

ALASKA LEGISLATURE SPECIAL COMMITTEE / SUBJECTS 8072

151 SCOMM 9: HOUSE SPEC. COMM. ON PERMANENT FUND 1977-78

Significantly, non-earning loans which amounted to 74% of total problem investments for these five REIT's seven quarters ago declined to only 39% of total problem investments in the latest quarter. Even more vividly, the dollar amount of non-earning loans declined 26% during this period while foreclosed properties increased 235%. Since earning foreclosed properties have increased to 41% of total foreclosed properties during this period, we expect some significant reduction of total problem properties in the next year and a dramatic reduction over the next two years.

Again, we emphasize the significance of this good news lies beyond the positive prospects for these five REIT's (in the form of higher dividends). The progress illustrated here and likely over the next two years, should mirror the progress . . . although in a somewhat premature way . . . likely to be experienced by banks with their problem real estate loans.

RR-77-65

-Research Department-

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COMMERCIAL BANKS

	Shares O/S (Mil.)	Recent Price	1977 Price Range	Mkt. Cap. (Mil.)	EPS		Earnings Per Share*				P/E		Book Value	Premium (Discount) on Book	Indicated		
					Growth Rate	10 Yr.	5 Yr.	1974	1975	1976	1977 E	1976			1977	Div.	Yield
Eastern																	
Bankers Trust	11	\$38	\$42-36	\$ 418	1%	Neg	\$6.82	\$5.88	\$4.76	\$5.25	8.0X	7.2X	\$61.80	(38)%	\$3.00	7.9%	
Chase Manhattan	32	30	33-30	960	Neg	Neg	5.00	4.30	2.94	4.00	10.2	7.5	52.00	(42)	2.20	7.3	
Chemical New York	14	42	45-40	588	4	6%	5.96	6.35	5.92	6.50	6.6	6.0	60.01	(30)	2.88	6.9	
Citicorp	125	29	34-27	3,625	13	16	2.51	2.73	3.08	3.50	9.4	8.3	20.67	40	0.96	3.3	
Manufacturers Hanover	30	39	41-36	1,170	9	15	4.28	4.59	4.82	5.30	8.0	7.4	36.57	7	1.92	4.9	
Mellen National Bank	10	55	58-53	550	6	10	6.18	6.49	6.62	7.10	8.3	7.7	67.19	(18)	2.60	4.7	
J. P. Morgan	39	51	57-50	1,989	11	12	4.69	4.96	5.04	5.30	10.1	9.6	37.61	36	2.00	3.9	
Southern																	
NCNB Corp.	17	\$12	\$12-10	\$ 204	9%	Neg	\$1.05	\$1.10	\$1.20	\$1.40	10.0X	8.6X	\$12.53	(4)%	\$0.52	4.3%	
Wachovia Corp.	11	18	21-17	198	7	3%	1.78	1.96	2.03	2.10	8.9	8.6	14.60	23	0.54	3.0	
Midwestern																	
Continental Illinois Corp.	18	\$55	\$60-56	\$ 990	11%	13%	\$5.53	\$6.84	\$7.45	\$8.20	7.4X	6.7X	\$51.54	6%	\$2.40	4.4%	
First Chicago Corp.	40	20	22-19	800	8	4	2.65	2.67	2.35	2.80	8.5	8.5	24.12	(17)	0.96	4.8	
National City Corp.	7	43	45-41	301	10	13	3.91	4.56	5.00	5.40	8.6	8.0	32.42	33	1.85	4.3	
National Detroit	12	26	29-25	312	9	6	3.42	4.05	4.38	4.70	5.9	5.5	39.07	(34)	1.52	5.8	
Southwestern																	
First City Bancorp of Texas	10	\$34	\$37-31	\$ 340	12%	12%	\$2.70	\$3.11	\$3.45	\$3.80	9.9X	8.9X	\$24.08	41%	\$1.00	2.9%	
First International Bancshares	15	38	43-38	570	14	14	3.11	3.51	3.80	4.15	10.0	9.2	25.14	51	1.20	3.2	
Republic of Texas	11	32	34-30	352	12	17	3.48	4.01	3.98	4.40	8.0	7.3	28.65	12	1.20	3.7	
Texas Commerce	12	35	39-34	420	14	15	2.50	2.97	3.27	3.70	10.7	9.5	19.73	77	1.10	3.1	
Western																	
Bank America	146	\$26	\$30-25	\$3,796	11%	15%	\$1.86	\$2.19	\$2.40	\$2.75	10.8X	9.4X	\$15.78	65%	\$0.80	3.1%	
Crocker National	12	27	29-25	324	5	3	2.29	3.35	3.40	3.80	7.9	7.1	33.20	(19)	1.66	6.1	
Seafirst	9	34	35-32	306	11	13	3.28	3.61	4.05	4.50	8.4	7.6	30.45	12	1.24	3.6	
Wells Fargo	20	26	28-26	520	9	11	2.53	2.80	3.16	3.75	8.2	6.9	27.08	(5)	1.12	4.3	

* Fully diluted where appropriate

SAVINGS AND LOAN ASSOCIATIONS

	Shares O/S (Mil.)	Recent Price	1977 Price Range	Mkt. Cap. (Mil.)	Earnings Per Share						P/E		Indicated Div.	Yield	
					1971	1972	1973	1974	1975	1976	1977E	1976			1977
First Charter	29.6	\$15	\$17-13	\$440	\$1.50	\$1.73	\$1.34*	\$1.64	\$1.70	\$1.50	\$3.10	6.0X	4.8X	\$0.60	4.0%
Gibraltar	8.6	10	10- 8	86	0.87	1.24	1.41	0.95	1.18	1.95	2.70	5.1	3.7	0.40	4.0
Great Western	14.9	23	24-20	345	2.03	2.50	2.75	2.25	1.53	3.30	4.35	7.0	5.3	0.50	2.2
Imperial Corporation	13.7	16	17-15	219	1.22	1.60	1.81	1.72	2.06	2.98	3.60	5.4	4.4	0.24	1.5
United Financial	6.5	12	13-11	78	1.16	1.28	1.56	1.27	1.40	2.30	3.20	5.2	3.8	0.40	3.3

*After a loss from security transaction of 43¢.

REAL ESTATE INVESTMENT TRUSTS

	Fiscal Year	Shares O/S (Millions)	Mkt. Cap.	Earnings Per Share				1977 Price Range	Recent Price	Book Value	Quarter Div. X4	Yield on Last Quarter Div.
				FY 1976	Last 12 Mos.	Last Qtr. 4X	Est. FY 1977					
Long-Term Trusts												
Conn. General *	March	5.7	\$103	\$1.68	\$1.64	\$1.64	\$1.60	\$20-16	\$18	\$19.24	\$1.60	8.9%
Equitable Life	Oct.	5.6	128	2.07	2.16	2.36	2.40	26-23	23	23.66	2.20	9.6
Mass. Mutual	Oct.	4.7	66	1.09	1.11	1.16	1.30	15-12	14	19.38	1.16	8.3
Mony	May	8.8	88	0.84	0.87	0.88	1.00	11-10	10	9.92	0.92	9.2
Northwestern Mutual	March	4.8	62	0.52	0.76	0.88	0.90	14-12	13	19.08	1.00	7.7
Hotel Investors	Aug.	1.5	18	1.01	0.98	1.28	1.30	13-12	12	17.78	1.28	10.7
PNB Mortgages	Sept.	2.4	19	0.46	0.48	0.52	0.75	9- 8	8	18.49	0.40	5.0
RAMPAC	Nov.	1.9	23	1.14	1.14	1.28	1.00	12-10	12	18.08	1.16	9.7
Equity and Short-Term												
General Growth Corp.	Sept.	6.2	136	1.16	1.12	1.16	1.30	23-21	22	6.14	1.40	6.4
Lomas & Nettleton	June	3.7	56	1.16	0.71	0.84	0.90	16-14	15	31.61	0.84	5.7
Property Capital	July	2.1	23	1.19	1.20	1.20	1.25	12-11	11	13.67	1.20	10.9
Saul (B.F.)	Sept.	5.7	17	NA	-	-	-	4- 3	3	7.27	0.00	-

PRIVATE MORTGAGE INSURERS AND MISCELLANEOUS

	Fiscal Year	Shares O/S (Millions)	Mkt. Cap.	Earnings Per Share					1977 Price Range	Recent Price	1977 P/E	Yield	
				1972	1973	1974	1975	1976					1977E
AMIC	Dec.	2.2	\$ 31	\$0.98	\$1.27	\$1.03	\$1.07	\$2.44	\$3.10	\$18-14	\$14	4.5X	0.3%
FNMA	Dec.	48.3	773	1.79	2.25	1.90	2.00	2.18	2.30	17-15	16	7.0	5.1
MGIC	Dec.	22.0	330	1.28	1.95	1.20	0.10	1.15	1.80	21-15	15	8.3	0.5
Rouse*	Dec.	12.9	65	0.67	0.77	0.05	0.42	0.34	0.65	5- 4	5	7.7	0.0
United Guaranty	Dec.	3.8	48	0.77	1.05	0.85	0.11	1.86	2.40	14.11	12	5.0	0.0

*Cash flow per share instead of earnings per share used.

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ATLANTA	DENVER	NEW CANAAN, CT	ST. LOUIS	WASHINGTON, DC	HONG KONG
BOSTON	HARTFORD	NEW HAVEN	SAN FRANCISCO	WILMINGTON	LONDON
CENTURY CITY	HOUSTON	NEW YORK	SEATTLE		MONTREAL
CHICAGO	KANSAS CITY	OMAHA	TULSA	INTERNATIONAL	PARIS
CLAYTON, MO	LOS ANGELES	PHILADELPHIA	TROY, MI	CARACAS	ZURICH

David H. Kopf
Money Market Economist

April 15, 1977

Prices of fixed income securities traded in a narrow range until Thursday morning when the scrapping of the Administration Economic Stimulus Program sent prices soaring. A massive increase in the monetary aggregates, and a strong gain in March industrial production, announced on Thursday, produced only modest re-trenchment, and by mid-day on Friday intermediate Government issues were yielding roughly 30 basis points less than a week earlier. Over the near term, prices may move down slightly from present levels as some of the initial exuberance over the Carter tax decision fades away.

The monetary aggregates surged in the week ended April 6: M1 rose \$5.0 billion to \$319.1 billion and M2 rose \$6.8 billion to \$761.5 billion. M1 is now-- (on a weekly basis)--above its long run target and is probably above the short run target as well. (M2 is at the top of its ranges.) The Federal Open Market Committee meets on Tuesday, but tightening action seems unlikely until the money managers get a better reading on the money supply for April.

The decision to cut back the Administration Stimulus Program, together with spending shortfalls and higher than projected revenues, have substantially reduced the projected Federal deficit. It would now appear reasonable to place the fiscal year deficit at \$58 billion including off-budget financing. (Or \$48 billion on the popular unified budget basis--\$20 billion under the earlier official estimate of \$68 billion.)

With the projected deficit reduced, the Treasury has considerable leeway in its financing operations, particularly in the current quarter, when the deficit will be modest, and might actually show a surplus. However, the Treasury cash balance is normally built up in the April-June quarter. In addition, the success of the policy of regular financing patterns would support the view that new cash will be raised, but in somewhat reduced volume, now that the stimulus package has been abandoned. The May refunding, to be announced about April 27 could thus follow the traditional pattern: new cash of \$1 billion through 3 year notes, a like amount through the 7 to 10 year issue and perhaps \$0.5 billion through a long bond. Regular two year issues at month end and a four year note could, as needed, comfortably raise additional cash by September 30. There is considerable speculation that the debt managers may make increasing use of the bill market, possibly beginning in early June. At that time some temporary cash needs develop, and the volume of maturing bill shrinks somewhat. However, Treasury use of the bill market to raise new cash may be moderated by the knowledge that the volume of Government securities in the one year and under category will automatically rise by more than \$3.0 billion this quarter because of maturity shifts of coupon issues.

Economic data, all for the month of March, to be released next week include: housing starts out Monday which may equal the 1.8 million February rate, and personal income (to be released on Tuesday), expected to rise at a 10.0 per cent annual rate. On Thursday the erratic series on new orders for durables could show a strong gain, on the order of 20.0 per cent at an annual rate, and the consumer price index is expected to gain at a 7.0 per cent rate. Quarterly income and product data, to be released on Wednesday, is expected to confirm a slow first quarter, with real GNP up at a 4.5 per cent rate.

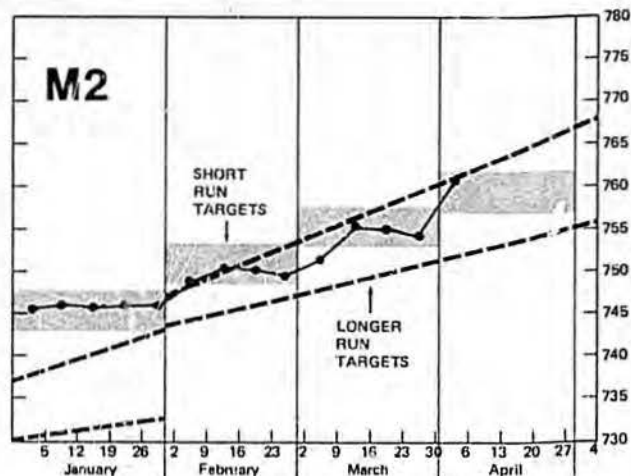
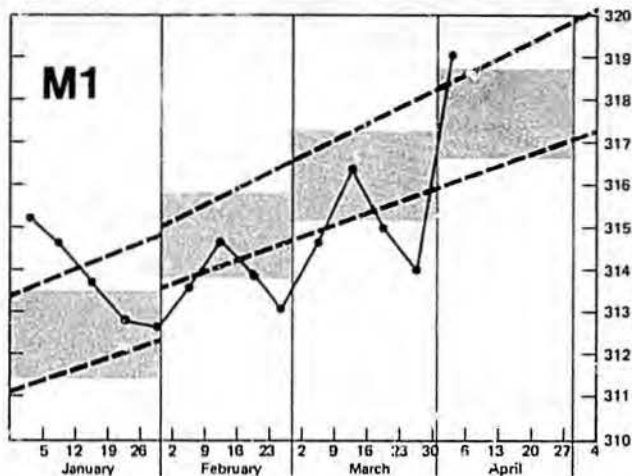
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THE MONETARY AGGREGATES

(Daily Average, Billions of Dollars)



GROWTH RATES: Latest Four Weeks, Annualized, From:

	4 Weeks Ago	13 Weeks Ago	26 Weeks Ago	52 Weeks Ago
M1	8.7%	4.0%	5.5%	5.9%
M2	10.0	8.2	10.5	10.6

GROWTH TARGETS: Annualized Rates

Short Run (Feb-Apr) Est	Longer Run (From 1976-IV)
3-7%	4½-6½%
6-10	7-10

INTEREST RATES

(Average, Week Ended Wednesday)

	Short Term				Medium and Long Term				
	Fed. Funds	Fed. Funds Target	90-Day Bills	90-119 Day Comm. Paper	3-5 Yr. Treasury	Long Treasury	Corporate Bond (Aaa)	Utility Bond (Aa)	GNMA
Mar. 16	4.62	4.63	4.59	4.75	6.72	7.73	8.11	8.48	8.03
Mar. 23	4.77	4.63	4.57	4.75	6.68	7.71	8.08	8.48	8.02
Mar. 30	4.74	4.63	4.59	4.75	6.70	7.74	8.10	8.51	8.05
Apr. 6	4.60	4.63	4.56	4.75	6.70	7.72	8.09	8.54	8.01
Apr. 13	4.65	4.63	4.58	4.75	6.70	7.77	8.10	8.54	7.98

Other Rates (Apr. 13) Discount Rate: 5.25 per cent. Prime Rate: 6.25 per cent.

BANK RESERVES AND FEDERAL RESERVE OPERATIONS

(Average Levels, Millions of Dollars. Sign Indicates Effect on Excess Reserves.)

