Federal Reserve Board Oral History Project

Interview with

Frederick M. Struble

Former Associate Director, Division of Banking Supervision and Regulation
and Former Deputy Associate Director, Division of Research and Statistics

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Interviewers: Michael Martinson and Myron Kwast

Federal Reserve Board Oral History Project

In connection with the centennial anniversary of the Federal Reserve in 2013, the Board undertook an oral history project to collect personal recollections of a range of former Governors and senior staff members, including their background and education before working at the Board; important economic, monetary policy, and regulatory developments during their careers; and impressions of the institution's culture.

Following the interview, each participant was given the opportunity to edit and revise the transcript. In some cases, the Board staff also removed confidential FOMC and Board material in accordance with records retention and disposition schedules covering FOMC and Board records that were approved by the National Archives and Records Administration.

Note that the views of the participants and interviewers are their own and are not in any way approved or endorsed by the Board of Governors of the Federal Reserve System. Because the conversations are based on personal recollections, they may include misstatements and errors.

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MR. MARTINSON. Today is Monday, August 17, 2009. I am Michael Martinson, a retired associate director in the Board's Division of Banking Supervision and Regulation. I'm here at the Board with Myron L. Kwast, a retired associate director in the Division of Research and Statistics. As part of the Board's Oral History Project, we are interviewing Frederick M. Struble, also a retired associate director in the Banking Supervision and Regulation Division. He also worked in the Board's Division of Research and Statistics and was deputy associate director of that division. Fred worked at the Board from 1969 to 1996.

Let's start with what brought you to the Board.

Early Years at the Board

MR. STRUBLE. When I completed graduate school at the University of Colorado working on a Ph.D., I needed a job. The Kansas City Federal Reserve Bank was interested in interviewing somebody from the University of Colorado, and so one Sunday morning I drove to Denver from Boulder to meet Lyle E. Gramley at the airport. And, for reasons I don't know entirely, he was sufficiently impressed to invite me to Kansas City for an interview with the Kansas City Reserve Bank. It was my good fortune to get a job offer from the Bank that I accepted. I worked there for seven years as an economist. Then someone at the Board called and asked me to interview for a job there. I went to Washington and was offered a job that I accepted. That was in 1969.

MR. KWAST. So William McChesney Martin was still the Chairman?

MR. STRUBLE. William McChesney Martin was still the Chairman.

MR. KWAST. Do you remember anything about how the Board was run at that time?

MR. STRUBLE. I was rather far down in the ranks, so I knew little about the policy questions that were being discussed. I was first assigned to the Banking Section. There I worked on that section's drafts for the Greenbook that discussed recent banking developments, on Monday morning briefings for the Board, on drafts of letters responding to inquiries from the Congress and the public, and on various special projects.

That's about all I remember, except that the work atmosphere was considerably more relaxed than it subsequently became. For example, it was routine for members of the staff to take a break in the middle of the morning and the afternoon, most times by retiring to the cafeteria. That luxury, as you know, did not last long.

MR. KWAST. It wasn't too much later that Arthur F. Burns became Chairman.

MR. STRUBLE. Arthur Burns came in 1970. Chairman Burns was a bit more contentious and put a bit more stress on the staff than Chairman Martin did. Chairman Martin was very gentlemanly about matters when he asked questions; Chairman Burns sometimes skewered you if you didn't know the right answer.

MR. KWAST. Do you remember anything about what the Fed did under Burns or people that stood out?

MR. STRUBLE. With the Vietnam War accelerating and the Great Society program in full swing, budget deficits ballooned and inflationary pressures increased. One result of all this was the introduction of "Whip Inflation Now," the price control program introduced by the Nixon Administration. Chairman Burns participated in its formulation.

MR. KWAST. We're sitting in Stephen H. "Steve" Axilrod's old office. Would you talk about the relationship between the staff and the Board in those days? Did Steve become really powerful under Martin or under Burns?

MR. STRUBLE. I think J. Charles "Chuck" Partee had this office after Burns came in. He was promoted to managing director of the Office of Managing Director for Research and

Economic Policy, a new position. Robert C. "Bob" Holland had been executive director of the Office of Executive Director and then was appointed to the Board. Chuck took over from him under the new name.

