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# FEDERAL INTERMEDIATE CREDIT BANKS DEBENTURE INTEREST RATE LIMITATION

GOVERNMENT

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## HEARING BEFORE THE COMMITTEE ON AGRICULTURE HOUSE OF REPRESENTATIVES

EIGHTY-NINTH CONGRESS

SECOND SESSION

ON

**H.J. Res. 1217**

AUGUST 3, 1966

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FEDERAL INTERMEDIATE CREDIT BANKS  
DEBENTURE INTEREST RATE LIMITATION

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# FEDERAL INTERMEDIATE CREDIT BANKS, DEBENTURE INTEREST RATE LIMITATION

WEDNESDAY, AUGUST 3, 1966

HOUSE OF REPRESENTATIVES,  
COMMITTEE ON AGRICULTURE,  
Washington, D.C.

The committee met, pursuant to notice, at 10:30 a.m., in room 1301, Longworth House Office Building, Washington, D.C., Hon. Harold D. Cooley (chairman) presiding.

Present: Representatives Cooley, Poage, Gathings, Hagen of California, Stubblefield, Purcell, Olson, Matsunaga, O'Neal, Resnick, Stalbaum, de la Garza, Vigorito, Redlin, Bandstra, Greigg, Callan, Dague, Belcher, Teague of California, Mrs. May, Harvey of Indiana, Findley, and Walker of Mississippi.

Also present: Christine S. Gallagher, clerk; Hyde H. Murray, assistant clerk; John J. Heimburger, general counsel; Francis LeMay, consultant; and Fowler C. West, staff.

The CHAIRMAN. The committee will please be in order.

We have before us this morning House Joint Resolution 1217, by Mr. Poage.

(H.J. Res. 1217, and the Department report dated July 20, 1966, follow:)

[H.J. Res. 1217, 89th Cong., 1st sess.]

JOINT RESOLUTION To delete the interest rate limitation on debentures issued by Federal intermediate credit banks

*Resolved by the Senate and House of Representatives of the United States of America in Congress assembled, That the second sentence of section 203(b) of the Federal Farm Loan Act, as amended (12 U.S.C. 1042), relating to debentures issued by Federal intermediate credit banks, is amended by deleting "not exceeding 6 per centum per annum" therefrom.*

JULY 20, 1966.

The Honorable the SPEAKER OF THE HOUSE,  
*House of Representatives.*

DEAR MR. SPEAKER: There is transmitted herewith a proposed joint resolution to delete the interest rate limitation on debentures issued by Federal intermediate credit banks.

The 12 Federal intermediate credit banks, one in each farm credit district, finance the 468 member-controlled production credit associations and over 100 privately capitalized other financing institutions that make short- and intermediate-term loans to farmers and ranchers. The credit banks do this financing by discounting for the production credit associations and the other financing institutions, with their endorsement, the notes taken by them from the farmers and ranchers, and also by making loans to the associations and other financing institutions. The total of such financing by the credit banks during 1965 was \$5.3 billion. Over 90 percent of it was for the production credit associations.

The loan funds of the credit banks are obtained chiefly through the sale of their consolidated debentures to the investing public. Under existing law the interest rates in such debentures are determined as follows (12 U.S.C. 1042):

"Rates of interest upon debentures and other such obligations issued under said section shall, subject to the approval of the Farm Credit Administration, be

fixed by the Federal intermediate credit bank making the issue, not exceeding 6 per centum per annum."

The proposed joint resolution would delete "not exceeding 6 per centum per annum" from the foregoing. This would permit the Federal intermediate credit banks to issue debentures with an interest rate of more than 6 percent if the higher rate is required for the debentures to be marketable.

Issues of Federal intermediate credit bank debentures, which are of 9-month term and average about \$350 million, mature monthly. To assure that these issues will be paid as they mature, it is vital that ready access to money market funds be uninterrupted; if any issue were permitted to become in default it would seriously impair not only operations of the credit banks, but the future sales of bonds and debentures of the Federal land banks and banks for cooperatives which also are under the supervision of the Farm Credit Administration.

On the sale of credit bank debentures for delivery on July 5, 1966, the market then prevailing required an interest rate of 5.6 percent. On July 20, 1966, an issue of credit bank debentures required a price of 5.9 percent. If the present upward trend of interest rates continues, the Federal intermediate credit banks might soon be precluded from obtaining further loan funds. Should this happen, they would not be in a position to continue to perform their function of financing the production credit associations and other financing institutions. This would result in an intolerable situation since the credit banks would be faced with maturing issues of debentures and an important source of credit upon which hundreds of thousands of farmers depend would be extinguished.

The Bureau of the Budget has advised that there is no objection to presentation of the proposed joint resolution from the standpoint of the administration's program.

Very truly yours,

R. B. TOOTELL, *Governor.*

PROPOSED JOINT RESOLUTION TRANSMITTED BY FARM CREDIT ADMINISTRATION

JOINT RESOLUTION To delete the interest rate limitation on debentures issued by Federal intermediate credit banks

*Resolved by the Senate and House of Representatives of the United States of America in Congress assembled, That the second sentence of section 203(b) of the Federal Farm Loan Act, as amended (12 U.S.C. 1042), relating to debentures issued by Federal intermediate credit banks, is amended by deleting "not exceeding 6 per centum per annum" therefrom.*

The CHAIRMAN. We have as witnesses Mr. Paul O. Ritter, General Counsel, accompanied by Paul Fankhauser, Deputy Director of Short-Term Credit Service, and W. H. Albright, Chief, Finance Division, Farm Credit Administration.

We will be pleased to hear from you now, to present the views of the Department.

