The original documents are located in Box K29, folder "Rockefeller, David (2)" of the Arthur F. Burns Papers at the Gerald R. Ford Presidential Library.

November 6, 1973

Dear David:

Thank you very much for your letter of October 17 with which you enclosed a copy of your presentation and that of Mr. Butcher to the security analysts. I appreciate your bringing to my attention the remarks you made about Chase's earnings objectives.

With kindest regards.

Sincerely yours,

(signed) Arthur

Arthur F. Burns

Mr. David Rockefeller
Chairman of the Board
The Chase Manhattan Bank
1 Chase Manhattan Plaza
New York, New York 10015

NB:slc
#2231

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM

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OFFICE OF THE CHAIRMAN

THE CHASE MANHATTAN BANK
National Association

1 Chase Manhattan Plaza, New York, New York 10015

DAVID ROCKEFELLER *Chairman of the Board*

October 17, 1973

#2231

NB-7

Dr. Arthur F. Burns, Chairman
Board of Governors
Federal Reserve System
20th Street & Constitution Avenue
Washington, D.C.

Dear Arthur:

I hope you got back safely from Africa and that you had a pleasant visit to Kruger Park. I heard a bit on your activities from Dr. Diederichs in South Africa.

I was extremely pleased that we could have a talk together in Nairobi. Your comments and advice on the subject of particular concern to me personally were very much appreciated.

During the course of our conversation in Nairobi, mention was made of Bill Butcher's and my presentation to the Security Analysts. You had gained an impression from the press of what had been said which I believe was misleading. In any event, I enclose a copy of our two presentations and would ask you most particularly to look at page three of my talk where I speak specifically of our expectations and ambitions with respect to earnings. I hope you will feel that this was a reasonable statement under the circumstances.

With best regards,

Sincerely,

David

Enclosure

The Chase Manhattan Corporation
Investment Community Presentation
September 12, 1973

Remarks by David Rockefeller
Chairman of the Board
The Chase Manhattan Corporation
At Investor Community Presentation
New York, September 12, 1973

NEW DIRECTIONS FOR CHASE MANHATTAN

Good afternoon, ladies and gentlemen, and welcome to Chase Manhattan! My associates and I are delighted that so many of you are able to be with us today.

Our purpose is straightforward. We plan to tell you how we are building upon a traditionally strong commercial banking base so as to expand and diversify further into an aggressive, high quality international financial services corporation. We will be completely forthright, both in our presentations and in the question-and-answer period.

I will outline our overall management philosophy, setting forth the primary policy objectives we established to strengthen our profitability and our position in the financial community. In other words, where we are headed, what we have done so far to get there, and what we are going to be as an institution.

Our President, Bill Butcher, will give a detailed account of the strengths of our global business base, and our problems and how we are curing them. In other words, just where we are and how we intend to do better.

Banking today is substantially different than it was when I joined Chase 27 years ago. Then, our major challenge was to invest our resources. Now, it is to fund our assets profitably.

We didn't have many overseas locations at that time, but we were in Shanghai, Tientsin and Havana. Today, we haven't yet made it back to those cities, but we do have a presence in some 2,000 locations in 92 countries.

Banking,in the past few years, has undergone many very basic changes in national and international financial structures, asset and liability management techniques, computer applications, payments systems, retail services, corporate planning and budgeting methods, information sciences and a host of other areas.

Moreover, many of the underlying concepts of the banking business have changed, and competition for its business is far keener.

The provision of broader worldwide financial services has made our job exceedingly complex with many new opportunities and many new problems. Moreover, banking and all other businesses must now incorporate in their planning such social and political factors as nationalism, populism, consumerism and protectionism -- issues that have a profound effect on a major international institution like Chase, not to mention their broader impact on the thrust and posture of our country as a whole.

This questioning climate demands public-spirited as well as aggressive performance, and has necessitiated basic structural changes in our organization. These have included the refocusing of many of our operations, and the devotion of enormous quantities of time, attention and resources to developing innovative ways to serve new markets profitably but with sensitivity and respond affirmatively to fundamental shifts in the global economy.

Some of these forces of change have had a direct impact -- some negative, some positive -- on an item of overriding concern to us and to you -- namely, our bottom line performance. At the end of 1972, our five-year compounded earnings growth rate was 6.6%, or 2.2% lower than that of the previous five years. Since I became Chairman in 1969 with sole responsibility as Chief Executive Officer, our four-year growth rate has been 7.1%, a reduction of 1.7% from our 1962-67 standard.

Quite frankly, these figures are not satisfactory to me or any of us responsible for the management of Chase. We are convinced, however, that they do not reflect a lasting slippage in basic performance, but rather a temporary slackening due to a vital repositioning for improved and more aggressive performance in the changing world of the future.

While, for many reasons, we will not give you a specific earnings growth target this afternoon, I can tell you this. We are resolutely determined to meet your definition of a growth corporation in the nearer term. We also fully intend, in the longer run, to achieve a level of earnings performance among the very best in the industry.

Our overall management philosophy has had three major objectives. Our <u>first</u> has been and is to accelerate our transition into a multi-faceted international financial services corporation in the truest sense.

In 1969, we realized clearly that our traditional domestic and overseas business base would by itself neither enable us to achieve significantly higher earnings growth, nor to service emerging global financial needs profitably. We therefore moved decisively to create the geographic and functional business base essential to penetrate expanding markets and increase our earnings growth rate.

Internationally, we have emphasized new branches, commercial banks, finance companies, retail banks, merchant banks, Edge Act corporations, mortgage banks, and leasing, investment advisory and consulting companies. Altogether, we have built a very substantial and widespread base in these areas.

As you know, a field of particular interest to me has been East-West trade, which I believe has a very promising future. We have established the first representative office of a U.S. bank in Moscow, set up a special East-West trade unit in Vienna, and become the sole American correspondent bank for the Bank of China. We have also created The Chase World Information Corporation, another first of its kind, that is initially focusing on providing East-West trade information and counseling to our customers.

Domestically, we have been moving to expand our geographic and market reach. We have broadened our branch network and moved rapidly toward establishing Chase throughout New York State. We have also strengthened our already substantial real estate business with a series of new subsidiaries and services, created a successful alliance with BankAmericard, and positioned ourselves in a number of other markets such as factoring, leasing, economic consulting and small business finance and investment.

Our plan to merge with the Dial Financial Corporation should be ruled on by the Federal Reserve Board by the end of this year. When the merger is consummated, as we are confident it will be - given the merits of the case - Dial will put us in the consumer finance business and bring additional outstanding retail people to our management team. It will also further our domestic mission to become a truly national financial services corporation.

Our objective now is to increase the effectiveness of our domestic and international business base, and to expand and diversify it further.

In this regard, there are five markets we believe hold particular opportunities. These are retail, real estate, innovative international banking mechanisms, medium-sized corporations, and management information.

We have already made a number of significant strides in the retail and real estate areas. Internationally, our Orion and Libra consortia are the type of new banking forms which we are convinced are going to be highly successful in today's international economy.

Our strategies with regard to medium-sized corporations and management information, on the other hand, are not yet as well developed, but we are pushing forward and see promise.

As we have expanded geographically and functionally, the job of management and control has become far more difficult and complex. This fact sharply underscores the critical importance of our second major objective -- that is, to be second to none in management.

There are two key factors in management -- quality managers placed effectively and the necessary tools to enable them to function efficiently.

Since 1969, we have devoted a great deal of effort to modernizing and streamlining our management structure. We have completed a comprehensive realignment of our corporate organization along functional lines. We have adopted a number of new management techniques. We have worked hard on developing the management tools and teamwork vital to producing sound results on the bottom line.

With regard to effective management tools, we have come a long way. Let me tell you where we stand.

We made our first formal attempt at planning long-range, five-year strategies in 1971, following the reorganization of our corporate structure. We realized the difficulties we would encounter because of the many people in new positions, but we felt that important strategic ideas would emerge which would be worthy of full development, . . . and we were right.

The new planning system identified gaps where team efforts had to be mounted in many parts of Chase to assure the proper development and effective implementation of our strategies. This process also helped us to reexamine some strategies, take remedial action where necessary, and identify new opportunities.

The 1972 long-range plan was a decisive improvement over its predecessor. The 1973 plan was still better, leading to the first definitive tying together of our long and short-range planning processes.

In short-range planning, we adopted management-by-objective and responsibility budgeting. Each of our major responsibility centers plans its objectives and budgets annually within the context of our long-range strategies. After approval, the performance of each center against plan is measured monthly. The same system which monitors this critical decision and performance measurement process also meets our needs for financial accounting and tax planning purposes.

Even though we used only a modified version of this system in 1970, while the automated system was being put in place, the result was that the rate of increase of controllable expenses was halved from that of 1969. This rate was again roughly halved in 1971. Since the 1971 budget cycle, we have used the whole system in an increasingly sophisticated way both for income, expense, asset, liability and capital planning and for performance measurement.

