's good or bad.

New clothing styles will show off shapely bodies...men and women. Fitted to the silhouette...no billows or bagginess to hide the bulges. For men, broad shoulders and tapered jackets. Women, molded to the form.

A mix of formal and informal apparel. Patterned sports jackets and fancy slacks for men. More skirts, blouses and dresses for women. Execs won't feel they must wear suits to look as if they mean business.

Tuxedos and formal gowns will be in demand...return to tradition.

Fancy fragrances for men & women are hot, not just for Christmas. New, expensive items...average sale $30 to $50...sales up by about 10%. Cheaper whiffs for the mass market won't do as well...buyers want class.

Sales of sunglasses are booming year round. Mostly imports. They're inexpensive, so flashy dressers can buy a pair for each outfit.

Halley's comet fans jam phone lines at U.S. Naval Observatory. Now it should be easier to get through to a 4½-minute taped message... tips on comet watching. Dial 900-410-USNO. The phone charge is $1.90.

GE-RCA: The merger is indicative of what is going on all over in American business...a quest for leadership in technology and services, a constant reshuffling, restructuring to compete better in world markets.

Part of a resurgence of our major industries. A new resiliency. We see it happening in companies large and small...prodded by competition from overseas...managers willing to invest more for LONG-term results. Pouring money into R&D, computer systems, telecommunications, robotics.

We'll be sending you a special Letter on this in a few weeks.

In state legislatures, business matters on 1986 calendars:

Insurance...a search for ways to improve availability, cut costs of business coverages. Caps on damage awards, contingency fees, etc.

Banking...letting out-of-state banks operate within their borders and removing barriers that keep banks out of many commercial activities.

Spending and taxes...budgets will be lean, few tax cuts OR hikes.

Workers' compensation...higher employer costs are the prospect from rewriting state laws, especially in area of occupational diseases.

Telecommunications...measures to spur competition in many states could benefit high-volume telephone users but raise rates for others.

Toxic waste...top issue in many states. Bottom line for business is higher costs, even for smalls such as dry cleaners and gas stations.

Health care...promoting greater competition to help lower costs.

Important labor-management issues will be decided soon by NLRB... National Labor Relations Bd., which has a pro-business tilt under Reagan:

Temporary hires for locked-out union workers...how much leeway?

Nonunion temporaries...can an employer fire them for refusing to cross a union picket line barring the way to a customer's premises?

Handbills...can unions use them in shopping centers when fuss is with one tenant? Can the contents of union handbills be limited?

Natural gas...Congress may ease the rules a bit on burning it to generate electricity and in heavy industry if gas remains plentiful. Won't be enough to keep prices from falling or to absorb excess supplies.

U.S.-Soviet joint research into fusion energy is a safe venture. Scientific & technological breakthroughs are decades away, capital costs of fusion are high and application of fusion tech to weapons seems nil.

For year-end tax planning, a couple of reminders:

Gifts to charity...checks mailed in '85 count as '85 deductions for income tax purposes. Doesn't matter when charities deposit them.

Checks to relatives, etc...count as '85 gifts if cashed in '85. Make sure the checks are deposited to get gift tax exclusion this year.

Prospects for tax revision affect long-term planning, of course. No matter what the House does in next few days, there will be a tax bill passed by Congress in 1986. And it will mean tax increases for business.

No way deficits can be cut without tax hikes. Better plan on it. Revenue-raising parts of tax reform will be picked up in new legislation if Reagan fails to marshal enough troops to get it through the House now.

Yours very truly,
Austin Kiplinger
THE KIPLINGER WASHINGTON EDITORS

Dec. 13, 1985

THE KIPLINGER WASHINGTON LETTER—(ISSN 0023-1770)
SUBSCRIPTION RATES $48-ONE YEAR $80-TWO YEARS $118-THREE YEARS $162-FIVE YEARS
SECOND-CLASS POSTAGE PAID AT WASHINGTON, D.C.

February 2, 1986

I. US economy perking up.

A. Manufacturing sector, battered by cheap imports, revving up.
B. Consumer demand remained strong despite record hh debt.
C. Employment surging.

II. Strong drive has changed outlook for interest rates.

A. Fed no longer needs to easy monetary policy, therefore
B. The markets have lost any incentive to push interest rates down more.

III. Rates will remain stable for a few months and then probably up.

IV. Several factors have caused turnaround

A. Boom in stock and bond markets has generated a great deal of wealth.
B. Consumers, while indebted, remain in a buying mood.
C. US industry making a comeback.
D. Inventory adjustment behind us. Firms will start building anew.

V. Gramm-Rudman suggests that the Fed should ease to make up for the shortfall in budget stimulus. But seems unnecessary now.

EPIC

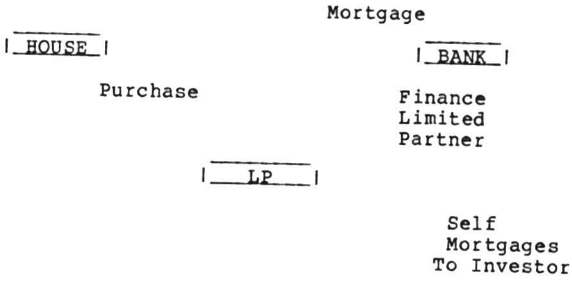
1975 -

EPIC arrange limited partnerships to purchase model homes from developers and leftover homes builders couldn't sell.

Partnerships financed the house by securing mortgages.

EPIC pooled mortgages and resold as mortgage backed securities.

Partners - tax benefits
Builders - sold for cash
EPIC - got fees


Mortgage
HOUSE
BANK
Purchase
Finance
Limited
Partner
LP
Self
Mortgages
To Investor

When L.P. mature, must sell house to pay out Mortgage, but house values declined - NO CASH. Also since negative carry, requirement that cash be diverted from new partnerships.

FHA

Jan. 28, 1986

OMB Proposed Sale FHA

OMB proposal to sell FHA to private investors by 1989.

MBA: ridiculous

Why:

1. Reduce amount of credit available for housing and the availability of mortgages with 5% down payments, which are especially important to 1st time home buyers.

2. Jeopardize operations of Ginnie May, which guarantees securities backed by FHA and VA mortgages.

3. Doubtful that consortium of private mortgage insures, alone or in tandem with others would have financial resources to buy FHA or could provide same volume and quality of mortgage insurance that the FHA now provides. PMI industry not strong enough to undertake such an obligation.

OMB fiscal requirements for FHA (proposed for 1987):

1. FHA mortgage insurance premium increase from 3.8% to 5%.

2. premium must be paid in cash and not included in mortgage amount.

3. All FHA borrowers have annual income at least 40M.

a. Currently, 70% fha loans going to household less than 40M.
b. 26% less than $27M

4. Top 20% of Ginnie Mae security would have to be backed by a private entity, and only the remaining 80 percent would carry a federal guarantee.

5. Fee on FNMA mortgage-backed securities would be five basis points in 87 and 10 basis points in 1988. Fees for other mortgage backed securities.

MBA EVP Lasko said that the fees, if adopted by Congress, would shut down the secondary mortgage market.

Lill.

December 13, 1985

FSLIC - Peter Sterns story

Aug 1984 - industry in turmoil

FSLIC - diminishing resources
FHLBB - Ed Gray - penchant for centralized authority
Congenial rship between bb and industry

BB - oversees 3200 institutions including fed chartered thrifts and state-chartered thrifts with fslic insurance

Sterns wall street background did not prepare him for regulation of West Coast-dominated industry that had traditionally enjoyed a collegial r ship with regulators. Nor did his training prepare him for maneuvers required in dealing with idy and its lobby, the US League of Savings Institutions.

BB chairman is also chmn of fslic.

Management consignment program. Day to day management duties of ailing thrifts are taken over by strong thrifts while long term solutions are put together. 23 now in place. Fslic staff bypassed in creation of this program and are skeptical of its work ability. Created by FHLBB in San Fran on whose board sits the captains of the SB idy there. FSLic ordered outside consultants to evaluate the process and BB later rescinded. Much mistrust.

FSLIC bypassed in other ways. Not much inptu into formulation of Federal Asset Dispositon Assn. Major player there also FHLBB San Francisco.

William O'Connell - pres. US League of Savings Institutions

Issue: is the fund large enough? Gray has pushed for increased premiums, but the strong League lobby says that FSLIC's strong cashflow can allow time for probs to be solved sans recap of fund. An additional set - aside premium could weaken strong thrifts and put others out of business.

Idy leaders believe that Fed Asset Disposition Assn and the management consignment program will enable fund to hold out until conditions in the industry and economy improve.

Do caretaker managements only postpone day of reckoning? D'apres Sterns says thrifts now in mgt consgnmt program will need 1 to 1.2 billion in capital in next 6 months.

Main prob is asset quality - not spreads, gaps etc. Fraud in 1/3 of the s and l's related to asset quality.

DEC. 13, 1985

S and L Regulation

Regulator's recent moves to stabilize troubled thrifts set double standard. Help to push up idy cost of funds.

Some district offices of FHLBB have been telling some troubled thrifts to curb interest rates and put brakes on too rapid growth and "risky lending."

Yet, many of highest rates available in US are at institutions declared insolvent and taken over by regulators. Regulators say they are trying to get the banks solvent again and then they will lower the rates. The good thrifts say that these activities are putting upward pressure on rates.

Dec. 13, 1985

Faulty Appraisals cause for S and L losses

Faulty appraisals justified billions in troubled re loans on books of federally insured banks and thrifts. Congressional investigation shows bank regulators have been slow to address problem.

Cause for insolvency of 322 thrifts.

Fhlbb found evidence of bad appraisals in 848 banks, or 25% of federally insured institutions.

FDIC bought $400MM in prob real estate d=from ~Continental Illinois appraised at $518MM but revalued for 184.4MM or 36% of orig value.

Bad appraisals will account for 40% of VA loan guaranty program losses of $300Mmm to $400mm.

G

Housing Prices

Housing Market

High potential demand over next 20 years due to low level of housing starts relative to Bally Boom household formations in early 80's.

Houses too costly late 70's, early 80's.

Study: Median price for home is $75,000

Forty-six metropolitan areas are listed in the U.S. League of Savings Institutions' study of median-home sale prices released Wednesday. USA median price: $75,000. Here's a look at the 46 metro areas, 1985 median sales prices and median monthly housing expenses: **(Related stories, 1A, 1B)**

City	Price	Expense
Akron, Ohio	$56,000	$624
Albuquerque, N.M.	$83,500	$796
Anaheim-Santa Ana-Garden Grove, Calif.	$122,000	$1,133
Atlanta	$87,250	$821
Baltimore	$75,157	$790
Bloomington-Normal, Ill.	$55,900	$668
Boston	$126,000	$1,166
Bremerton, Wash.	$83,500	$853
Chicago	$87,000	$882
Cincinnati	$55,300	$626
Cleveland	$62,500	$704
Dallas-Fort Worth, Texas	$94,750	$965
Danbury, Conn.	$95,950	$954
Dayton, Ohio	$54,750	$619
Detroit	$61,000	$783
Washington, D.C.	$105,000	$1,000
Fort Lauderdale-Hollywood, Fla.	$74,900	$739
Gary-Hammond-East Chicago, Ind.	$62,000	$701
Greensboro-Winston-Salem-High Point, N.C.	$68,625	$661
Harrisburg, Pa.	$67,200	$732
Houston	$88,350	$986
Kansas City, Mo.-Kansas City, Kan.	$62,250	$726
Lansing, Mich.	$58,500	$739
Los Angeles-Long Beach	$123,000	$1,206
Miami, Fla.	$82,400	$863
Milwaukee	$69,750	$778
Nashua, N.H.	$82,000	$891
Nashville-Davidson, Tenn.	$69,000	$688
Newark, N.J.	$116,000	$1,139
New Orleans	$90,500	$858
New York	$129,700	$1,141
Oklahoma City	$80,500	$777
Orlando, Fla.	$58,200	$604
Philadelphia	$69,450	$733
Pittsburgh	$54,152	$673
Portland, Ore.	$69,900	$739
Raleigh-Durham, N.C.	$73,825	$802
Reading, Pa.	$56,000	$621
Rochester, N.Y.	$66,000	$699
St. Louis	$67,000	$702
Salt Lake City-Ogden, Utah	$66,000	$706
San Diego	$120,750	$1,164
San Francisco	$152,000	$1,370
Tampa-St. Petersburg, Fla.	$63,750	$545
Trenton, N.J.	$66,000	$703
West Palm Beach, Fla.	$69,900	$765

Source: League of Savings Institutions

Product Description

Interstate Banking

Inflation

- $ rebound
- Oil price ↓ } outlook good
- Farm price ↓

SAVINGS BANK STGY

S.B Probs
- .Low rate Fixed rate loans
- .Competition for deposits, non banks etc
- . high losses, bad publicity

Now what
- niche
- multiservice } ?