STATEMENT OF PAUL O. RITTER, GENERAL COUNSEL, ACCOMPANIED BY PAUL FANKHAUSER, DEPUTY DIRECTOR OF SHORT-TERM CREDIT SERVICE, AND W. H. ALBRIGHT, CHIEF, FINANCE DIVISION, FARM CREDIT ADMINISTRATION

Mr. RITTER. Mr. Chairman and members of the committee, Governor Tootell is in Colorado today, attending the Federal Farm Credit Board meeting which begins tomorrow, so that we three are here from the Farm Credit Administration, and our purpose is to urge favorable and early action on House Joint Resolution 1217 which would delete the 6-percent interest rate limitation that is in the existing law with reference to the debentures issued by the Federal intermediate credit banks.

We do not have a prepared statement to distribute, but I thought that I would undertake an explanation of this by saying something

about the Federal intermediate credit banks, their function, how the debentures are issued by the banks and how they serve its function, and why the present 6-percent interest rate ceiling on such debentures should be removed and at an early date.

The Federal intermediate credit banks consist of 1 in each of the 12 farm credit districts and were established in 1923, under title II of the Federal Farm Loan Act, which was added by the Farm Credit Act of 1923.

The function of these credit banks is to finance the 468 production credit associations that make loans to farmers and ranchers at the local level.

The funds with which they do this financing are mostly obtained through the sale of debentures of the 12 banks to the investing public. These debentures are consolidated collateral trust debentures. They are the joint and several obligations of the 12 Federal intermediate credit banks. There is no liability in the United States for these debentures. They are not guaranteed by the Federal Government.

The CHAIRMAN. Will you please pull that mike up to you so that we may hear you?

Mr. HARVEY of Indiana. I cannot hear the gentleman.

Mr. RITTER. I am sorry.

We have 12 Federal intermediate credit banks, 1 to serve each of the 12 farm credit districts. They were established in 1923 pursuant to the acts of Congress and their function is to finance the 468 production credit associations and some other financing institutions which, at the local level, make loans to farmers and ranchers.

The credit banks, when they get the money with which to do this financing, do so mostly through the sale of debentures to the investing public. These debentures are collateral trust debentures. They are the joint and several obligation of the 12 banks which issued them, and there is no liability on the part of the United States, either as to principal or interest.

Mr. HARVEY of Indiana. Or what?

Mr. RITTER. Or interest.

In selling these debentures, the interest rate is fixed with reference to the market which is then prevailing.

The credit banks usually have an issue of debentures each month. The average amount of these issues is about \$350 million. The customary term is 9 months for each issue. So that each month there is an issue maturing, and it must be paid when it does mature. So, this means that the succeeding issue must be in an amount sufficient to pay off the maturing issue, and if additional funds are required, an additional amount of debentures must then be issued.

If, at the time of any of these monthly periods when debentures are issued, the credit banks are unable to issue or market the debentures because of this 6-percent ceiling in the statute and because the market requires a higher rate, it just means that they would not be able to continue to function as was intended. It means that this source of loans for the farmers and the ranchers would be immediately curtailed, and, of course, if this continued indefinitely it would terminate.

The volume for the fiscal year ending 1966 of this financing done by the Federal intermediate credit banks was \$5.9 billion.

I mentioned that for each issue the interest rate must be determined in the light of the market then prevailing. I thought that we would review the experience of the 8 months of this calendar year which would point out the urgency of removing this ceiling now and, we think, as promptly as possible.

For the July issue, the rate was 5.60 percent; for the August issue, it was 5.875 percent. That is an increase of 0.275 percent in 1 month. On six occasions of this calendar year, the debenture rate has increased over the previous month ranging from one-tenth of 1 percent to three-tenths of 1 percent.

If there was a similar rise for the September issue—and, incidentally, the September issue will have the interest rate fixed on August 17. To repeat, if there were a similar rise for that issue, or if the rate increases more than one-eighth percent, which it did for 5 months during the calendar year, it would mean that we would be above the statutory 6-percent ceiling, and the debentures could not be issued.

It is, therefore, for this reason that we think it is very urgent—that is, I mean the Farm Credit Administration feels and desires to make it clear that it is very urgent that this present 6-percent ceiling rate limitation should be removed, and promptly. And we would hope that it could be done, that action could be taken by August 17.

The CHAIRMAN. You said, in effect, that unless the ceiling is removed, the Farm Credit Administration would be embarrassed, because it could not sell the debentures; is that correct?

Mr. RITTER. We would be embarrassed; yes, sir, if we could not issue them.

The CHAIRMAN. How would the rate be established?

Mr. RITTER. If the 6-percent ceiling is removed, it means then that the issuing banks, subject to the approval of the Farm Credit Administration, will determine the rate of interest on each issue, and that will be done in the light of what the market requires in order to make those debentures salable.

The CHAIRMAN. How about a State like North Carolina, where we have a legal rate of interest? Would it cover it in that State without violating the law?

Mr. RITTER. Yes, sir. If I am not mistaken, the limitation you mention there refers to loans which are made to the farmers and the ranchers and individuals.

The CHAIRMAN. That is right. You can borrow money, but not in excess of 6 percent without violating the usury law, and you would sell the debentures at a higher rate.

Mr. RITTER. I do not believe that the limitation on the amount of the interest that may be charged—that is, the State limitation on the amount of interest that may be charged for a loan would apply to these debentures.

The CHAIRMAN. What effect would the State law have on other financial transactions that occur within the State? We have a fight going on right now between the building and loan associations and the commercial banks, where people are taking money out of the building and loan associations and putting it into commercial banks and into certificates of deposit to get more interest than is guaranteed by the building and loan associations. If you go ahead with this, you would have a similar situation there, would you not?