We have thus been able to tie our controllable expenses directly to income objectives. We know who is producing planned results and why these results are what they are. It is our policy and intention that managers who produce, and, indeed, those who do not, be rewarded appropriately. The key is performance.

In 1970, we also began the extensive work of updating and expanding our global cost-accounting system to prepare for profitability planning and measurement. Bill will tell you a good deal more about how we are beginning to use this tool.

I will just say that we are now beginning to measure with considerable accuracy the profitability of our major business areas. By the end of this year,we will have up-to-date information on all significant product costs and production standards on a worldwide basis. Coupled with an automated system we are putting in place, we will be able to follow and evaluate in a much more definitive way the profitability of individual accounts, of relationships consisting of more than one account,and of specific products. Our goal here is to enable management to appraise marginal product lines critically and thus be able more accurately to place emphasis where the income potential is greatest.

Other tools with a heavy impact on profitability are those we have developed for production management and control. Their use has achieved very substantial savings domestically over the past four years, and we see more on the way. Modern industrial engineering techniques have led to new approaches to how we organize, plan and measure our production systems. We intend to use these same techniques in our rapidly growing overseas production areas where applicable.

Better quality control tools are also critical to increasing our market share and profitability. We and other financial institutions have had a number of problems in maintaining satisfactory quality of service in the face of increased volume, and this has hurt us. We are, however, making a determined effort to improve our service performance. Quality is absolutely essential to meeting our business growth goals.

The ultimate objective of all these management tools is two-fold.

First, we want to create a lean structure that puts a premium on sales, performance, and profitability. If we didn't have these tools, that would be impossible.

Second, at the corporate level, we are aiming at greater sophistication and flexibility in our asset-liability management -- especially with regard to critical interest margin implications. We will shortly have a system that will show us the expected results of alternative business strategies so that we can accommodate more quickly to unanticipated changes in business conditions. The forerunners of this system which we have developed over the past four years have already been helpful. We expect the benefits to be even greater in the future.

On the people side of our management objective, we have also made real progress.

We have sharply clarified management responsibilities at all levels.

My own objective and overriding interest is to do my utmost to strengthen Chase in its endeavors to provide first-rate financial services on a worldwide basis.

In this connection, my principal responsibility is the development of overall policy and strategies which will enable us to meet our corporate objectives. It is also my responsibility to see that these objectives are carried out.

In this latter regard, I continually monitor, through a formal review system, and informally both within and outside the chain of command, the performance of the Corporation and the fundamental issues facing it. This way, I keep up to date on the vital inside workings of the bank, evaluate progress, and alter policies or strategies quickly where necessary.

In addition, I devote a considerable amount of my time to direct involvement with regard to the governmental and other external forces that impact our future. Likewise, I participate in many activities within and without the bank which are designed to enhance specific customer relationships.

Bill Butcher, with the help of our Vice Chairmen George Roeder and Lee Loree, is directly responsible for the day-to-day functions of the Corporation and for carrying out our plans.

Needless to say, good people at all levels are the raw material of good management, and we are working to create a climate at Chase conducive to retaining and attracting highly talented and inventive people with a broad range of skills. We encourage freedom of expression and initiative within a framework of team play aimed at accomplishing our goals. We are satisfied that Chase has the scope, diversity, job richness and spirit to challenge top-quality talent.

We have always been able to meet our banking expansion objectives with skilled commercial bankers we have trained ourselves. More recently, to meet the multiple line and staff needs of our broadening business base, we have been reaching our increasingly to hire topflight specialists.

Our senior management includes the Executive Office, 12 Executive Vice Presidents and 47 Senior Vice Presidents. The average age of the whole group is 46, and we have each been with Chase an average of 20 years. From these figures, you can see that our management combines relative youthfulness with considerable experience. It is also important to note the diversity of responsibility to which our senior managers have been exposed. Over 80% of them have different jobs now than they did when I became Chairman in 1969.

These changes in management responsibilities have, of course, necessitated a great deal of fast on-the-job personal growth, but, although this may have placed heavy pressures on some, we have achieved substantial longer-range gains in terms of a more aggressive, more innovative and more exciting management climate.

Changing our management climate, structure and methods of operation has not been an easy task. There have been disruptions both internally and externally. If we had it all to do over again, we would undoubtedly do some things differently. But, on the other hand, I know of no way to change a complex organization at a quick tempo without some disruption, and in our case change was absolutely essential.

The accomplishment of both our first and second objectives is basic to meeting our third major objective -- to build Chase earnings growth.

There are many aspects to this, and Bill will detail the ways in which we are approaching this objective. However, I would like to touch on the policy framework within which we focus on profitability.

First, let me state flatly that we will not sacrifice potential future earnings growth for the sake of immediate gains. Rather, we are aiming for an effective and productive balance between present profit and longer-range returns.

Second, we believe the profitability cannot be achieved at the expense of the business environment in which we function. When we talk about the environment, we are really talking about our own markets. We are increasingly finding social needs that we can meet profitably -- thus moving toward the integration of our social and economic objectives. Moreover, in the environment in which we live today, a corporation that is not responsive to the broader concerns of society is not likely to be tolerated over the long term.

Finally, we believe that profitability depends on outstanding team performance, and we are moving to insure just that by emphasizing bottom line results and creating stronger individual incentives.

These, then, are Chase's primary objectives -- expansion and diversification of our business base, excellence of management, and a sharp focus on the bottom line.

What we have endeavored to do is to chart a course we think is best for us at Chase Manhattan.

It builds on our substantial new and historic strengths, and corrects identified weaknesses.

It reflects fundamental changes in the basic character of our business.

In pursuing this course, we are unequivocally determined to maintain a position of leadership, to optimize earnings for our shareholders, and to do this within a framework that will enable us to discharge our duties to the communities and the customers we serve.

Obviously, objectives are nothing without effective implementation. And the man here at Chase who is responsible for that is my associate, Bill Butcher.

Bill's 26 years at Chase have been marked by unique drive and outstanding performance. He joined us right out of Brown University where he had a distinguished record. His early career was with our domestic branches, after which he spent several years in the International Department, including three years as its head. At the beginning of last year, he was named Vice Chairman for Planning, Expansion and Diversification -- a post he held until becoming President in October.

His broad background, keen abilities and decisiveness will play a key role in our future progress . . . Bill Butcher.

Remarks by Willard C. Butcher
Presiden t
The Chase Manhattan Corporation
At Investor Community Presentation
New York, September 12, 1973

OUR MISSION: PERFORMANCE

I propose to be entirely blunt and candid in outlining the problems and strengths of Chase.

I will relate these to my own prime mission, which is translating objectives into reality -- that is, performance.

By performance, I mean excelling in our jobs, not just doing them.

I mean using flexible new management structures to innovate, grow and sell effectively in key future markets.

I mean, above all, orchestrating all of our efforts to make Chase reflect on the bottom line its advantages and potentials as a true growth corporation.

My remarks may run longer than either you or I would desire. My intention, however, is that you know this financial services corporation better than you have known it before, and better than you know others.

I will do three things -- define in detail our earnings base; discuss our overall profit picture and financial policies; and finally, pinpoint some of our strengths and problems and what we're doing about them.

Let me begin first with a description of our earnings base.

We have made major strides in improving our financial disclosure in recent years, but I will go considerably beyond what you have seen before -- covering our activities on an international, domestic and overall geographic and functional basis, as well as outlining our capital investment program.

Because I have been closely involved in our international operations, I will start with those. (SLIDE ONE)

As you can see at the top, since the end of 1968, the base year we will use for most of our comparisons, our overseas branches almost doubled from 50 to 95 by year-end 1972. Geographic emphasis has remained relatively constant, with some 60% of this growth in the Caribbean and Latin America, and the rest spread about evenly among Europe and Africa, and Asia and the Middle East.

Subsidiaries, defined as entities in which we hold more than a 50% interest, went from 11 to 26. Activities in Europe and Africa more than doubled, and we established two subsidiaries in Asia. As a result, at the end of 1972 we had 35% of our subsidiaries outside of the Caribbean and Latin America, compared to 27% five years ago.

Affiliates, defined as entities in which we hold an interest of 50% or less, more than tripled from 7 to 23. The greatest growth here was in Asia and the Middle East, but Europe and Africa also more than doubled. These two areas combined had 83% of our affiliates in 1972 versus 71% in 1968. Of course, the data for both subsidiaries and affiliates include only operating units, and exclude administrative and holding companies and venture capital investments.

So far this year, we have added overseas five new branches, six subsidiaries, six affiliates and the representative office in Moscow.

Now, I want to turn to the source of earnings by country in our overseas network, regardless of the form of representation. Both the number of countries (SLIDE TWO) contributing to our international earnings and the size of their contributions have increased substantially. This slide does not include countries where Chase was only less than a 20% interest in any entity.

As you can see at the top, the number of contributing countries has risen from 35 to 50. Countries producing more than $1 million pre-tax have nearly doubled from 8 to 15. Countries making between $250 thousand and $1 million increased from 7 to 10, and countries yielding up to $250 thousand from 20 to 25.

The next slide (SLIDE THREE) shows how the contributions of various countries have developed.