Choices – trusts
stockbroking
family financial plng
insurance

Wash Fed went "niche"; chose RE
- . immediate profit opportunity
- . knew mortgages as SB

Step 1. – JV Mortgage co with Columbia First Federal. Offers eq. steps to other S+L's

Products; 1sts, 2nds, construc, commercial RE, equity line lndg and R-E synd.

Interest rate risk control
asset and liAB Mgt.

Step 2. – Hire right people

Jupiter

LIABILITIES

MARKET - MID-ATLANTIC

Mortgage Regulation

MORTGAGE AND CONSUMER BANKING NETWORK

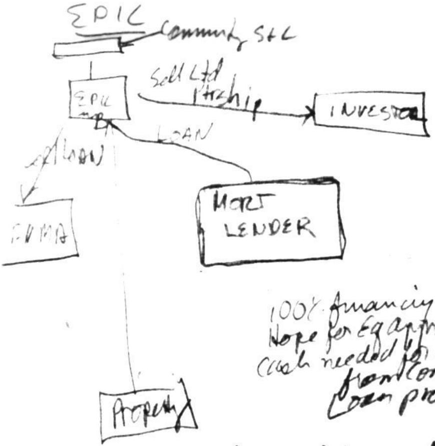
KEY ISSUES

- BUILDING UPON CURRENT POSITIVE MOMENTUM
- PRUDENT LENDING PARAMETERS
- "SALEABLE" MORTGAGES
- DISTRIBUTION AND TECHNOLOGY PLAN
- PROCESSING DISCIPLINE
- INSURANCE TURNAROUND
- RELATIONSHIP MANAGEMENT ROLLOUT
- RELOCATION BUSINESS STARTUP
- CUSTOMER SERVICE PROGRAM
- SECOND MORTGAGE BUSINESS STRATEGY
- INDUSTRIAL BANK STRATEGY

MORTGAGE

Deficit

One reason that the deficit has not caused rates to skyrocket is the large amt. of Japanese capital inflows.


EPIC
Community S&L
EPIC
Sell Ltd Ptship
INVESTOR
LOAN
1st LOAN
FNMA
MORT LENDER
Property

100% financing
Hope for Eq appreciate
Cash needed for Op losses
from Community or
Loan proceeds.

Typical of Single family Syndications
You can't get enough cash from limited partnership and from rent on houses to pay operating losses and purchase price ∴ milk the lenders
Partner/investor/Mortgagor bets on appreciation.

Most Syndications go Office or appartment where rentals exceed costs

Lenders + PMI also at risk

Deal designed to lose money over life of partnership with ultimate bailout by appreciating value of home

Cash Flow prob. Ponzi – Paying out more than taking in.

Market Trends [illegible]

- Shift to FHA / VA

Sept 9

IMPACT FNMA Guidelines

- disqualify xxx new homebuyer.
- Intensification of appraisal reviews force ~~home buyers~~ to lenders to repurchase more mortgages than planned
- Differing stds FNMA / FHLMC force more testing in more markets

↳ Congress happy

↳ Mortgage insurers happy.

Housing starts falling despite lower [illegible] rates.

°o. Prognosis for housing:
Belt tight
Why - Econ Malaise and Tighter Credit standards

No Buydowns
3,5 yr and graduated pmt mortgages

Retain 2+5 CAPs

only 90% LTV - No more 5% Downs

Non OOP + Creative financing are trouble spots.

Income at 25-33 down from 28-36

No Buydowns

But Freddie Mack Still
- 5% DP
- uncapped to 5 years

How will appraisers adapt?

S&P - Long Term Concern

- Investors more careful about insurers
- S+P, Moody Mort Ins. Rating down-t.
- More pressure to limit fluid involvement in R.E.
- More pressure against securitizing ~~&~~ category or limited partnership loans
- Limited partnerships w/ cash flow deficits hard to sell.

MBS Market 300 Bn
Privately Insured Conventional Mortgage Pool market 37 Bn

FNMA also doubled the # of appraisal reviews.

EPIC

deficit
High LTV
50% Texas

- Missionary Work
- Perfecting of Saints
- Work for Dead

[illegible]

- Family Lead [illegible]
- Harrisburg offic

FHA Program

Amt Financed - Lower of Statutory dollar limit or appropriate LTV

Term - 30 years or 3/4 remaining econ life of property.

Rate - HUD determined

Fee - Not to exceed 1% or 16

Ratios - Various - depend on New/old/const
Vet or Not

Capacity - Housing Exp not to Exceed 35% of net

VA

ARM - 1,3,5

- To 500
- Adj period 1,3,5
- Term 180-360
- annual Cap 2% on 1 and 3; 3% on 5
- lifetime Cap 15%
- RMO TBill Float (FNMA)
- Margin 220 - 250 over Rate
- 33/38 Ratios No Shortfall
  28/36 w Shortfall
  Higher LTV then Lower Ratios of 25/33

DURATION

critic: Duration is a measure of the elasticity of asset and liability values with respect to yield changes only if these yield changes are quite small and only if all yields change by the same amounts (short + long)

Solve? - Duration Vector provides more complete immunization for yeild changes that are both large and non parallel (short rates increasing more or less than long rates).

RE Market.

- Three circumstances won't affect today's RE market as in past
- Income produc prop mkt no longer cyclical
- No pent up demand to ~~[illegible]~~ eliminate current saturation

No return to inflation

- Capital for invest (RE) remain abundant
- Builder put reserves in projects knowing already overbuilt so no ~~[illegible]~~ shortage of supply

HOUSING STARTS

July 2.4% decline to 1.65MM Rate
But should get better:
- Backlog permits rising

MI

Losses mounting. 50% greater: '85 than '84.
Close to $700MM.

Higher premiums

EPIC will default on $1.4BN (Loss potential $394)

Much of MI losses on greater than 95% LTV

EPIC Silver Lining:

- Unlikely that MI losses will reach industry max exposure
- 3 year to solve EPIC claims
- EPIC could be bailed out by outside investor
- Long time to pay out claims (spread)

Total losses still only 18% of capital of MLI Co.

FNMA

Stricter underwriting --

- 25/33 for >90
- Seller contribution 3% on 90%; 6%<90; 0% on >90%
- Co-borrowers must occupy and take title.

WE underwrite PMI

Four basic changes in marketplace:

- Many lenders precede FNMA moves
- Appraisal process hightening
- Kick-outs (approved loans, but later rejected due to PMI refuse) on the rise.
- Lenders moving away from high LTV

WG&L Real Estate *Outlook*

Winter issue, 12/85

- The maximum monthly housing expense cannot exceed 25 percent of the home buyer's gross monthly income, reduced from the previous figure of 28 percent.
- Housing expense plus all the other installment debt cannot exceed 33 percent of gross monthly income, reduced from 36 percent.
- The amount of a seller's contributions cannot exceed 6 percent on a 90 percent conventional mortgage or 3 three percent on a 95 percent fixed-rate mortgage. No seller's contributions are allowed on a 95 percent adjustable-rate mortgage (ARM).
- Negative amortization mortgages and graduated-payment mortgages will no longer be allowed.
- ARMs without ceilings to protect against increases in the interest rate have been eliminated.

"These stricter requirements mean increased protection for low-equity home buyers. They are less likely to qualify for mortgages that may create major financial problems," Pappas concludes.

WG&L

1985 MID-ATLANTIC REGION MARKET SIZE

	EXISTING HOME SALES (000)						
	POTENTIAL		MSAs COVERED*		ORIGINATIONS		
REGIONS	UNITS	%	UNITS	%	$, MM	%	
NORTH	203	34	116	41.4	5,307	25	<---
CENTRAL	184	31	115	41.1	10,842	51	
SOUTH	210	35	49	17.5	5,125	24	<---
TOTALS	597	100%	280	100%	21,274	100%	
% OF USA	19%		9.4%		9.5%		<---
USA	3,142		2,982		217,523		

* Existing one family home sales

MID-ATLANTIC EXISTING HOME SALES
REGIONS BY STATE (IN THOUSAND UNITS) 1985

	MID-ATLANTIC REGION		REGIONS					
			NORTH		CENTRAL		SOUTH	
	%	UNITS	%	UNITS	%	UNITS	%	UNITS)
DELAWARE	1.7	10.0	1.7	10				
DIST. OF COL	1.3	7.8			1.3	7.8		
GEORGIA	10.1	60.1					10.1	60.1
MARYLAND	11.2	66.8	11.2	66.8				
N. CAROLINA	17.3	103.2					17.3	103.2
PENNSYLVANIA	28.5	170.4	28.5	170.4				
S. CAROLINA	7.7	46.0					7.7	46.0
VIRGINIA	16.4	98.1			16.4	98.1		
W. VIRGINIA	5.8	34.6			5.8	34.6		
TOTALS	100.0%	597	41.4%	247.2	23.5%	140.5	35.4%	209.3

NOTE:

MID-ATLANTIC REGION %	19% of USA

1983 NATIONWIDE HOME BUYER SEGMENTS PROFILES

		1ST TIMER		REPURCHASER	LONG DISTANCE	
	NATIONWIDE	FHA	UNMARRIED	CONVENTIONAL	RELOCATOR	
A. WHO THEY ARE						
-MEDIAN AGE (YRS.)	34 yrs	29 yrs	33 yrs	38 yrs	44 yrs	<---
-UNMARRIED (%)	26%	35%	100%	19%	12%	
-MEDIAN INCOME ($,000)	36	30	30	41	49	<---
-1ST TIMERS (%)	40	100	56	0	16	<---
B. WHAT THEY BOUGHT						
-OVER 25 YRS OLD (%)	34	46	40	26	DK	
-PURCHASE PRICE (%,000)	65	55	57	69	90	
-SIZE (SQ.FT,00)	14.5	12	13	16	DK	
C. HOW THEY AFFORDED						
-LESS THAN 20% DOWN	55%	70	60	45	DK	<---

o 1ST TIMER AND UNMARRIED - YOUNGER, LESS FINANCIALLY STABLE AND SMALL HOME AND VALUE

o REPURCHASER AND RELOCATOR - STABLE, BIGGER HOMES AND VALUE, HIGHER EQUITY

DK = Don't Know

PORTFOLIO/REPURCHASER MARKETS

	D.C.	ATLANTA	CHARLOTTE	REPURCHASER CONVENTIONAL
A. WHO THEY ARE				
-MEDIAN INCOME ($,000)	55	42	47 <---	41
-1ST TIME BUYER (%)	28	26	28 <---	0
B. WHAT THEY BUY				
-25 YRS OR OLDER	24	15	36	26
-MEDIAN PRICE ($,000)	121	81	92 <---	75
C. HOW THEY AFFORDED				
-10% OR LESS DOWN	31	31	25	18

- o HIGHER INCOME AND HOME PRICES
- o LOWER PERCENTAGE OF 1ST TIME BUYERS
- o CONVENTIONAL LOANS, JUMBO LOAN MARKETS

NEW HOMES-BUILDER MARKETS

	D.C.	RICHMOND	ATLANTA	NATIONWIDE
B. WHAT THEY BUY				
NEW HOMES (%)	42	36	40 <—	19
MEDIAN PRICE ($,000)	121	75	81 <—	65
C. HOW THEY AFFORDED				
10% OR LESS DOWN (%)	31	20	31 <—	27

- HIGHEST PERCENTAGE OF NEW HOMES
- STRONG MEDIAN PRICES

LOW DOWN PAYMENT/FHA MARKETS

	COLUMBIA	BALTIMORE		FHA BUYER
A. WHO THEY ARE				
MEDIAN INCOME ($,000)	43	37	<---	30
1ST TIME BUYER (%)	39	52	<---	66
B. WHAT THEY BUY				
MEDIAN PRICE	73	64	<---	56
C. HOW THEY AFFORDED				
10% OR LESS DOWN (%)	53	43	<---	64