I am not arguing against the bill, because I am going to vote for the bill—I am sure of that.

Mr. RITTER. Whenever the credit banks' debentures are marketed they are competitive, and I do not see how that can be avoided.

The CHAIRMAN. The debentures are sold to the investors?

Mr. RITTER. Yes, sir.

Mr. STALBAUM. For what term?

Mr. RITTER. These are customarily a 9-month term.

Mr. POAGE. There are a number of States that have 6-percent interest limitations. My State does not. But a great many States do have a 6-percent interest limitation, but that does not mean that you can borrow money at 6 percent in these States. You could not any more sell debentures for 6 percent in North Carolina than you could in Texas, could you, if the general money market goes above 6 percent—you are not going to be able, just because there is a State law, to go into a State that limits the interest rate to 6 percent. You are not going to be able to go into that State and sell debentures just because they have a State limitation on their interest rate. Nobody is going to buy the debentures at 6 percent if the going rate is 6.5 percent.

Mr. RITTER. I think that is right.

Mr. POAGE. As a matter of fact, you are not going to sell these debentures in North Carolina or in Texas anyhow, are you?

Mr. RITTER. I do not know about the distribution, but I would think that we have many of these debentures held in both States.

Mr. ALBRIGHT. Yes, we do.

Mr. POAGE. I did not say they are not held in the States. Do you sell them in the States?

Mr. RITTER. The sale, customarily, that is the offering, is made in New York.

Mr. POAGE. That is what I thought.

Mr. RITTER. By a fiscal agent.

Mr. POAGE. That is what I thought. You do not make any sale in either Texas or North Carolina?

You make the sale in New York City, do you not?

Mr. RITTER. And then they are shipped pursuant to——

Mr. POAGE. I know that, but that is none of your business, is it?

Mr. RITTER. No, sir.

Mr. POAGE. I understand that they passed those on to the purchasers, but you are not selling any debentures in any State where there is a 6-percent interest law, are you?

Mr. RITTER. I believe there are dealers through whom these debentures are marketed in those States, and I am sure——

Mr. POAGE. What I am trying to get at is: Do you, the Farm Credit System, offer anything for sale in Texas?

Mr. RITTER. Well, in a sense we do, and I may want to refer this to one of my associates. In a sense they may be offered.

Mr. POAGE. I know there are people who own debentures in the State of Texas. I understand that full well, but do you offer any in the State?

Mr. RITTER. The offer is made by the fiscal agent.

Mr. POAGE. In the State of New York, in the city of New York?

Mr. RITTER. Yes.

Mr. POAGE. Of course.

Mr. RITTER. That is right.

Mr. POAGE. All I am trying to get at is: Is there any reason for being involved with this 6-percent law, because you are not violating it?

Mr. RITTER. Yes, sir.

Mr. POAGE. Of course, I know that the debentures are scattered all over the country but you do not sell them all over the country. Is that not right?

Mr. RITTER. I think that is right. That is, the fiscal agent offers them and makes the sale.

Mr. POAGE. I know that they offer them. I am asking what you offer. Where do you offer to sell them? Do you offer to sell me a debenture in Waco, Tex.? Could I write to the bank at Houston and get one of these debentures?

Mr. RITTER. Not normally.

Mr. POAGE. Of course not. So, why do we not just nail this down. I am just trying to get a record here that is clear and unambiguous, and I think it perfectly clear that you are selling these debentures in New York City, and anybody in the world who wants, so far as you are concerned, can get them, and you are paid for them, regardless of where they turn up, but you are not selling them in Texas, are you?

Mr. RITTER. No.

Mr. POAGE. Or in North Carolina or in any State that has a 6-percent limitation.

Mr. RITTER. That is right.

Mr. POAGE. Let us get that on the record without equivocation, if that is correct.

The CHAIRMAN. Mr. de la Garza.

Mr. DE LA GARZA. Mr. Chairman, supposing a State has a 6-percent interest law. Are you going to sell your debentures for 6.5 percent or 7 percent? What about the loans? Would the interest on your loan cover the higher rate, or would you be prohibited from making loans in a State that has a 6-percent interest limitation law?

Mr. RITTER. Well, in the case of these Federal intermediate credit banks, if the interest they pay for their debentures rises, eventually the interest they charge to finance the Production Credit Association will also rise, and when that happens, then, eventually the Production Credit Association must increase its interest rates on the loans that they make to the farmers and the ranchers, and at that level there might be a question as to whether there is a limitation in the State law which applies to the Production Credit Association loans. And our position is that those limitations do not apply, but that is another question, and at the moment, these Production Credit Associations are making loans not to exceed the State law limitations.

Mr. DE LA GARZA. What is the level of your present interest rate, if there is an average?

Mr. RITTER. In the case of the Federal intermediate credit banks, 10 of the banks are charging 6 percent; 1 is charging 6.25; 1 is charging one-half of 1 percent above the cost of money.

Mr. DE LA GARZA. So that it is very probable then that the funds will go beyond 6 percent everywhere—that they will do that?

Mr. RITTER. If the market would continue in that direction that would be applicable to selling these credit bank debentures, too.

Mr. DE LA GARZA. Let me ask you one more question, and that is about the direction private money is moving, at what rate it is

moving. What is the benefit of going to your organization, if the farmers can now get it for less than that?

Mr. RITTER. It is very important. We think that this source of credit should continue to be available to the farmers and the ranchers, and in order for it to continue to be available, it is necessary to remove this 6-percent ceiling if the debentures can only be sold at more than 6 percent.

Mr. DE LA GARZA. That is what I mean. Where do you justify your system if the farmer can get the money locally for the same interest rate that he will have to pay you or the intermediate bank?