At that time, Steve Axilrod took over this office in the Board building and Chuck's job as staff director of the Office of Staff Director of Monetary Policy. Steve was responsible for lots of things, but primarily he oversaw the production of the Bluebook, which was a main document used by the FOMC (Federal Open Market Committee) in specifying monetary policy directives from meeting to meeting. I participated in this preparation along with six or seven other people. We worked first on a summary of money and bond market developments since the previous FOMC meeting. Then there was a second section that provided our staff forecast of what would happen to the various measures of the money supply and to conditions in the short- and long-term debt markets under alternative possible decisions of the FOMC—that is, alternatives of no change in the fed funds rate and reserve targets or an easing or tightening of these targets. Steve was very much in charge of this formulation of the Bluebook to the extent of approving every word in its text. At the subsequent meeting of the Committee, Steve would make a presentation explaining and defending the staff's (really his) projections.

When I first started coming to these staff meetings, I was thrilled to hear all this fancy stuff. Darwin Beck and Edward R. "Ed" Fry, in the Banking Section, did most of the work in setting down the preliminary scenarios forecasts. They did this by looking at records of how the variables—interest rates and money measures—had performed in previous times, taking into account, in addition to cyclical forces, such seasonal factors as holidays, tax payment dates, et cetera. These were strictly "judgmental" forecasts, meaning they did not have a fixed model of variables with fixed weights that they referred to each month. These forecasts were primarily used when I first started attending the meetings.

Soon thereafter, however, the Board began beefing up its basic research capabilities and hired a good number of additional economists trained in econometrics and formal monetary theory. I remember that James L. "Jim" Pierce and Thomas D. "Tom" Thomson began coming to the meeting and offered projections on the key financial and monetary variables based on formal econometric models. So reference was then made to Darwin's and Ed's predictions and those of the econometric models. Well, it turned out that Darwin and Ed weren't too bad at it! [Laughter] In fact, they almost always beat the models. Once a quarter or maybe every half a year, Steve would ask for an evaluation of the accuracy of the models, and mostly Darwin and Edward did better than the econometric model. If I remember, it got to the point that, about two or three days before everybody was to come in and present their predictions, the guys doing the models would call up Darwin and Ed and ask them, "How are you coming out?" After that, there would be a change in the intercept of a model or something, so they came out a little better. [Laughter]

MR. KWAST. So this is the origin of this entrenched—maybe that's an unfair word—system we have now where we have the judgmental forecast and we have the model forecast, right?

MR. STRUBLE. I think that's right.

MR. KWAST. When I came here, it was already a well-established system that you had two forecasts, the model and the—

MR. STRUBLE. But the judgmental was there obviously before the econometric, because econometrics was just coming into its own at that point.

MR. KWAST. Right, but the judgmental forecast was just two guys, basically.

MR. STRUBLE. Well, that is not entirely accurate, because Steve would impose his own judgment—that is, he didn't automatically adhere to either the judgmental or the econometric projections. And, of course, we are talking here of the Bluebook projections, and there were the projections on the nonfinancial economy presented in the Greenbook, which were initially judgmental before becoming the product of both the judgmental and econometric models.

Working in the Division of Research and Statistics

MR. KWAST. Do you remember how your career progressed in research?

MR. STRUBLE. Well, I started at the Board in the Banking Section. I was there for two or three years, something like that, and then I moved to the Government Finance Section, which was when I got involved in the Bluebook preparation. The Government Finance Section was involved because, in part, it was responsible for monitoring developments in the money and bond markets and the activities of the New York Fed in achieving the targets for the fed funds rate and reserves specified by the FOMC. Steve Axilrod used to have a conference call every morning with Peter D. Sternlight or one of his assistants who were responsible for managing the New York Bank's trading desk. The talk would be about what the New York Fed was going to do that day in order to get the money markets to behave in accordance with the guidance that the FOMC had given.

I was with the Government Finance Section, and half of our job there was to keep track of the government securities markets, the Treasury financing in the market, and the Federal Reserve's activities in trading and securities and in the federal funds market. The other half of the Government Finance Section dealt with the fiscal policy of the federal government. I was there about a year. Helmut F. Wendel was chief at the time when I first moved. Then Helmut was promoted to an officer, and I was made chief of the Government Finance Section. I was chief of the Government Finance Section for two or three years, and then I became an assistant director. Then two or three years later I was deputy associate director, and that's where I was when I left the research division to go to the supervision division around 1985.

MR. KWAST. How did the role of economic research in providing policy advice to the Board evolve over time?

MR. STRUBLE. As I indicated, for a long time, policy advice was based on the judgment of the senior staff in the division who formed these judgments by drawing on their education in economics, their subsequent readings of the professional literature, and their consultation with outside economists, bankers, and businessmen. Then, when the research staff was enlarged by the addition of basic research sections, they began to have an important influence in the process.