	Apr. 6 Change	Apr. 13		Apr. 20 Change (Est)
		Change	Level	
Treasury Deposits, Float, Currency	+3216	+147	-96664	-1300
+ Required Reserves and Other Accounts, Net	+ 711	+528	- 2660	-1700
+ Federal Reserve Security Holdings, Outright	-1733	-966	+99180	+3537
+ Securities Held Under Repurchase Agreement	-2237	+321	+ 410	- 410
+ Estimated Effect of Action Required This Week				- 127
= Net Free Reserves	- 43	+ 30	+ 266	0
+ Borrowing	+ 7	- 25	+ 26	0
= Excess Reserves	- 36	+ 5	+ 292	0
Memo: Matched Sale/Purchase Agreements	-1688	-717	- 3547	

Fed Action for own Account, week of Apr. 13: 7 day reverses announced for April 7, on April 6; 3 day matched sale, April 11; overnight repos, April 13.

OUTSTANDING MONEY MARKET INSTRUMENTS, BUSINESS LOANS

(Billions of Dollars)

	Mar. 23	Mar. 30	Apr. 6	Apr. 13
Commercial Paper	55.2	55.0	56.4	NA
Commercial and Industrial Loans:				
All Weekly Reporting Banks	117.2	116.8	117.2	NA
New York Reporting Banks	33.9	33.9	34.1	33.8
Bank Certificates of Deposit:				
All Weekly Reporting Banks	60.2	61.8	60.9	NA
New York Reporting Banks	20.6	20.8	20.3	19.8
Treasury Bills	163.6	163.6	168.1	168.1

White, Weld & Co.

Incorporated

John H. Charlesworth
Fixed Income Marketing

April 7, 1977

FIXED INCOME POLICY COMMENT

OUR VIEW

Relative stability in all sections of the Fixed Income markets over the past two months has alleviated a good bit of the apprehension that was evident in mid-January. While the majority of forecasters still believe a further increase in long rates is probable, the size of the increase and its timing are now subject to more divergent views. We continue to hold the view that long term rates will be no higher at year-end 1977 than they are today, even though short rates could move higher by 50 to 75 basis points as the year progresses.

Of practical concern to money managers, there is a significant interest opportunity cost to holding short term securities, given the slope of the yield curve. The spread between T-bills and 7 year Notes is about 250 basis points, which would discount as much as a 60 basis point sell-off in intermediates. We remain constructive on the market, and favor the quality end of the spectrum. We believe the most attractive area for current investment is in the 7 to 10 year maturities, with long maturities also at good working levels.

LOOKING BACK

Recent secondary market activity has diminished considerably. New issue volume continues at a reduced pace as well, both in the public and private sector. During March, the volume of new issues was about two-thirds of the year earlier level. Most issues that came were reasonably well received, selling to tag ends while still in syndicate.

One measure of the solidity of the market occurred on March 25th, when six syndicates broke in one day. While there were sharp mark-downs for one or two names, the remaining balances were readily absorbed and had little or no effect on over-all market prices.

While we are seeing reduced market participation on both the demand and supply sides, the fact that some extensive swapping is taking place is encouraging. It is evidence that at least some portfolio managers see current prices as stable enough to permit such activity without risk of sharp corrections in either direction.

Municipal markets also showed stability in the past month, even firming a bit in prices. In this area, similar characteristics obtain on the supply side as in the corporate market, but the demand side remains very strong. New bond funds, large pools of institutional money, and individual concern about taxes all are contributing factors.

In the light of many forecasts by others earlier this year of higher rates over the balance of 1977, it is interesting that there has not been a rush by corporations to do some advance borrowing. Several major concerns have announced the opposite. Cash balances continue to build at major firms (IBM, Exxon, GE), and AT&T recently stated that 80% of current capital needs would be financed internally.

LOOKING AHEAD

THE POSITIVES

1. Visible supplies of new issue Corporate debt are only about 2/3 of last year's record monthly pace. The internal "self-sufficiency" ratios of major corporations continue to improve, and are now well above pre-recession levels. Even widespread forecasts of higher rates have not prompted major borrowings.

2. The economy is recovering from the winter's distortions. In addition, recent National Weather Service and Department of Agriculture projections are more optimistic regarding the outlook for feed-grains and farm commodities. While the threat of drought or near-drought conditions is still a very real one, the affected areas should be smaller than recently feared.

3. No major case for Federal Reserve tightening seems evident, even in the light of recent acceleration in the Money Supply growth rate. These rates are still comfortably within Fed targets, both near and longer term, and we continue to believe the Fed will be able to accommodate the Administration's fiscal programs without raising target Federal Funds rates.

4. The shape and slope of the yield curve is now penalizing those who are in the very short end of the market. Recently noted has been a growth of "re-intermediation", the movement of funds back to time accounts at banks from short term instruments. Lacking matching growth in loan and/or mortgage demand, these funds are an additional positive force on the demand side for intermediate and long fixed income markets.

THE NEGATIVES

1. The overriding negative continues to be concern over higher rates of inflation. While inflation will surely ease from the high January-February level in the coming months, it will be higher than we were forecasting as recently as three months ago.

2. President Carter's inflation fighting program (to be announced this week), energy program and tax reform package have yet to see the light of day. Until these are quantified to some degree, their potential impact will trouble portfolio managers, as unknowns are most often perceived pessimistically.

3. The diminished volume in secondary markets over the past three months has made traders reluctant to hold inventory. The fact that much of the new issue calendar is being done against swaps means that there is a strong moderating force in any rallies that develop, and additional weight in periods of weakness.

4. The potential for "crowding out" still exists as a negative over the balance of the year. Although forecasts of Treasury needs, particularly for the third quarter, have recently been reduced, government borrowing will still be at near-record levels. The growth of corporate profits (and associated tax payments) could help ease the pressures in the second half. Our view is that this will be a diminishing threat if consumer and corporate borrowings do not surge upward.

CBN-77-3

EARNINGS WILL MATTER (AGAIN)

Summary of taped discussion of Investment Policy
by Harold W. Janeway & H. Carroll Mackin, 3/18/77

Conclusion: Relative earnings performance is likely to become a much more important determinant of stock price movements in the months ahead than over the last 1-2 years. We recommend that investors downplay the non-earnings-related investment strategies that have dominated trading over the past year or so and instead focus on those companies most likely to show significantly above-average earnings gains over the next two years (and beyond). Such stocks should prove to be the best performing investments, regardless of what happens to the economy and inflation.

Background: A number of non-earnings-related investment themes have dominated the market over the past couple of years. Among these are secondary (vs large) companies; domestic (vs international) operations; underowned (vs overweighted) in institutional portfolios; indexation (vs stock selection); market timing; top down (vs bottom up); and current dividend income. Most of these appear largely to have run their course or are at least reflected in current stock prices. Probably the most popular strategy stresses high current income. Indeed, there is a high correlation over the past several years between a stock's performance and its yield. Since June 1975, a portfolio consisting of the five highest yielding industry groups at that time would have provided an investor with a 27% total return to date, while a portfolio of the five lowest yielding groups would have shown a 9% loss for a 36 percentage point performance spread between the two. If you look strictly at industrial companies (a sample of 1600), the 10% providing the greatest yield in June '75 would have given investors a 70% total return to date, while the lowest 10% would have rendered only a 40% gain. In June '75, the yield spread between the top-yielding 10% and the bottom 10% was 8.4 percentage points; today it is only 6.9 points, with almost all of the change reflective of stock price changes. Taking another approach, at the 1974 market bottom the utilities were yielding an average of 12.4% vs a 2.5% yield on the drug stocks for a 10 percentage point spread vs 5.5 points at the end of February - a tremendous compression of the market's yield distribution.

The narrowing of these spreads has reduced the relative attractiveness of the higher yielding stocks. Focusing on the up-front dividends without factoring in future dividend and earnings growth is likely to be much less rewarding over the next year. The natural response is to look at the traditional growth stocks as the alternative, but are they? Still among the lowest yielding stocks in the market, most of the "nifty fifty" still carry P/E premiums that appear to be discounting roughly twice the growth rate of the rest of the market for the next ten years - a bit much to swallow. Consequently we do not expect the growth stock group to be market leaders in the next up cycle, except those that show earnings gains well in excess of corporate profits overall.

The best buys in the market today probably lie somewhere between the high current yielders and the low-yield growth stocks - those undifferentiated stocks with above-average earnings prospects, below-average yields, and below-average payouts (The S&P 500's dividends currently have a 43.7% payout.). What we're saying is buy those stocks that have the prospect of becoming high yielders in the future.

Outlook: Investors' primary concerns today are the possible resurgence of inflation and sharply rising interest rates. The present structure of both the stock and bond markets reflects these worries. The yield spread between stocks and bonds is at its narrowest level since 1970, and the gap between the yields on 1- and 20-year government bonds is wider than it has been in over a decade (250 basis points); both indicate expectations of higher interest rates. We believe these fears are overdone and do not expect a renewal of prolonged inflation above the 5-6% level. Nor do we foresee a sustained rise in interest rates, but rather look for interest rates to be no higher and possibly lower at yearend than currently. If our forecast of moderate (5-6%) growth and inflation are correct, then the narrowness of the yield spread between stocks and bonds argues for further investment in equities.

Looking ahead, we are forecasting aggregate corporate profits growth of about 12% this year with a slightly lower (10%) advance in 1978. These gains will be widely scattered rather than concentrated in one or two areas. Given this environment, investors should approach stock selection with an open mind, de-emphasizing the popular themes mentioned earlier and focusing primarily on relative earnings prospects and the potential for higher dividends.

Some examples would include the Aluminum Industry, whose earnings we foresee doubling over the next two years (vs our expectations of 20-25% increase in the S&P's earnings over the same period). Yields on this group are currently below average, but within a few years these should be considerably higher on today's stock prices. Among the other basics, ALLIED CHEMICAL (ACD-45 7/8) yields less than 4%, but we foresee a sharp rise in earnings to roughly the \$10.00 level by 1979-80 accompanied by a substantial build-up of cash. OCCIDENTAL PETROLEUM (OXY-25 5/8), a beneficiary of North Sea oil also has substantial dividend increases in prospect. SOHIO (SOH-83 1/4) (yield 1 1/2%) is a more extreme example, with the prospect of a \$5.00 dividend (\$1.36 currently) by the late 70's when the North Slope oil starts to flow.

A more detailed policy statement will be out shortly.

William F. Boyd
Sales/Research Liaison

SRL-76-20

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March 25, 1977

Investment Strategy—A Change

**SUMMARY—
EARNINGS
WILL
MATTER**

We believe earnings will become a much more important determinant of stock price performance over the balance of this year and next. Thus, investors should emphasize those companies that are most likely to show significantly greater than average earnings gains in the next two years and beyond. Such stocks are likely to prove to be the most rewarding holdings regardless of the trends in inflation and the economy. If growth in the economy proves disappointing, and overall profits rise only moderately, relative earnings gains will be important. The same should be true if the economy is stronger than expected this year and 1978 turns out to be another good year. If inflation fails to moderate, contrary to our expectations, then strong earnings gains should provide at least a partial offset.

Although the market seemed preoccupied over the past year with a number of investment themes not directly related to earnings, disappointing earnings did not go unnoticed. In a year in which overall corporate profits rose 29%, those companies that fell short of expectations were far more impacted than those recording sharp gains. However, with overall corporate profits expected to be up only about one-half as much this year as last, sharp earnings gains should be more noteworthy. Moreover, the gains are likely to be scattered, not concentrated in one or two areas. Thus, investors should approach the selection process with an open mind, de-emphasizing the popular investment theories that have come to be widely accepted as universal truths. Increased emphasis on earnings gains does *not* imply a return to traditional growth-stock investing. Companies with outsize earnings gains should qualify; those with average gains are more likely to be average performers. Above-average price performance is most likely in those cases where the earnings gains are converted to dividends over the next two or three years.

**WHY
CONCENTRATE
ON
EARNINGS
GAINS?**

There are four reasons why we believe investors should stress companies showing substantial earnings progress over the next two years: first, to offset inflation. Over the past few months investors have raised their inflation assumptions, but do not appear to have made a corresponding adjustment in their investment selections. Second, big earnings should be less common in 1977-78. We estimate the average earnings gain for the two year period in the 20-25% range. Third, the market in general appears reasonably priced with little downside risk. However, we do not expect a material expansion in P/E ratios. Consequently the increase in the market averages will reflect primarily earnings growth. Individual stock selection will also be of prime importance. Fourth, dividend growth will take on more importance than current yield. Major earnings gains are likely to lead to larger dividend increases.

**1. Offsetting
Inflation**

Virtually every 1977 inflation forecast was revised upward during the winter months, ours no exception. Most forecasts were increased for 1978 and beyond as well. Investors in general are more pessimistic on inflation than they were last fall. However, with the exception of the weakness in the insurance stocks, which are considered the most inflation-sensitive group, there has been little discernible change in the make-up of the stock market. High yielding stocks held up better than most.

We believe most people over-reacted to the winter's effect and expect that inflation will begin to moderate in the second quarter and ease further in the last half of the year to around a 5% rate. Mother Nature permitting, price increases need not accelerate in 1978. If inflation were to decline to lower levels, the prospects for the market as a whole obviously would be enhanced. In such a case we believe greater appreciation would occur in issues providing more exposure to the earnings potential inherent in a sustained economic improvement. If inflation does *not* moderate as much as we expect, then the market as a whole will be disappointing, but those companies with sharp earnings gains would stand out. Companies can compensate for inflation, but not always immediately, not under price controls, and not when the inflation is unexpected. All of these conditions prevailed in the early 1970's, but do not exist today. Inflation-consciousness among businessmen now is high—if anything too high. The estimated average 1976 return on equity of 14%, above the 12% considered reasonable a few years ago, is evidence (at last!) that equities do afford initiation protection. Larger earnings increases provide more long-run protection.

**2. Overall
Profit
Gains
Moderating**

By the fourth quarter of 1976 profit increases had eased significantly from the high rate earlier in the year. We are projecting corporate profit gains of around 12% for 1977 as a whole and tentatively estimating gains of roughly 10% in 1978. Thus, the period of sharp profit recovery is now behind us. From here forward those companies recording exceptionally large earnings gains over the two years, rather than in 1977 alone, should stand out more clearly. Among the 425 companies that we follow we have attempted to identify those which appear capable of recording gains that are at least double the average expected increase. (A list of these companies appears on page 8). A number of the lower-multiple stocks with large earnings increases in prospect have outperformed the market over the past 3-6 months, indicating that relative earnings gains have had an influence in the market. However, the lower-yielding, higher P/E stocks have continued to lag making some of them particularly attractive. We see the influence of earnings expanding in the months ahead. If anything, the fear of higher inflation should focus greater attention on the increase in earnings.

**3. Overall
Stock
Market
Outlook
Satisfactory**

We believe the stock market is reasonably priced. With the S&P 500 selling at about 9 times estimated earnings to yield nearly 4½% on prospective 1977 dividends, the risks are modest indeed. The following charts serve to underscore our view showing that the earnings yield on stocks is now moderately above bond yields, a relatively uncommon experience over the past decade, (Chart 1), and that the bond stock yield spread has declined substantially from the highs of early 1976 to the lowest level since 1969 (Chart 2).