- LOWER MEDIAN INCOME
- HIGHEST PERCENTAGE OF 1ST TIME BUYERS
- LOWEST DOWN PAYMENT

PASS-THRU 1ST TIME BUYER MARKET

	PHILADELPHIA	PITTSBURGH	RALEIGH		FIRST TIME
A. WHO THEY ARE					
MEDIAN INCOME ($,000)	40	34	34	<---	30
1ST TIME BUYER (%)	52	53	46	<---	100
B. WHAT THEY BUY					
MEDIAN PRICE ($,000)	70	56	63	<---	55
C. HOW THEY AFFORDED					
10% OR LESS DOWN (%)	28	21	23	<---	39

- LOWER MEDIAN INCOME
- AVERAGE MEDIAN PRICE

MID-ATLANTIC & REGIONS BY MSAs

EXISTING HOME SALES AND ORIGINATIONS

AREA	YEAR	EXISTING ONE FAMILY HOME SALES		ORIGINATION					
				TOTAL		NEW		EXISTING	
		UNITS,000	%	$,MM	%	$,MM	%	$,MM	%
TOTAL NATIONWIDE	85	2,982	—	224,000	--	60,414	—	163,623	--
	86	2,840	—	217,523	--	58,962	--	158,562	--
MID-ATLANTIC (% of total USA)	85	279.1	9.4	21,274	9.5	7,287	12.1	13,984	8.5
	86	317.5	11.2	27,371	12.6	7,009	11.9	20,363	12.8
REGIONS (% of Mid-Atlantic)									
NORTH	85	115.5	41.4	5,307	25.0	1,297	17.8	4,008	28.7
	86	117.9	36.4	6,525	24.0	1,215	17.3	5,309	26.1
CENTRAL	85	114.5	41.0	10,842	51.0	3,408	46.8	7,434	53.2
	86	144.2	45.4	14,992	55.0	3,489	49.8	11,504	56.5
SOUTH	85	49.1	17.6	5,125	24.1	2,582	35.4	2,542	18.2
	86	55.4	17.4	5,854	21.4	2,305	32.9	3,550	17.4

NORTH REGION BY MSA
HOUSING AND ORIGINATION STATISTICS

								MEDIAN	
		EXISTING		ORIGINATION		HOUSE STOCK		HOUSE PRICE	
		HOME SALES		($000,000)		(UNITS,000)		($000)	
MSAs	YEAR	(UNITS,000)	TOTAL	NEW	EXISTING	SINGLE	MULTI	NEW	EXISTING
BALTIMORE									
	'85	26.5	1,603	590	1,012	584	217	70	71
	'86	28.9	1,852	487	1,364	589	220	74	74
PHILADELPHIA									
	'85	63	2,722	552	2,169	1,125	471	72	61
	'86	63	3,413	560	2,853	1,121	490	80	67
PITTSBURG									
	'85	26	982	155	827	632	222	67	57
	'86	26	1,260	168	1,092	631	231	74	62
NORTH TOTALS									
	'85	115.5	5,307	1,297	4,008	2,341	910	—	—
	'86	117.9	6,525	1,215	5,309	2,341	941	—	—
USA									
	'85	2,962	224,000	60,414	163,623	—	—	83	74
	'86	2,840	217,523	58,962	158,562	—	—	86	78

CENTRAL REGION BY MSA
HOUSING AND ORIGINATION STATISTICS

MSAs	YEAR	EXISTING HOME SALES (UNITS,000)	ORIGINATION ($000,000) TOTAL	ORIGINATION ($000,000) NEW	ORIGINATION ($000,000) EXISTING	HOUSE STOCK (UNITS,000) SINGLE	HOUSE STOCK (UNITS,000) MULTI	MEDIAN HOUSE PRICE ($000) NEW	MEDIAN HOUSE PRICE ($000) EXISTING
D.C.	'85	79.3	7,476	2,355	5,121	788	566	119	109
	'86	106.8	10,894	2,430	8,464	806	580	128	115
RICHMOND									
	'85	13	1,282	404	878	175	66	90	109
	'86	14	1,590	418	1,173	178	68	95	113
NEWPORT NEWS, HAMPTON	'85	4.5	350	55	295	86.7	31	87	105
	'86	4.7	453	72	381	86.5	31.5	91	109
NORFOLK,VA BEACH, PORTSMOUTH	'85	17.7	1,734	594	1,140	188	104	88	103
	'86	18.7	2,055	569	1,486	194	108	90	107
CENTRAL TOTALS									
	'85	114.5	10,842	3,408	7,434	1,238	767	—	—
	'86	144.2	14,992	3,489	11,504	1,265	788	—	—
USA									
	'85	2,982	224,000	60,414	163,623	—	—	83	74
	'86	2,840	217,523	58,962	158,562	—	—	88	78

SOUTH REGION BY MSA
HOUSING AND ORIGINATION STATISTICS

MSAs	YEAR	EXISTING HOME SALES (UNITS,000)	ORIGINATION ($000,000) TOTAL	NEW	EXISTING	HOUSE STOCK (UNITS,000) SINGLE	MULTI	MEDIAN HOUSE PRICE ($000) NEW	EXISTING
ATLANTA									
	'85	19.7	2,915	1,769	1,146	541	316	91	92
	'86	24.9	3,390	1,598	1,792	555	329	98	97
CHARLOTTE-GASTONIA	'85	11.4	847	292	554	152	54	69	81
	'86	11.8	958	264	694	154	57	71	83
RALEIGH/DURHAM									
	'85	12.9	1,016	376	640	153	77	70	83
	'86	13.6	1,150	334	816	158	80	73	85
COLUMBIA									
	'85	5.1	347	145	202	78	24	60	70
	'86	5.1	356	109	248	79	25	62	72
SOUTH TOTAL									
	'85	49.1	5,125	2,582	2,542	924	471	—	—
	'86	55.4	5,854	2,305	3,550	946	491	—	—
USA									
	'85	2,882	224,000	60,414	163,623	—	—	83	74
	'86	2,840	217,523	58,962	158,562	—	—	88	78

January 29, 1986

Va Supreme Court ruled that a lender cannot evade the state's small loan act by making a loan in the form of a real estate mortgage. Borrowers of loans that fit within the ceiling of the Consumer Finance Act will be entitled to its statutory protections regardless of whether the loans are characterized as mortgages, the court ruled, as long as the loans are made by persons in the business of making loans below the ceiling amount.

A borrower of a small sum of money should not be allowed to put his one substantial asset - his home - at risk. The Act's ban on "additional charges" usually associated with mortgages, and which were applied to both the loans in question, indicates further the legislature's intent that all loans below the ceiling amount should be considered small loans.

Network - Key issues

September 2, 1986

NOTES:

Aggregate balances at Savings institutions declining. People investing in Ginnie Maes and bonds. If interest rates increase, these will prove to be poor investments. Investment in a CD is a better consumer protection risk.

Appraisal, credit check, and title search cause for logjam in processing Mortgage applications. Refi the cause. Refis are 3 times 1985. Savings Industry will account for $233 billion in refinanced and residential purchase loans.

CAPITAL ADEQUACY

Much regulatory pressure on S and L's. The industry is more profitable, but will continuing pressure to increase capital, and change accounting practices render industry impotent?

FHLBB says more capital is required to insure viability of insured institutions and shield the FSLIC from excessive losses. More capital will also force ownership to be more vigilent. FHLBB wants to increase from 3% to 6% over six years.

But add to this the special assessment: 1/32 of 1% of insured deposits each quarter; massive mortgage refinancings have set back institutions' effort to restructure their portfolios eg. move to fixed from variable. FHLBB restrictions on growth. Potential changes in accounting standards.

HOUSING MARKET

2 million units in 1986. Mortgage originations headed toward a new all-time high, and the interest rates available on most new mortgages have made the median-cost home affordable for a family with an average income and a 25% down-payment.

Compare with 1982: Market at 1 MM units and 15% rates; widening gap between the price of a median cost home and what prospective first time home buyers could afford to pay.

ACCOUNTING FEES

Proposal would require origination income to be recognized over loan life. Loan origination costs, however, would have to be recognized as current expenses.

Current practice: Take up to 1% of loans's initial balance as current income so long as the fee can be offset by an origination expense. Change in this could carve $4 billion in revenue from the bottom lines of s and l's in next six years.

C

Regop No Frills Checking

Personnel Delegations

Pricing

Product - OEHE

PMI

DELEGATION OF APPROVAL AUTHORITY FOR PERSONNEL PROGRAMS

SALARY PROGRAMS	Sector Executive/ Personnel Planning Committee	Group Executive	Division Head
o Administration			
o N.Y. Core Program Structure	Final Approval	-	-
o Non-N.Y. Program Structure	-	Final Approval	-
o Salary Adjustments to and over $140,000 and all 2-downs From Sector Executive	Final Approval	-	-
o Hires/Titles/Salary Adjustments at $100,000 to $139,999; and all 2-downs from Group Executive	-	Final Approval	-
o Hires/Titles/Salary Adjustments below $100,000 (except 2-downs from Group Executive)	-	-	Final Approval ||
JOB EVALUATION			
o W level and higher	Final Approval	-	-
o Below W level	-	-	Final Approval
BONUS PROGRAMS			
o CORE Nominations and Awards	Final Approval	-	-
o Individual Performance Award (IPA)			
o Funding:			
o Within approved IPA plans	-	Final Approval	-
o Outside of already approved and in place IPA plans	Final Approval	-	-

BONUS PROGRAMS (continued)	Sector Executive/ Personnel Planning Committee	Group Executive	Division Head
o Individual Performance Award (IPA) continued			
o Administration	-	Approve: - IPA awards for recipients with ASR at $100,000 or higher - Single awards at 25% of ASR or higher - All awards for 2-downs from Group Executive	Final Approval on IPA awards less than 25% for recipients with ASR below $100,000 (except for Direct Reports)
STOCK OPTION AWARDS			
o Funding	Final Approval	-	-
o Administration	Final Approval on awards at 1500 shares and above	Approve: - Awards at 750 to 1495 shares (CORE or non-CORE participants) - All awards for 2-downs from Group Executive	Final Approval on awards of less than 750 shares to Non-CORE participants (except Direct Reports)

N.B. PROCESS:

- o All recommendations requiring the approval of a Group Executive are to be secured via the responsible GSPO's office.
- o All recommendations requiring the approval of the Sector Executive/Personnel Planning Committee are to be secured via the Sector Personnel Office.

Approved: R.S. Braddock 10/21/85

Riggs - No Frills Checking

- No minumum balance
- No maintenence charges
- No fee for up to 8 checks monthly
- No returned checks
- 6 photocopies free per year
- Free initial order of checks

GREAT WESTERN ARM

Index: Fhlbb 11th District of Columbia plus 2% margin

Points: No discount. All origination

Rate: Fixed for six mo from closing, then adjust monthly. Customer is billed monthly showing what the new note rate and margin is. Customer is given the choice of capping the new payment at 7 1/2 (with neg am) or paying full required payment. If rates are declining the lower rate applies.

Caps: No annual rate cap, 14 1/4% lifetime cap.

Processing: Accelerated

Convertible: No.

Assumable: Yes

Jumbo: Yes - but premium priced

PMI: No

Tax on Ins/Escrows: No

Underwriting ratios: 33/38

LTV: 75% and below

A/E's originate, process own loans

85. 03. 08 [illegible]:56 P02 *

Blow up to Brown Book

CITICORP MID-ATLANTIC REGION

PRODUCT BENEFITS

	Plus's*	Minus's*
1. Fixed Seconds - - purchase money	Affordabililty - use in conjunction with a lower rate (assumed) First Mortgage to lower total interest costs.	Not as affordable - a totally new 1st Mortgage may be more affordable.
	Peace of mind - know the monthly cost (due to "fixed" rate feature).	More downpayment required - we only loan up to 90% LTV on our Seconds vs. 95% on Firsts.
- non-purchase money (e.g. debt consolidation, home improvements, etc.)	Affordability - more affordable (lower interest costs) than other borrowing alternatives.	Peace-of-mind - consumers concerned about tapping into their home's equity.
	Affordability - lower monthly payments than other borrowing alternatives due to longer repayment terms.	"Locked in" if rates ~~decrease.~~
	Low rates - now is the time to "lock into" low 2nd Mortgage rates.	
2. OEHE (Variable Rate)	Affordability - lower interest costs and monthly payments than other credit alternatives. No points or annual fees.	Peace-of-mind - consumers concerned about tapping into the equity of their home.
	Flexibility - use the amount wanted, whenever needed (due to check-writing/draft feature).	Peace-of-mind - future interest rate increases uncertain.
3. 30 Yr. Fixed	Affordability - low rates vs. past year.	"Locked in" if rates decrease.
	Peace-of-mind - know the monthly cost ("fixed").	Upfront note rate is higher than some other 1st Mortgage alternatives.
		Harder to qualify (due to higher note rate).

