FEDERAL RESERVE BANK OF ST. LOUIS

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Central Banker

News and Views for Eighth District Bankers

Studies Confirm Electronic Payments Have Surpassed Checks

For the first time in history, Americans are favoring electronic payments in greater dollar amounts than checking transactions—a trend the Federal Reserve expects to continue. The Fed recently commissioned several studies and discovered that electronic payment transactions totaled $44.5 billion in 2003, while the number of checks paid only totaled $36.7 billion. This represents an annual rate of decline of 4.3 percent for checking transactions since 2000.

The 2004 Federal Reserve Payments Study contained two research components, the *Depository Institutions Payments Survey,* which included responses from more than 1,500 depository financial institutions, and the *Electronic Payment Instruments Study,* which included responses from 68 organizations involved in originating, switching or processing electronic payments.

The *Electronic Payment Instruments Study* revealed that the fastest growing method of electronic payment is debit card transactions, with an estimated annual growth rate of 23.5 percent.

"There is no question that check usage will continue declining," says Dave Sapenaro, senior vice president of the Federal Reserve's Treasury Relations and Support Office. "And with the recent trend toward traditionally cash-based retail establishments such as fast food stores offering electronic payment options, cash usage may decline over time, too."

For more information about the studies, visit www.frbservices.org. ■

Federal Reserve Introduces New BHC Rating System

The Federal Reserve has introduced a new bank holding company (BHC) rating system emphasizing risk management. The new rating system uses a 1 (best) to 5 (worst) scale. Each BHC will be assigned a composite rating (C) that is based on an evaluation of three essential components: the effectiveness of its risk management program, its financial condition and the impact of its operating practices on its depository subsidiaries.

The specific rating components are:

- risk management (R);
- financial condition (F);
- potential negative impact (I) of the parent company and nondepository subsidiaries on bank and thrift subsidiaries;
- depository institution (D), which mirrors the primary regulator's assessment of the subsidiary depository institutions.

Thus, the new rating is displayed: **R F I/C (D)**.

To provide a consistent framework for assessing risk management, the R component is supported by four subcomponents:

- board and senior management oversight;
- policies, procedures and limits;
- risk monitoring and management information systems; and
- internal controls, reflecting the effectiveness of the banking organization's risk management and controls.

The F component is also supported by four subcomponents reflecting the amount and quality of the BHC's capital, asset quality, earnings and liquidity.

For the vast majority of BHCs with assets below $1 billion, a simplified version of the new rating will contain only the R and C ratings. More information about the new rating system can be found on the Fed's online course, http://stlouisfed.org/col/courses/bhc/why/index.cfm. ■

Feditorial

How Bankers Can Simplify Their Conversion to Image Clearing (Check 21)

By Ron Byrne, vice president, Regional Sales

We've been talking to bankers about electronic check services (Check 21) for quite some time now, and we're very happy to report that our District's banking community is very interested in moving to this new technology. If your bank is thinking about taking advantage of the new services the Fed has created to support Check 21, I'd like to offer you some practical tips and advice.

Register for the Fed's Free Online Seminar, Destination Check 21. This seminar presents case studies that will help you and your staff:

- realize how the Fed's Check 21-related solutions can help your institution achieve your business objectives;
- understand the Fed's new value-added products (FedForward[SM], FedReturn[SM] and FedReceipt[SM]); and
- assess whether your institution is ready to take advantage of check-image-clearing.

You may take this course at anytime of the day or night from any place you have Internet access. Register online at www.destinationcheck21.com.

Take Inventory of Your Current Operations and Technology. Your operations staff will need to find out if your software vendor can create properly formatted files—ANSI 9.37—and if your institution can receive images via the web. More technical information can be found at www.frbservices.org/Retail/check21TechInfo.html.

Keep Yourself Informed. In addition to FedForward, FedReturn and FedReceipt, we will continue to announce new Check 21 products and services on our national web site, www.frbservices.org/Retail/check21CustComm.html. To make sure you receive the latest news, I also encourage you to subscribe to both our District's and the Fed System's e-mail alert services. A link to the Eighth District's e-mail alert service can be found on our home page, www.stlouisfed.org. The direct link to the national e-mail alert service is www.frbservices.org/HomePage/EASubsMgr.html.