Chart 1
Bond/Stock
Yield
Comparisons

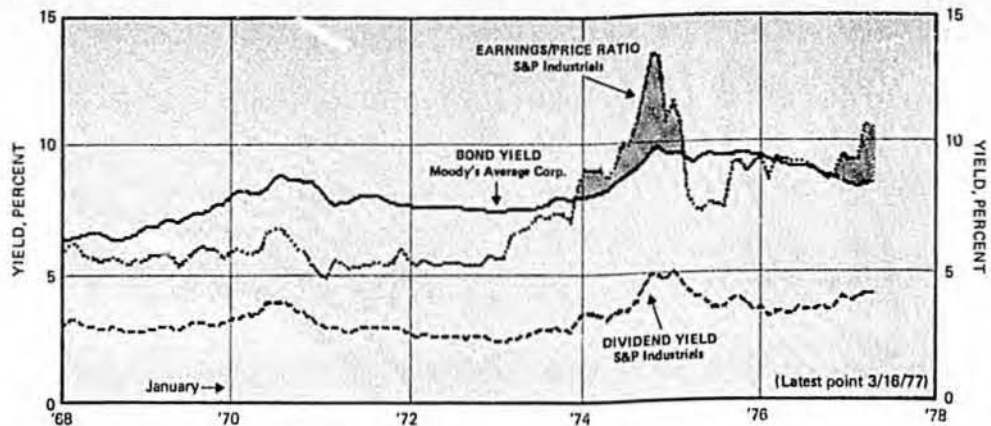
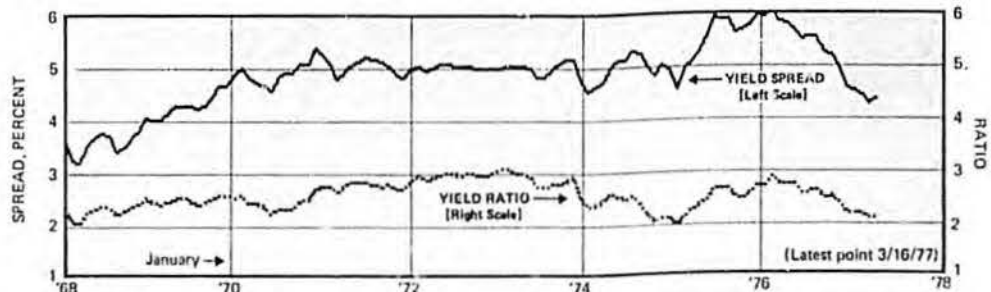


Chart 2
Bond/Stock
Yield
Differentials



We have felt for some time that investors should assume a continuation of a relatively low-confidence market environment. This remains our view. We believe that P/E ratios will not rise materially and that the gains in the market over the coming 12 months are likely to approximate the increases in earnings and dividends that we foresee this year and next. This implies a market level 10-15% higher in a year. Therefore, we expect selectivity and stock price-sensitivity to be extremely important to achieving satisfactory investment performance. To a much greater degree than in 1976, the discriminator to apply in selecting stocks should be relative earnings performance. We do not mean to imply that the *only* stocks to buy are those with the prospect of unusually sharp earnings gains. There are other values among companies whose earnings in 1975-76 were particularly impressive that are not fully reflected in today's prices and among companies where earnings may be currently flat or down, but show promise of large gains starting in 1977 or 1978.

Some of the companies for which we see substantial 1976-78 earnings gains provide little or no current return. In such cases good earnings growth in the past few years and poor market performance have brought their P/E's to levels that seem low by any reasonable standard. Their P/E's relative to the market are as low as at previous bear market lows. The following tables compare current P/E's on the growth stocks we consider attractive with those prevailing at previous market-cycle lows.

COMPARISON OF CURRENT P/E WITH PAST BEAR MARKET YEARS

	P/E Level				Relative P/E to S&P 500			
	1966	1970	1974	1977E	1966	1970	1974	1977E
Digital Equipment	37.5	32.0	12.6	16.1	2.8	2.4	1.8	1.8
General Reinsurance	14.7	13.5	17.6	16.6	1.1	1.0	2.5	1.2
Hewlett Packard	23.9	21.1	16.9	17.2	1.8	1.6	2.4	1.9
IBM	29.9	24.6	12.0	15.3	2.3	1.8	1.7	1.7
Kresge	14.3	18.0	17.7	14.0	1.1	1.3	2.5	1.5
Lowe's	—	15.4	10.5	14.1	—	1.1	1.5	1.5
McDonald's	10.7	18.8	12.4	13.9	0.8	1.4	1.8	1.5
Sony	—	13.5	8.7	13.9	—	1.0	1.2	1.5
Tektronix	14.3	16.5	5.9	10.6	1.1	1.2	0.8	1.2
S&P 500	13.2	13.5	7.0	9.2	—	—	—	—

4. Earnings Growth— Dividend Growth

The market has been dominated by interest in high-yielding stocks (and bonds) over the past year. We remain optimistic on the outlook for dividends, estimating a 21% increase in the S&P 500 dividends from \$4.05 in 1976 to \$4.90 in 1978. The estimate assumes a comfortable payout-ratio of only 40-41%. If return on equity is maintained at last year's 14%, the plowback rate would equal 8½%, an historically high level. Thus, even if earnings decline or inflation accelerates somewhat, dividends could continue to rise in real terms. With the exception of a few non-capital-intensive companies—Avon, Coke, IBM for example—and some high-return, low-payout companies such as Halliburton, Kresge or Schlumberger, investors should not assume a major rise in payout ratios. Thus, the biggest dividend gains generally will parallel earnings. Higher prospective returns on today's stock prices should be attained by focusing on long-term dividend prospects. Increased emphasis on earnings gains does *not* necessarily imply a return to traditional growth-stock investing. Those companies with outside earnings gains should qualify regardless of the type of stock.

INVESTMENT THEMES— FADING IMPACT

By this time last year investors had set their sights on a good economy and a profit recovery at least as large as that which materialized. Since that time the market has remained in a narrow range, but as most investors are well aware, the trendless pattern of the overall market camouflaged substantial gains and losses among different sectors and industry groups.

There are five investment themes that played a major role in relative stock price performance of these different groups during the past one to two years. These are: emphasis on current income, companies with primarily domestic rather than international exposure, portfolio diversification (indexation), institutional over- and under-ownership and secondary companies. These are all valid considerations that we have espoused, but markets have a way of adjusting and much adjustment has occurred.

1. Current Income

There is no question about investors' increased emphasis on yield. The reasons for this are well known and understandable. However, it is important to recognize that the trend has been underway for the better part of two years. The data in the table below shows how significantly the distribution of yield has changed over the past three years. In brief, the yield spread, which was extreme at the market lows in 1974, is now much more narrow. At the end of 1973 the drug group provided an average yield of 1.4% while the electric utilities yielded 8.0%. On September 30, 1974 (close to the market low) the yields were: drugs 2.5%, electric utilities, 12.4%. At the end of February, 1977 the drugs yielded 2.9%, the electrics 8.4%, a narrowing of the spread from 9.9 percentage points to 5.5 points. Our recent study of the 50 largest companies in the S&P 500 (see March Research Review) made clear how a number of relatively low yielding stocks with below-average payout ratios and high returns on equity compared favorably from the standpoint of future income with higher current-yield stocks when approaching the valuation process on the basis of prospective yields reflecting estimated growth in dividends. We advise more emphasis on *growth in dividends* and less emphasis on current income. Long-term dividend growth of course increases the importance of earnings growth. This will be particularly true from this point forward because we do not believe the payout ratios of most groups with high current yield will increase materially.

DISTRIBUTION OF DIVIDEND YIELD OF INDUSTRIAL STOCKS

	Average Yields Of Groups		
	(Sample of over 1,000 Industrial Companies)		
	Highest Yielding 10% Issues	Lowest Yielding 10% Issues	Yield Spread
December 1973	9.43	0.0	9.43
December 1974	8.92	0.0	8.92
July 1975	8.47	0.0	8.47
December 1975	8.68	0.9	8.68
December 1976	6.99	0.0	6.99
March 1976	6.91	0.0	6.91

2. Stress Domestic— Avoid International Exposure

A variety of problems has led investors to adopt the now familiar Buy American theme: the poor performance of foreign economies, the cumulating problems of the oil payments deficits, the sharp fluctuations in foreign currencies and accounting rule FASB #8 that requires quarterly currency translation losses and gains. All of these considerations contributed to the portfolio managers' decision to minimize their exposure to these problems. We believe investors are right in their concerns just as there is considerable logic to the new emphasis on yield. However, many leading multi-national companies have come through the problems of the past few years reasonably well. Moreover, their earnings in 1976 were in many instances particularly adversely affected by currency adjustments. Even if translation losses are as high this year as last, which we believe is unlikely, there would be no further negative earnings impact. What seems more likely to us is that a 30¢ per share translation charge in 1976 might become a 20¢ per share charge in

1977 10% boost to the year-to-year earnings comparison. Thus, while we would not single out multi-nationals per se for emphasis, we would not shun those that qualify in terms of recording strong earnings gains.

**3. Diversification-
Indexation**

The trend to diversify portfolios, running parallel to the greater emphasis on current income, has been an important stock market factor for some two years. While we believe the trend is unlikely to reverse and that money will continue to flow to the index funds, the portfolio manager with the courage of his convictions, who is willing to invest with an eye to potential gains rather than self-protection, will find the best opportunities in those companies whose earnings are rising rapidly. We believe that many investors may be confusing portfolio balance and indexation. To us, portfolio balance means a reasonable mix of types of stocks and industries reflecting an assessment of the probabilities and risks, but it should not mean matching the make-up of the market. To hold a market weighting in an industry or group implies an unwillingness to take a stand. It is our impression that most investment portfolios are now more balanced and diversified than at any time in recent years. This should imply opportunities for investors willing to exercise a greater degree of individual judgment. That judgment is best exercised on a case-by-case basis, again with the emphasis on earnings.

**4. Underowned
versus
Overowned**

Part of our investment policy for the past year and a half has been to stress those companies less widely researched and owned by major institutions—what we refer to as the companies with the thin files. We continue to feel that a stock that is less widely owned by institutions is more attractive than one with a high level of ownership, all other things being equal. However, here too investors should avoid adopting the strict constructionist's view, avoiding a stock just because it is overowned. In this regard, IBM's recent tender offer did much to dispel the illusion of overownership of that particular issue. While the degree of institutional ownership can be set forth reasonably accurately from the data available, it is important to realize that overownership is also a state of mind. Positions are always too large in the stocks that are going down and too small in those that are strongest. Given IBM's dividend growth prospects and market price, there was no reason for investors to be concerned if they had more than the market weighting in the stock. The company's highly successful unsuccessful tender offer served to make this clear. The overowned theory is becoming overworked and should be given less weight in making investment decisions.

**5. Secondary
Companies**

The popularity of secondary companies has increased along with their performance over the past two years. Only during the third quarter of 1976 did the S&P average outperform the unweighted average last year. This reflects a number of the other investment themes noted above—yields tended to be higher on secondary stocks, their business mix less international, they enabled portfolio managers to diversify and they were generally underowned. We continue to like a number of the secondary companies but do not believe that their emphasis will be the key to investment performance in 1977. Big companies with big earnings gains also should do well.

For those accustomed to viewing the market in terms of broad themes, the message that earnings are once again the driving force may not be readily apparent simply because the stock price gains are likely to be scattered through numerous categories. For example, we believe that the aluminum industry is in a position to double earnings over the next two years. However, we do not expect particularly sharp gains from other basic industries and do not maintain that basics per se are attractive. Similarly, the chemicals as a group continue to present a very mixed picture. However, Allied Chemical, thanks primarily to earnings from the North Sea, could double its earnings between 1976 and 1978. In the energy area SOHIO's earnings could triple and Occidental Petroleum's earnings could double, neither of which appears to be fully reflected in their stock prices, despite good relative performance over the past six months.

All of the growth stocks that appear on our list on the following page are still under the influence of the non-earnings-oriented themes discussed above. In the case of these stocks it is likely that investor recognition of their good earnings prospects will be gradual and could well be delayed. Nevertheless, those investors operating with more lead time should be accumulating the stocks now. The same comments apply to the smaller companies on the list.

IP-77-3

Harold W. Janeway
Director of Investment Policy

Within the last three years, White, Weld & Co. Incorporated co-managed public offerings of Pizza Hut and H.J. Wilson. White, Weld & Co. Incorporated makes a market in the shares of Lowe's Cos. General Reinsurance and H.J. Wilson but may discontinue at any time, without notice, maintenance of such market. Officers of White, Weld & Co. Incorporated are directors of Lowe's and Imperial Corp. Information received by them as directors is confidential and cannot be communicated to our personnel or clients.

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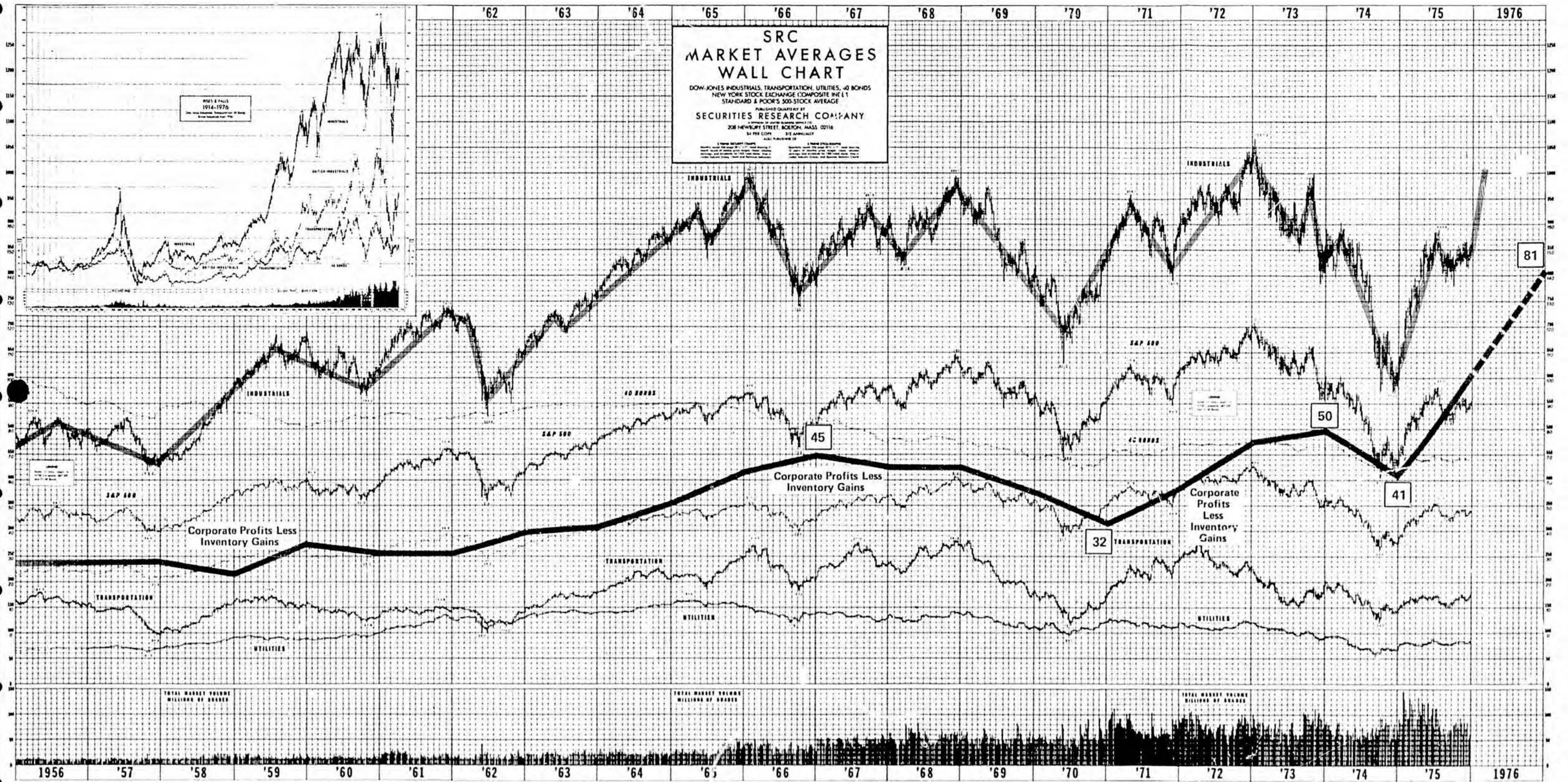
RECOMMENDED COMPANIES WITH 40% EARNINGS GAIN, 1976-78