	Plus's	Minus's
4. 15 Yr. Fixed	Build up equity faster for little extra cost - 15 year amortization schedule; increases cost only slightly.	May not qualify with 15 yr. amortization.
	Peace-of-mind - know the monthly cost ("fixed).	"Locked in" if rates decrease.
		Up front rate is higher than some other 1st Mortgage alternatives.
		Tax advantages are less than some other 1st Mortgage alternatives.
5. 10 Yr. Balloon	No real "plus's" in current environment.	Peace-of-mind - may not qualify for refinancing when balloon is due.
		Peace-of-mind - rates may increase so pay more when balloon is due.
		As expensive as 30 Yr. fixed.
6. REM/Step REM	Build up equity faster- 15 yr. term.	Rate higher than ARM and 15 Yr. fixed.
	Lower initial rate than 30 Yr. fixed.	"Locked in" if rates decrease.
	Peace-of-mind - know the percent of yearly increase in advance.	Payment increases.
	Easier to qualify vs. 15 Yr. Fixed.	
7. FHA/VA	Lower closing costs (FHA - costs normally paid by seller; VA - no up front cost).	Only small loan sizes available.
	Peace-of-mind - rate is fixed.	Up front fees usually loaded into price of house.
	Lower downpayment required.	Citicorp is expensive vs. other FHA/VA lenders.

	Plus's*	Minus's*
8. 1 Yr. ARM	Affordable - low rates Rate can fall if Treasury securities fall. Easier to qualify.	Peace-of-mind - rate (payment) can increase.
9. 3 Yr. ARM	Affordable - lower rates than 15/30 Yr. Fixed. Rate can fall. Easier to qualify. Less risk - rate can't increase as quickly as 1 Yr. ARM.	If rates go down, won't get benefit as quickly as 1 Yr. ARM. Rate can increase. Higher note rate than 1 Yr. ARM.
10. 5 Yr. ARM	Affordable - lower rates than 15/30 Yr. fixed. Peace-of-mind - fixed rate for 5 years. Rate can fall (after 5 yrs.) Easier to qualify vs. 15/30 Yr. fixed.	If rates go down, won't get benefit as quickly as 1 & 3 Yr. ARM's. Rate can increase.

* In current rate environment.

Product Management Path

Years Experience	Position	Compensation	Responsibilities
Career	Marketing Director	$80-120K + Lrg Bonus	- Overall business/business portfolio management
Career	Marketing Manager, (V.P.)	$80-120K + Lrg Bonus	- Overall business/business portfolio management
10+	Group Prod. Mgr. (Category Mgr.)	$60-80K + $25-50K Bonus	- Strategic plan, financial plan, mktg. plan
5-8	Senior Prod. Mgr.	$50-70K + 10-25K Bonus	- Strategic plan & tactics
4-7	Prod. Mgr.	$50-70K + 10-25K Bonus	- Strategic plan & tactics
2-4	Associate Prod. Mgr.	$38-45K + 5-10 Bonus	- Promo/agencies/package
0-2	Assist. Prod. Mgr. (Brand)	$35-40K	- Vol. analysis/forecasts
Entry -	Marketing Asst.	$25-35K	- Numbers crunching

- Most B.A./B.S. individuals enter as Marketing Assistants, while MBA's enter as Assistant Product (Brand) Mgrs.

- Above path is typical for "1st tier" companies including: P&G, General Foods, Cheeseborough Ponds, etc. "2nd tier" like General Mills, Bristol-Meyers, Richardson Vicks, etc. pay a little lower and don't have all of the rungs of the ladder.

———————— Indicates a major promotion cut point.

December 12, 1985

Open Ended Home Equity (OEHE)

Total home equity in US: $3 trillion

Implications: if 50% of this equity tapped, then it would double the amount of consumer credit currently outstanding in country.

Logical modification of traditional second mortgage lending in response to modern market conditions.

Product Description:

Revolving credit plan that is secured by the equity in the account holder's principal dwelling and may be accessed through a check, credit card, or ATM. Amount of line determined by equity value in home. Rate tied to index - creditors prime rate. Usually interest payment due each month (and perhaps principal reduction). Flexible repayment schedules - usually 5 to 10 years. Certain initial costs: orig fees, appraisal costs, and mortgage taxes.

Product Advantages:

* rates lower because fully secured
* advances as needed rather than lump sum
* access process not complicated; expensive due to repeated financings.
* bank can offer larger line of credit
* well suited to upscale customer who does not fear financial
* innovation and want to carefully leverage self in manner suited
* personal financial plans

Disadvantages

* consumer risks losing home if he can't meet relative
  small repayments.

Bank's Viewpoint

* loan risk reduced due security
* improvement in profitability due larger loan balance
* healthy spread due variable rate feature

Marketing

* need upscale, sophisticated
* direct mail exec level customers
* mortgage customer cross-sell
* higher income deposit customers
* upsell to card, unsecured, or other oehe customers

Documentation

* account agreement
* mortgage/deed of trust
* possible state tax law recording requirements

Disclosure

* truth in lending

* implementing regulation z
* disclosure statement outlining terms and conditions
* periodic statements recapping account activity
* care should be taken in drafting

Security Problems

* be careful where some state laws do not permit the security interest in future advances to date back to the original filing. In this event, residentially secured loans made by other creditors during the period between advances under the plan may attain a higher lien priority than subsequent advances
* need due on sale clause in event customer sells
* look at first lien. a. is there a negative am feature? If so, loan principal could grow to 125% decreasing the remaining value that secures the second position. b. if ARM, make sure that the borrower can make payment in future and that first lien holder won't be forced in to repossess.

Right of Recision

Federal law: In connection with a credit plan in which a security interest is or will be retained in the consumer's principal dwelling, each consumer whose ownership interest is subject to the security interest has the right to cancel the loan within three business days.

North Area

Philadelphia

Requested Pricing - 15 year fixed

RORA				
.49%	Note Rate	10.625%	Discount	2%
	Origination	1.0%		

LK

RORA	Suggested Pricing - 15 year fixed			
.56%	Note Rate	10.75%	Discount	2%
	Origination	1.0%		

Philadelphia

Requested Pricing 30 Year FNMA 125 basis point discount on current pricing.

Suggested pricing 30 Year FNMA 100 basis point discount on current pricing.

Note Rate	10.75%	Discount	2%
Origination	1.0%		

Average loan size	$70,000
Passthru premium (108 b.p.)	750
Origination fee (11%)	700
Discount (1%)	(700)
*Variable Expenses	(350)
Contribution to fixed Expense	350
*Fixed Expenses	1300
Net per loan	(950)

[illegible] $ Rate

* Estimates due to updated origination expense per loan not being submitted.

Rationale here is that at least we would be making a contribution to fixed costs. Loans must be delivered within 60 days to avoid pricing hits.

PRICING

Strategy: Offer below minimum market rates in markets where we have idle capacity. Reestablish relationships with realtors.

South Area

Atlanta - Suggested Pricing - One Year ARM

RORA				
.94%	Note Rate	9.5%	Caps	2/14.5
	Margin:	250	Origination	1.25%

Carolinas - Suggested Pricing - One Year ARM

RORA				
.94%	Note Rate	9.75%	Caps	2/14.5
	Margin	250	Origination	1

Virginia

Vienna - Stategy - Lifetime cap is of major importance. Also, they desire to offer a lower margin than competitors because they feel there is a target market.

- Suggested Pricing - One Year ARM

RCRA						
.93%	Note Rate	8.00%	Caps	2/14.5		
	Margin	275	Discount	3%	Origination	1%
.81%	Note Rate	8.00%	Caps	2/14.0		
	Margin	275	Discount	3%	Origination	1%
.89%	Note Rate	8.50%	Caps	2/14.0		
	Margin	275	Discount	3%	Origination	1% *
.92%	Note Rate	9.25%	Caps	2/14.5		
	Margin	220	Discount	2%	Origination	1%

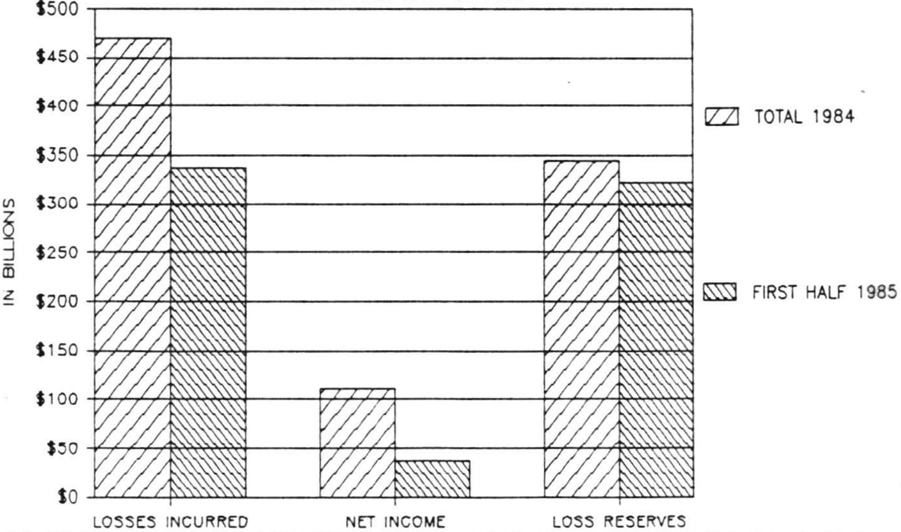
Suggested Pricing -30 Year FNMA

Average loan size 100M	
Origination fee (1%)	$1000
Passthru premium (108 b.p.)	$1080
Discount (50 b.p.)	$(500)
Variable Costs	$(310)
Contribution to fixed costs	$1270
Salary Expense Per Loan	$ 936
Fixed Cost per loan	$ 317
Net per loan	$ 17

Richmond/Tidewater - Advised Lance to discontinue premium pricing.

MORTGAGE INSURANCE INDUSTRY PROFILE

THROUGH FIRST HALF OF 1985



EPIC EXPOSURE COMPARISONS

Company	Moody's Ratings	Est. Combined Pool & Primary Maximum Loss Exposure to EPIC	June 1985 Total Risk	June 1985 Total Capital
TICOR Mortgage Insurance Co.	B1	$166	N.A.	$198
Republic Mortgage Insurance Co.	U.R.	$100	$1,579	$72
Wisconsin Mtg. Accep. Corp.	A1	$60	$16,356	$500
Mortgage Guaranty Ins. Corp.	Aa3	$15	$4,732	$217
Commonwealth Mortgage Assur. (PA, MD)	U.R.	(Est. $8m) N.A.	$1,264	$63
PMI Mortgage Insurance Co.	A1	$7	$4,244	$193
Investors Mortgage Insurance Co.	U.R.	$6	$2,333	$95
United Gty. Residential Ins. Co.	Aaa	$4	$5,203	$219
VEREX Assurance, Inc.	A2	$3	$6,769	$243
Foremost Guaranty Corp.	A2	$2	$1,261	$81
General Elect. Mtg. Ins. Co. (OH)	Aa2	$2	$2,586	$110
U.S. Mortgage Insurance Co.	N.R.	N.A.	N.A.	$11
General Elect. Mtg. Ins. Co. (NC, CA, FL)	N.R.	---	$2,536	$115
Industry Totals		$394	$53,295	$2,117

NOTE: UR means under review for a rating. NR means not rated. NA means not available for dissemination. Capital is defined by contingency reserves plus policyholder surplus. UGRIC is United Gty. Residential Ins. Co., GEMICO is General Elect. Mtg. Ins. Co. (OH, NC, CA, FL), MGIC is Mortgage Guaranty Ins. Corp., PMI is PMI Mortgage Insurance Co., WMAC is Wisconsin Mtg. Accep. Corp., VEREX is VEREX Assurance, Inc., FGC is Foremost Guaranty Corp., TMIC is TICOR Mortgage Insurance Co., RMIC is Republic Mortgage Insurance Co., CMAC is Commonwealth Mortgage Assur. (PA, MD), IMI is Investors Mortgage Insurance Co. SOURCE: Moody's Investors Svc.

January 29, 1986
PMI COMPANY LOSSES

* $600 million losses first nine months of '85

* 28% more than record total 1984 losses

* Larger losses projected for 1986

* Loans that were originated in 1984 enter their third year of maturity, the year in which the highest number of claims are usually filed. The price appreciation of those homes has been low, giving homeowners who are financial strapped less incentive to try to continue payments.