On the left hand side, you see the countries in the first three lines as they stood in 1968 by size of contribution. In the three right hand columns, you see where those countries stood in 1972. On the first line, all eight of the more-than-$1 million producers in 1968, remained in that category in 1972.

Of the seven yielding between $250 thousand and $1 million in 1968 on the second line, two moved up to the highest category, two stayed in the middle group, and three slipped back into the lower group -- pointing up the fluctuations in individual countries that make international diversification so important.

Of the 20 countries earning up to $250 thousand in 1968 on the third line, three had moved to the top rank by 1972, and eight had advanced to the middle rank. Moreover, lower down on the next to last line, you will see that two of the 15 new countries, in which operations were started since the end of 1968, had already joined the largest producers by 1972.

It has been our policy overseas to employ a mix of branches or wholly-owned subsidiaries, controlled by not wholly-owned subsidiaries, and affiliates in order to achieve our expansion and diversification goals in the most efficient and effective way. We make these decisions in the light of our reading of the situation in each country. Many of you may wonder how well this policy has worked.

This slide (SLIDE FOUR) gives a breakdown of our international subsidiaries and affiliates by type of business at year-end 1972. Commercial banks lead the list with 16, followed by 11 finance companies, 7 merchant banks and 4 Edge Act corporations. Mortgage banking, leasing, investment advisory, consulting and 4 other types of companies round out the list.

Together, these 49 subsidiaries and affiliates contributed $13.6 million in pre-tax equity earnings in 1972, compared to $3.4 million from our 18 subsidiaries and affiliates in 1968 -- a four-fold increase.

Last year, five of these made more than $1 million, eight produced between $250 thousand and a million dollars, and the rest had up to $250 thousand in earnings or modest start-up losses.

So far in 1973, we have added 1 commercial bank, 1 finance company, 5 merchant banks, 3 leasing companies, and 2 consulting companies and have applied for 2 more Edge Act corporations in Houston and Chicago.

While the growth of our earnings base on the international front has been most dramatic, we have also substantially strengthened the potential of our domestic network. (SLIDE FIVE)

Between 1968 and 1972, our New York metropolitan-area branches increased from 147 to 178, our domestic operating subsidiaries from 2 to 10, and our total domestic locations from 149 to 191 including three upstate branches.

In addition to one leasing and one small business investment company in 1968, the added subsidiaries include three commercial banks as part of our statewide expansion, three mortgage banking companies, an investment advisory corporation, and a consulting company.

In addition, we have three bank-related activities within our domestic operations -- the factor and finance division, formerly Shapiro Factors; the BankAmericard Division; and the provision by our Real Estate Department of investment and financial advice to the publicly-owned Chase Manhattan Mortgage and Realty Trust in Boston as well as other clients.

These domestic subsidiaries and three bank-related activities contributed $14.8 million of income before taxes in 1972, compared to $600 thousand from such activities in 1968. Last year, four had more than $1 million in earnings, two produced $250 thousand to $1 million, and the rest earned less than $250 thousand.

So far this year, we have added twelve metropolitan area branches, for a total of 190, and three domestic subsidiaries for a total of 13. Two of these new subsidiaries are commercial upstate banks with four more branches, and the other is a mortgage banking company.

Let me now bring together our international and domestic operations and explain what they mean in terms of geographic profitability and asset deployment.

This chart (SLIDE SIX) shows the geographic sources of our bottom line profitability, using a two-year comparison because of our lack of precise corresponding figures for 1968.

Between 1971 and 1972, the domestic share of our profitability slipped from 71% to 66% of our total or from about $106 million to $97 million. This is a fact about which we are not at all happy, and you'll hear more on this subject shortly.

On the other hand, our international operations, after internal distributions of supporting expenses and overhead, contributed 34% or about $51 million of last year's bottom line, compared to 29% or $42 million in 1971.

Europe and Africa kept the same 12% share and $17 million of profitability in both years. Asia and the Middle East increased to about 9% from 7%, or by about $3 million. The Caribbean and Latin America increased their share from 10% to about 13% or by around $6 million.

There is an important overall correlation (SLIDE SEVEN) between our geographic profitability and the deployment of assets.

While domestic assets increased by $200 million between 1971 and 1972, the share of world-wide assets employed domestically dropped by 4% and the share of earnings on the last slide declined by 5%. Europe and Africa in green increased their share of assets by about 1% while the earnings share remained the same. Asia and the Middle East also increased their share of assets by 1% and profitability by 2%. The Caribbean and Latin America increased their share of assets by 2% while their share of profitability increased 3%.

From such figures, the spreads between assets employed in various areas and business lines and the profits earned become apparent. Analysis of these and other trends shows that we must be more aggressive in deploying earning assets efficiently, and we are facing up to this challenge.

Total capital outlays by Chase net of depreciation from the end of 1968 through 1972 amounted to some $180 million, of which one third was in fixed assets and two thirds in investment assets. Moreover, of the total, three quarters was used internationally and one quarter domestically.

During this same period, we increased internationally in staff from some 3,500 to about 6,600 -- an average annual growth of 775, reflecting our aggressive expansion and diversification efforts. Our domestic staff grew slightly from 17,200 to 18,800, or an average of 400 people each year. Here, needs for expansion were partially offset by the efficiency and control mechanisms David has described. We estimate roughly that these measures have saved us about $40 million pre-tax.

These, then, are some of the major trends and facts affecting our earnings base.

Now I think it would be useful to look briefly at a <u>second</u> area -- our overall profitability and financial policies.

Internationally, at the end of 1972 our four-year compound earnings growth rate, after taxes, was over 20%. That average rate is our minimum goal over the next several years, and we are confident we will meet it.

The earnings drag in starting up overseas activities is generally reasonably short. Many of our newer international activities are now breaking into the black while others are advancing to higher levels of profitability.

Moreover, our increasing geographic spread internationally reduces overall risk and enables us to take advantage of offsetting economic growth patterns between various countries and areas. It also provides us more earnings flexibility when and if we encounter special problems with any single venture.

One such challenge we now face is the announcement by the

Federal Reserve regarding our investment in Standard and Chartered Bank. We are actively seeking ways to avoid disinvestment in this case. But, should it be necessary, Chase fully intends to have its share in these markets.

Domestically, our compound earnings growth rate since the end of 1968 has, after taxes, been down slightly.

Last year, after internal distributions of supporting expenses and overhead, three of our six major domestic earnings areas were not profitable. As you know from our first and second quarter reports, we are still off a little in total domestically so far this year. However, I am happy to say that five of the same six areas have generated profits in the first half and the trend is encouraging despite very difficult interest spread problems.

Still, strengthening domestic earnings is our clearest challenge and our overriding goal.

It is not a healthy situation when our nation's largest financial institutions must consistently look abroad for meaningful growth opportunities. Given a sensible approach by the government to diversification and monetary and fiscal policy, however, I think we can do something about it.

Before moving on to some of the ways we plan to reach that objective, let me say a few more words about our financial policies and the way we evaluate profit performance.

Our dividend policy is generally to pay out 40%-to-45% of normalized income before security transactions -- that is, profits adjusted for unusual or non-recurring items.

Our capital financing policy recognizes that debt capital is less expensive to our shareholders than equity financing because of the tax savings arising from the deductibility of interest expenses.

Our policy also reflects the fact that, though convertibles are often a more expensive way to raise capital than straight long-term debt, they are still a less expensive way of raising equity. Our longer-range plans show that we will need the stockholders' equity that our outstanding convertibles will eventually represent.

Beginning with 1969, long-term debt, including our convertibles, has represented between 24% and 31% of our total capital funds, and it is now over 28%. We believe that a proper minimum target would currently be about 25%. Naturally, acquisitions mady by issuing new equity or conversions of outstanding convertible debt may reduce our long-term debt ratio below the minimum target from time to time, but such reductions would be temporary.

With regard to operating leverage, defined as average assets less average capital divided by average capital, we have had an increasing trend since 1969. In that year, the multiple was 12.9 which grew to 14.7 in 1972. Currently the multiple is 13.9 and our present minimum target is 14.

We are aware that when you analyze earnings growth rates, you are interested in two separate factors which affect that rate and which have a marked impact on a corporation's price earnings ratio.

The first factor is how we are doing on our average return on capital. To measure this ratio we add average after tax interest on long-term debt, including our convertibles, to average income before securities transactions. We then divide the total by average capital funds. From 1969 to 1972, Chase's average return on capital was 9.2%.

The second factor influencing earnings growth is the rate of new investment, which measures how much on an average annual basis we are increasing our capital as a percent of our earnings level. We calculate this by dividing the change in total capital funds by total earnings, including the after-tax interest on long-term debt, over the same time span. From 1969 to 1972, Chase's rate of new investment was nearly 66%.

If we multiply these two factors, the resulting rate of earnings growth would be 6.1%. The difference between this figure and the 7.1% previously mentioned as our earnings growth rate since 1969 is the result of the financial leverage provided by our most recent convertibles. Consequently, you can see that we can improve our rate of earnings growth by either increasing the return on average capital funds or increasing our new investment rate. We plan to do both.