Keep Your Software Vendor Informed. We also have created a secure web page just for vendors. Once your institution or vendor has filled out a vendor profile sheet, your vendor can go to this secure, online resource to find out what it needs to do to get ready for Check 21. The link is www.frbservices.org/VendorInfo/index.html.

Allow Enough Time. And most important, a successful conversion to electronic payments requires extensive planning and coordination. There is an implementation protocol that must be followed. To get the ball rolling, contact your local account executive. ■

"FedForward," "FedReturn" and "FedReceipt" are either registered or unregistered trademarks or service marks of the Federal Reserve Banks. A complete list of marks owned by the Federal Reserve Banks is available at www.frbservices.org.

FFIEC Issues Additional Guidance on HMDA Reporting

Several Regulation C amendments that were adopted in 2002 took effect Jan. 1, 2004—the first year the new data must be reported. Based on analysis of some preliminary 2004 data, the Federal Financial Institutions Examination Council (FFIEC) believes that Home Mortgage Disclosure Act (HMDA) reporters need additional guidance to ensure that the data they report are accurate.

The additional guidance pertains to:

- transition rules;
- ethnicity, race and sex (government monitoring information);
- property location information on refinancings and pre-approvals;
- lien status reporting;
- loans subject to the Home Ownership and Equity Protection Act (HOEPA loans); and
- reporting the sale of home purchase loans.

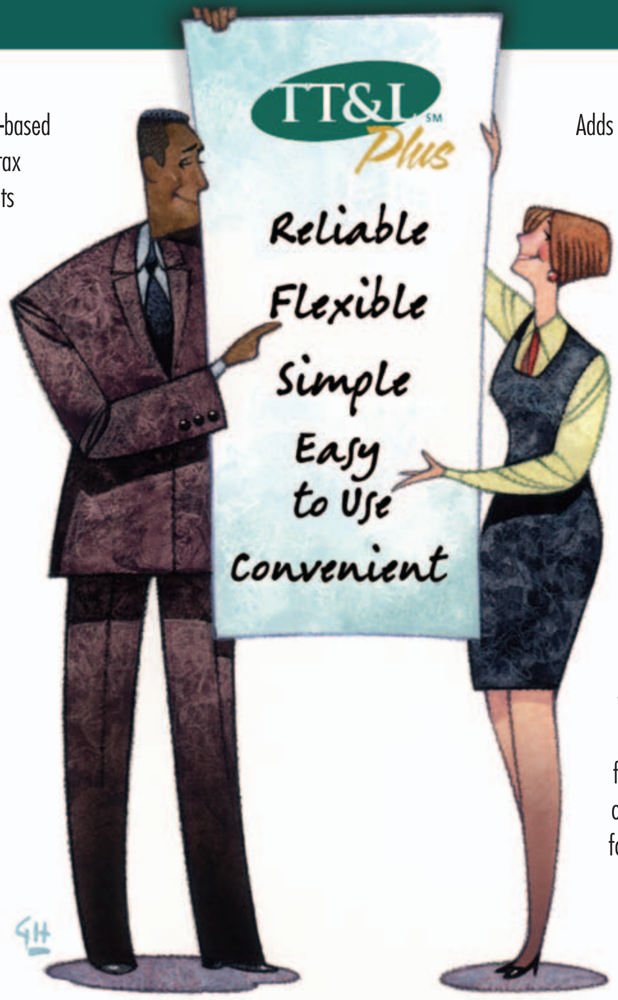
The transition rules cover fields including ethnicity, race and sex for applicants and co-applicants. Ethnicity is a new field that was added to the HMDA Loan Application Register (LAR) beginning Jan. 1, 2004. An applicant and/or co-applicant can designate up to five racial designations. Institutions must report a code in both the ethnicity field and at least the first race field for both the applicant and co-applicant on every LAR record.

The 2004 reporting deadline was March 1, 2005. In the coming months, be on the lookout for edit reports, which are used to verify data accuracy, and your institution's disclosure statement—available in early third quarter.

Complete guidance can be found on the FFIEC's web site, www.ffiec.gov/hmda/pdf/FFIECguidance2004.pdf. If you have any questions about the new guidance, contact Bob Dowling at (314) 444-8532. ■

TT&L Offers Web-Based Access and Greater Flexibility

Treasury Tax and Loan (TT&L) Plus℠ replaces DOS-based FedLine® for accessing Treasury services. The Federal Reserve made the decision to move away from DOS a few years ago because the technology is old, and web-based applications are much more convenient to use.