* Mortgage insurance losses may peak in 1986 if claims from 1982 and 1983 loans finally begin to decline. These are loans entering their fourth and fifth year of maturity, but because of the values of homes have not been appreciating as much as buyers and lenders expected, delinquencies and defaults continue to mount.

* Positive side: most mi companies have tightened underwriting and are scrutinizing lenders more carefully and have raised premiums on higher-risk products.

* Fall in rates has helped mi companies as discounted loans won't see radical rise in payments.

* Nat'l Assn of Realtors expects that home values will rise only 3.5% in 1986 and will continue to grow in value at a slower rate than the general rate of inflation. This suggests that claim frequencies in foreclosures will remain high, especially on lower-downpayment mortgages.

* Problem areas in 1986 will likely continue to be those states heavily dependent on the oil market and lumber products.

Ready Credit
Re Finance
Rates

September 11, 1986

NOTES FROM NOTES FROM THE BEACH

"...the business has suffered the severe economic burdens of inflation which have been working on a distribution system designed for the `banking business' when in fact there is no such thing. As a retail system - the branches are overdesigned - as a corporate presence they are unnecessary."

"...it is clear that some relevant new delivery technologies are available to the business and will have an important bearing on both the economic dynamics and the institutional and legal/regulatory framework within which we work. The existence of these technologies strongly suggest that we should either reconfigure and reinvigorate our own efforts or get out of the business - our current posture is not economically viable over the long run."

"...I refer to a fundamentally new business starting with a dedication to the consumer and to the proposition that we can offer a set of services that will substantially satisfy a family's financial needs under terms and conditions that will earn the shareholders an adequate profit while creating a healthy, positive and straightforward relationship with the customer."

"Our objective cannot be to be in the loan business or the deposit business. The task is not to run branches nor to issue cards. These are but means to an end - the business is an effort on our part to manage resources so as to satisfy consumer needs."

"[...I categorize the results of our efforts] in three ways: the occupation of space, profits and the character of the business organization itself. That is -

(A) Occupation of Space - along three dimensions:

1. our share of the relevant market:
2. within that share - our tier position or the share of the total actual uses of financial services for a family unit that is a customer; and
3. our psychological position - i.e., how "well" do we satisfy, to wit, how healthy is the relationship.

(B) Profits - along two dimensions:

1. absolute contribution or PCE: and
2. quality or RORA.

(C) Character of the Organization - along three dimensions:

1. to what extent does the work organization provide a healthy environment for each of us;

2. to what extent does the organization learn and regenerate itself developing skills and people to cope with new and different problems; and

3. to what extent is the organization a healthy contributing part of Citicorp.

"...a set of priorities has been stated: namely, control, profitability and then growth..."

"...we rejected a functional organization so as to build around the concept of the Business Manager. In doing so we recognized that we may have sacrificed some time but were persuaded that the "business manager" was a better long term concept because: (1) it would build more good people; (2) it implied that we would break the CSG into manageable pieces; (3) it forces operating level business responsibility down into the organization; and (4) it insures a balanced "full business view."

"The key to day to day management slot is that of the Business Manager. The tone of the organization and the extent to which we "pull together" is very much dependent on the efforts at that level. it is important to recognize that the "people" dimension of our job is a line responsibility. A staff function-personnel - is not going to maintain the fabric of the organization. Insuring that people are listened to, talked to, properly paid, etc., is one of the prime jobs of management.

"...most of our credit problems can be related to one of two problems. First, poorly conceived credit products or second, loss of control of routine collection/receivable management processes."

"...the notion of a "business proposition" or perception on the part of a given manger of that which has to be created in order to achieve a business success is key to the concept of running a business and distinguishes the manager from the administrator. Presumably when embraced, a business proposition is flushed out and fought for as the model of what needs to get done in running our business."

" margins: The issues of margins is a tough one yet the previous comments on pricing should make clear that we may well have an opportunity to restructure the business. At least in our "supermarket banking" businesses the current situation is unacceptable - margins are too low and depositors are subsidizing borrowers."

"...the economics of the distribution system is a strong negative."

"...we have relatively little feel for the capacity of our distribution systems - hence for their economics. It would seem that the "output" of the distribution system is (a) minutes of transaction time; (b) minutes of service time; and (c) minutes of platform time.... ...The cost of distribution is very high - on average (worldwide) eating up some 85% of the net revenues provided by customers. While there would seem to be promise of cost reductions - these seem most likely to be available by re-thinking and re-configuring our distribution system rather than through efficiencies. Such redesign does not stand alone but relates to the fundamental business proposition being supported."

"...There are some 35 of us - Division Heads, Business Managers, GMO Staff and key operating and marketing officers - who in the aggregate have responsibility to manage the consumer effort. It is fundamentally important that we share views and forge common beliefs in the thrust of our effort. In my mind, we will not succeed unless all of us succeed."

"The business managers are clearly key. As described earlier, this job was created as the focal point for day-to-day business responsibilities. The rest of the organization is designed to support this role. Division Heads are strategic managers. They have responsibility to act as "player coaches" with the business managers and insure the success of that effort but, more importantly, they provide an overview of their constituent businesses and give direction to the development of our efforts...."

RATES 5/13/86

Mortgage rates continue decline but pace slows. Single digit for 5 weeks now.

Problem Banks 5/13/86

Angermeuller:

Why bother to buy, say, a Texas bank when preference given to in state bidders, and when there are restrictions on expansion once the purchase is made.

It's a buyers market.Under deluge of refinancing requests, some lenders reluctant to cut rates further.

Some analysts believe bottom reached in late summer, dropping another 50 bp.

Average term mortgage loan down to 24.7 years in April from 25.3 years in March. Loans average 74% of purchase price. Average purchase price is 112,700.

Yeilds on 30 year treasuries, a bellweather of rates, fell to lowest levels since 1975 - 7.37%. May 7 Bond action sold record $2.7 billion in debt.

Rates: 1

8/5 - Stable to down
- Govt to sell > 20B new debt issues
- Biggest ever govt financing
- usually such debt issues depress prices/but traders prepared this time (eg ↑ rates of depress prices)

8/6 WSJ
- slightly up but expected stable thru 86
- Ave 30 year fixed 12.17 (14.68 1 yr ago)
- Ave Arm 10.72
- Ave term abt 26 years

Market Trend MB Magazine July '85

- 85 good year for Mort Banker
- Rates low + likely to stay (30 yr Fixed @ 12)

Future Course of Rates? Depends on ~~[illegible]~~ Monetary Policy

↓ Background

- Weak manu sector
- Bus invest + Consumer Expd. up, but domes manu still hurt bec strong $ value has caused demand to be satisfied via imports. More, strong $ has hurt exports and this plus relatively weaker foreign econ has created trade gap

↓ impact on money markets?

1. Red'n bus loan demand
2. Fed highly accomodative policy to stimulate

∴ Red loan demand + accomodative policy has allowed ↓ rates.

Will this change soon?

NO:

a. $ Still strong + likely to stay.
b. Fed will keep rates low in attempt
to appreciate value of $

Conclu. House remain strong +
maybe enough to keep
economy out of recession

1.8 M starts
Total Originations 48-50 BN

RATES

1/86 - 30 yr fixed-rate mortgages closest to single digit in 7 years. Govt. insured mortgages have a shot at it. Few expect single digit to go single digit. Borrowers can get an adjustable-rate mortgage currently with an initial interest rate of 9%. And even if 30 year fixed conventional mortgages don't dip below 10%, 15 year fixed mortgages might.

Motives for Refinancing

1. Reduce interest cost

   Keep the after tax cost of the interest saved over the term of the mortgage. Be sure prepay penalty on orig. loan plus cost of obtaining loan is less than the pu of the net interest savings.

2. Realize tax-free cash

   Increase total loan amount

   New loan = orig. loan amt then investor has recouped loan amortization paid during ownership.

   New loan > orig. loan then investor realizes portion of appreciation in his investment.

3. Increase cash flow

   o Loan amt. same - rate reduced

   o New Loan with longer amortization period

Network – Key issues

September 2, 1986

NOTES:

Aggregate balances at Savings institutions declining. People investing in Ginnie Maes and bonds. If interest rates increase, these will prove to be poor investments. Investment in a CD is a better consumer protection risk.

Appraisal, credit check, and title search cause for logjam in processing Mortgage applications. Refi the cause. Refis are 3 times 1985. Savings Industry will account for $233 billion in refinanced and residential purchase loans.

CAPITAL ADEQUACY

Much regulatory pressure on S and L's. The industry is more profitable, but will continuing pressure to increase capital, and change accounting practices render industry impotent?

FHLBB says more capital is required to insure viability of insured institutions and shield the FSLIC from excessive losses. More capital will also force ownership to be more vigilent. FHLBB wants to increase from 3% to 6% over six years.

But add to this the special assessment: 1/32 of 1% of insured deposits each quarter; massive mortgage refinancings have set back institutions' effort to restructure their portfolios eg. move to fixed from variable. FHLBB restrictions on growth. Potential changes in accounting standards.

HOUSING MARKET

2 million units in 1986. Mortgage originations headed toward a new all-time high, and the interest rates available on most new mortgages have made the median-cost home affordable for a family with an average income and a 25% down-payment.

Compare with 1982: Market at 1 MM units and 15% rates; widening gap between the price of a median cost home and what prospective first time home buyers could afford to pay.

ACCOUNTING FEES

Proposal would require origination income to be recognized over loan life. Loan origination costs, however, would have to be recognized as current expenses.

Current practice: Take up to 1% of loans's initial balance as current income so long as the fee can be offset by an origination expense. Change in this could carve $4 billion in revenue from the bottom lines of s and l's in next six years.

Regop No Frills Checking

Personnel Delegations

Pricing

Product - OEHE

PMI

DELEGATION OF APPROVAL AUTHORITY FOR PERSONNEL PROGRAMS

SALARY PROGRAMS	Sector Executive/ Personnel Planning Committee	Group Executive	Division Head
o Administration			
o N.Y. Core Program Structure	Final Approval	-	-
o Non-N.Y. Program Structure	-	Final Approval	-
o Salary Adjustments to and over $140,000 and all 2-downs From Sector Executive	Final Approval	-	-
o Hires/Titles/Salary Adjustments at $100,000 to $139,999; and all 2-downs from Group Executive	-	Final Approval	-
o Hires/Titles/Salary Adjustments below $100,000 (except 2-downs from Group Executive)	-	-	Final Approval
JOB EVALUATION			
o W level and higher	Final Approval	-	-
o Below W level	-	-	Final Approval
BONUS PROGRAMS			
o CORE Nominations and Awards	Final Approval	-	-
o Individual Performance Award (IPA)			
o Funding:			
o Within approved IPA plans	-	Final Approval	-
o Outside of already approved and in place IPA plans	Final Approval	-	-

BONUS PROGRAMS (continued)	Sector Executive/ Personnel Planning Committee	Group Executive	Division Head
o Individual Performance Award (IPA) continued			
o Administration	-	Approve: - IPA awards for recipients with ASR at $100,000 or higher - Single awards at 25% of ASR or higher - All awards for 2-downs from Group Executive	Final Approval on IPA awards less than 25% for recipients with ASR below $100,000 (except for Direct Reports)
STOCK OPTION AWARDS			
o Funding	Final Approval	-	-
o Administration	Final Approval on awards at 1500 shares and above	Approve: - Awards at 750 to 1495 shares (CORE or non-CORE participants) - All awards for 2-downs from Group Executive	Final Approval on awards of less than 750 shares to Non-CORE participants (except Direct Reports)

N.B. **PROCESS:**

- o All recommendations requiring the approval of a Group Executive are to be secured via the responsible GSPO's office.
- o All recommendations requiring the approval of the Sector Executive/Personnel Planning Committee are to be secured via the Sector Personnel Office.

Approved: ______________ 10/21/85
R.S. Braddock

Riggs - No Frills Checking

- No minumum balance
- No maintenence charges
- No fee for up to 8 checks monthly
- No returned checks
- 6 photocopies free per year
- Free initial order of checks

GREAT WESTERN ARM

Index: Fhlbb 11th District of Columbia plus 2% margin

Points: No discount. All origination

Rate: Fixed for six mo from closing, then adjust monthly. Customer is billed monthly showing what the new note rate and margin is. Customer is given the choice of capping the new payment at 7 1/2 (with neg am) or paying full required payment. If rates are declining the lower rate applies.