I outline these policies for an important reason. We believe the market pays a discount for uncertainty, not a premium, and we want you to understand the financial factors that Chase management can influence and how we intend to influence them. Should we change our policy regarding these financial factors in the future, we will make the changes public.

Another major point I would like to clarify is how we view and evaluate the profitability of our various activities.

We review the performance of our department managers in two frameworks -- responsibility and profitability. Let me explain these terms.

Since 1970, we have had responsibility budgeting which measures performance against plan regarding expenses and income controlled by the manager.

Profitability planning, on the other hand, is strictly oriented to the corporate bottom line, and includes interdepartmental charges or credits for services rendered.

While Chase has emphasized responsibility more than corporate profitability performance at the department level, increasing the emphasis on profitability is a very high priority with which all of our senior managers are involved. The simple reason we did not emphasize this more previously is, as David said, that our cost accounting system had to be expanded and improved to provide the necessary measurements. That work is now nearly complete, and sufficient data are at hand to point our major problems for resolution, though we will clearly improve the system further as we go.

Profitability planning and measurement is a crucially important tool to tie together all of the factors arising from alternative business strategies and to determine their effect on the bottom line. Contingency planning in our rapidly changing economic environment is thus more effective, and we can have a far better feel for relative opportunities in our various business lines. The end objective of profitability planning is, of course, profit-per-share performance by each senior manager within a context of better and more innovative corporate asset-liability management.

A swing in the interest rates we must pay for money market funds affects the profitability of various business lines in quite different ways. For example, in times of lower money market rates, the value of our retail deposit base in funding Chase's total assets is less than it is in times such as 1973. One of our objectives in this area is to expand retail assets, not only to attain increasing profits from this business line, but also to moderate distortions caused by rate cycles.

Our real estate business, on the other hand, generates about the same percentage of profits whether interest rates are high or low.

Our domestic Corporate business is constantly affected by political pressure on the prime lending rate, which is a major reason we so actively supported the creation of the dual rate structure.

Though interest rates and the interest spread clearly have a huge impact, profitability planning gives us far greater flexibility. It encompasses and emphasizes other income as well. It spotlights the impact of direct, indirect, and overhead expenses for management consideration and decision. Most importantly, it is a vital management tool for evaluating strategic options, constantly focusing on the bottom line and driving the Corporation forward.

Individuals must continue to be evaluated on how well they do in their own areas of responsibility within the overall profit plan. But senior management, especially major department heads, must primarily be measured by one criterion -- how they are doing in terms of bottom line performance.

This brings me to the <u>third</u> point I would like to cover today -- some of the strengths and problems we face in achieving our goals.

You have undoubtedly deduced a number of both from the facts we've given so far. But let me touch on those we feel to be especially important, first with regard to our domestic earnings.

It has been said that we've had problems with the growth of our domestic trust and fiduciary profits, and that is correct. Both performance and profits in these areas have slipped over the past years.

We have, however, moved decisively to reverse this. We have restructured these operations to provide more management flexibility, including the creation of the Chase Investors Management Corporation New York as a subsidiary. We have introducted effective portfolio performance measurement. We are now compensating officers for their individual performance on the same basis as the rest of the Street.

So far this year, these steps appear to be paying off. While one sip doesn't make a spring, our portfolio performance has improved against standard measures. We want to do still better, but for the moment we believe we're on the right track.

It has been said that our position in correspondent banking has slipped, and I believe that is now incorrect.

The widely quoted statistics here are of a one-day nature and concern only one aspect of our institutional business. But if one uses these numbers,figures for last June 30 show that we have a substantial lead in gross deposits from commercial banks, both domestic and foreign. In fact the total lead over our nearest competitor is more than double what it was at a high point at the end of 1968.

Moreover, we are on the offensive. We have sharpened our emphasis on results and recently added a number of major accounts.

New products are being put in place, and we have returned to an aggressive posture with regard to our competition.

Another area on which we are placing real emphasis, as I mentioned before, is the management of our interest margins, the mix of our assets and liabilities, and the mix between our investment and commercial banking portfolios.

We are not yet satisfied with our asset/liability management or control of the net interest margin, but we're moving in the right direction and are making significant progress toward our goal -- the ability to orchestrate the entire Corporation for optimum profitability.

Our profitability evaluation mechanisms, which help us choose between options, are far better than they were five years ago, and they will be even sharper by the end of this year. Other management tools, which you have heard about, have greatly decreased our reaction time to change.

Moreover, we have created the new position of Chairman of the General Loan Committee with responsibility for loan portfolio policy, instituted monthly reviews of loan related performance against the overall business scenario, and established a program to upgrade the quality of our portfolio. These things have been done to reduce the level of loan losses from the overly high rate in recent years -- a rate which, as you know, has considerable impact on our bottom line.

Finally, we are strengthening our teamwork.

As our business becomes increasingly complex and interdependent, pulling together also gets tougher. But is also gets just that much more essential.

We have already noted a number of programs we have put in place to force cooperative effort -- a factor that is now a major aspect in our performance reviews of individual managers. These steps are working, and the growing emphasis on profitability planning is designed to tighten our teamwork even more.

In addition, we have created Executive Vice President level teams focused on specific interdepartmental problems which impede profit performance. One group is devoting itself to clearing up costly lapses between departments which create non-earning assets. Another group is making recommendations concerning the effectiveness, innovativeness and cost efficiency of the indirect and overhead expense areas of the Corporation. Groups such as these are designed to keep senior management attention on what is needed to orchestrate Chase better and make the cash register ring.

These joint undertakings are, we believe, enhancing everyone's spirit of competition, "can do" and common cause.

They are also creating a management climate that attracts and motivates the critical ingredient of our future success -- our people. As you have heard, we have a relatively young team, and we're very proud of it. Our people are eager to perform, not set in their ways, and determined to make the Corporation work as a whole.

What's more, our managers are clearly attuned to the growing emphasis on sales and service quality. We are sharpening our marketing capability by developing entirely new products, adapting existing services to meet broader needs, and exercising firmer quality control. But the key is people who want to sell, know how to sell, and know what to sell -- and, more and more, our people do!

Our people, new management tools, enhanced capacity to implement and sales orientation are all basic as we move to capitalize on our strengths and special future opportunities. Five of these have been mentioned by David -- retail, real estate, the middle market, management information and additional forms of international banking. I would like to expand on them briefly.

In the retail area domestically, you are well aware of our statewide expansion, which will make us the first down-state bank in all of New York's banking districts. In addition, you have heard of a number of other efforts designed to strengthen our retail distribution network.

Dial is particularly important. We feel strongly that the price we are prepared to pay is fully justified in view of Dial's excellent management, the quality growth record of the Dial operation, and the possibilities presented to serve the public through a retail presence in 33 additional states.

Internationally, our retail strategy is equally aggressive. Buttressing a rapidly growing base of finance companies, we have initiated retail banking operations in Germany, with others on the way elsewhere, and are expanding our credit card operations to the Caribbean. These steps will bring Chase retail products to markets with rapidly increasing consumer affluence. and the banking entities will also reduce our reliance on money market funds to finance our traditionally substantial international commerical banking business.

Additionally, we continue to emphasize and expand our real estate operations which provide a substantial percentage and growing amount of our earnings in both low and high interest rate periods.

Internationally, our real estate network is focused on a number of growing markets and we plan shortly to enter more. Domestically, fees for advisory services have increased and our entry into the Florida market has been a real success. The recently established Chase Manhattan Realty Capital Corporation will provide a vehicle for more intense and broad-scale penetration of nationwide markets.

Two other areas we believe offer opportunity for growth are the so-called middle market and the provision of financial information.

In all candor, our objectives in these fields are not yet matched by fully-developed strategies and tactics. We are, however, moving ahead with a number of plans both domestically and internationally, and we see both markets as a way to expand our earnings base. We see our evolving middle-market strategy, in particular, as an excellent chance to get in on the ground floor with today's smaller companies that will be the giants of tomorrow.

The Chase World Information Corporation, Chase Econometric Associates, and our other important information collection and analysis potentials, as well as other activities we are now considering, form a significant base for the development of a business which we believe has considerable long-term potential. The possible changing position of government regulation with regard to consulting services for correspondents and others holds major promise which we are ready and able to take advantage of.

We have already spent a great deal of time on the international area, so I will only say that we fully intend to intensify, not just maintain, our overseas efforts and profitability.

We are going to continue to search out aggressively innovative mechanisms, such as our Orion and Libra consortia, that place us in a leadership position, fill real financial needs, and impact positively on our bottom line.

In the future, we are also going to continue to expand actively our geographic coverage and range of services.

To this end:

-- We will continue supplementing our European efforts with more intensive marketing and new near-banking facilities.

-- We will focus increasingly on the Middle East and Africa, and we have created a new group devoted exclusively to this area.

-- And we will continue the pace we have set in the Pacific Basin and the Far East which will be an area of even faster growth.