Customers that previously used DOS-based FedLine for reporting their institution's tax deposits and managing their TT&L assets began migrating to TT&L Plus last November. The next release is slated for mid-2005, and the Fed expects to convert all existing FedLine customers by June 2006.

"It took a while for us to launch the new service, but we're really pleased that our customers have begun transitioning to TT&L Plus," says Jean Lovati, vice president of the National TT&L function for the Federal Reserve System.

The conversion process to TT&L Plus is a phased approach, coordinated with other Federal Reserve services that are moving to the web. TT&L Plus users can connect via any computer that has an Internet connection. Since most financial institutions already have e-mail and web access, users will not experience much of a learning curve when they convert.

"The training was simple, and everyone caught on quickly," says Patty McElligott, a teller supervisor at Cass Bank in St. Louis.

Dale Buxton, the chief operating officer of Lewiston State Bank in Lewiston, Utah, agrees. "We're very happy. The only struggle we had was getting our users into the system. But once we figured out how to solve that problem, we had no trouble training our staff or getting them to use TT&L Plus."

Financial institutions enjoy using TT&L Plus because it eliminates a lot of steps. DOS-based FedLine requires a special, single-use terminal, and every Advice of Credit (AOC) entered through FedLine requires dual-verification. Teller #1 signs on to the FedLine terminal, prepares the initial deposit and must sign off right away. To complete the AOC, teller #2 signs on to the terminal, confirms the deposit amount and sends the transaction.

With TT&L Plus, no special terminal is required. The same employee who enters the AOC also can confirm and send the deposit from his or her Internet browser.

"We love TT&L because it only requires one transaction, and when you're finished you can get on with the rest of your day," says Linda Hunt, assistant manager of operations at First State Bank in Conway, Ark.

Adds McElligott, "And it's much more efficient because right after we complete a transaction, we receive a real-time receipt showing us that the payment has been accepted."

With TT&L Plus, users can:

- view and print all reports from one screen;
- archive reports to their PCs using easy tools, such as Adobe;
- view reports for their financial institution, customer American Bankers Association numbers (ABAs), merged ABAs, respondent ABAs and secondary ABAs;

and request archived reports any time—not just during business hours.

Most TT&L Plus reports are available for the last seven calendar days. End-of-day (EOD) reports can be retrieved for up to 35 days. In addition, activity statements are available on TT&L Plus for up to 18 months.

"I really like the fact I can get web-based reports at any time," says Buxton. "With FedLine, I could only request reports during business hours, and then I had to wait for them. TT&L Plus reports are there whenever I need them."

But it's not just the simplicity and enhanced reporting that customers enjoy. They also have come to rely on the accuracy of all TT&L data.

"I'm not finding any errors," says Marie Bauman, a senior accounting associate responsible for balancing TT&L at Cass Bank. "Everything that should be posted is posted. Everything that is supposed to balance, balances."

Buxton agrees. "My bank's conversion to TT&L Plus can be summarized in one word: 'reliability.'"

For more information about TT&L, visit www.frbservices.org. If your institution is interested in learning more about TT&L Plus, contact the TT&L National Customer Service Area (NCSA) at 1-888-568-7343. ■

"TT&L Plus" is a service mark and "FedLine" is a registered trademark and service mark of the Federal Reserve Banks. A complete list of marks owned by the Federal Reserve Banks is available at www.frbservices.org.

Eighth District Announces New and Returning Board Members

The St. Louis Fed has announced several new and returning members on its four boards of directors. They include:

- Sonja Yates Hubbard, reappointed to the Little Rock Branch board;
- Sharon Priest, appointed to the Little Rock Branch board;
- Steven E. Trager, appointed to the Louisville Branch board;
- J.W. Gibson II, appointed to the Memphis Branch board;
- Levon Mathews, appointed to the Memphis Branch board to fill an unexpired three-year term ending Dec. 31, 2005;
- Thomas G. Miller, appointed to the Memphis Branch board;
- Paul T. Combs, elected to the St. Louis board;
- Irl F. Engelhardt, appointed to the St. Louis board;
- David R. Pirsein, elected to the St. Louis board to fill the unexpired portion of a three-year term ending Dec. 31, 2006; and
- Lewis F. Mallory Jr., re-elected to the St. Louis board.