Mr. RITTER. Well, the farmer must make that choice. There are about 500,000 members of the Production Credit Associations, and they must have thought there was an advantage to them in this.

Mr. DE LA GARZA. I am sure that there was, but it does not look like it will be. That is my question.

Mr. RITTER. I do not see how they can go to another source and get a better interest rate, in general, than through the System. In some instances they may be able to do so.

Mr. DE LA GARZA. That is all. Thank you.

The CHAIRMAN. Mr. Stalbaum.

Mr. STALBAUM. Is it not true that in some instances the source of credit from other sources is just not there?

Mr. RITTER. There are such areas.

Mr. STALBAUM. I think that should be made clear in the record, because this is not necessarily a case of your competing with private sources but in many instances, in rural areas, you are the main source of rural credit, and if there is some other source it is because you are there to set a standard for them.

Mr. RITTER. That is right, and if this source became unavailable they would have no place to which to turn, if no other source is available.

Mr. STALBAUM. My reason for asking these questions is to get into the record—to give us, if you would, possibly, the rate which must be charged by the Production Credit Associations, either as an override over the debenture rate or the percentage interest rate that would now prevail. Historically, about what is the interest rate for lending purposes of the Production Credit Associations as compared to their cost of money?

Mr. RITTER. I do not know if I will respond at once to that, but on July 1, 1966, the interest rate in effect in the Production Credit Associations ranged from 4.75 percent to 8 percent. There were 118 associations charging 6 percent; 127 charging 6.5 percent, and 119 charging 7 percent. Thirteen associations had a rate in excess of 7.5 percent.

Mr. STALBAUM. Is the interest rate about 5.5 percent; that is, the debenture interest rate as of that time?

Mr. RITTER. As of recent date the average rate of interest on outstanding debentures was 5.39 percent.

Mr. STALBAUM. So that, actually, then it would appear that the Production Credit Associations have to have a spread of somewhat over 1 percent for operating expenses, and this includes also the cost of the Federal intermediate credit banks—is that not about right—to oversimplify this?

Mr. RITTER. I believe it would be that or perhaps more.

Mr. STALBAUM. Just slightly over 1 percent?

Mr. RITTER. Yes.

Mr. STALBAUM. That is all, thank you.

The CHAIRMAN. Are there any further questions?

Mr. OLSON?

Mr. OLSON. You said that the debentures are sold to finance the intermediate credit banks. Are they the individual and several obligations of the banks?

Mr. RITTER. They are the liability of—

Mr. OLSON. Of all of the banks?

Mr. RITTER (continuing). Of all of the banks.

Mr. OLSON. Collectively, they are offered these debentures?

Mr. RITTER. That is right.

Mr. OLSON. At a fixed rate per month. Who fixes the rate?

Mr. RITTER. Well, the rate is fixed by the issuing banks, subject to the approval of the Farm Credit Administration.

Mr. OLSON. Each individual bank fixes the rate?

Mr. RITTER. It is collective.

Mr. OLSON. Collectively?

Mr. RITTER. Yes. They work through a committee of presidents.

Mr. OLSON. So that collectively they fix a rate that applies to the debentures issued by all of the 12 banks.

Mr. RITTER. It is a consolidated issue of debentures, and it is issued on behalf of the 12 banks.

Mr. OLSON. And carries a uniform interest rate?

Mr. RITTER. Yes.

Mr. OLSON. If that be so, why is it that your interest rate by the Production Credit Associations can vary as much as 1.5 percent?

Mr. RITTER. I may want someone to supplement this, but I think that it is because the cost of administration and operation by the different associations produces that difference.

Mr. OLSON. That is the only thing that you can think of?

Mr. POAGE. If you will yield there?

Mr. OLSON. Yes.

Mr. POAGE. As a matter of fact, is not part of that due to the fact that some of these Production Credit Associations are charging very high rates in order to pay out their stock, or they were doing this for a long time? I am sure that our Production Credit Associations charged about 1 percent more to get rid of the Government stock, but they are now paid out. Then, do you not have a number of Production Credit Associations that are operating at a loss, eating up their savings, to avoid raising the interest rate? And they can do it as long as they have money in hand. Are not some of them actually doing that?

Mr. RITTER. There are all of those variations. So far as retirement of Government capital is concerned, there are now two associations only with Government capital, a total of \$530,000. The others have accomplished the return of their Government capital.

The CHAIRMAN. All have returned the Government capital except two?

Mr. RITTER. Yes.

Mr. POAGE. That is, the Production Credit Associations, not the intermediate credit banks.

Mr. RITTER. The Production Credit Associations, yes.

Mr. OLSON. Do you have a policy of checking into—or does the individual intermediate credit bank have a policy of checking into the operation of individual Production Credit Associations—as to why the interest rates do vary, with a view toward the possibility of helping them administer their program so that they can lower their interest rate?

Mr. RITTER. Well, each Production Credit Association is examined once a year by the Farm Credit Administration. In addition, the Federal intermediate credit banks of the district closely watch the operation of each Production Credit Association. They will make suggestions to improve operations, and so forth.

Mr. OLSON. All right. Now, getting back to the setting of the interest rates for the debentures. The interest rate is set collectively by the banks for each issue, with the advice of the financial board, and then the offer is made. Can you give me any idea as to how they determine what interest rate they have to offer for a certain month? In other words, what I am trying to find out is do you not ask what you have to pay for money or you make an offer. If you market debentures by offer instead of bids, could you tell me if you have ever been turned down?

Mr. RITTER. No, sir. Once the interest rate is fixed, it is marketed on that basis.

Mr. OLSON. Have you ever found it impossible to sell debentures at the rate fixed?