The basic economic research people produce many papers for journals and conferences. But, at the same time, they were very interested in having an input into the decisionmaking process of the FOMC. So, as I have said, they immediately began coming up with models to predict what was going to happen in the economy, the interrelationship between what the conditions in the financial markets were going to be, and the impact that was going to have on the real economy. I think it was fairly soon after these guys came that they became an integral part of the advice given to the FOMC.

At the same time—I wasn't always involved on the real side of the prediction—the final projection offered to the FOMC was "judgmental" in essence, in that the staff director took into account both the forecasts of the econometricians and the judgmental staff but relied on his assessment of information available to him. Lyle Gramley is very good at forecasting to begin with, and he was working out some of the projections. And, of course, Chuck Partee was excellent. He was bright, intelligent, and very capable. He would oversee the final Greenbook projection of what the economy was going to be doing and how it was going to be. Well, that was originally. When Lyle became the division director, I think that continued the same way. James L. "Jim" Kichline was the director after Lyle. And he, too, had an impressive ability to come up with sensible staff projections based on the work of both the judgment and econometric staff. That is not to say, of course, that these projections always turned out to be accurate. Then as now, there was good conformance between projection and actuality until some unforeseen and unusual development brought on unexpected and unwanted surprises.

MR. KWAST. Yes, then Michael J. "Mike" Prell became the director. Let me ask you: Did Arthur Burns, who was a former professor, demand economic research? I guess what I'm asking is, how did the process get started? Did Burns, as a former professor, demand that sort of thing?

MR. STRUBLE. I don't think so. He might have certainly acquiesced to it, encouraged it, but I think it was more that the economics profession was progressing and the econometrics was coming into its own. It took 10 years, to the end of the 1970s, before it really became anything of any great significance.

MR. KWAST. And once we had computers, we could actually run some.

MR. STRUBLE. Yes, right. But I don't think it was just that Burns came in and said "I want this," because I had the impression that he was not all that enthralled with econometrics. He was very much a data-oriented person, having come from the National Bureau. But I don't think he was an advocate, or least not a strong advocate, of mathematical models.

Transition from the Division of Research and Statistics to the Division of Banking Supervision and Regulation

MR. MARTINSON. What prompted your move from the research division to bank supervision?

MR. STRUBLE. William "Bill" Taylor called and asked me if I would like to work in the supervision division, and I said, "Yes." That meant a promotion, and so I went. Now, how did that happen? Before I moved, Bill and I worked together on the silver bubble, the Hunt Brothers crisis, the futures markets, and all that sort of stuff. The financial futures started coming in, and the Treasury bill futures and the Treasury bond futures, and whether that was a good idea or not was a big issue when it first started out. I was involved in government finance and in financial markets in general, so it fell pretty much to me to look into this.

There were some guys over at the Treasury Department, too, that I worked with. I knew some people on the CFTC (Commodity Futures Trading Commission) staff. I also knew people at the Chicago Board of Trade and the Mercantile Exchange. I'd even been out with Roland (for the life of me I can't remember his last name) from the Treasury Department for a day's introduction to futures markets and how they perform. So I had some exposure to the futures issues and to the futures market. When the Hunt Brothers crisis flared up, Chairman Volcker said, "This is not a job for Struble. This is a job for Taylor, but Struble can go along and introduce Taylor." [Laughter] Now, that's not too far from the truth, I think. So Bill and I worked together there.

The other thing was that I used to sometimes play Governor when the visiting bankers associations came in for a discussion of the Fed's policies and activities. I didn't know a damn thing about supervision, and I'd always call Bill and say, "Will you please come so I don't have to display my ignorance?" So we had a little connection there, too.

I interviewed in banking supervision. I went to see John E. "Jack" Ryan [the director]. I don't think he was exactly enthralled with the idea of my moving over to banking supervision, but Bill Taylor [who later became the director] was a pretty powerful personality, and he'd made up his mind that he wanted me to come, so that's what happened.

MR. KWAST. Fred, I got involved with you on a financial futures and options project.

MR. STRUBLE. Right, indeed.

MR. KWAST. Was that before or after you went to BS&R (Banking Supervision and Regulation)?

MR. STRUBLE. It was before. That was 1984. The study was published at the end of 1984, and then I moved over to BS&R in April or May 1985.

Hunt Brothers Silver Crisis

MR. MARTINSON. Some thought the Fed's involvement in the silver crisis was odd. Do you have any recollection of why the Fed was involved?