Company	Fiscal Yr.	3/25/77 Price	1972-77 Range	EPS			% Chg. 1976-78	1978-81 Growth Rate Est.	1977 P/E	Cur. Div.	Yield	Market Capital. (Mil.)
				1976	1977E	1978E						
SO. II ^o		\$79	86-30	\$3.55	\$5.50	\$14.10	297%	5	14.4X	\$1.36	1.7%	\$3,177
Raynolds Metals		40	43-12	3.74	5.25	8-9.00	127	10	7.6	1.20	3.0	736
Alcoa		58	61-26	4.14	6.00	8-9.00	105	10	9.7	1.40	2.4	1,998
Intel		48	78-10	2.37	3.30	4.75	100	25	14.6	-	-	516
MGIC		15	98-6	1.15	1.80	2.30	100	12	8.3	0.20	1.3	391
Louisiana Pacific		16	24-7	1.51	2.40	3.00	99	10	6.7	0.20	1.3	423
Allied Chemical		43	54-23	4.07	6.00	8.00	97	12	7.2	1.80	4.2	1,278
Occidental Petroleum		26	27-7	2.27	3.25	4.35	92	12	8.0	1.00	3.9	1,521
Tektronix	5	59	69-18	3.30	4.55	5.75	74	18	13.0	0.30	0.5	525
Digital Equipment	6	44	61-15	1.98	2.70	3.40	72	25	16.3	-	-	1,633
Lowe's Cos.	7	26	48-12	1.33	1.72	2.20	65	18-20	15.1	0.24	0.9	342
Sony	10	10	18-4	0.50	0.65	0.80	60	15	15.4	0.06	0.6	2,021
Hewlett-Packard	10	76	121-46	3.23	4.10	5.10	58	18	18.5	0.40	0.5	2,143
Polaroid		33	150-14	2.40	3.00	3.60	50	12+	11.0	0.50	1.5	1,166
duPont		128	204-85	9.30	11.50	13.50	45	13	11.1	5.50	4.3	6,416
McDonald's		42	77-21	2.72	3.30	3.90	43	18	12.7	0.10	0.2	1,828
Crown Zellerbach		40	49-20	3.88	4.55	5.50	42	12	8.8	1.80	4.5	1,016
First Charter		17	29-1	2.50	3.00	3.50	40	10	5.7	-	-	451
General Reinsurance		157	257-9.7	11.48	14.80	16.00	39	12-14	10.6	1.20	0.8	871
NCR		37	46-14	3.60	4.35	5.00	39	15	8.5	0.80	2.2	971
Imperial Corp.		17	20-5	2.98	3.50	4.10	38	10	4.9	0.24	1.4	219
Kresge	1	33	51-18	2.15	2.50	2.90	35	15	13.2	0.32	0.9	4,289
Smaller Capitalization												
Pizza Hut	3	21	31-8	2.50	3.10	3.70	48	15-20	6.8	0.40	1.9	159
Technicare	6	39	50-4	2.51	5.40	7.50	200	20	7.2	0.40	1.0	112
Wal-Mart	1	14	18-4	1.12	1.40	1.75	56	18-20	10.0	0.10	0.7	197
Wheelabrator-Frye		26	33-7	2.21	2.75	3.25	47	13	9.5	0.63	2.4	192
Wilson, H.J.		15	30-3	1.65	2.10	2.45	48	20	7.1	-	-	37
S&P 500		99	120-63	9.85	11.00	12.00	22	8	9.0	4.40	4.4	-

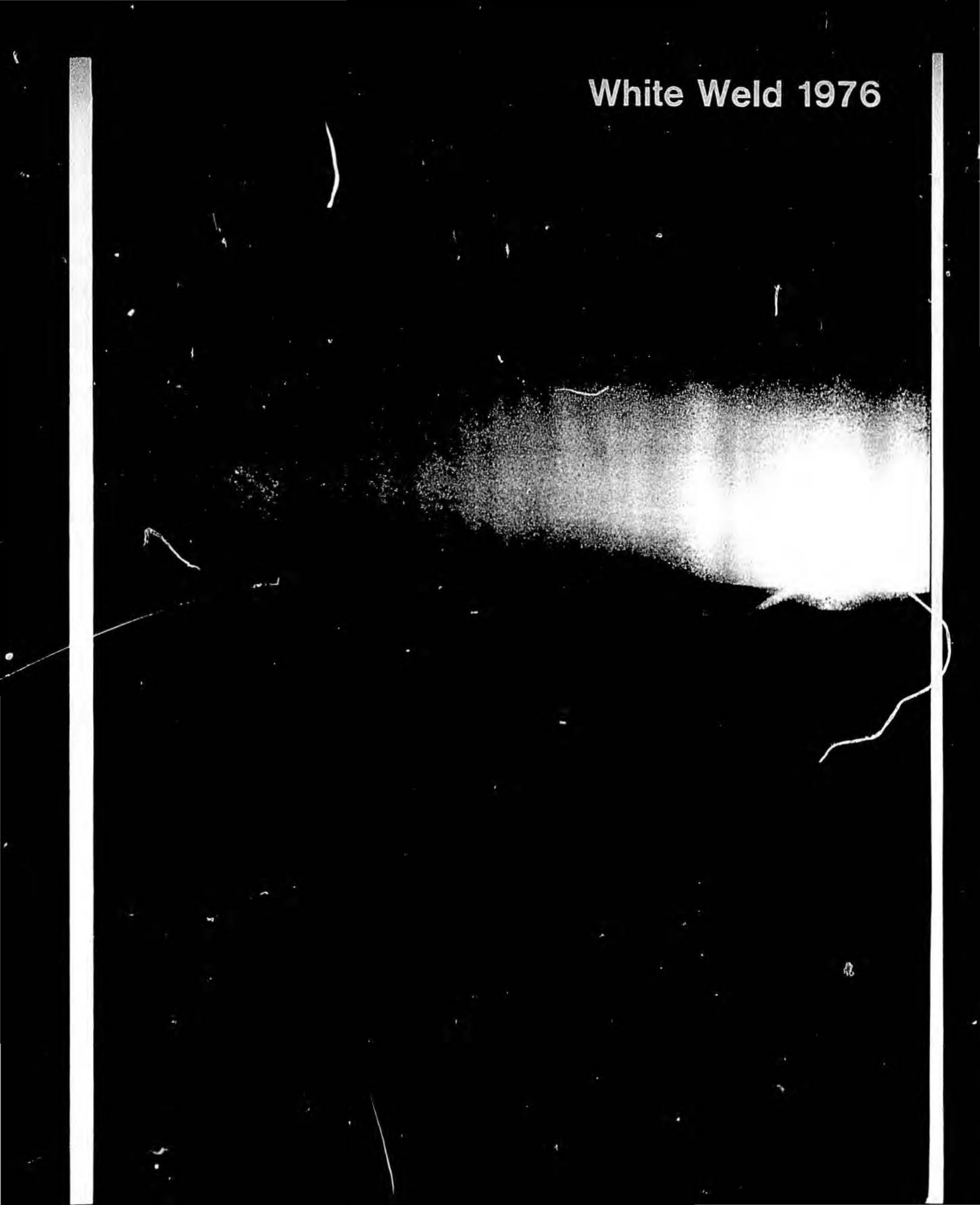
WALL & WALL
1914-1976

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White Weld 1976





From the windows of White Weld's headquarters in New York City can be seen the panorama shown on the front and back covers of this annual review. At the left are the towers of Wall Street, center of the greatest financial market place in the world. In the far distance is the Verrazano Bridge, with the open Atlantic beyond.

White Weld opens doors to the capital markets of the world. Together with its associated company abroad, White Weld serves the needs of customers through investment banking and financial service units in thirty-eight cities on four continents.

White Weld & Co. Incorporated is a wholly owned subsidiary of White Weld Holdings, Inc., which has over \$50 million in stockholders' equity and \$70 million, on a consolidated basis, in total capital funds. It provides a full range of investor services and investment banking facilities for clients in the United States and foreign countries. The firm employs close to two thousand people in thirty-one cities around the globe (shown as circles above).

Société anonyme financière du Crédit Suisse et de White Weld represents the combined international investment banking vehicle of White Weld and Credit Suisse, one of the leading banks in the world. With equity capital in excess of 130 million Swiss francs (\$52 million), Financière offers a full complement of international investment banking services. Its operating units maintain offices in five cities in Europe and Asia (shown as squares above).

White Weld 1976



From the windows of White Weld's headquarters in New York City can be seen the panorama shown on the front and back covers of this annual review. At the left are the towers of Wall Street, center of the greatest financial marketplace in the world. In the far distance is the Verrazano Bridge, with the open Atlantic beyond.

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Highlights

Outlook and Review	3
Access to money markets broadened, and users of capital found opportunities to raise capital at improved rates of interest.	
The Teamwork that Raised \$1 Billion for the Energy Industry	5
White Weld's corporate finance, public finance, research, and other departments are devoting greater resources to this vitally important sector of the economy.	
Trends in Corporate and Public Finance	6
The firm established new records for volume of underwritings and significantly improved its market share.	
A Unique Collaboration in International Finance	11
With a strong position in major capital markets, White Weld and its associated company in Europe give flexibility to financial management around the world.	
Innovation in the World Marketplace	12
1976 was a record year for the Eurobond market and for White Weld and Credit Suisse White Weld, as they continued to pioneer new techniques in financing.	
An Expanding Commitment to Trading	15
White Weld's success in strengthening its role in trading is reflected in a growing share of volume in corporate, U.S. Government, and municipal securities.	
Full Service for Institutional Investors	16
White Weld provides institutions with top-quality economic and research analyses together with trading and execution capabilities in a full line of securities.	
Special Programs for the Individual Investor	18
The services White Weld provides professional money managers are adapted to the needs of individual investors.	
Continuous Supervision of Client Portfolios	19
White Weld offers a balanced approach to portfolio management for individual clients, tax-exempt corporate and union pension funds, and endowment funds.	
Support Services for White Weld Clients	21
White Weld is adapting its worldwide communications and securities processing systems as financial markets grow in size and complexity.	
Statement of Financial Condition	22
White Weld Directors	25
Management Directory	26



Outlook and Review

Economic uncertainty and political transition dominated the news here and abroad during 1976. In the United States the deceleration of the recovery and the lengthy election campaign seemed to reinforce the cautious attitude with which business executives, consumers, and investors emerged from the recent recession. We view this restraint as a constructive development because we believe that the economic excesses of the sixties and early seventies can best be unwound through gradual recovery. It now seems probable that the pause in 1976 did indeed refresh and that 1977 will see the U.S. economy leading the rest of the free world in a more vigorous phase of growth with more intensive employment of people and plant.

Although stock prices in 1976 failed to follow through on their explosive January-February rise and the bond market did not stage its strongest rally until the year-end, the financial markets on the whole were friendly territory compared to recent years. Our financing clients found opportunities to raise capital at generally improving rates of interest. Our investing clients were able to select from a broad range of securities, both debt and equity, that offered reasonable returns.

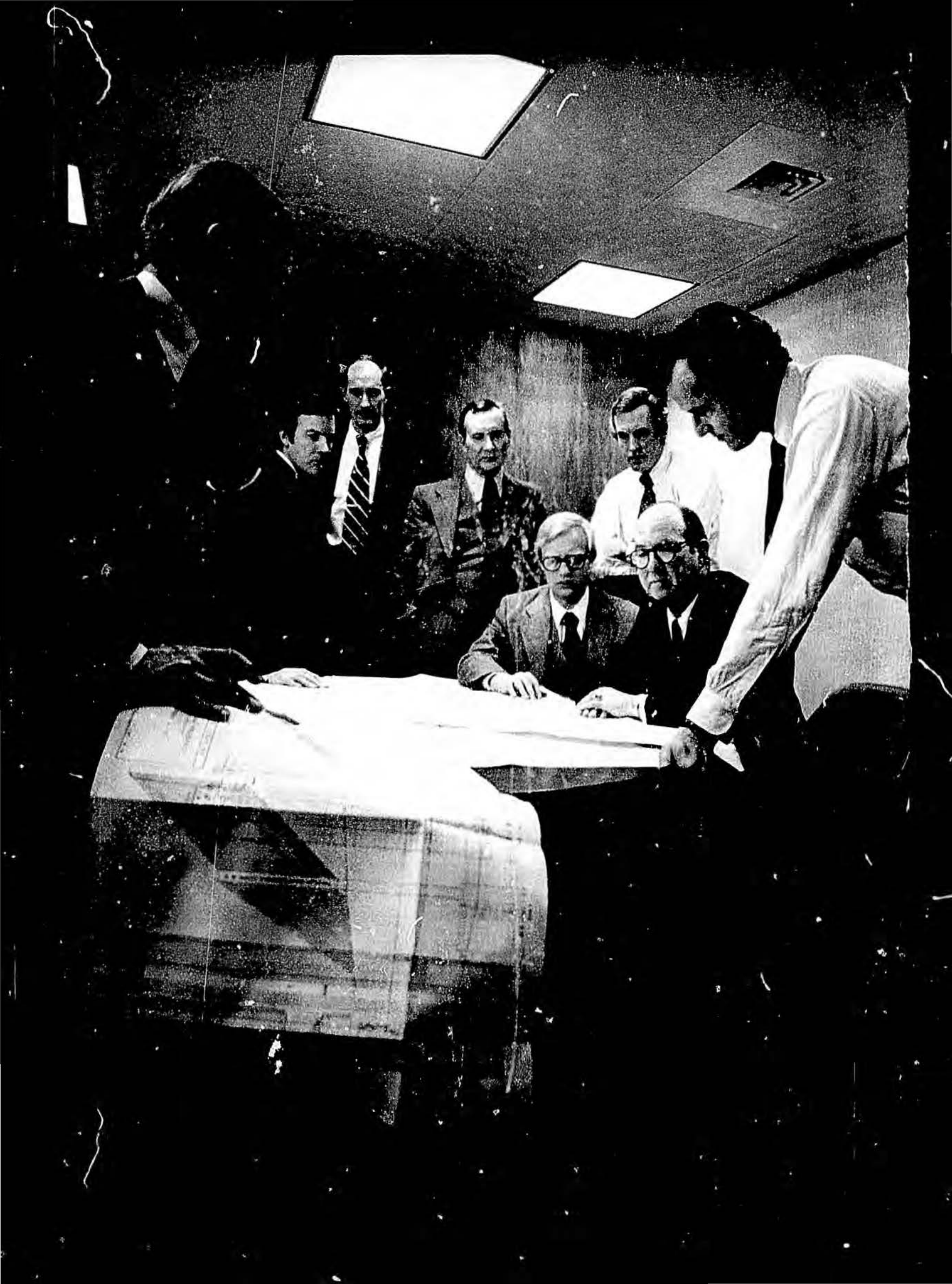
Access to debt capital markets broadened. Companies with credit ratings of Baa and below were able for the first time in several years to sell long-term debt securities through both public underwritings and private placements. Equity markets, although open for financings by major companies whose names were known to investors, were highly selective in accepting new issues of common stock.

For White Weld, revenues and profits reached record levels in 1976. In the prevailing favorable business environment, our firm benefited from its deep involvement in the corporate and public finance sectors and from its broad exposure to the activity of institutional and individual clients in all securities markets. As we continued to expand our capital and professional resources, we gained share of market in all major areas in which we operate.

Our international affiliate, Société anonyme financière du Credit Suisse et de White Weld, also realized sharply higher revenues and net income as financing in international markets expanded and as secondary market operations benefited from declining interest rates and rising bond prices. While most of the major free-world economies face more difficult conditions than our own, we nevertheless expect them to grow more rapidly in the aggregate than in 1976, leading to continued active financial markets abroad.

The keynote of the recovery cycle that began in 1975 has been moderation and caution. History tells us that speculative excesses do recur, but as yet we see little evidence that such pressures are building. On the contrary, we detect a widespread desire for fiscally responsible conduct on the part of individuals, businesses, and governments. Although the new Administration faces a delicate task in keeping the recovery on track and proceeding at a moderate pace, we believe 1977 will be a good year for both our financing and investing clients.