For a full listing of each branch's board of directors or to read more about each director, visit our web site, www.stlouisfed.org/about/board.html. ■

Fed's Educational Web Site Offers Resources for Bankers

The Fed has redesigned its educational web site, www.FederalReserveEducation.org, which offers online tools that community bankers can use to educate their employees and customers. The Personal Finance Education section houses Fed publications on a number of topics, including consumer banking, consumer protection, credit and loans, and interest rates. Fed101 contains an interactive lesson in the history and organization of the Fed, its monetary policy and regulatory functions, and the services it provides to depository institutions. *(This portion of the site requires the Macromedia Flash 7.0 player, which can be downloaded for free.)* ■

A New Resource for Entrepreneurship in Rural America

Growing Entrepreneurs from the Ground Up: A Community-Based Approach to Growing Your Own Business is a new resource that teaches community leaders how to promote entrepreneurship in rural areas. The guidebook includes a survey local leaders can use to assess whether their community is attractive to entrepreneurs. For information, call Doug Hermes at the Missouri Rural Development Partners at (816) 781-8631. ■

Seasonal Credit Is Available for Community Banks

The Federal Reserve offers seasonal credit to help qualifying community banks meet the seasonal needs of their local customers. Community banks that experience yearly fluctuations in their deposits and loans—caused by construction, farming, college or resort activities, municipal financing and other seasonal businesses—frequently qualify.

Banks can use their seasonal credit line either as a primary seasonal funding source or as backstop credit. Once established, credit may be drawn down incrementally as needed, and partial and full prepayments are allowed without penalty.

There is no expense involved in setting up or maintaining the seasonal line; however, all Federal Reserve loans must be secured to the Fed's satisfaction, and a flexible, market-based rate is applied to all outstanding loans.

To qualify, an institution must:

- be in sound financial condition,
- meet the general requirements of the program,
- complete an application that includes no more than three years of monthly deposits and loans, and
- include the monthly amount of credit it anticipates for the upcoming season.

If you would like to learn more about the program or obtain answers to questions you may have about collateral or the borrowing relationship, call the Credit office at 1-866-666-8316 or send an e-mail to creditoffice@stls.frb.org. For an application and a brochure, visit our web site, www.stlouisfed.org/banking/credit/credit.html. ■

What's Driving Oil Prices?

Richard G. Anderson is a vice president and economist, and Jason J. Buol is a research associate at the Federal Reserve Bank of St. Louis.

An earlier version of this article appeared in the January 2005 edition of *Regional Economist,* another publication of the St. Louis Fed.

The price of oil reached record dollar levels during 2004. (See the figure.) And because oil is such an important commodity, economists want to better understand the factors that influence its price. This article will answer to what extent supply and demand, speculation and other factors have affected current oil prices.

Demand

The International Energy Agency reported in August 2004 that world oil demand was growing at its fastest rate in 16 years. As developing countries have expanded their economies, they also have increased their oil consumption. Two countries that have significantly increased their oil demand are China and India.

China became the second largest consumer of oil in the world in 2003, currently demanding approximately 5.56 million barrels of oil per day (bbl/d). Estimates by the U.S. Energy Information Administration (EIA) predict that China will **double** its consumption of oil in the next 20 years, reaching 12.8 million bbl/d by 2025.

India has experienced 40 percent growth in oil demand—increasing its oil demand from 1.6 million bbl/d in 1995 to 2.2 million bbl/d in 2003. And the EIA predicts India will continue to expand and consume more oil, reaching 2.8 million bbl/d by 2010.

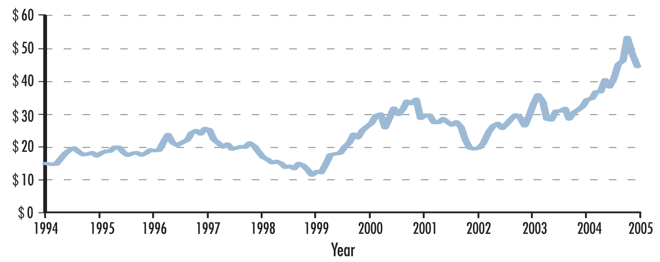
Supply

Compounding the demand factor, several oil-supplying countries have endured turmoil that has limited their production capabilities. The most obvious country is Iraq.