MR. STRUBLE. Well, it was potentially a destabilizing financial development. Paul Volcker was the Fed Chairman, and the Fed generally gets involved in damn near anything that comes along that touches on finance. And finance was most surely involved because the Hunts had financed a substantial proportion of their silver acquisitions with loans from banks. At the time, the CFTC was not thought to be experts with financial matters; its traditional expertise was in agriculture and other commodities. I think Volcker and the Treasury Secretary thought the Fed should look into it and be very much involved in it, and we were. Bill Taylor took over an awful lot of the investigation. I always wondered about what the Hunt Brothers were doing. It's against the law to corner a market, I think, so why would you try to do it, because if you're successful, you go to jail! [Laughter]

MR. MARTINSON. Once "the powers that be" intervened, they turned the market around on the Hunts.

MR. STRUBLE. Right. It was the silver bubble, but remember, it was a gold bubble, too. Gold was going up like mad in price, but it wasn't a concentration of activities by any one or two people, like the Hunts were involved in.

Crisis Management

MR. KWAST. When I left the Board, we had this staff umbrella group on financial stability. We were starting to organize ourselves to have a group of crisis managers that were expected to be able to step up and do things depending on the type of crisis. But my recollection from my early days—and you were there long before I was—was that it wasn't anything close to that. The people who got involved in crisis management were much more of an ad hoc group, and it was more personality dependent.

MR. STRUBLE. Well, it was also dependent on their position. For example, somebody that was the head of supervision or the associate director of supervision, as Taylor was, would naturally be called upon to do some things in a crisis situation. I think it was ad hoc because there were only a few little events along the way. They all look like chump change compared to what we've had recently. My impression was that probably the director of research or the director of supervision would say, "We need to put somebody on this." Then they would pick somebody that they thought would be pretty good at dealing with the problem and tell them to coordinate things. And I think that worked pretty well. There was cooperation among the divisions. It was a pleasure to work here, because everybody pretty much tried to do what they thought was the best for the country.

William "Bill' Taylor

MR. MARTINSON. When you moved over to bank supervision, Jack Ryan was the director. Then, later, Bill Taylor was the director. Tell us about Bill.

MR. STRUBLE. There's no question that Bill Taylor was one impressive man. He could surprise you. He could be just as sweet as pie and so damned nice to you it wasn't funny, but if you didn't do something right, he could blow up, too. When he was unhappy, you knew Bill was unhappy, and he was not reluctant to say that. I never got a scolding word from Bill Taylor for two years. Everybody else had—Stephen C. "Steve" Schemering and others. And I kept wondering, "When is my day coming?" [Laughter] I can't remember the issue, but one day I'd been over at the OCC (Office of the Comptroller of the Currency), and I said, "I got it all worked out with the OCC and the FDIC (Federal Deposit Insurance Corporation). We're going to do it this way." And, wham, I got it from Bill over the telephone. I'm sorry I can't remember the issue, but I soon realized that was not the way to solve this problem.

The other thing I remember about Bill is that he was always saying, "Check this." He was always sensitive to whether something could go wrong, or whether something was wrong and something needed to be done to fix it. I don't know that he was always ahead of the curve, but he was able to respond to the curve rather quickly once the problem arose and became manifest.

We used to have war rooms. On Saturday and Sunday, Bill would set up a room. We would keep track of what was happening at the various banks in distress or whatever the heck was going on, and there'd be about eight or nine of us in there. It added a little zest to the job, because you thought you were involved in something big. Bill would come in, and that added to the intensity of the gathering. We'd be working until 6:00, 7:00, or 8:00 at night or later many times. That was the way Bill handled things.

I also remember that he was a past master at dealing with Chairmen. He was very close to Volcker and to Greenspan. On many nights, around 5:30 or so, Bill would head over to the Chairman's office to spend a half hour to 40 minutes talking. What the heck they were talking about, I don't know, but he would go over to do that. Then, about a year or so before he moved over to the FDIC, when all those crisis situations were going up, Bill would be over at the Treasury Department sitting in with the Secretary of the Treasury, meeting with him for a half hour to 45 minutes. I recall the day he came back and said to me, "They're going to offer me the FDIC chairmanship." He was surprised, because it was unusual for a staff member to move over to the FDIC. But, my gosh, in a couple of weeks, he was over there.

Savings and Loan Crisis

MR. MARTINSON. Do you remember particular problems that you dealt with when you were in banking supervision?

MR. STRUBLE. The savings and loan crisis was a fairly big problem. FIRREA (the Financial Institutions Reform, Recovery, and Enforcement Act of 1989) established the RTC (Resolution Trust Corporation). When the crisis first began, there was a heck of a lot of concern about the dimensions of the problem and how to handle it. But once the Congress decided to establish the RTC, the resolutions went pretty smoothly. At the time, about $125 billion worth of assets were disposed by the RTC. Is that what you remember?