Mr. RITTER. Well, there is a nationwide group of dealers, and when there is an offering made, these dealers write in and they say that they want a participation of so much. When that offer on their part is confirmed, then the dealer is obligated to take that amount of debentures, and if the interest rate is not attractive enough, it means that the dealers will just have to hold them until they can dispose of them in the market.

Mr. OLSON. In other words, the dealer offers to take  $x$  amount of your debentures even before you establish the rate?

Mr. RITTER. No, he knows the rate. That is announced.

Mr. OLSON. The rate is announced?

Mr. RITTER. Yes.

Mr. OLSON. And then he makes an offer to take——

Mr. RITTER. Yes.

Mr. OLSON (continuing).  $x$  amount of your debentures?

Mr. RITTER. That is right.

Mr. OLSON. I do not see how a purchaser could be hurt by that. That is the point that I am trying to get at. The interest is already established from your experience. Does the dealer ever refuse to buy your debentures at the offered rate?

Mr. RITTER. Have they? No, the answer is "No."

Mr. OLSON. All right. Have you then made any effort to comparing interest rates in other areas to see if you would have to offer that higher rate?

Mr. RITTER. All that study should be done before the rate is fixed and the offer is made. In other words, they tap all sources of information that they can to arrive at what they think is the appropriate rate in the market at that time.

Mr. OLSON. I am not going to pursue it any further, but it would seem to me that if I wanted to insure that this was being conducted

in an area of competition and if I kept being on the higher side, evidenced by the fact that I never once failed to be taken up on my offer, I would wonder if my system was as good as it ought to be. I am just wondering where and when is this merry-go-round on interest rates going to stop these days?

Mr. HARVEY of Indiana. Will you yield?

Mr. OLSON. Yes.

Mr. HARVEY of Indiana. I think that somebody told me that during the Farm Credit Administration marketing procedure, the interest rate the debentures brought in the market usually was about two-tenths of 1 percent in excess of the actual Federal offering itself. That is, the Treasury offering. Is that correct?

Mr. RITTER. Up until this year, that was correct.

Mr. HARVEY of Indiana. In other words, that has been pretty much a fixed pattern. I think, probably, that may be an answer to your question, Mr. Olson.

Mr. OLSON. That is more information than I have received so far. You said, up until this year. What happened this year?

Mr. RITTER. Will you answer that?

Mr. ALBRIGHT. This year, sir, because of the tremendous competition in the money market, the spread between the Treasury's cost of money and our cost of money has tended to increase. It is now, I would think, in the neighborhood of one-half of 1 percent rather than the one-quarter of 1 percent which prevailed for many, many years. This is a competitive thing.

Mr. OLSON. Just one last question as to the amount of  $3\frac{1}{2}$  million per month—I believe that is your debenture offering; is that right?

Mr. RITTER. \$350 million per month.

Mr. OLSON. \$350 million per month?

Mr. RITTER. Yes.

Mr. OLSON. Obviously, you are not a deciding factor in the setting of interest, but you do contribute in determining the cost of money and like everyone else you deny any responsibility for this question as to the cost of the money.

Mr. POAGE. I just want to comment on what Mr. Olson has been talking about. That was the point that I was discussing with a representative of the bank before we started this morning. I was pointing out that it seemed to me that their present procedure operates as a ratchet; in other words, that the general rate of interest is going up, so the banks have to offer an increase in their interest rate, just as Mr. Olson pointed out, and that contributes to this high interest. It does not control, but it is a contributing factor in determining what the interest rate is going to be next month, because the higher people offer to pay the higher the general level will go, and when you put \$300 million worth of debentures on the market at an attractive price, you tend to force other people to raise their interest rates, and as they raise their interest rates that, in turn, raises the general level of interest rates, so that next month when you come into the market and offer more, you have to pay a higher rate. That is the situation in which they are now. I do not see any practical alternative than to give them the right to go above the 6 percent, but I would like for them to stop this "bidding up" the interest rate.

Like Mr. Olson, I think that the banks ought to give serious consideration to fixing an interest rate probably not to exceed 6 percent,

plus the ability of discounting your paper at such a figure, so that it would move into the market. That would, as I see it, remove this effect that you now have on the market.

There is not anything at all to keep you from selling your debentures at a discount, is there?

Mr. RITTER. Yes, sir. We think that we would not be permitted—if this present statutory ceiling continues, the 6-percent ceiling, we think that we would not be permitted to fix a 6-percent rate on the issue and then sell the issue at a discount, in order, for instance, to give the purchaser, in effect, a 6.5 percent return.

Mr. POAGE. That is just the question I am asking. You think that the present law prohibits you from discounting?

Mr. RITTER. I do. In the case of municipals, there are cases both ways. I believe that the Treasury in their case—that there has been an earlier opinion that they could do that, but they have never done it, as a matter of policy.

Mr. POAGE. You say “municipals.” Most of them do sell at a discount, do they not?

Mr. RITTER. The cases go both ways. It depends to some extent on how specific the statute is, as to the ceilings that are specified. Some may even specify without discount, and so forth.

Mr. POAGE. There is nothing of that kind in your statute, is there?

Mr. RITTER. Our statute has the bare words “Not exceeding 6 percent per annum.”

Mr. POAGE. Yes.

Mr. RITTER. Those are the words that the resolution before you would repeal.

Mr. POAGE. I understand that. What I am saying is that there is nothing in your statute that says that you cannot sell at a discount, is there?

Mr. RITTER. We are hoping that we will not be faced with that question here, because of the removal of the limitation, but we had this, you know, in 1959, when there was a 5 percent limitation on the interest rate that could be paid on Federal land bank bonds, and then we were faced with it, and the conclusion was, as I gave it to you, that they could not be issued at a discount.