Since the start of the war, Iraq's oil production has been uncertain at best. A central reason is the continued violence and sabotage of facilities. Throughout 2004, insurgents were able to destroy pipelines and oil production facilities and disrupt a steady flow of oil coming from the country. Until these attacks are stopped, it is unlikely that Iraq will be seen as a reliable supplier of oil to the world market.

Another oil country with political turmoil is Venezuela. Political problems were exacerbated with a nationwide strike in December 2002. The strike, which lasted until early 2003, led to significant reductions in the country's GDP and oil production. Since that time, production has been returning to levels seen before the strike; however, there are still reasons to doubt the country's progress. Political uncertainty continued when President Hugo Chavez survived a recall vote to remove him from power in 2004.

U.S. Spot Oil Price, 1994-2004 Monthly Averages of Daily Data



Speculation

Many people, including Acting OPEC Secretary General Maizar Rahman and Federal Reserve Chairman Alan Greenspan, believe that speculation has driven up the cost of oil by $10 to $15. Greenspan testified in September 2004 before the House Budget Committee that one possible source of higher prices was speculators, who influenced prices by taking larger positions in crude oil futures. This theory suggests that more active trading was taking place before and during the period when oil prices were reaching record nominal levels. A cursory examination of petroleum futures volume data in the *Wall Street Journal* demonstrates that the volume of trades was up during this time period, which indicates that enhanced speculation did contribute to increasing oil prices.

Other Factors

Because oil prices are so volatile, we also need to examine other variables that can affect prices. The recent series of hurricanes disrupted the flow of oil into the United States and damaged oil facilities. Oil refineries also shut down periodically for maintenance, regulatory changes and other reasons. But neither of these factors will have a long-term impact. As hurricane damage is repaired and oil refineries are reopened, production will resume.

What our research indicates is that significant changes in oil supply and demand behavior will continue to impact the price of oil. As China, India and other developing countries expand their economies, they will likely follow the same pattern of sharply increasing their demand for energy. ■

FedACH Lowers Rates to Mexico

The Federal Reserve has reduced the spread, or commission, for Automated Clearinghouse (FedACH) payments for any U.S. depository institution that wants to send electronic payments to Mexico. The Fed also has entered into an agreement with Mexico's Banco del Ahorro Nacional y Servicios Financieros (Bansefi) to enlarge the distribution channel for bank-to-bank account transfers from the United States to Mexico. The agreement is expected to make it easier for Mexicans living in the United States to send money home through formal channels. For more information, contact Larry Schulz of the Fed's International Retail Payments Office at (404) 498-8792. ■

Fed Eliminates Large-Dollar Item Surcharge on Image Cash Letter Deposits

The Federal Reserve has eliminated the large-dollar item surcharge on items $10 million and over deposited in forward and return image cash letters. This includes large-dollar items deposited in a mixed forward or return image cash letter or in an electronic endpoint group sort. Large-dollar items deposited in paper-to-image cash letters, Check 21 cull products and all traditional paper deposits remain subject to the $50 surcharge.

These changes became effective Feb. 1. For more information, contact your account executive. ■

Fed Publishes Survey Results on Bank Lending Practices

The Federal Reserve Board of Governors has published the January 2005 Senior Loan Officer Opinion Survey on Bank Lending Practices. The survey addressed changes on supply and demand for bank loans to businesses and households. A special question asked the reasons why nonbank investors recently have increased their participation in the commercial and industrial loan market. In addition, banks were asked about the changes they have made to terms on commercial real estate loans during the past year and why the share of industry assets accounted for by residential real estate loans has increased during the past three years.

The complete survey results can be found on the Board's web site, www.federalreserve.gov/boarddocs/snloansurvey/200501/default.htm. ■

CalendarEvents

UPCOMING FED-SPONSORED EVENTS FOR EIGHTH DISTRICT DEPOSITORY INSTITUTIONS

Promises & Pitfalls: As Consumer Finance Options Multiply, Who Is Being Served and at What Cost?

Washington, D.C.
April 7-8

The Federal Reserve is hosting its Fourth Community Affairs Research Conference, and the keynote speaker is Alan Greenspan. For more information, visit www.stlouisfed.org/community/.

Striking the Right Notes on Entrepreneurship

Memphis, Tenn.
April 18-20

This unique event will provide people working with small businesses and entrepreneurship a chance to discuss challenges and opportunities for advancing the field. For more information, visit www.stlouisfed.org/community/.

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