MR. KWAST. My recollection is that total losses were on the order of $125 [billion to] $130 billion. I think they disposed of a lot more assets than that.

MR. STRUBLE. Yes, that's probably right.

MR. KWAST. Four or five hundred banks and savings and loans a year failed there.

MR. STRUBLE. I remember Greenspan and, I think, the other members of the Board, the RTC Board, and the [RTC] Oversight Board, had said at the very start, "We're not going to sit here and speculate with these assets.[1] We're not going to hold them until we can get a good price. That's not a good way to do this thing. We're going to liquidate them as quickly as we can get a reasonable market price. We're going to sell it." And they pretty much did that. And at the end of the last [RTC] Oversight Board meeting, I remember Greenspan saying, "This has been a rather remarkable achievement. We have disposed of this huge volume of assets, and there's been no fraud, no known underhanded dealing or any of that." I don't think any evidence has come to the fore that would contradict the Chairman's assessment. So it was a reasonably successful effort, even though the generation of the problem was not the finest hour for American financial supervision.

Recall that interest rates rose sharply in the early 1980s, and that created great strains on S&Ls in general and many commercial banks because of Regulation Q restrictions on deposit rates. Then, when restrictions were lifted and strains changed from deposit losses to rising deposit costs, great latitude was given to S&Ls in their asset acquisitions. And the problems of the S&Ls spilled over to the banks as, under the influence of "heady" times, they joined in the process of financing real estate activity, particularly of the commercial variety.

Commercial Real Estate Lending

MR. KWAST. Were you in research or supervision when you gave a briefing to the Board on the state of commercial real estate?

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[1] Editor's note: Chairman Greenspan served as a member of the RTC Oversight Board (later renamed the "Thrift Depositor Protection Oversight Board"), which was established under the 1989 FIRREA legislation to oversee RTC management of failed thrift institutions and related asset sales.

MR. STRUBLE. I was in supervision.

MR. KWAST. I remember you pointing out that vacancy rates were high, and that many banks had invested a large percentage of their portfolios in commercial real estate. And I think the implication of your briefing was that the Board should take some action to restrain commercial real estate lending. But my recollection is that the Board didn't do anything. And my question applies to the current crisis as well. What is your sense of the main constraints that the Board members feel in being proactive to constrain something that they see as an imbalance in the economy but which, at the time, is a big profit-making operation for a bank, be it the broker deposits, or commercial real estate, or residential real estate?

MR. STRUBLE. That briefing was to reinforce Bill Taylor's stance on this whole matter. I don't know what Bill was saying to the Chairman, but he had stated in Board briefings that he was concerned about the potential problems posed by developments in the real estate markets. The purpose of my briefing was to reinforce Bill's message by providing hard data on the matter.

Those were very speculative times. Let me illustrate. About eight or nine big Texas bank holding companies had failed and been bought up by North Carolina National Bank and a bunch of others. They were brought down by excessive real estate exposure, primarily. So when representatives of Boston banks would come in, after the Texas problems were clearly apparent, we'd say, "Are you noticing what happened down in Texas?" Bill used his moral suasion, and when they came in, the rest of the staff would beat up on these guys and say, "You saw what happened." But they just continued right on, because the deals looked so good and the profits looked so good. Soon, the Boston banks were experiencing the same problems, from which some failed and others barely missed doing so. What are you going to do? It's a free country.

You could put an injunction on them or something, but that takes a lot of power. The Fed didn't have such power then and doesn't have it now.

MR. KWAST. Do you have any recollection of the bankers going through the Congress to try to constrain any sort of supervisory action that the Board might have taken?

MR. STRUBLE. Well, by the time that the commercial real estate market began to cause banks and S&Ls serious problems, the Congress was in the mode of being hard-nosed about financial problems due to errant practices, so I don't think the bankers were able to exert much influence. But I do remember that earlier, when farmers were encountering great difficulties because a bubble in land prices had burst, the Congress placed great pressure on the Fed and other regulators to show forbearance in enforcing regulations and guidelines.

Relationship between the Fed and the Other Federal Banking Agencies

MR. KWAST. What are your thoughts on the relationship between the Fed, the FDIC, the OCC, and the predecessor to the OTS, the Federal Home Loan Bank Board, at that time?