Caps: No annual rate cap, 14 1/4% lifetime cap.

Processing: Accelerated

Convertible: No.

Assumable: Yes

Jumbo: Yes - but premium priced

PMI: No

Tax on Ins/Escrows: No

Underwriting ratios: 33/38

LTV: 75% and below

A/E's originate, process own loans

Blow up to Brown Book

CITICORP MID-ATLANTIC REGION

PRODUCT BENEFITS

	Plus's*	Minus's*
1. Fixed Seconds - - purchase money	Affordabililty - use in conjunction with a lower rate (assumed) First Mortgage to lower total interest costs.	Not as affordable - a totally new 1st Mortgage may be more affordable.
	Peace of mind - know the monthly cost (due to "fixed" rate feature).	More downpayment required - we only loan up to 90% LTV on our Seconds vs. 95% on Firsts.
- non-purchase money (e.g. debt consolidation, home improvements, etc.)	Affordability - more affordable (lower interest costs) than other borrowing alternatives.	Peace-of-mind - consumers concerned about tapping into their home's equity.
	Affordability - lower monthly payments than other borrowing alternatives due to longer repayment terms.	"Locked in" if rates decrease.
	Low rates - now is the time to "lock into" low 2nd Mortgage rates.	
2. OEHE (Variable Rate)	Affordability - lower interest costs and monthly payments than other credit alternatives. No points or annual fees.	Peace-of-mind - consumers concerned about tapping into the equity of their home.
	Flexibility - use the amount wanted, whenever needed (due to check-writing/draft feature).	Peace-of-mind - future interest rate increases uncertain.
3. 30 Yr. Fixed	Affordability - low rates vs. past year.	"Locked in" if rates decrease.
	Peace-of-mind - know the monthly cost ("fixed").	Upfront note rate is higher than some other 1st Mortgage alternatives.
		Harder to qualify (due to higher note rate).

	Plus's	Minus's
4. 15 Yr. Fixed	Build up equity faster for little extra cost - 15 year amortization schedule; increases cost only slightly.	May not qualify with 15 yr. amortization.
	Peace-of-mind - know the monthly cost ("fixed).	"Locked in" if rates decrease.
		Up front rate is higher than some other 1st Mortgage alternatives.
		Tax advantages are less than some other 1st Mortgage alternatives.
5. 10 Yr. Balloon	No real "plus's" in current environment.	Peace-of-mind - may not qualify for refinancing when balloon is due.
		Peace-of-mind - rates may increase so pay more when balloon is due.
		As expensive as 30 Yr. fixed.
6. REM/Step REM	Build up equity faster- 15 yr. term.	Rate higher than ARM and 15 Yr. fixed.
	Lower initial rate than 30 Yr. fixed.	"Locked in" if rates decrease.
	Peace-of-mind - know the percent of yearly increase in advance.	Payment increases.
	Easier to qualify vs. 15 Yr. Fixed.	
7. FHA/VA	Lower closing costs (FHA - costs normally paid by seller; VA - no up front cost).	Only small loan sizes available.
	Peace-of-mind - rate is fixed.	Up front fees usually loaded into price of house.
	Lower downpayment required.	Citicorp is expensive vs. other FHA/VA lenders.

	Plus's*	Minus's*
8. 1 Yr. ARM	Affordable - low rates Rate can fall if Treasury securities fall. Easier to qualify.	Peace-of-mind - rate (payment) can increase.
9. 3 Yr. ARM	Affordable - lower rates than 15/30 Yr. Fixed. Rate can fall. Easier to qualify. Less risk - rate can't increase as quickly as 1 Yr. ARM.	If rates go down, won't get benefit as quickly as 1 Yr. ARM. Rate can increase. Higher note rate than 1 Yr. ARM.
10. 5 Yr. ARM	Affordable - lower rates than 15/30 Yr. fixed. Peace-of-mind - fixed rate for 5 years. Rate can fall (after 5 yrs.) Easier to qualify vs. 15/30 Yr. fixed.	If rates go down, won't get benefit as quickly as 1 & 3 Yr. ARM's. Rate can increase.

* In current rate environment.

Product Management Path

Years Experience	Position	Compensation	Responsibilities
Career	Marketing Director	$80-120K + Lrg Bonus	- Overall business/business portfolio management
Career	Marketing Manager, (V.P.)	$80-120K + Lrg Bonus	- Overall business/business portfolio management
10+	Group Prod. Mgr. (Category Mgr.)	$60-80K + $25-50K Bonus	- Strategic plan, financial plan, mktg. plan
5-8	Senior Prod. Mgr.	$60-70K + 10-25K Bonus	- Strategic plan & tactics
4-7	Prod. Mgr.	$50-70K + 10-25K Bonus	- Strategic plan & tactics
2-4	Associate Prod. Mgr.	$38-45K + 5-10 Bonus	- Promo/agencies/package
0-2	Assist. Prod. Mgr. (Brand)	$35-40K	- Vol. analysis/forecasts
Entry -	Marketing Asst.	$25-35K	- Numbers crunching

- Most B.A./B.S. individuals enter as Marketing Assistants, while MBA's enter as Assistant Product (Brand) Mgrs.

- Above path is typical for "1st tier" companies including: P&G, General Foods, Cheeseborough Ponds, etc. "2nd tier" like General Mills, Bristol-Meyers, Richardson Vicks, etc. pay a little lower and don't have all of the rungs of the ladder.

———————— Indicates a major promotion cut point.

December 12, 1985

Open Ended Home Equity (OEHE)

Total home equity in US: $3 trillion

Implications: if 50% of this equity tapped, then it would double the amount of consumer credit currently outstanding in country.

Logical modification of traditional second mortgage lending in response to modern market conditions.

Product Description:

Revolving credit plan that is secured by the equity in the account holder's principal dwelling and may be accessed through a check, credit card, or ATM. Amount of line determined by equity value in home. Rate tied to index - creditors prime rate. Usually interest payment due each month (and perhaps principal reduction). Flexible repayment schedules - usually 5 to 10 years. Certain initial costs: orig fees, appraisal costs, and mortgage taxes.

Product Advantages:

* rates lower because fully secured
* advances as needed rather than lump sum
* access process not complicated; expensive due to repeated financings.
* bank can offer larger line of credit
* well suited to upscale customer who does not fear financial
* innovation and want to carefully leverage self in manner suited
* personal financial plans

Disadvantages

* consumer risks losing home if he can't meet relative
  small repayments.

Bank's Viewpoint

* loan risk reduced due security
* improvement in profitability due larger loan balance
* healthy spread due variable rate feature

Marketing

* need upscale, sophisticated
* direct mail exec level customers
* mortgage customer cross-sell
* higher income deposit customers
* upsell to card, unsecured, or other oehe customers

Documentation

* account agreement
* mortgage/deed of trust
* possible state tax law recording requirements

Disclosure

* truth in lending

* implementing regulation z
* disclosure statement outlining terms and conditions
* periodic statements recapping account activity
* care should be taken in drafting

Security Problems

* be careful where some state laws do not permit the security interest in future advances to date back to the original filing. In this event, residentially secured loans made by other creditors during the period between advances under the plan may attain a higher lien priority than subsequent advances
* need due on sale clause in event customer sells
* look at first lien. a. is there a negative am feature? If so, loan principal could grow to 125% decreasing the remaining value that secures the second position. b. if ARM, make sure that the borrower can make payment in future and that first lien holder won't be forced in to repossess.

Right of Recision

Federal law: In connection with a credit plan in which a security interest is or will be retained in the consumer's principal dwelling, each consumer whose ownership interest is subject to the security interest has the right to cancel the loan within three business days.

North Area

Philadelphia

Requested Pricing - 15 year fixed

RORA				
.49%	Note Rate	10.625%	Discount	2%
	Origination	1.0%		

RORA	Suggested Pricing - 15 year fixed			
.56%	Note Rate	10.75%	Discount	2%
	Origination	1.0%		

Philadelphia

Requested Pricing 30 Year FNMA 125 basis point discount on current pricing.

Suggested pricing 30 Year FNMA 100 basis point discount on current pricing.

Note Rate	10.75%	Discount	2%
Origination	1.0%		

Average loan size	$70,000
Passthru premium (108 b.p.)	750
Origination fee (11%)	700
Discount (1%)	(700)
*Variable Expenses	(350)
Contribution to fixed Expense	350
*Fixed Expenses	1300
Net per loan	(950)

* Estimates due to updated origination expense per loan not being submitted.

Rationale here is that at least we would be making a contribution to fixed costs. Loans must be delivered within 60 days to avoid pricing hits.

PRICING

Strategy: Offer below minimum market rates in markets where we have idle capacity. Reestablish relationships with realtors.

South Area

Atlanta - Suggested Pricing - One Year ARM

RORA				
.94%	Note Rate	9.5%	Caps	2/14.5
	Margin:	250	Origination	1.25%

Carolinas - Suggested Pricing - One Year ARM

RORA				
.94%	Note Rate	9.75%	Caps	2/14.5
	Margin	250	Origination	1

Virginia

Vienna - Stategy - Lifetime cap is of major importance. Also, they desire to offer a lower margin than competitors because they feel there is a target market.

- Suggested Pricing - One Year ARM

RCRA					
.93%	Note Rate	8.00%	Caps	2/14.5	
	Margin	275	Discount	3%	Origination 1%
.81%	Note Rate	8.00%	Caps	2/14.0	
	Margin	275	Discount	3%	Origination 1%
.89%	Note Rate	8.50%	Caps	2/14.0	*
	Margin	275	Discount	3%	Origination 1%
.92%	Note Rate	9.25%	Caps	2/14.5	
	Margin	220	Discount	2%	Origination 1%

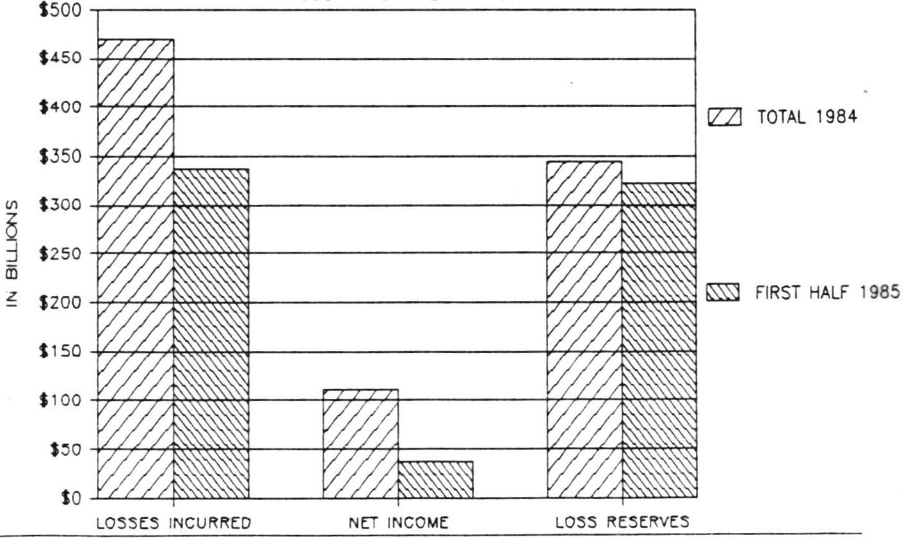
Suggested Pricing -30 Year FNMA

Average loan size 100M	
Origination fee (1%)	$1000
Passthru premium (108 b.p.)	$1080
Discount (50 b.p.)	$(500)
Variable Costs	$(310)
Contribution to fixed costs	$1270
Salary Expense Per Loan	$ 936
Fixed Cost per loan	$ 317
Net per loan	$ 17

Richmond/Tidewater - Advised Lance to discontinue premium pricing.