Senior officers of White Weld, reading counterclockwise from lower left, are Paul Hallingby, Jr., chairman; Frederick L. Wonham, president; Charles C. Tillinghast, Jr., Charles C. Lee, Jr., and Henry W. Meers, vice chairmen. Mr. Tillinghast, former chairman of Trans World Airlines, joined White Weld in January 1977.



The Teamwork that Raised \$1 Billion for the Energy Industry

The critical shortage of natural gas and the heavy dependence of the United States on imported oil, although long foreseen by us and other observers, have surfaced as issues of overriding national concern. Intelligent government policies on energy are absolutely essential at this time to enable companies supplying the energy requirements of the United States to raise the vast sums of capital they will need. In order to provide fully its creative assistance in all phases of financial planning, White Weld during the past five years has more than doubled its complement of investment banking and research specialists concentrating in the oil, gas, coal, and related industries.

Senior members of White Weld's corporate finance department specializing in natural resources are shown on the opposite page. From left to right they are Stephen W. Houghton, Wallace L. Bennett, Anthony V. Leness, Robert L. Huston, Theodore D. Sands, Jeremiah K. Ross, Robert K. Green, and Alexander M. White.

In 1976, White Weld raised over \$1 billion for the energy sector of the national economy through the development and management of public bond and equity issues, through private placements, and through such other financial techniques as leveraged leasing. This total placed White Weld among the top-ranking investment banking firms in volume of financing for the oil and gas industries.

White Weld's strong position in the energy field developed in the years following World War II, when the firm pioneered new financing techniques for the burgeoning gas-pipeline business. We helped supply the seed money, financial know-how, and organizational skill to spread a pipeline network throughout the United States and Canada. This activity led to the financing of other hydrocarbon and related industries.

Among White Weld's clients whose principal activity is gas transmission are The El Paso Company, Transco Companies, and United Energy Resources. In the gas distribution field we have acted as investment bankers for Brooklyn Union Gas Co., Entex, and Southern Union Gas Co. Among clients engaged primarily in oil and gas exploration and production are Helmerich & Payne, Pennzoil Company, Pennzoil Offshore Gas Operators, and Pennzoil Louisiana & Texas Offshore. Companies with diversified interests in energy and other industries include Houston Natural Gas Corp., MAPCO Inc., and Tenneco Inc.

Recently the firm has moved to explore the potential of the coal industry, which we expect to emerge as a central element in the nation's energy policy. We have been working with a number of clients in-

terested in this industry, utilizing our own skills and those of John Corcoran, former chairman of Consolidation Coal Company, with whom White Weld maintains a continuing relationship as an advisor.

To respond successfully to the complex needs of energy companies today requires expertise in many specialized aspects of finance. White Weld is able to furnish its energy clients with such expertise drawn from other sections of its investment banking team. A notable instance is provided by ship-construction financing under Title XI of the Merchant Marine Act. Financing under Title XI places the full faith and credit of the federal government behind guarantees of debt issued to finance new vessel construction. White Weld's clients have utilized such financing for liquefied natural gas carriers, a semisubmersible drilling rig, and supply boats that service the offshore oil and gas industry.

Most of the companies operating in the natural resources area are regulated by agencies of the federal government. White Weld has a long history of assisting its clients by supplying expert financial witnesses at regulatory hearings. Recently we have been particularly active in this regard, testifying to the financial feasibility of multibillion-dollar energy projects involving importation of natural gas from Algeria and Alaska.

We have for many years expressed our view in hearings before the federal regulatory agencies and in other forums that unrealistic and arbitrary controls maintaining wellhead prices of gas far below their intrinsic value as compared with other fuels could only result in extreme waste and ultimately a serious shortage of this valuable commodity. Recent partial decontrol has been a step in the right direction. While complete decontrol will not restore the vast amounts of natural gas which have been used for inferior purposes for so many years, a further freeing of market prices is now essential to encourage more exploration for natural gas as well as the additional use of all feasible sources of supplemental and synthetic gas.

We believe research competence is essential to our activities in the energy sector. A well-informed sales force supported by a strong research effort is in the best position to market our clients' securities. White Weld has strengthened and broadened its energy research capability, paralleling its increased commitment of investment banking resources to the area. Pictured at right are A. Hager Bryant, John L. Kalmbach, and Phillip L. Dodge, three of the six analysts who concentrate on coverage of the energy area.



Trends in Corporate and Public Finance

White Weld's overall investment banking activities in both the private and public sectors were at new high levels in 1976. White Weld managed or co-managed approximately \$5.6 billion of publicly offered corporate securities in 110 separate issues in the United States, exceeding the firm's previous record year by more than \$1 billion. The firm, acting as agent, helped thirty clients raise \$836 million in the private placement market, more than double the amount raised in the previous year. As a manager or major underwriter, the firm's municipal finance specialists in 1976 purchased 532 issues having a total dollar value of \$15.0 billion.

For the same period, Credit Suisse White Weld Limited, the investment banking arm of our associated company in Europe, managed or co-managed \$5.9 billion of underwritings, \$4.0 billion above the 1975 level, and ranked first in Eurobond underwritings. Its activities are described in detail later in this report.

A principal factor bringing about the high financing levels was the improving debt market as 1976 progressed. In January, Moody's Aaa Bond Ratings indicator¹ an 8.88 percent yield; in December the rate was 8.05 percent. Straight debt issues accounted for more than 70 percent of White Weld's managed corporate business, and most of this financing was done for utilities and larger industrial companies, although the market did broaden, as compared to recent years, to admit lower-rated credits.

The volume of preferred stock and common equity financing was substantial, but the bulk of these issues was for utilities and major industrial corporations. Small to medium-sized companies faced a situation in 1976 similar to that of 1975, with an uncertain response for offerings of their common stocks in the public market. The success ratio for those companies selling their shares for the first time was indeed low.

The breadth of the private placement sector of the market also continued to improve throughout the year. The availability of funds for companies enjoying ratings for their debt below the high-investment-grade categories improved materially over the previous two years. Rates also declined throughout the year. At the beginning of 1976, a typical industrial company whose debt carried a Baa rating might have paid a rate of 9.25 percent on its fifteen-year senior notes sold to insurance companies. By the end of the year, a rate of around 8.70 percent was more normal.

The municipal sector of the bond market benefited by the retreat of New York City and State from the brink of disaster and off of the front pages of newspapers across the country. Market stability was also enhanced by the return of buying interest from fire and casualty insurance companies, whose profits rebounded sharply during the year. The Bond Buyer's 20-Municipal Bond Index started the year at 7.29 percent and ended at 5.83 percent, an unusually large change for a one-year period.

Industrial and Financial

In addition to the financings for natural gas and oil companies, White Weld managed major offerings in 1976 for such diverse clients as American Cyanamid Co., Baxter Laboratories,

Commercial Credit Co., Copperweld Corporation, Eltra Corporation, Greyhound Leasing & Financial Corp., Honeywell Finance, Liggett & Myers Incorporated, Miles Laboratories, Reliance Insurance Co., and Time Inc.

The companies for whom we completed private financings included Arvin Industries, W. R. Grace & Co., Honeywell Finance, Lincoln Pulp & Paper, Marley Co., Powers Regulator Co., and West Point-Pepperell. In the leasing area, the firm assisted UMC Industries by arranging a leveraged lease of equipment to Southland Corp.

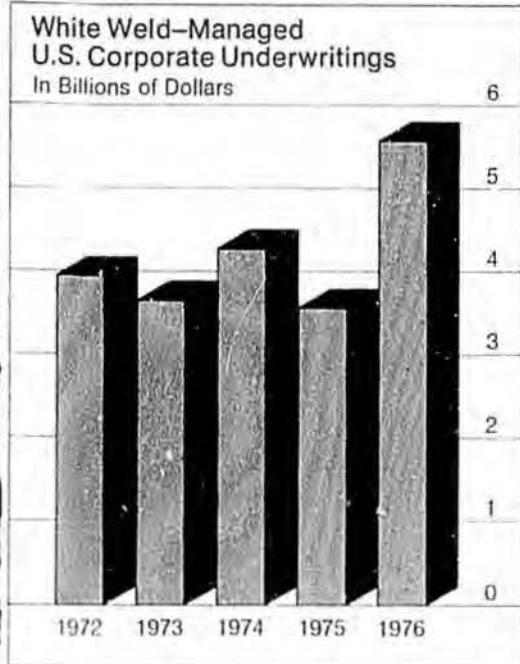
Merger often can function as an alternative to a company financing or to a secondary offering of stock for principal shareholders seeking liquidity. White Weld believes that its expertise in the merger and acquisition field is one of the key capabilities which it has to offer its clients. This phase of our business is expanding rapidly.

White Weld took an active role in 1976 in a number of merger, acquisition, and divestiture transactions. Among the clients for whom the firm acted were Arwood Corp., The Coca-Cola Company, Deseret Pharmaceutical Co., Di Giorgio Corp., Imperial Corp. of America, Walter Kidde & Co., Masoneilan International, Otis Elevator Co., Peoples Drug Stores, and Quaker Oats Co.

Because pollution control and general industrial revenue bonds on a tax-exempt basis have come to offer increasingly important means of raising capital for many different industries today, White Weld has made a specialty of these forms of financing. Working as a team, the firm's public finance and corporate finance experts completed a number of pollution-control and general industrial bond offerings for such clients as American Cyanamid Co., De Kalb AGresearch, Keystone Consolidated Industries, Madison Gas & Electric Co., Nevada Power Co., and Waste Management.

Special assistance in financing pollution-control equipment is now available to small business. In 1976, Congress enacted legislation to permit small businesses to take advantage of tax-exempt financing in constructing pollution-control projects through 100 percent debt guarantees by the Small Business Administration, which will make these securities readily marketable. White Weld played a key role in developing this legislation and was then selected by the SBA to work out a pilot program in California in collaboration with the Bank of America.

The managements of many corporate enterprises and governmental agencies call upon White Weld to provide its expertise on complex financial questions. Consulting assignments for American Can Co., Exxon Corporation, International Telephone and Telegraph Corp., and United States Steel Corp. were among those completed last year.





Utilities

As the rate of inflation subsided and interest rates declined, markets for the debt and equity securities of utilities improved over the situation of the past few years, when these companies had difficulty financing urgently needed expansion. White Weld improved substantially its ranking as a managing underwriter of negotiated issues and those offered competitively.

White Weld was a co-manager for the \$450-million Southern Bell Telephone & Telegraph Co. debenture offering, the largest single issue to date by a Bell System subsidiary. Among other major utility financings co-managed by the firm in 1976 were a \$30-million issue of first-mortgage bonds by Washington Water Power Co. and a \$75-million issue of preferred stock by Florida Power & Light Co.

White Weld's ability to serve its domestic utility clients is enhanced by the versatility in financing that it achieves through its international affiliations. In 1976, White Weld's associated company in Europe arranged lines of short-term credit for several U.S. utility companies on the London market, thus increasing the funds available to these companies and bringing them to the attention of the international capital markets.

Transportation

White Weld is developing significant capabilities in financing the transportation sector of the economy. We are expanding the investment banking services we provide to all elements of this highly capital-intensive field—shipping, airlines, trucking, and railroads. The addition to our senior management of Charles C. Tillinghast, Jr., TWA's former chairman, is an important enhancement of our staff in this regard. Paul E. Tierney, Jr., who was formerly director of finance with the U.S. Railway Association, specializes in the transportation sector. He is shown at left with Elisabeth N. Spector of the corporate finance department.

National policy inclines increasingly toward government assistance in various sectors of transportation, giving access to new sources of capital for corporate enterprise in the transportation industry. White Weld's expertise in Title XI ship financing has been mentioned. Acting as financial advisor, White Weld played an important part in bringing into being the government's unique \$2.1-billion investment in the securities of the Consolidated Rail Corporation (CONRAIL) in 1976. To develop the further opportunities we see arising in the railroad industry, we formed a syndicate to compete for railroad-equipment trust certificates. For the past twenty years there have been just two banking syndicates serving this very large market.

White Weld was advisor last year to Walter Kidde & Co. in its planned divestiture of the United States Lines, a major U.S. flag carrier, to WUI Inc. The firm believes that a period lies ahead in which divestiture and acquisition will constitute major means of mobilizing capital in the shipping industry. Similar possibilities are developing in trucking.

Public Finance

As the municipal market moved toward its record volume of \$33.8 billion in new underwritings last year, White Weld negotiated a number of important financings. Among other issues, it was senior manager for Platte River Power Authority, Colorado (\$60 million), Metropolitan Atlanta Rapid Transit Authority (\$50 million), Tennessee State School Bond Authority (\$60 million), and Port of Tacoma (\$38 million), and co-manager for South Carolina Public Service Authority (\$100 million). The creative approach that has distinguished White Weld's activities in energy, utilities, transportation, and other sectors also characterizes its efforts in public finance.

White Weld has a record of innovation in the field of mass transportation. It was instrumental in developing the legislation that made possible financing of the first regional consolidation of mass transportation, undertaken by the Massachusetts Bay Transportation Authority. The firm acted as advisor to the \$1.5-billion system for the Metropolitan Atlanta Rapid Transit Authority prior to negotiating the first \$50-million financing and is participating in an advisory capacity to the Chicago Regional Transit Authority.

White Weld has been the pioneer in financing facilities for converting municipal solid waste into energy and recoverable resources. Our approach blends public sector tax-exempt financing with the tax benefits of private ownership, offering to communities the lowest net cost of financing for these highly capital-intensive systems. White Weld has put together a solid waste project team consisting of municipal and corporate finance officers, who have been actively developing this new and important market. As a result, we have been retained as financial advisor for projects throughout the United States, including state governments (Hawaii, California, and Wisconsin) and several major cities and municipalities.

The firm is currently under contract with the Environmental Protection Agency to provide technical assistance to state and local governments in implementing federal resource recovery policy.

There is increasing overlap between the private and public sectors of the economy as a result of evolving national policy in transportation, pollution control, energy, and other similar areas. White Weld's corporate and public finance experts worked closely together to develop the financing concepts not only for waste recovery but also for SBA pollution-equipment bonds for small businesses, mentioned earlier. The teamwork approach has increased the firm's value as an advisor to the managements of both corporate enterprise and governmental agencies. White Weld's corporate and public finance departments, for example, are teamed as advisors to the Alaska State Investment Advisory Committee in connection with the Alaska Permanent Fund.



A Unique Collaboration in International Finance

White Weld's important role in international finance has been established over five decades of active and innovative participation in investment banking, brokerage, and market making. Within the last seven years, the firm has joined with Credit Suisse, a leading bank in Switzerland, in creating a flexible, talented organization to provide financial services for corporations, governments, and institutions dealing in international money markets.

The two organizations share in the ownership of Société anonyme financière du Credit Suisse et de White Weld (Financière), which is headquartered in Europe and which engages through subsidiary units in investment banking, trading, asset management, and certain specialized commercial banking activities.

Financière's operations extend across Europe, the Middle East, and the Far East. White Weld's international investment banking group, located in New York, covers the United States, Canada, and Latin America and also provides customers in all parts of the globe with entrée to the U.S. capital markets. In addition, through its brokerage and trading offices in London, Paris, Geneva, Zurich, Montreal, Hong Kong, and Caracas, White Weld provides our investor clients around the world with research, trading, and execution services in all types of securities traded in the U.S. markets. Together the two companies make available to our clients a highly effective partnership of talents.

Financière has several important operating units. The largest of these is **Credit Suisse White Weld Limited (CSWW)**, which is located in London. CSWW is the leading underwriter in the Eurobond market and an active participant in all forms of cross-border financial transactions, including mergers and acquisitions. It is a leader in handling a wide spectrum of mainly dollar-denominated money market instruments and has become the foremost market maker in London dollar certificates of deposit and medium-term tranche issues of CDs. It also leads in the floating of issues for banks in the international money market. CSWW is active in the management of international fixed-income investment portfolios. The trading arm of Financière, **White Weld Securities**, is one of the principal dealers in the secondary market for Eurodollar bonds and is also located in London.