MR. STRUBLE. There was always a little tension among agencies and certainly among the three agencies to some extent. In particular, the OCC was sensitive to its position—this is my interpretation—because the Fed, as bank holding company supervisor, was always concerned with what national banks were doing, while the OCC thought that was its province. The Fed and the OCC supervised the same organization from a slightly different angle, so we were always looking over the shoulder of the OCC, if nothing else. So there was some tension there. And, if I recall correctly, there was the same kind of thing with the Bank Secrecy Act and how to enforce it. I have a feeling that there were times when these disagreements on how to proceed took quite a bit of negotiating and meeting back and forth before finally something was worked out. I might add, and I think I am correct in this—the OCC staff was always a bit put out because the Fed was generally recognized to be the primary regulator of banking organizations.

MR. KWAST. You saw the various phases of the real estate problem, where it went from the savings and loans and the regional banks to finally the big banks at the end.

MR. STRUBLE. Yes. I remember that issues would all of a sudden come up that either had not been discussed or considered very much, like interstate banking. While this was happening, the banks were trying to broaden their powers and broaden their reach in the economy. Then, when the big holding companies in Texas all went under, there was no way for people in Texas or investors in Texas to pick up the pieces. So that made it necessary to allow holding companies in other states to come in and buy up these organizations. Well, once you have done that a few times, you're off to the races—you now have a whole different milieu of what's going to happen.

Supervision and Financial Innovation

MR. KWAST. Your career spanned a huge amount of innovation in the financial sector. We started out with financial futures and options on government securities, but that was just the start of this explosion in innovation. Once you moved to supervision, how did the supervisory process change in reaction to financial innovation? Was it your sense that the supervisors were able to adapt to this change in a timely way, or were the lags too long? Were they too short? Were they just right? It's always an issue of how any supervisor should react to an innovation—either in a positive, negative, or neutral way.

MR. STRUBLE. Well, capital requirements and how to treat futures and options, in accounting terms, took a long time. I don't know where we stand on it today. In a study we did, we said, "Futures and options offer opportunities for hedging against risk. They should reduce risk, so, from a supervisory point of view, you should probably be happy to have them innovated." But for a long time, the requirements were that they had to be marked to market at all times, whether there was a hedge or a speculative position. And, of course, there were issues of evaluating when was a hedge a hedge, because sometimes they could work out something that was not obvious as a hedge. Then there was the aspect of the kind of capital requirements to put on them and on what aspect of it. I think the capital requirements finally were just focused on the counterparty risk part of the process. Mike, do you recall that?

MR. MARTINSON. We put in the counterparty risk, but then we also had a charge on the value-at-risk (VaR) models. But it never really amounted to much, because, at that time, if you looked at them, nobody cared much.

MR. KWAST. That's a huge issue now. The Basel II market risk processes are being radically rethought.

MR. MARTINSON. Once you brought in credit derivatives, that was a whole different animal.

MR. STRUBLE. But the banks had over-the-counter options and forwards for years before futures came in, and I don't think we had any particular regulation at that time, did we? It was just taken for granted that they knew what they were doing.

MR. KWAST. We always checked the limits. They had a ton of limits.

MR. STRUBLE. Yes, but it wasn't a big issue until the futures and options markets came in, I think, and that was partly because the futures exchanges were in Chicago and not in New York. There was concern that the Chicago people didn't know how to be as prudent as the New York financiers. That's a real stretch, but I think there's some truth to it. [Laughter]

Robert H. "Bob" Bethke used to run one of the government security dealer firms. Bob was always talking with anybody at the Fed he could, because he was trying to get information on the Fed's policy and changes therein. It was always a little dangerous to talk to Bob, but he came in and said, "These guys are going to screw up the Treasury securities market with all this new stuff, and you should restrict them!" Bob and one or two of the old-line government security dealers were absolutely dead set against allowing futures markets to trade in futures based on government securities.

MR. KWAST. This is relevant today, because one of the responsibilities of a systemic risk regulator or a systemic risk council—whatever is eventually created, if something is created—is to identify financial innovations that have the potential to impose systemic risk and to be proactive in constraining those possibilities. You were involved in an awful lot of innovation over time. Do you think we felt confident in anticipating what innovations were going to be risk enhancing and which were going to be risk reducing and what the authorities should have done to manage that process? Is that a realistic point of view?

MR. STRUBLE. Well, that study we did was designed to evaluate and decide whether or not it was good for the economy and the financial markets. And you'll recall that we said that this was a good idea. It was not that we gave the innovators carte blanche. We endeavored to evaluate the proposed innovations before we gave approval for them. If we did not foresee obvious problems, we did not object even if we realized they might complicate our supervisory activities. We certainly did not wish to be an obstacle to innovation just because we had not seen it before.