This, then, has been a description of Chase and its earnings base, some of our efforts to correct weaknesses, and some of our initiatives to capitalize on what we view as our prime future strengths.

Let me end with a few quick overall observations.

Chase, today, is a basically different institution from what it was five years ago.

We have not only changed in terms of our business base, but in our fundamental focus and environment.

We have a management structure that can take better advantage of countercycles in our business, expand decisively, and deploy earnings assets more aggressively.

We are creating a climate that puts a premium on one thing -- bottom line performance.

To achieve that bottom line performance and become a real growth corporation, we must continue to do two things -- expand our earning assets, and improve our earnings on assets.

As I see it, to expand our earning assets, we must:

1. Develop more competitive business strategies.
2. Accelerate our expansion and diversification.
3. Build our base of talented, ambitious and creative people.
4. Sell.
5. Improve the quality of our services.
6. Reward our producers.

To improve the earnings on our assets, we must:

1. Improve our asset-liability management.
2. Employ profitability analysis to achieve the optimum balance among our business lines.
3. Control expenses.
4. Reward those managers who employ our resources with maximum efficiency and impact.

Our mission is to take these ten ingredients and make them our ten commandments.

There are no overnight miracles, but I believe we have a solid organization, an excellent and expanding business base, the necessary management tools, competitive strategies, and aggressive tactics.

We intend to use this base to achieve the hard-hitting type of performance you and we expect of a growth corporation.

Overseas Branches

	1968	1969	1970	1971	1972
Caribbean, Latin America & Canada	30	32	38	44	56
Europe & Africa	9	11	14	18	19
Asia & Middle East	11	12	13	15	20
Total	50	55	65	77	95

Subsidiaries

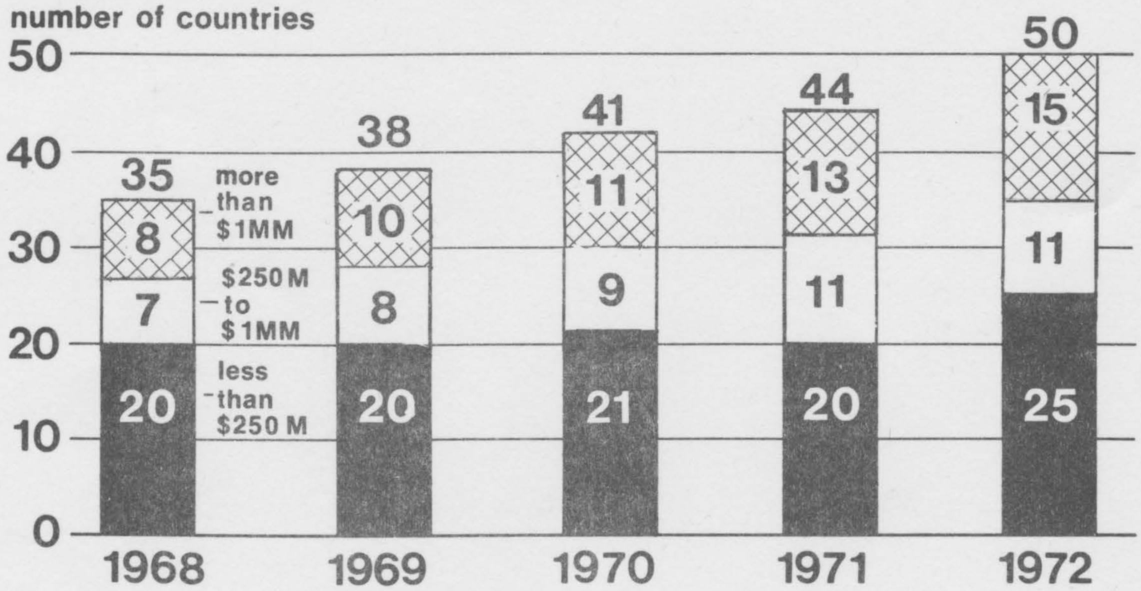
	1968	1969	1970	1971	1972
Caribbean, Latin America & Canada	8	10	12	14	17
Europe & Africa	3	5	5	5	7
Asia & Middle East	-	-	-	1	2
Total	11	15	17	20	26

Affiliates

	1968	1969	1970	1971	1972
Caribbean, Latin America & Canada	2	2	2	2	4
Europe & Africa	4	4	7	7	10
Asia & Middle East	1	4	4	6	9
Total	7	10	13	15	23

Slide 2

Countries by Size of Contribution to Pre-Tax Overseas Earnings



Slide 3

Growth in Size of Overseas Pre–Tax Earnings by Number of Countries

	1968	1972		
		Less than $250M	$250M to $1MM	More than $1MM
More than $1MM	8			8
$250–$1MM	7	3	2	2
Less than $250M	20	9	8	3
Total	35			
New Countries Since 1968	15	13	0	2
Total Countries 1972	50	25	10	15

Slide 4

International Subsidiaries and Affiliates

Commercial Banks	16
Finance Companies	11
Merchant Banks	7
Edge Corporations	4
Mortgage Banking Companies	2
Leasing Companies	2
Investment Advisory Companies	2
Consulting Companies	1
Other	4
Total	49

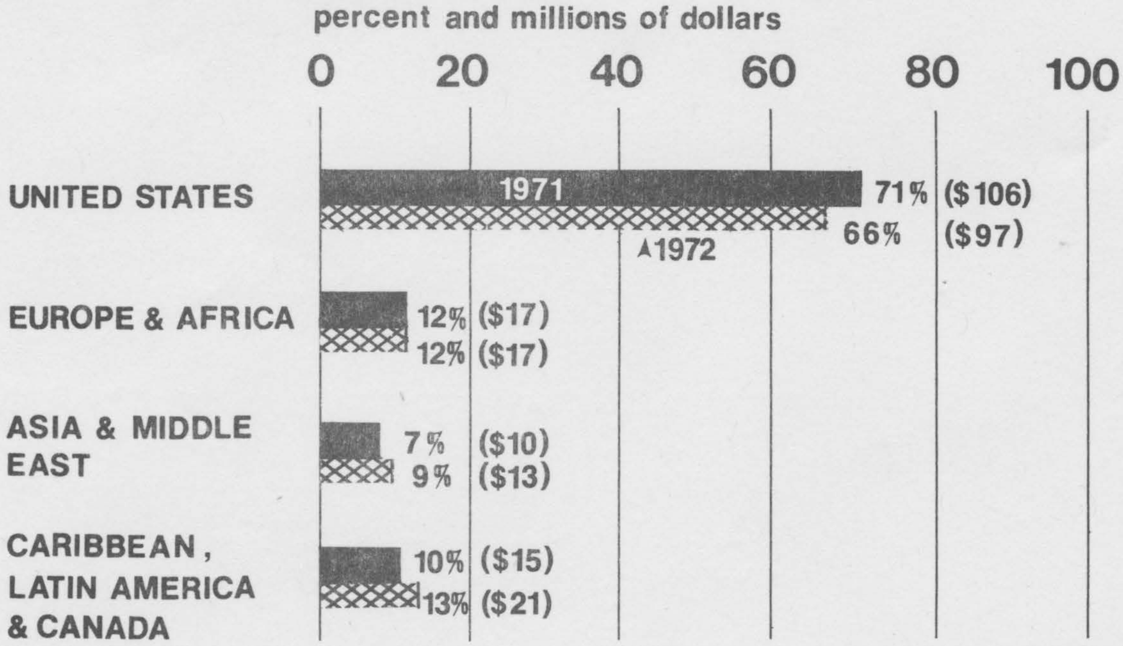
Slide 5

Domestic Network

	1968	1969	1970	1971	1972
Metropolitan Area Branches	147	152	158	170	178
Domestic Subsidiaries	2	3	3	5	10