Banque Française de Dépôts et de Titres (BFDT) handles commercial banking activities for both individual and institutional clients and conducts extensive money market operations in all types of instruments. Through active participation in Eurobond issues, BFDT contributes significantly to the combined placement power of the group. The bank also provides merger and acquisition services and has played a role in a number of important acquisitions of French companies by transnational enterprises. BFDT is active in arranging listings for issues of foreign companies on the Bourse in Paris. One of the bank's operations under the name **Forinvest** conducts research in French securities and provides financial consulting services for industrial clients in France and abroad.

Clariden Bank specializes in multinational investment management for a select group of investors spread around the globe. A growing part of its clients' funds is managed on a discretionary basis, and its investments are diversified among the principal capital markets—the North American, European, and Far Eastern stock exchanges and the Eurodollar and Eurobond markets. Clariden Bank maintains close contact with affiliated entities of Financière as well as with independent advisors in framing its worldwide investment strategy. In addition to this traditional activity, the bank has become more extensively involved in the Swiss capital markets and has initiated and successfully placed a growing volume of Swiss-franc-denominated, fixed-interest securities in both public offerings and private placements. The bank provides excellent contact with market trends in the growing Swiss capital markets.

The international investment banking group at White Weld in New York works closely with these affiliated companies overseas to achieve the best execution of our customers' diverse financial transactions. Through its offices overseas and in New York, White Weld distributes an important share of the Eurodollar issues originated by CSWW.

Innovation in the World Marketplace

As in the United States, the general recovery of the European economy from the trough of the recession stimulated activity in financial markets by governments and international companies on both sides of the Atlantic and in the Far East. The investment banking departments of both White Weld and CSWW arranged record numbers of financings and cross-border merger transactions for their clients during the year.

The Eurobond market reached new levels. Total volume for 1976 was \$12.0 billion in 274 issues as compared with about \$7.0 billion the previous year. CSWW ranked first in this market, managing or co-managing 107 issues valued at \$5.9 billion, almost 50 percent of the total amount raised. Of Eurobond financings, 66 percent were denominated in dollars, 17 percent in Deutsche marks, and the balance in other currencies or combinations thereof.

White Weld and CSWW are well known for their founding role in the Eurobond market. They have pioneered a substantial majority of the innovations introduced into this market, helping make it one of the most important sources of capital in the world. CSWW, in addition to its important role in internationally syndicated bond offerings, is a leading factor in the management and co-management of floating-rate note issues by major international banks. It also participated in the creation of the London dollar CD market, which has grown to outstandings of \$14 billion.

Financings by CSWW

CSWW is playing a lead role in developing financing for a major project undertaken by Norpipe to exploit the oil in the Ekofisk field in the North Sea. Norpipe is owned 50 percent by the Norwegian government oil company, Statoil, and 50 percent by the Phillips group of private companies. In connection with this project, CSWW was the lead manager on a \$50-million Eurobond issue. An unusual feature of this offering was its use as security of the throughput agreements made by the participants.

As mentioned earlier, several U.S. utility companies were introduced to the international capital markets in financings in which CSWW participated. Included among these were revolving loans with European banks for Puget Sound Power & Light Co. (\$25 million), Portland General Electric Co. (\$40 million), and Cleveland Electric Illuminating Co. (\$30 million).

CSWW also managed a number of financings for non-European borrowers in industry, banking, and other fields. Among some of these were debt issues for Australia, the European Economic Community, the provinces of New Brunswick and Saskatchewan, the Royal Bank of Canada, Fiat do Brasil, and Alusuisse International. Other private placements of debt securities were arranged successfully with Middle East lenders.

International Mergers and Acquisitions

White Weld and CSWW cooperate in assisting clients in North America, Europe, and elsewhere to make advantageous mergers and acquisitions. White Weld has completed a larger number of acquisitions of U.S. businesses on behalf of foreign acquirers than any other investment bank. As an example, White Weld negotiated the purchase of Disston by Sandvik Aktiebolag, enlarging the Swedish firm's U.S. presence and expanding its finished steel products business.

White Weld also assisted in the acquisition of two other U.S. companies by European interests. Midwestern United Life Insurance Co. was acquired by Nationale-Nederlanden, a Dutch insurance company. The Marx Toy division of Quaker Oats Co. was sold to Dunbee-Combex-Marx, a British manufacturer of toys, toiletries, and home improvement items.

Financings in the U.S. Market

During 1976, White Weld was co-manager of the largest public financing on behalf of a foreign borrower that has been made in the United States—a \$367-million bond issue for National Power Corporation, a Philippine government entity, to finance a major nuclear power facility in Luzon. A unique feature of the financing was its guarantee by the Export-Import Bank of the United States, the first time that the bank has guaranteed a public issue underwritten by private investment bankers.

One of the major financings for non-U.S. borrowers, managed in the United States by White Weld, was a \$100-million note for Banque Française du Commerce Extérieur (BFCE), the French equivalent of the Ex-Im Bank. A major borrower in the European and U.S. capital markets, BFCE also selected CSWW to co-manage two note issues in Europe in 1976 totaling \$100 million.





An Expanding Commitment to Trading

White Weld has expanded dramatically its presence in the major segments of the global financial markets in which it operates—corporate fixed-income securities, tax-exempt securities, U.S. Government and federal agency securities, Eurodollar bonds, certificates of deposit and other money market instruments, and listed and unlisted equity securities. We have added experienced staff in all trading departments and have steadily increased our commitment of capital for positioning. The firm's securities inventories are managed by our traders based on their assessment of the markets and our clients' needs. On average, trading positions have doubled over the last twelve months and quadrupled over the last two years. U.S. Government and agency securities account for the largest segment of typical total positions, but all trading activities have been enlarged substantially.

White Weld participated fully in the heavy volume of trading that was transacted during 1976 and increased its market penetration in all major sectors.

Principal transactions for clients in corporate fixed-income securities increased 32 percent over the previous year, and such transactions in tax-exempt securities increased 36 percent. Activity in government and federal agency securities increased so substantially that comparisons with previous years are not appropriate.

Foreign-dollar bond and Eurodollar convertible bond trading, long a major strength of White Weld, was also extremely active.

The volume of principal transactions effected for clients in over-the-counter equity securities increased 60 percent over the previous year, with the firm almost doubling its share of trading volume in the approximately eighty stocks in which it makes a market. Principal transactions in listed securities also increased, as did the firm's total share of market in listed securities.

In all, principal transactions effected for clients in the secondary markets last year averaged over \$250 million per day.

We have in place and continue to upgrade the capabilities of a worldwide high-speed communications system that transmits market and trade data to our offices and links them with securities exchanges and the trading desks of many of our large customers.

The photograph on the opposite page, taken in the trading room at White Weld's headquarters, shows one of the posts that handles U.S. Government and federal agency securities. Although trading in government securities is not a new function for White Weld, the firm in recent years has succeeded in becoming an important factor in this market and in 1976 was added by the Federal Reserve to its list of primary reporting dealers.

White Weld's enlarged commitment to trading is responsive to the importance that both issuing and investing clients place on ability to distribute new issues and to execute transactions at lowest net cost.



Full Service for Institutional Investors

Sophistication and diversity mark White Weld's institutional clientele today. The men and women who are primarily concerned with servicing this market in our sales, trading, and research departments deliver execution services and investment recommendations of superior quality. In virtually all trading departments, we have enlarged staff and capital to accommodate our customers' expanding needs. We utilize specialized sales forces for equities, corporate fixed-income securities, municipal securities, and U.S. Government and agencies in order to meet the needs of specific classes of institutions or investment functions within larger diversified organizations. These sales, trading, and research professionals are in daily contact with their counterparts at client institutions here and abroad.

Corporate Fixed-Income Securities

In 1976, White Weld's corporate fixed-income department expanded both its personnel and capital resources to keep pace with the record activity of customers dealing in corporate bonds and preferred stocks. A staff of bond trading and sales specialists numbering more than fifty provides institutional customers, who are increasingly oriented toward active management of their bond portfolios, with investment ideas and interpretations of market trends. As a major underwriter, we offer our clients opportunities to invest in most new issues. During the year we placed \$1 billion of new corporate debt and preferred stock issues, substantially more than the total of our underwriting positions.

U.S. Government and Federal Agency Securities

The continued buildup of market making in U.S. Government and federal agency securities has made this a major trading activity. As a primary reporting dealer to the Federal Reserve, the firm engages in direct transactions with the New York Federal Reserve Bank, which conducts the Fed's open-market operations. In addition to the direct benefits of dealing with the most important customer in the market, White Weld's capacity to make markets over the entire maturity range of government and federal agency securities is enhanced.

Tax-exempt Securities

White Weld maintains active trading markets in tax-free bonds on a nationwide basis. In addition to the substantial underwriting and trading activity conducted by our New York office, eleven of our larger regional branch offices are staffed with municipal specialists who underwrite and make secondary markets in local issues. These men and women offer institutional and individual clients a coverage of regional markets that is as comprehensive as any in our industry.

International Bonds and Arbitrage

White Weld has long been one of the principal market makers for foreign securities denominated in dollars. The firm trades in foreign bonds, coordinating with European markets by direct private wire. We also take positions in foreign securities for our own account to take advantage of price differentials between markets or between related securities of the same issue.

Equity Securities

A highly trained sales force specializing in equity securities covers major institutions. In addition, those actively involved in servicing these accounts include traders in listed and over-the-counter stocks and options, exchange-floor personnel, and specialists providing company and industry analyses, investment policies, and economic forecasts. Taken together, White Weld's professional staff servicing the equity needs of institutional clients number more than one hundred. Despite the continuing erosion of the institutional commission structure, White Weld's institutional commission revenues increased significantly during the year, as more clients concentrated their business on a smaller number of firms capable of providing them with the full spectrum of equity services.

Our staff of research analysts provides in-depth coverage on more than 375 individual companies and 30 industry groups, representing 80 percent of the stocks included in Standard & Poor's Composite Index of 500 Stocks. In the allied areas of investment policy, economics, and market and technical analysis, which are of particular concern to portfolio managers, White Weld has significantly expanded its capabilities and now has one of the largest professional staffs of its kind in our industry.

White Weld's equity trading network spans all twenty-six domestic and seven international offices. Virtually all major accounts are serviced directly from our own trading desks.

Economic Services

Financial institutions have looked increasingly to White Weld for in-depth analyses of economic trends. In 1976, White Weld Economic Services was established to provide a highly specialized series of commentaries on the economy and certain industries to industrial corporations. Dr. A. Gary Shilling, senior vice president and director of this new activity, is shown at left with his staff.



Special Programs for the Individual Investor

Through an experienced staff of account executives located in twenty-six domestic and seven foreign branches, White Weld offers sophisticated financial services to knowledgeable individual investors. The same broad array of financial products available to institutions is tailored to the needs of our individual clients.

Investment policy and research information is relayed to all account executives in daily conference calls and in written material, prepared and organized for timely transmittal to customers. The trading facilities described earlier are likewise available to execute transactions in common stocks and other securities. Our individual clients thus benefit from the market expertise of a trading staff that regularly fulfills the exacting standards required by professional investors.

In the last several years, individual clients have increasingly taken advantage of investment alternatives to common stocks. White Weld underwrites and makes markets in a multitude of utility, industrial, and finance company bonds and notes. We also offer our clients a broad range of tax-exempt investment opportunities including revenue bonds, general obligation bonds, pollution-control and other industrial revenue bonds, and municipal unit trusts. For investors interested in employing capital for the short term, we offer access to all short-term money market investments, including tax-exempt project notes.

Special Services

Directly related to White Weld's block-trading capability is its expertise in handling and executing securities sales that are restricted under Securities and Exchange Commission regulations. Such holdings often result from the sale of a private company to a public company. These transactions are therefore of special value to corporate officers and directors as well as to other large holders of listed and unlisted securities. Our legal and trading staff work together to provide the best execution permitted by the market and to ensure compliance with the technical provisions of the law.

For the investor interested in tax-sheltered investments, White Weld is active in offering equity participations in a variety of programs, principally in real estate and oil and gas. These investments are screened by staff specializing in the real estate and oil and gas industries and are selected on the basis of their intrinsic economic worth as well as on their tax aspects.

Listed options trading is an integral part of White Weld's overall trading and brokerage activity and an area of special interest to many of our individual clients. We offer access to listed options trading on all exchanges and the assistance of specially developed computer programs in tracking the changing relationships between options and their related common stocks.

Investment Advice

The cornerstone of White Weld's individual client service is the importance we place on matching the firm's overall investment policy to the particular and diverse needs of each client. The critical link between customers and our investment policy and research specialists is the account executive.



White Weld's *Money Manager Service*, introduced in 1976, provides continually updated material on the subjects relevant to investors. Richard A. Kimball, vice chairman of the institutional policy committee and director of marketing, is seen at left with a copy of the publication. This is the written portion of White Weld's overall service for money managers.

Money Manager Service contains, often in summary form, copies of most of White Weld's written investment policy statements, economic forecasts, research reports on industries and companies, selected stock lists, technical market information, and other essential data. James C. Blair and Brenda L. Landry, pictured on the opposite page, are among the senior analysts on the White Weld research staff who develop this information. *Money Manager Service*, brought up to date weekly, has been received enthusiastically by the professional money management clients of White Weld for whom it is designed. The service is also provided to all White Weld account executives for their use in counseling their individual clients.

Coordinated with *Money Manager Service* are conference calls each weekday morning that keep our account executives in continuous touch with markets and changing circumstances. In addition, each fixed-income department—corporate, U.S. Government, and municipal—includes specialists whose responsibility it is to interpret developments in their areas and to coordinate the execution of transactions for the benefit of individual clients.

Continuous Supervision of Client Portfolios

For the past twenty-eight years, White Weld has been engaged continuously in offering investment counsel to individual clients and to tax-exempt corporate and union pension funds and to endowment funds. Our objective is to achieve favorable performance consistent with the specific investment goals of each account.

It is our experience that a carefully conceived and clearly defined investment philosophy, applied with consistency and decisiveness, will provide superior investment results over any market cycle. We are most conscious of the risk-reward ratio in the investment selection process and regard conservation of capital as one of our prime investment objectives. Our investment approach utilizes equities, bonds, and short-term reserves, depending on the relative appeal of each through the economic cycle. Cash and fixed-income management are integral parts of our service. Careful supervision of each investor's portfolio by an experienced and well-informed manager provides protection against unnecessary losses that might result from oversight or lack of information.

Today, assets under management by White Weld exceed \$600 million, the highest total in our history. Our investment management staff under the direction of Edward D. Little, shown at lower left, includes sixteen senior portfolio managers. These professionals work closely with our research, economic, and investment policy groups to develop and execute appropriate investment strategies for each client.





Support Services for White Weld Clients

White Weld's operations and administrative personnel are dedicated to providing prompt and efficient service to the firm's clients. The operations group is responsible for processing of customers' orders, control of securities transfers, record keeping, and other support functions required for the administration of customer accounts. Customer services include securities safekeeping, the collection and payment of interest and dividends, the mailing of proxy materials and company reports, and the preparation of monthly statements of account.

White Weld's operations staff works in an environment characterized by change as a result of sharp fluctuations from month to month in the processing work load and, over the longer term, of new developments in the industry's clearance and settlement procedures.

Because of the growing complexity of the securities markets, White Weld places a high priority on maintaining substantial reserve processing capacity to accommodate peak trading volume. It is continually upgrading its data processing systems to improve service. Of particular importance is the development of data retrieval programs to give account executives, traders, and operations personnel immediate access to information they need in order to respond quickly to clients.

Financial Condition

At December 31, 1976, White Weld Holdings, Inc., had over \$50 million in stockholders' equity and, on a consolidated basis, over \$70 million in total capital, including borrowed funds. The company's principal asset is its wholly owned subsidiary, White, Weld & Co. Incorporated, which offers the full range of underwriting, brokerage, securities trading, and investment counsel services described in this report. (See Notes to the Statement of Financial Condition for further information about White, Weld & Co. Incorporated in the following section.) The other major asset owned by White Weld Holdings is its investment in Financière.