Mr. POAGE. Let us depart from the question of what you can do and think about what you should do.

Does not the fixing of the interest rate by discount, rather than otherwise, enable you to exactly follow the market?

Mr. RITTER. I am not sure I understand that.

Mr. POAGE. I mean, if you offered debentures at 6 percent or at 5 percent or at 2 percent or any other percent—if you offered them at 6 percent, would you not then be able to exactly follow the market by accepting discount and premium bids? If the market required 6.3 percent to move your debentures, then you would discount your 6 percent debentures enough to bring a 6.3 percent return? On the other hand, if the interest rates were to fall and you could move your debentures for 5.5 percent, then you would get a premium on your debentures, would you not?

Mr. RITTER. Well, we do some of that now. We do that in the other banks, do we not?

Mr. POAGE. We do it where?

Mr. RITTER. Let me say that the procedure is that 2 weeks before the issue, you set the interest rate, as it were, then you later set what we call the price, whether they would be sold at a discount or not a little later and close to the actual delivery date. So then you could do what you say, I mean, assuming that we are not faced with this 6-percent limitation. You could price them a little above or below par if the market on that later date seemed to require it. But sooner or later you have got to freeze up, and your offer is made, and the purchaser will either buy them or not.

Mr. POAGE. I understand that. But by using the discount as a premium device, you would not necessarily lead the market up, up, up each month.

Mr. RITTER. We use that procedure for other bonds and debentures, not for these.

Mr. POAGE. Why do you not use it for these?

Mr. RITTER. When we said we could not, we were talking about discounting when you are against the statutory limitation.

Mr. POAGE. You have not been up against the statutory limitation until this month. You certainly have not been up against the statutory limitation any time in the past, but you have been leading the market up, if I understand it. In other words, you have contributed to the inflation that is hurting the country, because you have deliberately raised the interest rate a little bit above the market each month. I do not mean that you have gone out and raised it 2 or 3 percent, but you have raised it two points above the market in order that you might be sure that your debentures would sell. And each month you have raised it a little higher than you thought the market was or would be. Is that right?

Mr. RITTER. I would like to take exception to "a little higher than we thought the market was," because the effort is to hit it right on the nose.

Mr. POAGE. Well, but in order to get it right on the nose, you have always put it high enough so that you thought your debentures would sell. And, as Mr. Olson explained, you had never undersold the market; that is right, is it not? You have never in the whole history of your organization underguessed the market one single time? You have, however, surely overguessed it in a great many occasions, because no human being nor group of human beings can ever hit that market exactly. If they could, you would not be working for the Government. You would not be sitting here before us. You would be up in New York City controlling this great maze of finance the world over. You cannot do that, however, and neither can anybody else—that is, hit that market everytime. So, you have overguessed the market most of the time. That is obvious, is it not?

Mr. RITTER. Well, without debating that, I would like to put in a disclaimer.

[Laughter.]

Mr. RITTER. Because they think they have gotten pretty skillful at it and that they guess it just about right. That is their effort now.

Mr. POAGE. I know that, but they have never underguessed it one single time. Am I right in that? Is that not right?

Mr. RITTER. Well, I think—I cannot give you the examples now, but I would say they have underguessed on those occasions when the dealers took their allotments and were not able to find buyers for

them immediately, so that it meant that the dealers had to carry them for a while. So that if you prove it by the fact that the public did not pick them up and bought them, if you prove that, you underset the interest rate. We have had that happen.

Mr. POAGE. Did you have it happen; or did the dealer have it happen?

Mr. RITTER. When the offer is made, the dealer commits himself for a certain amount, and in some instances they have had to hold some of those for a while before they could put them in the hands of the purchasers.

Mr. POAGE. There is where some people make their business; is it not?

Mr. RITTER. If I understood what you were saying, the interest rate was so low in those instances that it was not attractive enough.

Mr. POAGE. It was not attractive enough the next day to enable him to make a profit on it, but it was attractive enough so that he took it on the day that you made the deal with him.

Mr. RITTER. But the next day he found——

Mr. POAGE. And the next day he found that the interest rate had gone down. That happens, of course.

Mr. RITTER. No; it may not have been. The next day, he found that he could not sell them at par at the interest rate that was set, so that in that case we undershot.

Mr. POAGE. In that case, you what?

Mr. RITTER. In that case the interest rate was not fixed too high, but if anything it was on the low side, where the dealer was unable to move them immediately.

Mr. POAGE. The dealer would not have taken them if you had fixed it below the market price. The dealer did not take those debentures at less than the market price, did he?

Mr. RITTER. He must use his judgment, but he does it really no better than the people who fixed the rate.

Mr. POAGE. But on that day that was the market, was it not?

Mr. RITTER. It was set, and it was set to be appropriate to the market, but you do not test the market until you actually test it by placing it in the investors' hands.

Mr. POAGE. That is a pretty fine point. But certainly should you not remove this increase to whatever extent that it affects the market? Could you not remove it by using a discount-premium bid basis, rather than by fixing it in advance at a higher rate?

Mr. RITTER. I want to say it again, from information I have received here, that the credit banks have not been doing that except under certain conditions. In other systems, there has been some of that, but they set the interest rate at an earlier date and then a little closer to the delivery date; they decide whether they will sell at a discount or at a premium. We do some of that. This is not being done in the case of the Federal intermediate credit banks.

Mr. POAGE. So far as the intermediate credit banks are concerned you set on the 17th day of the month the interest rate for September. You are going to have to look at the money market then and say "This is going up a little bit; we think that we could sell those debentures at 6 percent, probably, this morning, but by the time they are out on the market, it will probably take 6.12, it may even take 6.15 to move

them, and in order to see that they move, we have got to put our rate at 6.15 percent. That is about the way you figure, is it not?