MORTGAGE INSURANCE INDUSTRY PROFILE

THROUGH FIRST HALF OF 1985



EPIC EXPOSURE COMPARISONS

Company	Moody's Ratings	Est. Combined Pool & Primary Maximum Loss Exposure to EPIC	June 1985 Total Risk	June 1985 Total Capital
TICOR Mortgage Insurance Co.	B1	$166	N. A.	$198
Republic Mortgage Insurance Co.	U. R.	$100	$1,579	$72
Wisconsin Mtg. Accep. Corp.	A1	$60	$16,356	$500
Mortgage Guaranty Ins. Corp.	Aa3	$15	$4,732	$217
Commonwealth Mortgage Assur. (PA, MD)	U. R.	(Est. $8m) N. A.	$1,264	$63
PMI Mortgage Insurance Co.	A1	$7	$4,244	$193
Investors Mortgage Insurance Co.	U. R.	$6	$2,333	$95
United Gty. Residential Ins. Co.	Aaa	$4	$5,203	$219
VEREX Assurance, Inc.	A2	$3	$6,769	$243
Foremost Guaranty Corp.	A2	$2	$1,261	$81
General Elect. Mtg. Ins. Co. (OH)	Aa2	$2	$2,586	$110
U.S. Mortgage Insurance Co.	N. R.	N. A.	N. A.	$11
General Elect. Mtg. Ins. Co. (NC, CA, FL)	N. R.	---	$2,536	$115
Industry Totals		$394	$53,295	$2,117

NOTE: UR means under review for a rating. NR means not rated. NA means not available for dissemination. Capital is defined by contingency reserves plus policyholder surplus. UGRIC is United Gty. Residential Ins. Co., GEMICO is General Elect. Mtg. Ins. Co. (OH, NC, CA, FL), MGIC is Mortgage Guaranty Ins. Corp., PMI is PMI Mortgage Insurance Co., WMAC is Wisconsin Mtg. Accep. Corp., VEREX is VEREX Assurance, Inc., FGC is Foremost Guaranty Corp., TMIC is TICOR Mortgage Insurance Co., RMIC is Republic Mortgage Insurance Co., CMAC is Commonwealth Mortgage Assur. (PA, MD), IMI is Investors Mortgage Insurance Co. SOURCE: Moody's Investors Svc.

January 29, 1986

PMI COMPANY LOSSES

* $600 million losses first nine months of '85

* 28% more than record total 1984 losses

* Larger losses projected for 1986

* Loans that were originated in 1984 enter their third year of maturity, the year in which the highest number of claims are usually filed. The price appreciation of those homes has been low, giving homeowners who are financial strapped less incentive to try to continue payments.

* Mortgage insurance losses may peak in 1986 if claims from 1982 and 1983 loans finally begin to decline. These are loans entering their fourth and fifth year of maturity, but because of the values of homes have not been appreciating as much as buyers and lenders expected, delinquencies and defaults continue to mount.

* Positive side: most mi companies have tightened underwriting and are scrutinizing lenders more carefully and have raised premiums on higher-risk products.

* Fall in rates has helped mi companies as discounted loans won't see radical rise in payments.

* Nat'l Assn of Realtors expects that home values will rise only 3.5% in 1986 and will continue to grow in value at a slower rate than the general rate of inflation. This suggests that claim frequencies in foreclosures will remain high, especially on lower-downpayment mortgages.

* Problem areas in 1986 will likely continue to be those states heavily dependent on the oil market and lumber products.

Ready Credit
Re Finance
Rates

September 11, 1986

NOTES FROM NOTES FROM THE BEACH

"...the business has suffered the severe economic burdens of inflation which have been working on a distribution system designed for the `banking business' when in fact there is no such thing. As a retail system - the branches are overdesigned - as a corporate presence they are unnecessary."

"...it is clear that some relevant new delivery technologies are available to the business and will have an important bearing on both the economic dynamics and the institutional and legal/regulatory framework within which we work. The existence of these technologies strongly suggest that we should either reconfigure and reinvigorate our own efforts or get out of the business - our current posture is not economically viable over the long run."

"...I refer to a fundamentally new business starting with a dedication to the consumer and to the proposition that we can offer a set of services that will substantially satisfy a family's financial needs under terms and conditions that will earn the shareholders an adequate profit while creating a healthy, positive and straightforward relationship with the customer."

"Our objective cannot be to be in the loan business or the deposit business. The task is not to run branches nor to issue cards. These are but means to an end - the business is an effort on our part to manage resources so as to satisfy consumer needs."

"[...I categorize the results of our efforts] in three ways: the occupation of space, profits and the character of the business organization itself. That is -

(A) Occupation of Space - along three dimensions:

1. our share of the relevant market:
2. within that share - our tier position or the share of the total actual uses of financial services for a family unit that is a customer; and
3. our psychological position - i.e., how "well" do we satisfy, to wit, how healthy is the relationship.

(B) Profits - along two dimensions:

1. absolute contribution or PCE: and
2. quality or RORA.

(C) Character of the Organization - along three dimensions:

1. to what extent does the work organization provide a healthy environment for each of us;

2. to what extent does the organization learn and regenerate itself developing skills and people to cope with new and different problems; and

3. to what extent is the organization a healthy contributing part of Citicorp.

"...a set of priorities has been stated: namely, control, profitability and then growth..."

"...we rejected a functional organization so as to build around the concept of the Business Manager. In doing so we recognized that we may have sacrificed some time but were persuaded that the "business manager" was a better long term concept because: (1) it would build more good people; (2) it implied that we would break the CSG into manageable pieces; (3) it forces operating level business responsibility down into the organization; and (4) it insures a balanced "full business view."

"The key to day to day management slot is that of the Business Manager. The tone of the organization and the extent to which we "pull together" is very much dependent on the efforts at that level. it is important to recognize that the "people" dimension of our job is a line responsibility. A staff function-personnel - is not going to maintain the fabric of the organization. Insuring that people are listened to, talked to, properly paid, etc., is one of the prime jobs of management.

"...most of our credit problems can be related to one of two problems. First, poorly conceived credit products or second, loss of control of routine collection/receivable management processes."

"...the notion of a "business proposition" or perception on the part of a given manger of that which has to be created in order to achieve a business success is key to the concept of running a business and distinguishes the manager from the administrator. Presumably when embraced, a business proposition is flushed out and fought for as the model of what needs to get done in running our business."

" margins: The issues of margins is a tough one yet the previous comments on pricing should make clear that we may well have an opportunity to restructure the business. At least in our "supermarket banking" businesses the current situation is unacceptable - margins are too low and depositors are subsidizing borrowers."

"...the economics of the distribution system is a strong negative."

"...we have relatively little feel for the capacity of our distribution systems - hence for their economics. It would seem that the "output" of the distribution system is (a) minutes of transaction time; (b) minutes of service time; and (c) minutes of platform time.... ...The cost of distribution is very high - on average (worldwide) eating up some 85% of the net revenues provided by customers. While there would seem to be promise of cost reductions - these seem most likely to be available by re-thinking and re-configuring our distribution system rather than through efficiencies. Such redesign does not stand alone but relates to the fundamental business proposition being supported."

"...There are some 35 of us - Division Heads, Business Managers, GMO Staff and key operating and marketing officers - who in the aggregate have responsibility to manage the consumer effort. It is fundamentally important that we share views and forge common beliefs in the thrust of our effort. In my mind, we will not succeed unless all of us succeed."

"The business managers are clearly key. As described earlier, this job was created as the focal point for day-to-day business responsibilities. The rest of the organization is designed to support this role. Division Heads are strategic managers. They have responsibility to act as "player coaches" with the business managers and insure the success of that effort but, more importantly, they provide an overview of their constituent businesses and give direction to the development of our efforts...."

RATES 5/13/86

Mortgage rates continue decline but pace slows. Single digit for 5 weeks now.

Problem Banks 5/13/86

Angermeuller:

Why bother to buy, say, a Texas bank when preference given to in state bidders, and when there are restrictions on expansion once the purchase is made.

It's a buyers market.Under deluge of refinancing requests, some lenders reluctant to cut rates further.

Some analysts believe bottom reached in late summer, dropping another 50 bp.

Average term mortgage loan down to 24.7 years in April from 25.3 years in March. Loans average 74% of purchase price. Average purchase price is 112,700.

Yeilds on 30 year treasuries, a bellweather of rates, fell to lowest levels since 1975 - 7.37%. May 7 Bond action sold record $2.7 billion in debt.

Rates: 1

8/5 - Stable to down
- Govt to sell > 20B [illegible] debt issue
- Biggest ever govt refunding
- usually such debt issues depress prices / but traders prepared this time (eg ↑ rates of depress prices)

8/6 WSJ
- slightly up but expected stable thru 86
- Ave 30 years fixed 12.17 (14.68 1 yr ago)
- Ave Arm 10.72
- Ave term abt 26 years

Market Trend MB Magazine July '85

- 85 good year for Mort Banker
- Rates low + likely to stay (30 yr Fixed @ 12)

Future Course of Rates? Depends on ~~Econ~~ Monetary Policy

✓ Background

- Weak manu sector
- Bus invest + Consumer Expd. up, but domestic manu still hurt bec strong $ value has caused demand to be satisfied via imports. More, strong $ has hurt exports and this, plus relatively weaker foreign econ has created trade gap

impact on money markets?

1. Red'n bus loan demand
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3. Increase cash flow

   o Loan amt. same - rate reduced

   o New Loan with longer amortization period

READY CREDIT OVERVIEW

Business Proposition

To leverage the mortgage relationship and deepen our consumer penetration by household in line with sales of Second Mortgages and Insurance.

Rationale

A ready Credit line is a natural response to a home buyer's financial needs. Home buyers are certain to need new furniture, carpeting, appliances, etc., after buying a home. Providing the means to make these purchases is our answer to Coldwell Banker's handing each new mortgagee a Sears credit card.

Market Opportunity

o Mortgage Sourced - the 1986 Plan calls for 400 Mid-Atlantic mortgage customers to accept Ready Credit. The Mid-Atlantic Region will cross-sell customers throughout its nine states, whereas the Central Region will sell the product only to Maine residents. Mid-Atlantic will use a combination of phone and mail to cross sell the product. Central, however, will be able to discuss cross-sell products when the mortgage application is taken.

Mortgage customers who accept Ready Credit are expected to exhibit almost perfect repayment behavior for the line of credit. Because the line of credit will be offered by the customer's mortgage institution, he is likely to feel a very strong responsibility to maintain an outstanding payment record. In fact, the few delinquent accounts in our portfolio were sourced as prospects; none of our cross-sell customers is in a past-due state.

o Direct Mail - Recent direct mail solicitations have demonstrated that prospective customers are very receptive to our pre-approved lines of credit. Growth of our Ready Credit portfolio through this medium will provide a large, highly profitable cross sell base for the Division's mortgage and liability products.

Mid-Atlantic will solicit homeowners whose household incomes are $25,000 or more in an effort to add approximately 6500 accounts. Central has targeted residents of Citibank Maine's branch trading area who have household incomes of at least $15,000. These direct mail programs are projected to yield new customers with an average line size of $4800.

Financials

PCE from Mid-Atlantic's portfolio will increase from ($77M) in 1985 to $81M in 1986. ANR will exhibit a sharp use from $4.4M in 1985 to $15.7M in 1986. Mid-Atlantic's account base will reach 15,000 next year, a 100% increase over our existing account base.

Secondary Market

Service, Customer

November 20, 1986

Problems facing S and L industry:

* Real Estate loan losses. Adverse effect on this type of lending due new tax regulations.

* Accounting standards. 1. Loan fees 2. New accounting rules for income taxes. Potential combined cost: $8 billion.

* Increasing mortgage business competition. Insurance companies, retailers, automakers and container manufacturers

* Spectre of rising rates. Some S and L's have not restructured funding out of fixed rate loans.

3 STRATEGY OPTIONS

- o Low cost supplier
- o Niche
- o Value added

C & S VALUE ADDED STRATEGY

- o Update technology
- o New products/services for upscale
- o Up fees on checking to scare off unprofitable relationships
- o Stem attrition w/new product-
  15 free checks, small service charge.

LOW COST SUPPLIER

- o Broad market place
- o Low priced products & services
- o Sustained high capital
- o Mass distribution thru low cost distribution system
- o Hold operating costs
- o Employee incentive compensation
- o Heavy technology investment
- o Tend to be largest firms

NICHE

- o One or narrow market segment
- o Not good for most banks due to weak Market Research/ Marketing
- o Creative
- o Can t afford high cost distribution so danger of competitors eroding niche

VALUE ADDED

- o Broad markets
- o Enhance products and services
- o Most viable strategy
- o Avoids massive scale investments of low cost supplier strategy
- o Require * service dedication commitment to customer and product development

STRATEGIC OBJECTIVES
FOR SAVINGS INSTITUTIONS

Foreword

This report on the strategic objectives for savings institutions is the result of intense study, debate and discussion among the members of the U.S. League's Committee on Economic Affairs under the chairmanship of William M. Waller (1984-85) and Theo H. Pitt Jr. (1986). The U.S. League's Executive Committee accepted the recommendations of the Committee on Economic Affairs in August 1986 and authorized their dissemination to the League membership.