The nerve center of White Weld's world-wide communications network is on Water Street, a few blocks from the firm's headquarters in lower Manhattan. The vastly increased volume of information flowing to and from White Weld's branches in this country and its own offices and those of its close affiliates overseas necessitates the continual expansion and upgrading of electronic communications and data processing equipment. Some four hundred and fifty men and women are now employed at the Water Street operations and administrative center, which opened four years ago.

Statement of Consolidated Financial Condition (unaudited)

December 31, 1976

Assets

Cash	\$ 5,710,000
Receivables:	
Customers	290,472,000
Brokers	68,694,000
Other	11,256,000
Securities—at market value (Note 2)	216,707,000
Investment in associated company (Notes 1 and 3)	16,815,000
Fixed assets—net (Note 1)	7,393,000
Other assets	3,442,000
TOTAL	<u>\$620,489,000</u>

Liabilities and Stockholders' Equity

Current liabilities:

Money borrowed on securities (Note 2)	\$233,214,000
Payable to brokers	69,564,000
Payable to customers	178,658,000
Drafts payable	15,532,000
Securities sold short—at market value	28,354,000
Other current liabilities	20,682,000
Total current liabilities	<u>546,004,000</u>
Promissory note due 1981 (Note 3)	4,000,000
Subordinated borrowings (Note 4)	19,544,000
Common stockholders' equity	50,941,000
TOTAL	<u>\$620,489,000</u>

See Notes to Statement of Financial Condition.

Notes to Statement of Financial Condition (unaudited)**1. Accounting Policies**

The statement of consolidated financial condition includes the accounts of White Weld Holdings, Inc., and its wholly owned subsidiary, White, Weld & Co. Incorporated (the "Subsidiary"), a member firm of the New York Stock Exchange, Inc. Total assets of the Subsidiary are \$598,932,000 and capital funds are \$54,329,000, consisting of subordinated borrowings of \$18,984,000 (Note 4) and common stockholders' equity of \$35,345,000.

Assets and liabilities relating to securities transactions are reflected in the statement on a settlement date basis.

Exchange memberships (included in other assets) are carried at cost (\$941,000) and, in the opinion of the Company, the current market value (\$623,000) does not indicate a permanent impairment in the value of such memberships.

The investment in the associated company, Société anonyme financière du Credit Suisse et de White Weld, is carried at equity in net assets. Undistributed income of the foreign associated company of \$7,992,000 is included in common stockholders' equity.

Fixed assets, which consist of furniture, equipment, and leasehold improvements, are stated at cost less accumulated depreciation and amortization of \$2,228,000.

2. Securities Pledged and Loaned

Money borrowed on securities and amounts due in connection with securities loaned and repurchase agreements are fully collateralized by marketable securities valued at \$315,133,000. Such collateral includes \$205,998,000 owned by the Subsidiary.

3. Promissory Note

The promissory note issued to a bank bears interest at 115% of the bank's prime rate and matures in January 1981. The Company's investment in the associated company is pledged as collateral for the note.

4. Subordinated Borrowings

Subordinated borrowings include senior capital notes, \$8,750,000, subordinated debentures, \$8,589,000, and secured demand notes, \$2,125,000.

The senior capital notes mature in 1987. The

Subsidiary is required to prepay, semi-annually, \$417,000 principal amount of the notes. The covenants of the note agreement contain restrictions on the Subsidiary as to minimum capital requirements and, under certain circumstances, certain stock payments, stock acquisitions, and the payment of cash dividends. The subordinated debentures mature in the fiscal years ending June 30: 1978, \$623,000; 1979, \$600,000; 1980, \$100,000; 1981, \$1,666,000; and 1982, \$5,600,000. The secured demand notes mature in 1981.

5. Capital Requirements

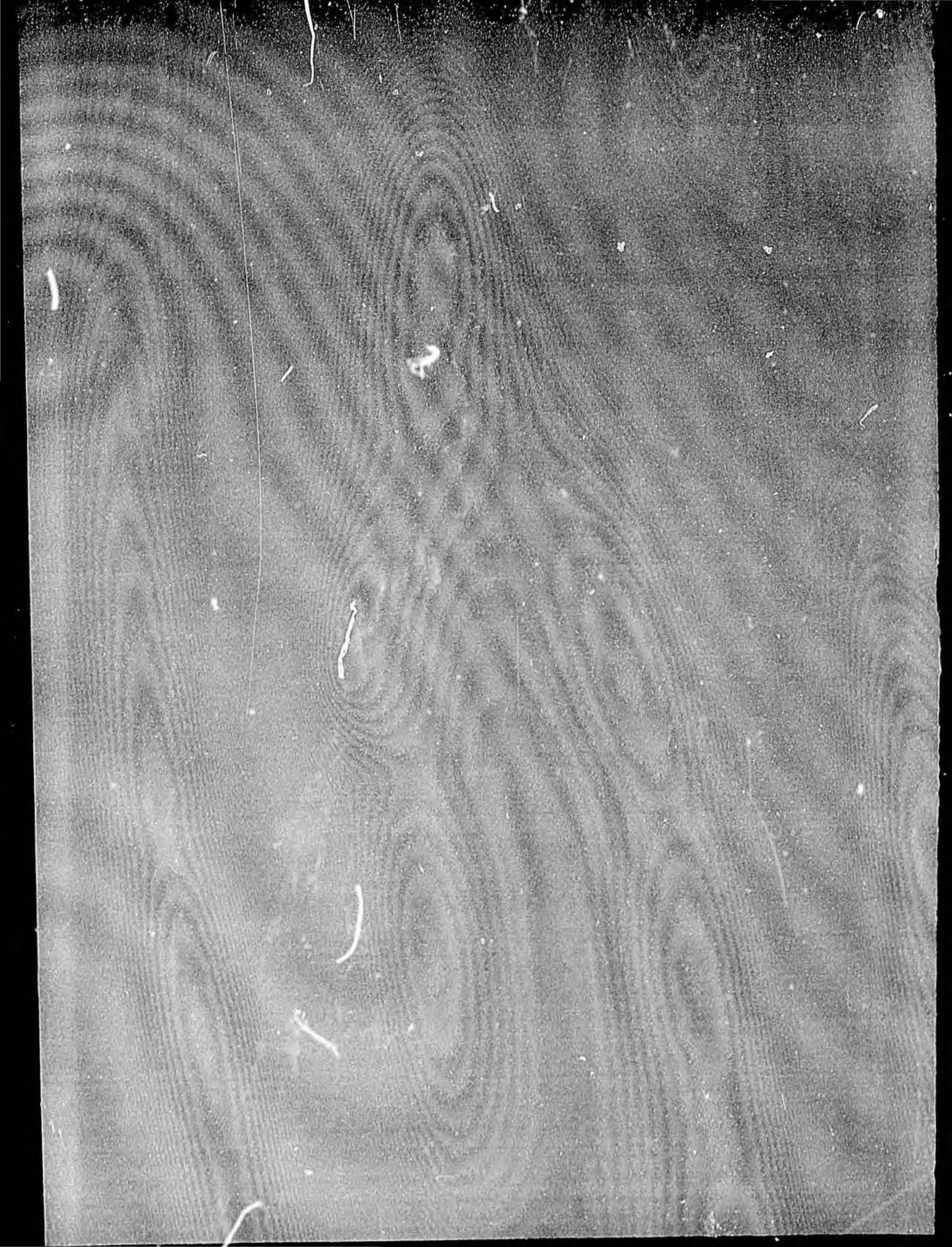
The Subsidiary is subject to the Uniform Net Capital Rule (Rule 15c3-1) of the Securities and Exchange Commission, which requires that aggregate indebtedness (as defined) shall not exceed fifteen times net capital (as defined). There are restrictions on operations of the Subsidiary if aggregate indebtedness exceeds ten times net capital. The Subsidiary's net capital and minimum net capital (as defined) were \$32,593,000 and \$14,555,000, respectively, and its aggregate indebtedness was 6.7 times its net capital.

6. Commitments and Contingencies

The Subsidiary's minimum rental commitments, net of sublease income, under non-cancelable leases are for the fiscal years ending June 30: 1977, \$7,171,000; 1978, \$6,848,000; 1979, \$6,596,000; 1980, \$6,009,000; and 1981, \$5,112,000; and for the five-fiscal-year periods ending 1986, \$22,904,000; 1991, \$15,795,000; and 1996, \$2,391,000. Included in the foregoing rental commitments are financing leases having a present value of \$4,064,000 based upon an approximate weighted average interest rate of 7.20%.

The Subsidiary has a contingent liability of \$11,642,000 in respect of irrevocable letters of credit aggregating \$12,100,000 which expire March 1, 1977 (renewable for six months thereafter) written in favor of certain option clearing associations to satisfy margin requirements.

The Subsidiary has been named in several civil actions in the ordinary course of its business which, in the opinion of management, will be resolved with no material adverse effect on its financial condition.



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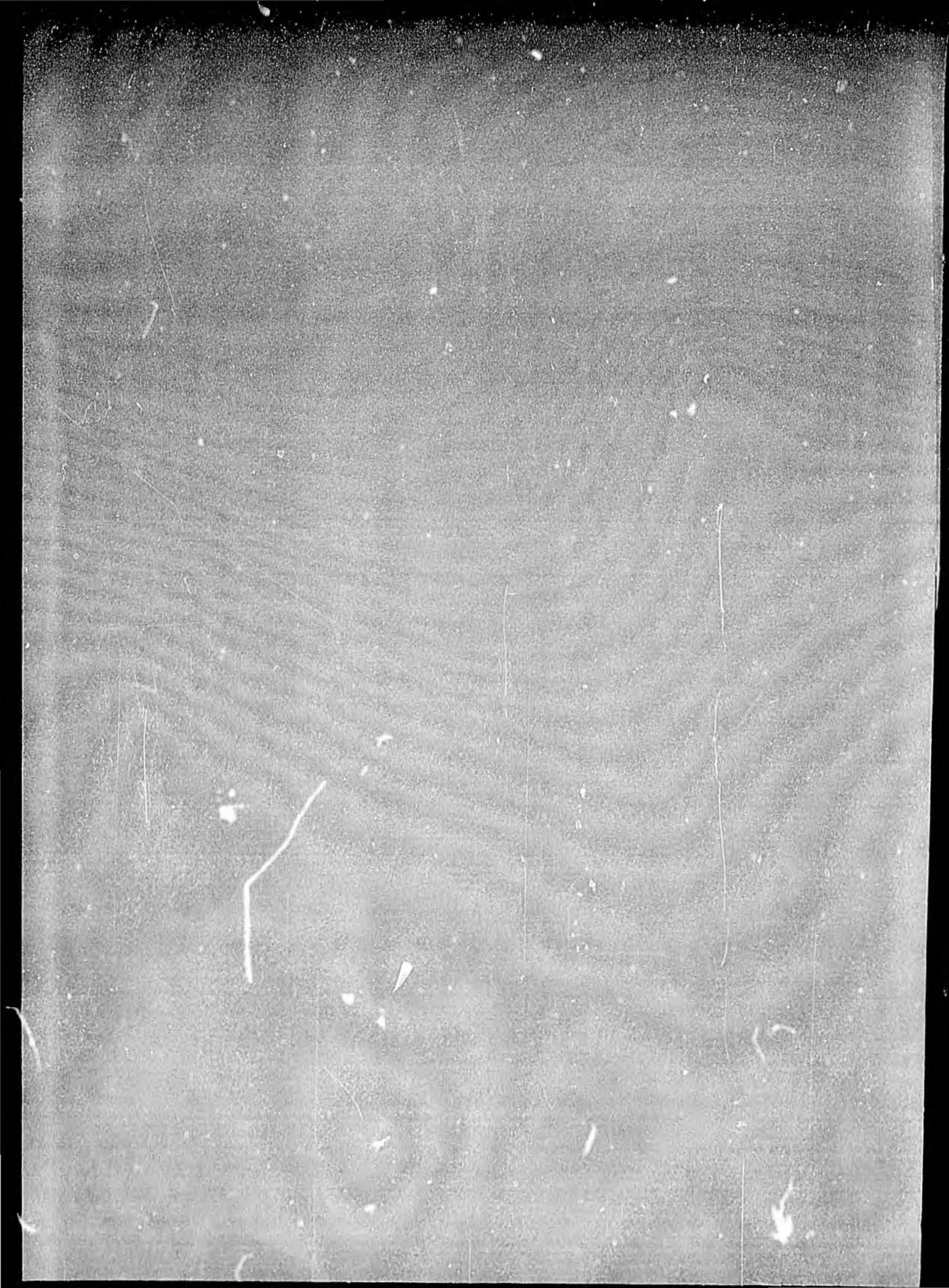
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CABLE ADDRESS "WHITEWELD"

December 9th, 1977

Mr. Clark Gruening, Chairman
House Permanent Fund Committee

Since the House Special Committee on the Permanent Fund is in the final stages of structuring legislation for consideration by the 1978 legislature, it is time to consider the use of the income of this "Permanent Fund".

The provisions of the Permanent Fund Constitutional Amendment include that "the income from the Permanent Fund shall be deposited in the General Fund unless otherwise provided by law". According to the best estimates of the Department of Revenue, the minimum amount (25%) of the funds received as mineral lease rentals, royalties and other payments will result in an accumulation by 1985 of some \$1.8 billion. The investment income from that amount, at an average 7% rate of return, would produce approximately \$126,000,000 in any one year. As the Permanent Fund continues to grow, its increased capital will provide additional annual income in excess of the aforementioned figure, however, for the sake of perspective, the ensuing discussion will be confined to the \$126,000,000 projected income.

If the estimates are correct as to the principal accumulated in the Permanent Fund by 1985 at a 25% rate, the remaining balance accumulated in the General Fund should amount to some \$5.4 billion. The effect of the addition of \$126,000,000 to such an accumulation would increase the 1985 accumulation by approximately 2%. Such an increase is minimal in relation to a General Fund accumulation of the magnitude as anticipated.

Therefore, the income of the Permanent Fund should be dedicated to doing more than just adding a small increment to the General Fund. Even though it may eventually return to the Permanent Fund, it should be channeled into projects with revenue producing capability that provide benefits for the majority of Alaskans, and simultaneously allow for long-term financings at the lowest possible interest rate.

The House Special Committee, during the conduct of public hearings, has received many proposals for the use of Permanent Fund's income. Many of these proposals appear to be meritorious from numerous points of view. However, in turn, many of these same proposals would seem to be better responded to through

the actions of the legislature and addressed through the General Fund as opposed to the Permanent Fund's income.

Essential to the lifestyle of all modern societies is the availability of electric power. Advocates of no growth, modest growth, rapid growth or controlled growth all share a need for power. The availability of power often determines whether desirable economic growth can take place. The cost of such power is of course, an important element. All other things considered, the cost of power influences the future direction in any modern society.

Whether power generation occurs through capital-intensive projects (hydro-electric) or fuel-intensive projects (coal or gas-fired) its financing is generally through issuance of long-term debt. Production costs of hydro are generally stable since the fuel (water) costs are practically non-existent. Production costs of coal or gas-fired facilities are subject to continually escalating costs of the fuel necessary for the electric generation.

Long-term debt sold for the construction of either type of facility, without regard to the operation and maintenance expense of each, must be amortized through the service of debt; principal and interest payments annually until the debt is extinguished. The total cost of the debt service is affected by the rate of interest which investors demand for the long term loan of money.

A 40 year debt instrument in the amount of \$100,000,000, bearing an interest rate of 6½% will require a level debt service (principal and interest) of \$7,069,400 annually to liquidate the debt. If the interest rate is 5½%, the annual debt service requirement is \$6,232,000. This represents a difference of \$837,400 per year and over a 40 year period involves a saving of \$33,496,000.

Since debt service is a major factor in determining the rates users must pay for electric usage, the rate of interest at which a debt instrument is financed is a significant element in the total cost to the consumer. Bonds payable solely from the revenues of the utility are judged by investors on their credit-worthiness. The more credit-worthy, the lower the interest rate, the less credit-worthy, the higher the interest rate.