Mr. RITTER. Yes, sir, not only that—

Mr. POAGE. There is nothing wrong with that, except this: that the day that they go on the market—we will assume the interest rate is still 6 percent—you offer 6.15 and that forces everybody else's interest rate up comparable to 6.15. Of course, as I understand, this company out in east Texas would have to pay a great deal more than you will have to pay—I mean, everybody who has a comparable credit rating will have to pay 6.15 instead of the 6 percent they were paying the day before—that is, the day your debentures hit the market, because that raises the market. It does not go down. It does not go down, because you bring everybody up to your level—because you have offered to pay this higher rate. You did not simply offer to take today's figures. You did not simply offer to take what the market would bring today, but you offered to pay 6.15, so that everybody else had to come up to 6.15. They do not go down, and the next month you figure that it will take something more, and so you put a price of 6.25 on your paper, and everybody else has to come up to 6.25. And the thing gets built up and up and up, without ever going back.

Mr. RITTER. What stops that? If money is available. That is a big factor.

Mr. POAGE. That is true. Whenever we get loose money, as it is termed—whenever we get money available, cheaper money, why, of course, then all of these things go down, but right now what you are doing, as I see it, is causing this interest rate to just inch up a little bit each month.

The CHAIRMAN. Do you think that this administration has influence enough in this great country of ours to fix the interest rate throughout the country for all others?

Do you feel that?

Mr. POAGE. What I am saying is that when you put \$300 million of debentures on the market—

The CHAIRMAN. I am following you.

Mr. POAGE (continuing). That you very seriously influence the market. Everybody else has to come up to that figure.

The CHAIRMAN. That is a small amount of money compared to the general money market. I do not think it is enough to influence the market unduly. Do you think so?

Mr. RITTER. No, sir; we have not felt so.

The CHAIRMAN. As I understand it, I thought that we were going to get this subject out of here without much fuss about it.

Mr. POAGE. I think that we will have to do that, but I am thinking that you ought to be giving some consideration to this method of selling debentures.

The CHAIRMAN. He said that they followed that in some systems.

Mr. POAGE. What we are talking about is the intermediate credit banks which do not follow it.

Mr. BELCHER. Will you yield?

Mr. POAGE. Yes.

Mr. BELCHER. I am not a financial expert in this to any degree, but I thought that the banks had something like a 5-percent ceiling.

The CHAIRMAN. They have had something like 5.5 percent in recent months.

Mr. BELCHER. Somebody told me that it was 5 percent.

The CHAIRMAN. It was 4.5 percent at one time, but I understand it is now 5.5 percent.

Mr. BELCHER. You cannot go to a bank and get 5.5 on your savings, can you?

Mr. RESNICK. It depends on the amount.

The CHAIRMAN. There is a bill that fixes it at 4.5 percent up to \$100,000.

Mr. BELCHER. As a matter of information, have those who are really competitors on this, been notified of this bill?

Mr. POAGE. All are competitors.

Mr. BELCHER. Everybody is trying to compete for money. I know that those building houses are positively crying for money, and they just cannot get the money.

The CHAIRMAN. They perhaps are interested in this homeowners bill—two bills, I understand.

Mr. BELCHER. What do they know about this bill?

Have they had an opportunity to be heard on this particular bill, or do they not care to be heard on it? Maybe it does not make any difference. On a bill like this, with the tight money situation as serious as it is, it may affect many people.

The CHAIRMAN. Let us go off the record.

(Discussion was had outside the record.)

The CHAIRMAN. Back on the record.

Mr. STALBAUM. I am curious as to this: When you moved away from the spread that Mr. Harvey made reference to, the two-tenths of 1 percent over the regular Government issues. This was true up to this year. When did you start to widen that spread?

Mr. ALBRIGHT. That began to occur gradually. I would say about last fall, when there began to be more and more what we call Federal agency securities offered in the market. You are aware, I am sure, of the increasing volume of Federal agency financing, the Federal Home Loan Banks, FNMA, and other Federal agencies. The supply of such securities has increased tremendously this year, which means that there is more of that kind of paper available than there is of the Treasury's obligations, relatively speaking, which has operated to widen the spread in rates.

Mr. STALBAUM. In other words, then am I right in assuming that each of these agencies is tending to widen the spread slightly to get a little competitive advantage over the other agencies in selling their debentures?

Mr. ALBRIGHT. There has been, as Mr. Poage referred to a while ago, a kind of ratcheting system operating in the market this year because of the fact, of course, that there is a demand for credit which is running far ahead of the supply of funds available.

Mr. STALBAUM. As to your relationship with selling debentures with other governmental agencies, has there been the same ratcheting effect happening there?

Mr. ALBRIGHT. I think to some extent, yes, sir.

Mr. STALBAUM. That is all.

Thank you very much.

The CHAIRMAN. Mr. Resnick?

Mr. RESNICK. Regarding what Mr. Belcher said, this one bill that we have up now, I believe FNMA, is going to go into the market with

some \$2 billion, if I am not mistaken. What interest rate will they go into the market at? Will they go in at the same rate that you have been going in at?

Mr. RITTER. No, not necessarily. I mean they will determine that.

Mr. RESNICK. What rate do you think they will get?

Mr. RITTER. I would not say, unless Mr. Albright would say.

Mr. RESNICK. I would just like to know.

Mr. ALBRIGHT. I would venture an opinion that they would have to pay somewhat more for this obligation than the Farm Credit Banks.

Mr. RESNICK. In other words, they are going way above the 6 percent?