MR. KWAST. Yes, this is a great idea! [Laughter]

Study on Federal Margin Requirements

MR. STRUBLE. At about the same time we did that study on financial futures, we did a study on federal margin requirements. One reason for undertaking this study was the introduction of the new financial futures markets, which required considerably lower margin requirements for positions of risk. Since it was clear that the futures and spot markets would be interacting—arbitrage would link the markets—the issue was raised whether security margin requirements should be adjusted. I kept meeting with Jim O'Brien. Jim did this intellectual work on the efficient market hypothesis and the implications of this hypothesis for whether there can be market bubbles.

MR. KWAST. He was an economist in the Government Securities Section then, right?

MR. STRUBLE. Either that or the Banking Section, one or the other. Jim was a smart guy, and when he believed something, he could be a strong advocate. We would get together for an afternoon meeting, and the fireworks would start.

To give background, Jim, through good research, had already established that margin regulations were not obviously necessary for financial firms, because in the 1929 crash, margin lenders lost very little money. So the issue devolved to whether margin requirements were needed to head off a stock market bubble. I thought intuitively that such requirements made good sense. Jim thought that the empirical evidence could not demonstrate that bubbles occur. That was the prevailing view of the many fancy economists of the country, I think. So I would yell at Jim. I was really not very nice to him, because I kept thinking that at the end of this conversation, I have to go see Chairman Volcker and say to him, "We don't think [we] need margin requirements."

Finally, I caved in, and we wrote up our study pretty much in accordance with the position of O'Brien and other economists. I went in to see Volcker and gave him my little spiel, and he said, "Oh, you economists!" [Laughter] And then he said, "I've been here now for three or four years. I have never had anybody come into this office and tell me that the margin requirements were a burden or that they needed to be changed, and nobody up there in the financial sector is calling for changes in margin requirements." After he said that, he dismissed me [laughter], and I don't think anything ever happened to our proposal.

MR. KWAST. My recollection is that, after you presented your report, he sent a letter to the Hill stating that the Fed would favor eliminating margin requirements.

MR. STRUBLE. Actually, I think he did! I'd forgotten. It was against his better judgment! [Laughter] It was not something he was enthusiastic about, that's for sure. And I think, as time has gone on, it looks like his instincts were right.

MR. MARTINSON. When I first came to the Board, the old Board Room had charts on the wall. One showed margin requirements and the stock market; they'd lower the margin requirements, the stock market would go up with a lag, then they'd raise the margin requirements, the stock market would go down. So I was always skeptical when people said they don't work. [Laughter]

MR. STRUBLE. I don't know, Mike, you may be right on that. There were a number of rigorous studies that didn't come to that conclusion.

MR. KWAST. Yes, that was definitely the consensus. I think it is still.

MR. STRUBLE. If you chart the movement of the stock indexes and chart the index, just chart the level of stocks bought on margin or margin credit, they tracked perfectly. There's a high correlation between the two.

BCCI (Bank of Credit and Commerce International)

MR. STRUBLE. Do you remember BCCI? Clark Clifford and Bob Altman would come in. Clark Clifford was a big honcho; he would be in Bill's [Taylor] conference room. Most of the staff didn't go into these meetings. I don't know what in the heck happened, but apparently Clifford and Altman played fast and loose with their commitments.

Attempts to Restructure the Banking Agencies' Fee Structure

MR. MARTINSON. During this period, there were several attempts to restructure the banking agencies. Did you work on any of those initiatives?

MR. KWAST. You were trying to figure out a rational fee structure for charging for exams at the OCC, remember? They had this model that predicted revenues that could be raised with different price structures, and we kept going back to Chairman Greenspan's office to show him the revenue projections based on the OCC model.

MR. STRUBLE. I sort of remember.

MR. MARTINSON. On one project, we were supposed to charge for our examination of U.S branches of foreign banks. We came up with this big complex model, but we never ended up charging! [Laughter] We decided the cost was zero or something!

MR. STRUBLE. Charging for the examinations seemed insignificant, given the overall picture. That was what happened, I think.

Being "Strublized"

MR. MARTINSON. There was a term at the Fed for people who wrote memos—that they'd been "Strublized"! [Laughter]

MR. STRUBLE. Well, there was a lot of truth in that. And as time has gone by and old age has set in, I regret that! I think the charge was accurate, and I think it was not one of my finest hours. I overdid it a good deal.

MR. KWAST. I remember the first draft of this report for the Financial Futures and Options Study. Fred didn't like it as well as I thought he should. He said, "Myron, let's go for a walk around the Martin Building." So we did, and you told me that you wanted to rewrite it. [Laughter]

MR. STRUBLE. Did I really?