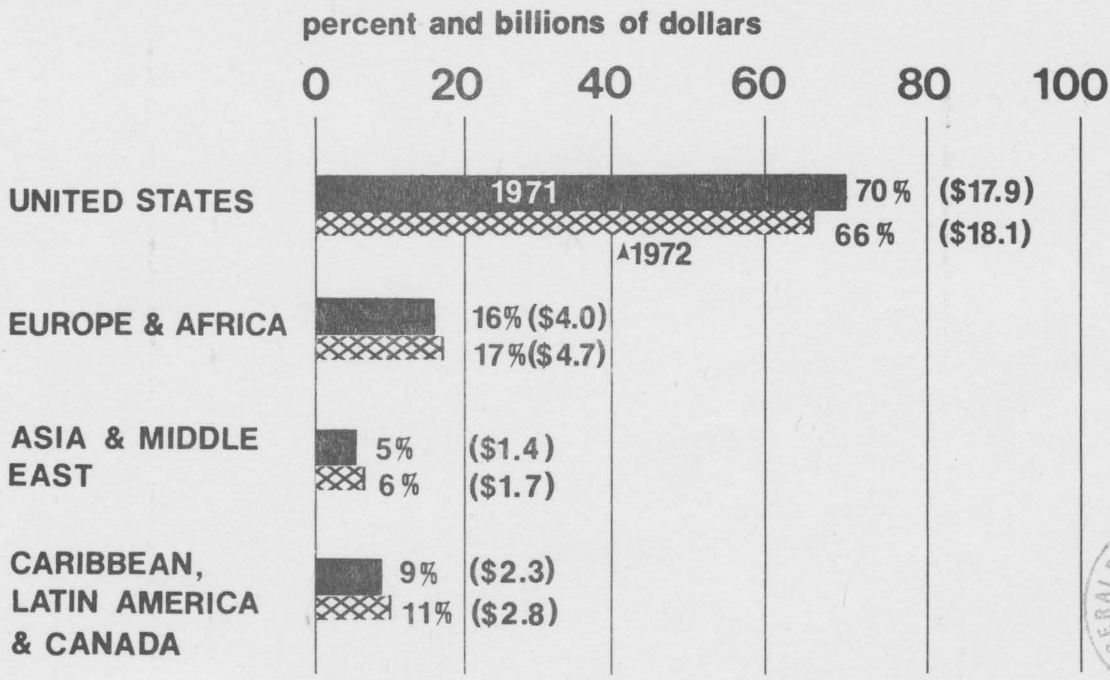
Slide 6

Geographic Sources of Income before Securities Transactions



Slide 7

Assets Employed by Geographic Area



THE CHASE MANHATTAN BANK
National Association

1 Chase Manhattan Plaza, New York, New York 10015

DAVID ROCKEFELLER *Chairman of the Board*

BOARD OF GOVERNORS OF THE FEDERAL RESERVE
1973 SEP 10 PM 12
RECEIVED
OFFICE OF THE CHAIRMAN

September 4, 1973

The Honorable Arthur F. Burns
Chairman, Board of Governors of the
Federal Reserve System
Federal Reserve Building
Constitution Avenue, N.W.
Washington, D. C.

Dear Arthur:

Vernon Jordan, Executive Director of the National Urban League, has asked me to serve as Dinner Chairman of this year's Equal Opportunity Day Dinner. On this occasion James A. Linen will be honored for his five years of dedicated service as President of the League and his distinguished contributions to equal opportunity for all Americans.

The Dinner will be held in the Grand Ballroom of The New York Hilton Hotel on Wednesday evening, November 14, 1973. Past award recipients have included former Chief Justice Earl Warren, Robert A. Sarnoff, Thomas J. Watson, Charles Evers, Kenneth A. Gibson, Walter Reuther, and Whitney M. Young, Jr.

Because I feel that Jim Linen is, indeed, a most worthy recipient for this year's Equal Opportunity Day Award, I was pleased to accept Vernon's invitation and I hope you will serve with me as a member of the Honorary Dinner Committee. Though the calls upon your time will be quite minimal, your counsel, cooperation and support will be invaluable in making this year's dinner a worthy tribute to Jim.

Our Committee will hold only one meeting on Tuesday, September 18, at 4:30 p.m. at the Chase Manhattan Bank offices, 410 Park Avenue (fourth floor). Please mark your calendar both for the Dinner date and the Committee Reception date. A reply card is enclosed for your convenience.

I look forward to having you on the Committee and to seeing you at the meeting on September 18.

Sincerely,

David

Called 9/18/73 — will serve on committee
CM

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM

1973 SEP 10 PM 1:26

RECEIVED
OFFICE OF THE CHAIRMAN

David Rockefeller

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM

Office Correspondence

Date: May 30, 1973

To: Chairman Burns

From: Brenton C. Leavitt B.C.L.

Subject: Acquisition of Standard-Chartered Bank Group Limited, London, by Chase Manhattan Bank.

In September, 1969, the Board approved the acquisition of about 15 per cent of the shares of Standard-Chartered Bank Group Limited, London, upon condition that an interest of Chartered in a California bank subsidiary be sold within one year or that domestically oriented banking business be eliminated within two years. Chase has been unable to comply with the Board's order, and on April 18, 1973, the Board informed the bank that a proposal to shift the shares of the California subsidiary of the Chartered Bank of London to a pension trust would not be acceptable.

On April 18, 1973, the Board ordered Chase to divest its shares in the group on or before April 18, 1974, to submit to the Board a plan of divestiture within 90 days, and to furnish reports at 90-day intervals thereafter of progress made in disposing of those shares.

The Board's letter dated April 18, 1973, (copy attached) refers to no deadline other than that Chase must submit a plan of divestiture within 90 days - July 18, 1973.

Leavitt

DR

Mr. Gardner

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM
WASHINGTON, D. C. 20551

ADDRESS OFFICIAL CORRESPONDENCE
TO THE BOARD

April 18, 1973

Mr. William S. Ogden, Executive Vice President
The Chase Manhattan Bank National Association
1 Chase Manhattan Plaza
New York, New York 10005

Dear Mr. Ogden:

Reference is made to your letter of March 16, 1973, requesting the Board to extend until April 18, 1974, the time in which your bank ("Chase") might take appropriate steps with regard to Chase's holding of shares in Standard and Chartered Banking Group Ltd. ("Group") that would constitute compliance with the Board's letter of April 18, 1972. Further reference is made to your letter of April 5, 1973, which requested a Board ruling that a proposal to shift the shares of the Chartered Bank of London, San Francisco, California, now held by the Chartered Bank Ltd. to a pension trust of one of the banks in the Group would constitute compliance with the Board's letter of April 18, 1972.

In the Board's opinion, the proposed pension trust arrangement would continue to place control of the California bank within the Group and the Group would consequently remain engaged in activities in the United States of a kind other than those incidental to an international or foreign business. Accordingly, the Board would not regard that arrangement as a satisfactory means of compliance with the conditions attached to the Board's consents to your holding of shares in the Group.

It appears to the Board that efforts to achieve a reorganization of the Group's activities in the United States or otherwise to meet the conditions in the Board's consents have failed. Therefore, the Board hereby orders Chase to divest its shares in the Group on or before April 18, 1974, to submit to the Board a plan of divestiture within 90 days, and to furnish reports at 90-day intervals thereafter of progress in disposing of those shares. This order shall be effective immediately and shall remain in effect unless within a period of

90 days from the date of this letter Chase shall have submitted, and the Board shall have found satisfactory, an alternative means of compliance with the conditions attached to the Board's earlier consents.

Very truly yours,

(signed) Tynan Smith

Tynan Smith
Secretary of the Board

Mr. Gardner

April 18, 1973

Eugene J. Keogh, Esq.
Halpin, Keogh & St. John
630 Fifth Avenue
New York, N. Y. 10020

Dear Mr. Keogh:

Reference is made to your request on behalf of the Standard-Chartered Banking Group, Limited, London, England, for a ruling that Standard-Chartered is engaged, directly or indirectly, in the United States only in activities that are incidental to its international or foreign business within the meaning of sections 25 or 25(a) of the Federal Reserve Act, and to your letters of January 10, January 22, January 25, February 22, March 1, and March 30, 1973, in support of that contention.

Chase Manhattan Overseas Banking Corporation, New York ("CMOBC"), acquired shares of Standard-Chartered pursuant to section 25(a) of the Federal Reserve Act which authorizes any corporation organized thereunder to purchase and hold, with the Board's consent, shares of any corporation not engaged in the general business of buying or selling goods, wares, merchandise or commodities in the United States and not transacting any business in the United States except such as in the Board's judgment may be incidental to its international or foreign business. Chase Manhattan Bank, N.A., New York, acquired those shares from CMOBC and holds them under a similar restriction pursuant to section 25 of the Federal Reserve Act which authorizes any national bank to acquire and hold, with Board approval, stock in any foreign bank that is not engaged, directly or indirectly, in any activity in the United States except as, in the Board's judgment, shall be incidental to the international or foreign business of such foreign bank.

Based on the information available to the Board and after full consideration of your views, the Board declines to make the requested ruling. It appears that Standard-Chartered is engaged indirectly through the Chartered Bank of London, San Francisco, California, in activities in the United States that involve the conduct of purely domestic banking business and that the Board would not consider to be incidental to international or foreign business.

Very truly yours,

(signed) Tynan Smith

Tynan Smith
Secretary of the Board

PG:jmcc
4-18-73

April 13, 1973

To: Board of Governors

From: Legal Division
(P. Gardner, Jr.)

Subject: Chase Manhattan Bank ("Chase") investment in the Standard-Chartered Bank Group Limited, London ("Standard-Chartered"), which owns all of the shares of Chartered Bank, London ("Chartered"), which owns all of the shares of the Chartered Bank of London, San Francisco ("Chartered-California").

ACTIONS REQUESTED

1. Disapproval of Chartered-California's request for a ruling that it is doing no business in the United States except such as is incidental to Standard-Chartered's international or foreign business and that Chase should therefore be permitted to continue to hold 13.5 per cent of Standard-Chartered's voting shares.

2. Disapproval of Chase's request for a ruling that it should be permitted to continue to hold such Standard-Chartered shares if Standard-Chartered places 60 to 100 per cent of Chartered-California's voting shares in its employee pension trust.