Mr. ALBRIGHT. It is quite possible.

Mr. RESNICK. Do they offer it under this same 6 percent limitation?

Mr. ALBRIGHT. No, sir.

Mr. RESNICK. They have no limitation at all?

Mr. ALBRIGHT. I do not know.

Mr. RITTER. We do not know what their limitation is, but the limitation that applies to the credit banks does not apply to anyone else.

Mr. RESNICK. In other words, all of these other governmental agencies can pay what they want, what the market is, and the one specifically limited then is the farm credit banks?

Mr. RITTER. It is the only limitation I have in mind. Now, whether there are limitations on those others, at the moment I just do not know about them.

The CHAIRMAN. Are there any further questions?

Mr. HARVEY of Indiana. I have just one question that I want to pose here, and that is, as I read this proposal, it would take the ceiling off completely. Is that right?

The CHAIRMAN. Yes.

Mr. HARVEY of Indiana. I am realistic enough to know that whatever we should do, if we were to write another ceiling in there, it would not necessarily control the money market; in fact, it would not at all, except that it does seem to me that for whatever psychological value it might have, it is a subject that we ought to give some thought to. I can visualize some of the financial publications saying that the intermediate credit banks have taken all ceilings off their debenture offerings; that is, the limitations as to the rates that will accompany the debenture issues, and I am wondering if we ought not, Mr. Chairman, to give some consideration to taking the ceiling clear off or whether we ought to simply raise the present ceiling?

Mr. POAGE. Will you yield?

Mr. HARVEY of Indiana. Yes.

Mr. POAGE. I would suggest that we ought to take it clear off. I have never approved of Chairman Mills' policy of cutting the dog's tail off an inch at a time. I thought that we should act in the beginning so that you did not have to act 3 months from then.

I think there are two other considerations: One is whether it is basically getting the results you think it will get. I am inclined to fear—and I cannot prove this, it is just a guess—that if you raise this limit to 6.5 percent or 7 percent it would be looked upon as a floor and would tend to become a floor rather than a ceiling. On the other hand, the other members of the farm credit system, to wit, the land banks and the banks for cooperatives, do not have any ceiling at all, as I recall it now.

Mr. RITTER. That is right.

Mr. POAGE. It seems to me to be highly desirable, in the interest of getting an orderly farm credit system going, that we apply the same rules across the board as far as they are applicable, and it seems to me that it is really applicable in this case. And if we are going to have a 7-percent rate on the banks for cooperatives, this ought not to go above that, but I think that the other two segments of the farm credit system, since they do not have any limits at all, it seems to me that there is not much justification in putting any limit here. That is one of the reasons that I thought we would be justified in taking this ceiling off.

Mr. HARVEY of Indiana. Let me say that I concur with your views, Mr. Poage, on this. I would not, and did not raise it for that purpose. I thought that it was a point that ought to be understood by the committee, because it will be the subject of some question, and I would like to ask the witness if he concurs in that same viewpoint?

Mr. RITTER. Our position would be in line with Mr. Poage's position just expressed.

Mr. HARVEY of Indiana. In other words, you concur in Mr. Poage's viewpoint?

Mr. RITTER. Yes, sir.

Mr. HARVEY of Indiana. That is all.  
Thank you.

Mr. BELCHER. What effect would this have on the Federal land banks, would it raise their interest rates?

Mr. RITTER. No, sir; we would not see any such effect.

Mr. STUBBLEFIELD. The procedure is that you set the rates and it is a matter of take it or leave it?

Mr. RITTER. Yes, sir.

Mr. STUBBLEFIELD. Is that correct?

Mr. RITTER. Yes, sir.

Mr. STUBBLEFIELD. Under Mr. Poage's suggestion, these debentures would be put up for sale at either a premium or a discount, in which case it could be more or less.

Mr. RITTER. That is a possibility. At different times, studies have been conducted as to whether there should be a change in the present procedures of marketing securities. That has been considered, but it has not been adopted.

Mr. STUBBLEFIELD. In your opinion, which procedure is the better procedure?

Mr. RITTER. Well, I believe that I would say that their present judgment is that their present procedure is appropriate. That does not foreclose further study. They do study this matter continuously.

Mr. STUBBLEFIELD. Thank you; that is all.

Mr. MATSUNAGA. By deleting the 6-percent ceiling as it now appears in the statute, there would not be any limitation, would there?

Mr. RITTER. There is a limitation. That is, if you delete this limit the interest rate will be fixed by the issuing banks, subject to the approval of the Farm Credit Administration and then overriding that is the market. So, the market will control it.

Mr. MATSUNAGA. You have not given it too much study, you said, or have you given study to the suggestion by our vice chairman, Mr. Poage, as to selling it by discount rather than by an increased percentage rate?

Mr. RITTER. Yes, sir; that has been studied within the Farm Credit Administration and among the groups of the different banks.

Mr. MATSUNAGA. And you prefer this method of removing the percentage limitation?

Mr. RITTER. Yes, sir, that is the present position.

Mr. O'NEAL. I would like to ask this question. I am certainly not a financial expert. I probably will show it by my question, but I do not understand how the market could be a limiting factor when the market wants all it can get. It wants all of the interest it can get, does it not?

Mr. RITTER. There are times when money is available for investment, and in those cases the effect is downward.

Mr. O'NEAL. It would not be a limiting factor right now, would it?

Mr. RITTER. Well, maybe I should not use the word "limiting," but the rate would be determined at what the market requires in order for the debentures to be marketable and salable.

Mr. O'NEAL. That is all.

Thank you.

The CHAIRMAN. Are there any further questions?

If not, we will go into executive session.

(Whereupon, at 11:30 a.m., the committee retired into executive session.)