MR. KWAST. We stayed friends and we still played golf with each other, so maybe it wasn't quite as bad as you said!

MR. STRUBLE. Anyway, I plead guilty. There's not much one could say! I wish I could go back and do it a different way, but you can't go back. That was true, I overdid it.

View on Board Senior Officials Working across Divisions

MR. MARTINSON. To my knowledge, you were one of the few senior officers who moved from one division to another. Sometimes, at lower levels, people move around, but even that's pretty rare, and it's even rarer, I think, at the senior levels. What's your perspective on that? Do you think the Board would be well served by having more senior officers spend time in other divisions—not necessarily moving over permanently, like you did, but spending a year or two in another division to get experience?

MR. STRUBLE. If it became a well-established program, it would probably be a good learning experience. But when someone comes into a senior position in any organization, whether it's from another division or from outside, it creates some problems for the division you're going into, because you've got a lot of younger people interested in getting ahead and getting promoted and so forth. They were probably looking at that particular spot that you just took and saying “Maybe that will be my spot at some point,” and there you are sitting there, so there’s a little tension. You have to recognize that when you go in.

When I went into the supervision division, we had a lot of stuff going on. It was 1985, and various staff groups were dealing with a crisis. Gerald “Jerry” Corrigan was here, and the guys from New York were coming down for this big working group, so it was easier to work into that than otherwise. I think you learn a lot. You begin to understand things you didn’t before or didn’t understand as well because the supervision division deals with actual day-to-day situations. Before that, it had always been a bit more theoretical or a little bit more conceptual than the actual what’s going on out there at the banks and what kind of people are doing what.

I think a rotation of officials would work, but there will be difficulties that go with it. When I moved from research to supervision, it helped that Bill Taylor was within a month or two of becoming the director. Since he had invited me over, my process in there was smoothed a good bit. In addition to that, at that time, the supervision division was expanding at a rapid rate. We were one of the major employers for the Federal Reserve. We brought in about 50 or 60 people.

MR. MARTINSON. It was a huge expansion.

MR. STRUBLE. A lot of positions were made available, and that helped a good deal.

MR. KWAST. Are you talking about here at the Board, or are you talking about the whole Federal Reserve System?

MR. STRUBLE. Here at the Board. We were going to do prompt corrective action, and we set up a whole new exam schedule. Jerry Corrigan was very much involved in it, and, of course, Volcker was looking over everybody’s shoulder.

Influential People

MR. MARTINSON. Were there people who influenced you?

MR. STRUBLE. Charles Partee was an extremely impressive, talented man and an extremely impressive Governor, for that matter. When he was on staff, he would come in on a Saturday afternoon and be there for two hours writing out his briefing to the FOMC on the economic situation. He then gave it to his secretary, and with only minor modifications, that was it. For everybody else's briefings, you would write it and rewrite it three times. Then you'd take it to a committee, and the committee would go through it line by line and rewrite it again.

MR. KWAST. Still do!

MR. STRUBLE. They still do, yes! But Chuck would just plow right through the thing. Lyle could do that pretty well, too, and Steve [Axilrod], too, as I recall. They were all pretty good at that. But of the three, Chuck just had a little extra something.

MR. KWAST. This explains a 30-year mystery to me. Early in my career, when Chuck Partee had become a Governor, I wrote a draft congressional letter for him about paying interest on demand deposits. John J. Mingo was my line officer. The draft went up to Partee. He didn't change a word, and the letter went out. Mingo was amazed. I got this note from John that said, "Partee didn't change a word of the letter!" And I thought, "Big deal. It was a pretty good letter!" [Laughter]

MR. STRUBLE. It must have been!

MR. KWAST. I never appreciated that until this day.

MR. STRUBLE. For a long time, Partee was the Governor responsible for banking supervision. When we were going to take a proposal to the Board, you'd always have this meeting ahead of time. Chuck would put us through the paces and, in the process, point out the weakness in our presentation or the weakness in our proposal and so forth, and we would respond, getting it pretty much in conformance with his suggestions. Then when you went to the Board, you were pretty sure that Partee was going to support you, because he had already approved it. In contrast, David Mullins [1990–94], who was one of the smartest Governors we ever had, became our Oversight Governor. We would meet with Mullins and go through a proposal, and he'd point out that this or that is weak and so forth. Then he'd say, "All right, you can go ahead and take it to the Board." Then we'd take it up to the Board, expecting him to be supportive. Instead, he would bring up the very weaknesses he had identified in our earlier meetings.

MR. MARTINSON. Well, thank you for the interview.