3. Staff* recommends that the Board order Chase to divest its shareholding in Standard-Chartered on or before April 18, 1974, and to make quarterly reports to the Board regarding progress in locating a buyer or buyers for Chase's shares.

HISTORY OF BOARD ORDERS

March 24, 1965 - The Board approves investment by Chase Manhattan Overseas Banking Corporation ("CMOBC") in not more than 20 per cent of the shares of Standard Bank at a cost not to exceed $25 million.

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* Concurrence: Division of Supervision and Regulation (Mr. Dahl).

November 17, 1965 - The Board rules that Standard Bank's agency in New York may invest temporarily idle funds in brokers' loans, prime commercial paper, Federal funds and short-term obligations of U.S. banks.

September 29, 1969 - The Board approves CMOBC's acquisition of approximately 15 per cent of the shares of Standard-Chartered through exchange of Standard Bank shares (as a part of the formation of Standard-Chartered as a holding company to own Standard Bank and Chartered Bank, and through purchase of additional shares) upon condition that Chartered Bank either sell its interest in Chartered-California within one year or eliminate the domestically-oriented banking business done by Chartered-California within two years.

January 23, 1970 - The Board makes an order essentially repeating the terms of the September 29, 1969, order, with time periods to run from the date of acquisition of Standard-Chartered's shares. It also rules that Chartered's branches or agencies in the United States may temporarily invest idle funds in brokers' loans, prime commercial paper, Federal funds, and short-term obligations of U.S. banks.

January 5, 1972 - The Board grants Chase Manhattan Bank permission to acquire CMOBC's 13.77 per cent shareholding in Standard-Chartered subject to the conditions in outstanding consents.

April 18, 1972 - The Board approves CMOBC's continued holding of Standard-Chartered shares provided that Chartered Bank shall sell its shares in Chartered-California on or before April 18, 1973.

ESSENTIAL FACTS

1. Chase's shareholding in Standard-Chartered is its largest foreign investment -- valued at approximately $90 million. (Chase has an unrealized capital gain of approximately $60 million.)

2. Chartered-California had total deposits of approximately $42 million as of December 31, 1971. It is very small in relation to Standard-Chartered's worldwide operations (total deposits $5,974,000,000). Chartered-California is engaged in general banking business, including local, purely domestic banking services as well as international financing.

3. Chase originally invested in Standard Bank to develop an operating capability in Africa. (It sold certain African subsidiaries to Standard.)

4. Chase has been undertaking studies looking toward possible realignment of its African strategy, since Chase anticipates further penetration of the U.S. market by Standard-Chartered that will cause additional regulatory problems under the Board's standard of business "incidental" to international or foreign business.

5. Chase has the contractual undertaking of Standard-Chartered to comply with requirements of U.S. law regarding its U.S. activities necessary to ensure that Chase will not be required to dispose of its Standard-Chartered shares.

6. Standard-Chartered has indicated that it does not regard itself as being legally obligated to dispose of its Chartered-California shares.

7. Standard-Chartered is alleged to be the last major independent among Britain's "overseas banks". Possibly, Chase's

13.7 per cent shareholding -- when combined with other substantial minority shareholdings -- suffices to prevent a takeover of Standard-Chartered by other British banks because a merger with another bank would reportedly require the support of 75 to 85 per cent of Standard-Chartered's voting shares.

8. It is alleged by Chase that disposal of Chartered-California shares by Standard-Chartered had been proposed at the specific request of Chartered's Chairman, W. George Pullen. Chase claims that competitive considerations associated with the success of Barclays in the U.S. market have led Standard-Chartered to realign its worldwide strategy toward increased interest in the U.S. market. Disposal of Chartered-California would run counter to such plans.

EDGE ACT PROBLEM

"Incidental" business test as applied to a minority investment.

CMOBC's shares in Standard-Chartered have been transferred to Chase, as a direct investment in a foreign bank under section 25 of the Federal Reserve Act. Even a minority noncontrolling investment in a foreign bank is subject to the condition that the foreign bank shall not be engaged, directly or indirectly, in any activity in the United States except as, in the Board's judgment, shall be incidental to the international or foreign business of such foreign bank.

The difficulties encountered in connection with this investment illustrate the problem in trying to regulate foreign minority investments. CMOBC took the precaution of obtaining a contractual undertaking from Standard-Chartered to refrain from activities, and cause its subsidiaries to refrain from activities, in the U.S. market that would require CMOBC (or its assignee, Chase) under U.S. law and regulation to dispose of its investment in Standard-Chartered. When such an agreement breaks down, the prospect of a lawsuit against a prestigious foreign bank in its home country does not offer an attractive alternative. Chase's practical options seem to be either to negotiate a reorganization of Standard-Chartered or to sell its shares.

Chase's counsel, in a telephone conversation with Mr. Gardner on April 12, 1973, indicated that all avenues for possible reorganization of Standard-Chartered have been explored, and that there is no acceptable reorganization plan that would sever Chase from any connection with Chartered-California, aside from the pension trust proposal discussed below. It does not appear that a further extension of time to work out a compromise solution would serve any useful purpose.

While the application of the "incidental" business limitation to minority noncontrolling investments operates harshly, perhaps this should simply be viewed as a business risk incident to this type of investment.

<u>Standard-Chartered's argument - redefining "incidental" business.</u>

The Legal Division does not concur in the argument of Standard-Chartered's counsel that Chartered-California's business (which includes domestically oriented banking activity) should be deemed to be "incidental" to Standard-Chartered's international or foreign business. This is essentially the same argument previously presented by Chase and rejected by the Board, and would involve a novel interpretation based solely on the small size of the domestic banking operation in relation to the worldwide business of the parent foreign bank.

BANK HOLDING COMPANY ACT PROBLEM

Multi-State banking operation.

Although the Board's orders were couched in terms of the "incidental" business standard of the Edge Act, an additional policy question under the Bank Holding Company Act arises by virtue of the fact that Chartered-California's operations are in a different State than Chase's head office. Section 3(d) of the Bank Holding Company Act prohibits the Board from approving any application by a bank holding company to acquire, directly or indirectly, under section 3 of the Act, the voting shares of an additional bank located in a State other than the State where the holding company's principal banking subsidiaries were located on the date it became a bank holding company.

Application of section 3(d) to the present situation is not clear; however, the policy behind section 3(d) would seem to support a narrow interpretation of the "incidental" business standard of the Edge Act. Here, Chase does not control Standard-Chartered and, arguably, therefore, does not own or control "indirectly" any voting shares of Chartered-California. However, the ownership scheme (Chase having a 13.7 per cent interest in a holding company that indirectly -- through its wholly-owned subsidiary, Chartered Bank -- controls all of Chartered-California's shares) may render legally supportable the contrary contention that Chase "indirectly" owns an interest in Chartered-California, through the device of an intermediate holding company, proportionate to its shareholding in the holding company.

Such problems of legal construction can be avoided altogether by a restrictive interpretation of the "incidental" business standard of the Edge Act, so as to preclude the incipience of a situation in which a member bank owns a minority interest in a foreign bank doing a domestically oriented banking business, directly or indirectly, in the United States.

In the Legal Division's view, it is important to avoid setting a precedent that would tend to support the legality of 6 to 24 per cent investments by bank holding companies in bank holding companies located in other States.[1/]

FOREIGN BANK ASPECT

Under the Edge Act, the Board has permitted financing of export-import transactions, but has not permitted financing of the purely domestic credit needs of foreign customers (e.g. - financing of local plant, equipment, inventory). Foreign banks such as Standard-Chartered are keenly interested in being able to finance all of the credit requirements of their foreign customers in the U.S. market on a multi-State basis. (Compare: Both Schroder and French American indicated dissatisfaction with the possible reorganization of their New York "investment company" operations to comply with the narrow Edge Act standard of business "incidental" to international or foreign business.)

Standard-Chartered's activities in the United States are consistent with present rules governing the activities of foreign bank

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1/ A further legal discussion of the Chase and Standard-Chartered arguments is contained in Attachment "C".

holding companies in the United States. A regulatory problem arises only because of Chase's investment in Standard-Chartered. For this reason, Standard-Chartered alleges that the Board's ruling discriminates against it as compared with its foreign bank competitors in the United States. However, technically, the Board's orders have been directed to Chase and not to Standard-Chartered. Disposition by Chase of its Standard-Chartered shares would cure any immediate U.S. regulatory problems for Standard-Chartered, but at the cost of losing Chase as an international partner.

PENSION TRUST PROPOSAL

Chase does not control Standard-Chartered or Chartered-California. It presently has an indirect 13.7 per cent interest in the equity of Chartered-California. Chase expects that Standard-Chartered may propose the reduction or elimination of this participation by Chase in the earnings of Chartered-California through the placing of 60 to 100 per cent of Chartered-California's stock in an employee pension trust of Standard Bank or another bank in the Standard-Chartered group. Such purchase by the pension trust would be largely financed by borrowings from a bank within the Standard-Chartered group. (Chase asks that this information be accorded confidential treatment.)