Like all such statements, the strategic objectives for savings institutions are offered in the spirit of policy guidance rather than policy direction. As such, they are broad in scope and reflect not only current economic and competitive circumstances, but also future circumstances to the extent that they can be foreseen.

Accordingly, the U.S. League will continue to review, evaluate and update the strategic objectives for savings institutions as future circumstances change.

Preamble

The growing affluence of American families and the development of new financial technology have increased both the demand of the household sector for a wide range of financial services and the number and variety of suppliers of those services. As long-standing providers of financial services to the household sector, savings institutions are a central force in this evolution of the American financial system.

Savings institutions have enjoyed remarkable success in the achievement of their original objectives; they are primarily responsible for establishing the primary mortgage market, one of the largest segments of the largest financial market in the world, and for providing the facilities through which all Americans can save and earn a market rate of return on their funds with convenience, safety and liquidity.

The opportunity for savings institutions to provide financial services profitably will continue to be found primarily in the household sector; households will continue to be the principal source of the funds that savings institutions mobilize, and households will continue to offer savings institutions the highest quality assets in both home mortgages and consumer loans.

In this sense, savings institution operations carry on a long-standing tradition that masks important and fundamental changes. Savings institutions once represented virtually the only institutions through which working class families could obtain financial services on reasonable terms. But today, the institutional infrastructure is in place to meet the financial needs of the vast majority of American families. The role of savings institutions is therefore less one of creating such an infrastructure and more one of maintaining and improving it.

In response to this change in emphasis and to the need to build a stronger capital base, the mutual form of organization of savings institutions is giving way to stock ownership. In this context, success ceases to be measured in terms of the personal saving rate and the homeownership rate and comes to be measured by profitability—a reflection of the economic efficiency and the quality of financial services rendered by these institutions.

As a matter of public policy and financial stability, however, savings institutions, along with other depository institutions, have been deemed to be vehicles for the preservation and prudent application of capital, not vehicles for the employment of venture capital. To assure that the public interest is served, regulatory agencies have been established to oversee the operations of savings institutions.

Until recently, the regulations promulgated by these agencies severely restricted the activities in which savings institutions could engage; specialization was determined at least as much by legislative and regulatory fiat as by market forces.

Today, these restrictions have been substantially relaxed, such that the regulatory function has become more that of preserving the safety and soundness of operation than one of directing the flow of credit.

Barring a financial crisis of cosmic proportions, the economic and competitive environment is likely to continue to encourage the replacement of mandated financial specialization with market-determined specialization.

In this context, the "market" that determines the particular mix of financial services will be the local or regional markets in which given institutions operate. Depending upon their market circumstances, savings institutions will therefore provide consumer lending and commercial lending services as well as their more traditional home construction and home purchase financing. Increasingly, the similarities among markets will be far more powerful determinants of similarities among savings institutions than the regulatory framework.

In short, in responding to market forces, savings institutions have already begun to adopt more generalized functions within the financial system, namely, to mobilize and manage funds for the acquisition of earning assets, rendering financial services to other economic entities in the process.

Thus, savings institutions are no longer just in the business of housing finance, nor even in the business of real estate finance; they are in the business of rendering financial service.

In recognition of these changing circumstances, the U.S. League of Savings Institutions offers the following strategic objectives.

Strategic Objectives for Savings Institutions

- *In recognition of the higher degree of interest rate risk and credit risk that is a product of both broader investment opportunities and a less stable economic environment, savings institutions seek to establish and maintain significantly higher net worth ratios.*
- *To preserve their traditional independence in securing funds for lending, savings institutions seek to maintain a strong retail deposit base built on customer loyalty through service quality.*
- *By virtue of their expertise and market position, savings institutions will continue to utilize a significant proportion of funds at their disposal in the financing of residential real estate.*
- *To minimize their exposure to risk and to stabilize their earnings over the business cycle, however, savings institutions seek to diversify their loan portfolios to include consumer loans, commercial loans and even direct investments in real estate and commercial ventures.*

Savings institutions recognize that these objectives cannot be attained fully through their efforts alone. Accordingly, savings institutions have a powerful interest in fostering an operating environment conducive to the achievement of its business objectives. Such an environment has four dimensions:

1. The Economy

a. *As portfolio lenders, savings institutions support economic policies that promote an economic environment characterized by stable, sustainable, noninflationary economic growth.*

b. *As lenders with an increasingly interregional scope of activity, savings institutions further support macroeconomic policies that foster regional economic balance and minimize disparities among regional economies.*

c. *Savings institutions recognize that such an economic environment does not now exist and may not exist for some time yet to come. It is in part for this reason that savings institutions include higher net worth ratios among its business objectives.*

2. The Regulatory System

a. *Savings institutions support the maintenance of a regulatory system that permits the marketplace and the available technology to determine the scope of financial services offered.*

b. *Savings institutions further support a regulatory system that places paramount importance on the preservation of safety and soundness rather than the allocation of credit. or the achievement of social objectives by regulatory dictate.*

3. The Competitive Environment

Savings institutions seek free and open competition with other elements of the financial system, requiring only that the treatment of the various types of financial institutions in law, regulation, support facilities, disclosure of information, and accounting and tax treatment be appropriate to their activities.

4. Support Facilities

***a.** Savings institutions regard deposit insurance as the cornerstone of consumer confidence in the financial system. Accordingly, savings institutions seek the maintenance of sound deposit insurance funds.*

***b.** Savings institutions regard the regional central banking facilities of the Federal Home Loan Bank and Federal Reserve systems as essential for the maintenance of orderly financial markets and seek to preserve and enhance their ability to support the operations of their member institutions.*

***c.** As savings institutions expand their lending range and take advantage of new financial technology to enhance their portfolio management flexibility, the secondary mortgage market becomes much more than a desirable adjunct to the housing finance system; it becomes an integral and indispensable part of that system. Savings institutions therefore seek* *to establish and maintain strong, efficient secondary market facilities that function in harmony, not in competition, with those of the primary market.*

d. *Savings institutions further support the judicious use of direct and indirect subsidies to assist low-income families to obtain decent shelter, but seek to eliminate subsidies provided by governments and government-sponsored agencies that distort or impair the functioning of the private mortgage market.*

Members of the Committee on Economic Affairs (1984-1986)

Chairman (1986)
Theo H. Pitt Jr.
Pioneer Savings Bank
Rocky Mount, North Carolina
1984, 1985, 1986

Chairman (1984-85)
William M. Waller
State Federal Savings
Tulsa, Oklahoma
1984, 1985, 1986

B.J. Adkins
Regional Federal Savings
New Albany, Indiana
1984

William O. Alexander
Continental Federal Savings
Oklahoma City, Oklahoma
1984

Billy Don Anderson
Valley Federal Savings
Sheffield, Alabama
1984, 1985, 1986

Mario Antoci
Home Savings of America FA
Los Angeles, California
1985

Edgar H. Bailey
Leader Federal Savings
Memphis, Tennessee
1986

Joe G. Baker
Pacific Savings Bank
Costa Mesa, California
1985

David S. Barrows
Oregon League of Financial Institutions
Portland, Oregon
1984, 1985, 1986

Richard E. Bolton
Pioneer Financial
Malden, Massachusetts
1986

N. Carson Branan
Great Southern Federal Savings Bank
Savannah, Georgia
1984, 1985

William G. Christensen
First Federal Savings
Madison, Connecticut
1984, 1985

Paul K. Clarkin
American Federal Savings
Denver, Colorado
1984

William J. Cody
Vermont Federal Bank
Burlington, Vermont
1984, 1985, 1986

David S. Cook
Buckeye Federal Savings
Columbus, Ohio
1984

J. Michael Cornwall
First Texas Savings
Dallas, Texas
1984, 1985, 1986

Gary Driggs
Western Savings
Phoenix, Arizona
1984

John Easterling
First State Savings
Spartanburg, South Carolina
1984

Peter J. Farmer
Horizon Financial FA
Southampton, Pennsylvania
1984, 1985

William F. Ford
First Nationwide Savings
San Francisco, California
1984, 1985

Richard G. Gilbert
Citizens Savings Bank
Canton, Ohio
1984, 1985, 1986

Robert F. Gorman
United Postal Savings
St. Louis, Missouri
1986

G. David Hanna
First Federal Savings Bank
Newton, Kansas
1986

James J. Heagerty
Crossland Savings
Bradenton, Florida
1984, 1985, 1986

Richard D. Heiserman
Capitol Federal Savings
Denver, Colorado
1985, 1986

Jock Hewitt
Provident Federal Savings
Boise, Idaho
1984, 1985, 1986

James C. Johnson
Loyola Federal Savings
Baltimore, Maryland
1984, 1985, 1986

Elliot Knutson
Washington Federal Savings
Seattle, Washington
1985, 1986

Ray Martin
Coast Savings
Los Angeles, California
1984

W.W. McAllister III
San Antonio Savings
San Antonio, Texas
1984, 1985

James F. McKenna
North Shore Savings
Brookfield, Wisconsin
1984, 1985, 1986

Francis M. Minor Jr.
Central Savings
New Orleans, Louisiana
1986

Joe C. Morris
Columbia Savings
Emporia, Kansas
1984, 1985, 1986

William S. Mortensen
First Federal Savings Bank of California
Santa Monica, California
1984

William E. Nodine
Pioneer Federal Savings Bank
Clearwater, Florida
1984, 1985, 1986

John M. O'Brien
Central Pennsylvania Savings
Shamokin, Pennsylvania
1986

James G. Perkins
Equitable Cooperative Bank
Lynn, Massachusetts
1984, 1985, 1986

Joseph C. Scully
St. Paul Federal Bank
Chicago, Illinois
1984, 1985, 1986

Kenneth D. Seaton
Detroit & Northern Savings
Hancock, Michigan
1985, 1986

Emil A. Voelz Jr.
Great Northern Savings Company
Barberton, Ohio
1985, 1986

U.S. League Staff

James W. Christian
Chief Economist

Mark Obrinsky
Economist

Mark Baumann
Associate Economist

Howard W. Kane
Associate Economist

USL

January 29, 1986

Bills for Multiple-Class Mortgage Securities

Chafee/Cranston bill pending that would permit the issuance of multiple-class mortgage pass-through securities that could be considered sales of assets rather than debt.

Bills would allow issuance of multiple classes of pass-through securities bearing different yields and maturities. The securities would be similar to collateralized mortgage obligations (CMO's) but CMO's are treated as debt obligations and involve taxation both at the issuer and investor level. Pass through securities, on the other hand, are treated as sales of the underlying mortgages and are exempt from taxation at the issuer level.

Chafee said his legislation is expected to reduce mortgage interest costs for homeowners by facilitating investments in mortgages, and to provide greater flexibility, higher yields, and reduced transaction costs to financial institutions seeking to liquidate portions of their portfolio of seasoned mortgages.

TASK FORCE

Thrift

THRIFT PROBLEM

1. Self regulating commission possibility (Preston Martin)

2. Thrifts should demand more of their accounting firms in evaluating asset quality.

3. Three hard choices in FSLIC recapitalization:
   1. Industry itself - burden on stronger
   2. Use fed tax dollars
   3. Merger with FDIC

4. Need risk related premium system.

↑ CL

↓ Rate

Equity

Sears

October 7, 1985

FSLIC Fund bailout. Separate corporation Federal S & L Asset Management Association. Pay non-government salaries to get better people.

Golden days of credit card business going?

- Pressure to lower rates
- Sears introduction
- Market saturated
- Rising credit losses
  - customers abusing bankruptcy laws ✓
  - Banks deteriorating standards ✓

Undervalued Yen cause of trade problem

- Since 1978 $ appreciated 25% vs. Yen
- U.S. exports reduced (capital equipment)
- Auto steel imports up
- Domestic auto and steel also squeezed by high interest rates. Therefore shrinkage of import competitive edge is eroding U.S. trade strenths.

Reg. Q now gone. 5¼% NOW ceiling and 5½% passbook ceiling gone.

Price not only feature to differentiate deposits:

- Location
- Differential pricing depending on balance
- Tellers call up customers
- Higher rate for no return cancelled checks

Benefits of Corporate takeovers:

- Keep management on toes
- Profits to raiders
- Economies of scale by forming larger corporations

FDIC/FSLIC should not bail out big institutions (Continental), only small depositors. Otherwise -- big banks not subject to market disciplines. Small banks who are allowed to fail not fairly treated.

Freddie Mack to adopt a cash equivalency basis to appraisals.

WIVES

W

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