Chase concedes that the proposal does not represent a long-range solution to the problem of anticipated further expansion of Standard-Chartered's activities in the U.S. market.

The pension trust proposal does not take account of sections 2(g)(2) and 2(g)(3) of the Bank Holding Company Act. Under those sections, Standard-Chartered would be presumed to continue to control Chartered-California after the transfer. Although, arguably, Chase would no longer have a stake in Chartered-California's earnings (assuming ability of the pension trust to carry the debt incurred to acquire Chartered-California), Chase's influence over the conduct of the California operations would be no different than prior to the transfer.

Since there is no long-range solution in view, the Legal Division doubts the merits of adopting a patchwork solution to the problem over the shorter run.

CONCLUSION

The Legal Division recommends that Chase be given an additional year to divest its shares in Standard-Chartered. Although this matter has dragged on for three years, considerations relating to (a) the disappointment of legitimate expectations that Standard-Chartered itself would take the necessary curative measures and (b) the overriding importance of Standard-Chartered's operations to Chase's strategy for the African market (and Chase's need for time to implement alternate plans) justify the length of the proposed divestiture period. Since Chartered-California is still quite a small competitor in California, it is doubted that such an extension of time would have any serious adverse effect on the public interest.

Attachments - "A" Correspondence with Chase
"B" Correspondence with Standard-Chartered
"C" Additional legal analysis

(Attachments "A" and "B" have been distributed to each of the Governors and are available in the Secretary's office upon request.)

/

ATTACHMENT "C"

LEGAL ANALYSIS OF CHASE AND STANDARD-CHARTERED CONTENTIONS

To grant the relief requested by Standard-Chartered (releasing Chase from the condition imposed in the Board's Order of April 18, 1972), the Board would have to accept one of the following propositions:

1. (a) That Congress intended, through the Bank Holding Company Act, to permit any bank holding company to acquire a noncontrolling (albeit more than 5 per cent) interest in the voting shares of any other bank holding company without Board approval and even though the banking operations of the two organizations are in different States, and

(b) That, despite the fact that paragraph 8 of the Edge Act (or paragraph 4 of section 25 of the Federal Reserve Act) is worded in such fashion as to literally prohibit even noncontrolling investments by member banks or Edge corporations in foreign banks doing a local, purely domestic banking business in the United States, the Board should rule that the governing standards are those of the more modern statute (the Bank Holding Company Act) and that a noncontrolling investment that would be permissible to a bank holding company under (a) above may also be made through a member bank or Edge Act subsidiary of the bank holding company. (In effect, the Bank Holding Company Act would be read as modifying or partially superseding the Federal Reserve Act, including the Edge Act, in such situations.)

COMMENT

The first part of this proposition conflicts with the staff's interpretation of section 3(d) of the Bank Holding Company Act. While it is not clear that section 3 approval is required for a bank holding company to make a noncontrolling (albeit more than 5 per cent) investment in another bank holding company, staff believes that the better view is that such an investment would require Board approval under section 3(a)(3) as an "indirect" investment in shares of an additional bank. Chase and Standard-Chartered contend that the word "indirectly" in section 3(a)(3) applies only if the investing bank holding company controls the intermediary bank holding company which is being invested in. At least where the intermediary bank holding company owns all of the shares of its subsidiary bank, staff believes that the Board is legally entitled to regard the intermediary bank holding company as a device whereby the investing bank holding company is able "indirectly" to own a 5 per cent interest in the former's subsidiary bank. (For example, the Savings and Loan Holding Company Act uses the word "indirectly" in juxtaposition to the words "through one or more subsidiaries" -- see 12 U.S.C. 1730a(a)(2). Court decisions on the subject of the meaning of the word "indirectly" are inconclusive. "Indirectly" signifies the doing by an obscure, circuitous method of something which is prohibited from being done directly, and includes all methods of doing the thing prohibited except the direct one.)

A variation of Chase's argument is that such minority noncontrolling investments are governed by section 4 rather than section 3, and may be permitted where the Board finds them to be consistent with the public interest under either section 4(c)(8) or 4(c)(9). Consistent with staff's recommendation, the Board has interpreted section 4(c)(9) as being applicable only to investments <u>by</u> foreign bank holding companies and <u>not</u> to investments <u>in</u> foreign bank holding companies by other companies. Also, staff believes that investment in a bank holding company at the minimum involves public interest considerations germane to section 3 (and would also involve section 4 questions only if the bank holding company to be invested in also engages in <u>nonbanking</u> activities, and not simply in managing or controlling banks). Staff believes that the scheme of the statute warrants treating the question of noncontrolling investment by a bank holding company in another bank holding company under section 3, rather than section 4. Staff concedes that the statute is ambiguous. (Section 4(a)(1) prohibits investment in the voting shares of any company other than a "bank". Literally, the prohibition would cover a "bank holding company".) The Board is free to rule either way. (<u>Note</u> that section 3(d) prohibits only certain approvals under section 3, and <u>not</u> approvals under section 4.)

2. (a) That Congress intended, through the Bank Holding Company Act, to permit any <u>domestic</u> bank holding company to acquire a noncontrolling (albeit more than 5 per cent) interest in the voting shares of <u>any foreign</u> bank holding company <u>with</u> Board approval and even though the banking operations of the two organizations are in different States, and

(b) Same line of reasoning as 1(b).

<u>COMMENT</u>

Since there is no special language in sections 2 or 3 of the Act suggesting that investments in foreign bank holding companies are to be regarded differently than are investments in domestic bank holding companies, the first part of this proposition relies upon the Chase variation discussed above, which would place the matter of noncontrolling investment by domestic bank holding companies in foreign bank holding companies under section 4(c)(9) rather than under section 3. Staff rejects this view, as discussed above.

3. (a) That Chartered-California's local, purely domestic banking business should be considered "incidental" to the international or foreign business of Standard-Chartered within the meaning of paragraph 8 of the Edge Act or paragraph 4 of section 25 of the Federal Reserve Act (because it is small in relation to Standard-Chartered's worldwide business), and

(b) That Chase's investment is governed by section 4, rather than section 3, of the Bank Holding Company Act, and is exempt under section 4(c)(5) as the kind of investment that a national bank can make under the Federal Reserve Act, including the Edge Act.

COMMENT

The first part of this proposition involves an interpretation that the Board has always rejected.

4. That the Chase and Standard-Chartered situation is unique and should be "grandfathered" under equitable principles, regardless of the literal wording of the statutes, since there is no evidence of inconsistency with any purpose of the Bank Holding Company Act or of the

Federal Reserve Act, including the Edge Act, so long as Chase does not exercise any control, direct or indirect, over the policies or management of Chartered-California.

COMMENT

There is some appeal to this proposition, since it may reasonably be asked what harm is done to the public interest, so long as Chase does not actually exercise any control over the operations of Chartered-California. Nevertheless, there are several considerations which lead staff to recommend against this alternative:

(a) There is no legal basis for "grandfathering" such a situation.

(b) The usual facts supporting a "grandfathering" approach are not present -- i.e., an investment that was legal when made, but is inconsistent with later statutory amendments, and where actual abuses with which the statutory amendments are concerned either are not present or are not of sufficient magnitude as to warrant requiring divestiture.

Concededly, CMOBC's investment in Standard Bank was legal when made. However, its subsequent (or successor) investment in Standard-Chartered never attained a permanent legal status because of inability or failure to comply with Board conditions regarding the making of such investment (i.e. - elimination of the domestic orientation of Chartered-California's business or divestiture of Chartered-California). Therefore, it cannot really be said that CMOBC's investment in Standard-Chartered was legal when made. Its legality was dependent upon conditions subsequent which have not been fulfilled. Those conditions were imposed by the Board prior to CMOBC's making of the investment in Standard-Chartered.

(c) An exception created for Chase would establish a precedent for similar action by other bank holding companies which may be confronted with similar problems -- (e.g. - Mellon's approximately 15 per cent noncontrolling investment in BOLSA, or Citibank's 40 per cent "non-controlling" investment in National and Grindlays Bank).

(d) There is value in a sanitary rule -- drawn at a level of 5 per cent ownership -- which obviates the need to make, and to police, difficult "control" determinations. For example, in the Banco di Roma case, involving an area of similar sensitivity to the multi-State banking question (the Glass-Steagall Act), the Board stated that "[W]hile there is no reason to doubt the sincerity of the Banco di Roma's plan to insulate the operations of its subsidiary bank in Chicago from the operations of EuroPartners [a securities broker], adoption of such a plan as a general guideline for conforming the operations of any bank holding company to the policies of the Glass-Steagall Act would pose very difficult supervision problems for the Board which, in the Board's judgment, render such a plan unworkable." (Sept. 1972 Bulletin 940, at p. 941.) A strict rule here would avoid similar problems with the policing of arrangements that potentially compromise the rule against multi-State banking operations.

Admittedly, Chartered-California (deposits $42 million) is not a large bank. However, there is no statutory basis for distinguishing according to the size of the bank, nor was there any inclination of the Board to make any such distinction in the Banco di Roma case, which involved a de novo bank.