Alaska possesses many sites which are suitable for hydro-electric generating facilities. However, in some instances, these sites are not located near the population centers which require the power generated. Due to its topography, long-range transmission lines bringing power to the load-centers are often not feasible. In other instances, the best development of such capital-intensive projects may require large-scale projects which in the near-term, produce a surplus of power. Smaller scale generation facilities using coal or gas-fired power production are required in those areas without large load demands or without good potential hydro sites. The fact that the latter use a precious commodity which is non-renewable is not the point. If the power is needed, it must be produced. Nevertheless, if the project can be financed at a lower interest cost, a benefit will accrue to the user through a lower cost of service.

It is suggested that the future power needs of Alaskans can be delivered at a lower cost whether such power is provided through hydro or fossil fuels. The ability to affect the interest rate on whatever long-term project is financed, can accomplish this. The following paragraphs suggests how this can be done without depriving the Permanent Fund of other uses of its income.

The income from the Permanent Fund will be derived from "investment grade" securities and as such represents a highly reliable and secure cash flow. This annual cash flow can be dedicated to assuring that principal and interest requirements on bonds issued to construct revenue producing power projects are met in the event of a revenue short-fall from the revenue producing project. The effect will make it possible for the revenue bonds to receive a high credit rating and high evaluation in the market place which will result in a significantly lower cost of borrowing for the project construction. At the end of a given period, (debt service year or monthly), income from the Permanent Fund dedicated to the revenue bonds debt service requirements not needed is released to the General Fund or for any other purpose directed by law.

The dedication of Permanent Fund income to revenue bond debt service would not be accomplished in the legislation itself, but rather in a "guarantee agreement" between the Permanent Fund and the entity issuing the revenue bonds and the "guarantee agreement" would actually appear on the face of the debt instrument. From the investor and rating agency point of view, if the guarantee is in the legislation it is legally subject to change by succeeding legislatures. If the guarantee is in an agreement as part of the revenue bond issue it is dedicated for as long as the bonds are outstanding.

It must be assumed for the purpose of this guarantee arrangement that the Permanent Fund will receive 25% of the oil and gas income because of the terms of the Constitutional Amendment. Based on that assumption, estimates (by the State) of the size of the Permanent Fund in 1985 will be \$1,800,000,000.

A reasonable assumption of 7% income from investment produces an annual cash flow available for guarantees of \$126,000,000. An annual cash flow of this magnitude, assuming a 6% interest cost on guaranteed bond issues, will support approximately \$1,800,000,000 of bonds.

The various projects to be supported by the guarantee would be financed by revenue bonds of any state agency or any subdivision of government in Alaska for electric generation and transmission. Each bond issue would capitalize interest during construction and fund its own debt service reserve to conform to the demands of the market for such bonds at the time of financing.

The act providing for a guarantee should be broad in form. The covenants relating to, and provisions of, each project will be structured into each bond issue.

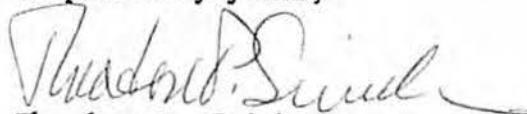
There might be some merit in including in the act certain findings and directives to the Board of the Permanent Fund, but it probably is more appropriate for the Board to outline its own guidelines as it relates to such guarantee on bonds of projects to be financed in its administrative rules and regulations. By this is meant, for example, considerations by the legislature in its deliberations leading to the approval of a project such as economic need, economic feasibility, geographic locations, social benefit, impact on locality, etc.

A draft of a bill has been provided to your committee which would, subject to redraft to conform to custom, constitutional requirements, the Permanent Fund Act and language usage in Alaska, creates the mechanism for such a debt guarantee program. A brief analysis of this draft follows.

- Section 1. Creates the mechanism by authorizing the Board of the Permanent Fund to enter into guarantee agreements. Limits the guarantee to income only. Provides for agreements with any entity of state or local government. Provides guarantee of principal payments, sinking fund payments and interest but prevents use of Permanent Fund income for optional early retirement of guaranteed debt. Limits the guarantee to electric generation and transmission. Leaves the details of guarantee agreements to the Board of Trustees.
- Section 2. In effect limits the amount of debt that can be guaranteed. This adds to the credit-worthiness of the guarantee from the lenders point of view. Depending somewhat on the actual portfolio of investments in the Permanent Fund, it is important to consider whether or not to limit the total of guarantees to something less than 100% of the Fund income. This could be done in the Act, which does not happen in this draft, or it could be a policy matter of the Board of the Fund.
- Section 3. Provides that the guarantee article appear on the debt instrument which clearly establishes that it survives as long as the bonds are outstanding. This definitely is stronger and distinguishes the guarantee from any similarity to the so called "moral-obligation" pledge.
- Section 4. Provides that a guarantee agreement can be entered into on the debt of projects only after approval by the legislature. Part of the thrust of this section is in contemplation of a centrally controlled State-wide power development plan that considers the needs and best interest of all of Alaska.
- Sections 5 & 6 These sections are simply "boiler-plate" provisions.

The draft bill clearly does not contemplate any subsidy of electric costs to energy consumers. However, there is no prohibition that any subsidy to energy users deemed to be appropriate by the State can be accomplished by the legislature through appropriation from the General Fund or other sources which would not interfere with the value of this guarantee program to finance the capital costs of meeting the power needs of Alaska.

Respectfully yours,



Theodore P. Swick

TPS/vmr

#49

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August 20, 1976

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Gentlemen:

This letter is for the purpose of presenting certain summary information for the first meeting of the expanded State Investment Advisory Committee in Anchorage on August 26, 1976.

Our firm has been retained by the State Investment Advisory Committee through Commissioner Sterling Gallagher, Department of Revenue, to provide consulting services concerning the establishment and operation of a Permanent Fund for the State of Alaska. Specifically, for this initial meeting, we have been asked to (I) outline the possible uses and advantages of the tax exempt financing privilege that could be available to the Permanent Fund, and (II) summarize our review to date of similar funds in other states and countries.

- (I) Outline of Possible Uses and Advantages of Tax Exempt Financing Privilege for the Permanent Fund

Once the Permanent Fund has been established, the legislature may create a variety of structures to facilitate taking advantage of the tax exempt privilege enjoyed by state and local government in the United States to finance public purpose projects within the limitations of federal, state and local statutes and regulations. Examples of public purpose projects which are traditionally financed in this manner are: (a) housing construction and rehabilitation; (b) educational facilities; (c) airports, harbors, highways and other transportation facilities; (d) power generation, transmission and distribution; (e) public recreational facilities; (f) pollution control and solid waste disposal and resource recovery facilities; (h) hospitals and health care facilities; (i) industrial development; (j) water and sewer facilities.

Tax exempt bonds are of two basic kinds: (1) tax supported and (2) user-pay. The first is used to provide non-revenue producing public services which are supported by the general taxing power of local government and the second are revenue producing projects that can be self supporting from income derived from charges to those who use the facilities. Briefly the bond purchaser, or lenders of money, look to the prospects of repayment of their loaned funds plus a fee, or interest rate, for the use of their money and the calculated risk they assume in making the loan, i.e., buying the bonds. The less the risk the lower interest rate they are willing to accept.

The principal role the Permanent Fund can play is in assisting the State of Alaska in providing services for its citizens as well as stimulating economic expansion and diversification and developing natural resources. Once the needs of the State have been studied and defined and political priorities have been established, the assets of the Permanent Fund can be used in a great variety of ways and combination of ways within the structure of the tax exempt market to maximize its effectiveness and impact on solving the needs of Alaska and achieving its economic goals.

Briefly stated, some of the opportunities are: 1) direct guarantee of debt, 2) make-up of revenue short-fall, 3) loans to projects or political subdivisions, 4) combination financing with public utilities or private industry, 5) industrial development financing, 6) pledge of specific assets and/or income of the Fund for certain projects and 7) others. We envision our role in the future as working with others on the task force to accomplish the defined goals by exploring and adopting traditional techniques and devising possible innovative combinations or new techniques which will maximize the effectiveness of the Permanent Fund.

(II) Summarization of Our Review to Date of Similar Funds in Other States and Countries

Alberta Heritage Savings Trust Fund

This fund appears to be the most closely related, of any so far investigated, to what we understand to be the purpose, goals and source of capital of the Alaska Permanent Fund.

The purpose of the Trust Fund is stated to be the setting aside of certain revenues accruing to the Provincial Government from the sale of non-renewable natural resources in a separate trust fund rather than in the General Revenues of the Government. Such trust funds are not to be utilized for normal operating and capital budgetary requirements, but are to be set aside for investment to assure that future generations of Albertans may have a better opportunity to sustain the same level of prosperity and benefits being enjoyed by present citizens.

The goals and objectives of the Trust Fund include the utilization of funds in investments which will help to create more and better jobs through a more diversified economy, less reliant on the sale of depleting resources. Further goals are to improve and sustain the quality of life within Alberta in the future and to earn interest and dividends to strive to maintain low personal taxation.

Further guidelines for the Trust Fund are that its resources should be invested with a minimum of interference with private sector activity and any investments should not unduly disrupt existing financial institutions. In addition it is planned that most investments will be made within Alberta and only normal commercial or money market investments will be committed outside the Province.

Legislation creating the Trust Fund was enacted May 19, 1976 and there is presently being transferred total assets of \$1,500,000,000 from the General Revenue Fund of the Province to the Heritage Saving Trust Fund. This sum is composed of previously accrued royalty payments through the end of the 1975-76 fiscal year. No investments have as yet been made by the Trust Fund. The Trust Fund is administered by an investment committee made up of all members of the Executive Council of the Province. The Executive Council consists of the cabinet level appointees of the Governor.

Thirty percent of non-renewable resource revenue received in each fiscal year is to be transferred from the General Revenue Fund to the Trust Fund but only if the transfer is authorized by a Special Act enacted by the legislature in the preceding fiscal year.

The assets of the Trust Fund shall be used for the following purposes:

- a) Investments in projects which will provide long-term economic or social benefits to the people of Alberta but which will not, by their nature, yield a return to the Trust Fund.
- b) Investments by way of loans to:
 - (i) The Canadian Government
 - (ii) Any other Province of Canada
 - (iii) Any other person, if the repayment of the loan and the payment of the interest thereon is guaranteed by the Canadian Government or any Provincial Government of Canada.
- c) Investments which, in the opinion of the Investment Committee or in the opinion of the Legislative Assembly as expressed in a resolution of the Assembly:
 - (i) will yield a reasonable return or profit to the Trust Fund, and
 - (ii) will tend to strengthen and diversify the economy of Alberta.

Investments referred to in subsection (a) shall only be made if moneys are first appropriated from the Trust Fund by an Act of the Legislature specifically for a purpose described in subsection (a) and these investments shall not exceed 20 percent of the assets of the Trust Fund.

Investments referred to in subsection (b) shall be made or approved by the Investment Committee in accordance with directions contained in any resolution of the Legislative Assembly and these investments shall not exceed 15 percent of the assets of the Trust Fund.

Investments referred to in subsection (c) shall be made or approved by the Investment Committee in accordance with directions contained in any resolution of the Legislative Assembly.

The Legislature retains control of the Trust Fund in several ways as can be seen in the above listed criteria and restrictions. All funds are held and administered by the Provincial Treasurer. The Provincial Auditor is required to audit the Trust Fund at least once each year.

Government Development Bank for Puerto Rico

We have not as yet reviewed the operation and structure of the Government Development Bank for Puerto Rico (GDB) in as much depth as the Alberta Heritage Savings Trust Fund because it did not appear to us that there would be sufficient similarity to the operation and structure of the Alaska Permanent Fund. The only source of capital available to GDB is borrowing in the public or private money market.

GDB is an instrumentality and public corporation of the Commonwealth of Puerto Rico. It was created in 1948. The GDB charter provides for its perpetual existence and no amendment to this Charter or any law of the Commonwealth shall impair any outstanding obligations or commitments of GDB. The Development Bank was created as an industrial development bank. The governing body is a 7-member Board of Directors who serve 4-year overlapping terms. The Board is appointed by the Governor with approval of the Council of Secretaries (equivalent to the Cabinet of the Executive Branch). GDB is exempt from budgetary controls of the Executive Branch of the Commonwealth and from provisions of Puerto Rico Banking Law. GDB is, however, subject to supervision and examination by the Commonwealth's Secretary of the Treasury.

GDB serves primarily as fiscal agent for the Commonwealth and its various public agencies. As fiscal agent, GDB is responsible for the timing and sale of bonds and notes by the Commonwealth and its agencies. There is no limit to the amount of debt that can be issued by GDB which is not guaranteed by the Commonwealth. Debt which does carry this guarantee is limited to \$450 million. The limit was raised from \$300 million in May, 1976.

From its inception through the 1975-76 fiscal year, GDB had arranged or provided for nearly \$11 billion of borrowing by various governmental units. GDB also arranges or provides loans for the private sector. As of 6/30/75 GDB has reportedly disbursed over \$337 million in such loans (approximately 47% for manufacturing, 22% for commercial buildings, and 6% for hotels). As of 6/30/76 there were \$165.4 million business loans outstanding (45% industrial, 14% commercial buildings, 3.6% hotels). The Bank also issues its

own full faith and credit notes. As of 6/30/75, these amounted to \$40 million issued to major mainland and Puerto Rican Banks. On 9/11/75 GDB negotiated a \$612 million note purchase agreement (guaranteed by the Commonwealth) with major mainland and Commonwealth Banks to provide a revolving line of credit for the Commonwealth and its public agencies.

In June, 1974 a subsidiary of GDB, Government Investment Company of Puerto Rico was formed to provide venture capital for economic development. The total amount of such capital provided to date is \$2,600,000

Pennsylvania Industrial Development Authority

The Authority was created in 1956 for the purpose of making loans through local industrial development agencies for industrial development in areas of high unemployment. Such areas are determined solely by the Authority. Historically, the Authority's primary source of funds for these loans were appropriations from the State of Pennsylvania General Fund and income received from payments on outstanding loans. In 1973 the Authority was authorized to issue tax exempt revenue bonds (primarily secured by earnings of its loan portfolio) to finance its loan programs. To date the Authority has sold two bond issues totaling \$70 million. From 1956 through 1975 some \$350 million of industrial loans have been made by the Authority for some 1300 different projects which had a total estimated development cost of over \$987 million and have reportedly provided some 166,000 new jobs within the state. The primary ingredient for success of this program is that the rate of interest charged by the Authority on these loans has been significantly below prevailing commercial loan rates.

Perhaps a portion of the proposed Alaska Permanent Fund could be designated to initiate a similar program. Properly administered, such a program could become self-supporting and require no additional capital outlays from the Permanent Fund.

University of Texas, Permanent University Fund

The Permanent University Fund of Texas came into existence in the nineteenth century by certain acts of the Republic of Texas and later was re-organized and perpetuated by constitutional provisions by the State of Texas. Its assets are now 2,100,000 acres of land in several western counties in the State. Practically all of the acreage is under grazing leases which create income in excess of

\$1 million per year. In addition, the proceeds from sale of leases for oil and gas exploration and extraction become part of the Fund. State Supreme Court decisions and opinions of the Attorney General of the State decree that the Permanent University Fund shall be kept forever intact. The assets of the fund may be invested in certain securities, the earned income of which may be used to secure loans for capital construction of University facilities.

Permanent University Fund tax exempt bonds are secured by covenants which require (1) that assets of the Fund equal in amount to bonds outstanding will be invested in direct U.S. Government Obligations, (2) that the income from said U.S. Obligations equal at least the maximum annual interest payments of the bonds, and (3) that the entire income of invested funds equal at least 1½ times the maximum debt service requirements on all outstanding bonds. In addition, total bonds may be issued only in amounts not to exceed 20 percent of the total assets of the Fund. Income is defined as net proceeds after Fund management expenses which may never exceed 1/5 of 1% of the value of the Fund.

We have initiated research on several economic development funds that exist throughout the world and will report on them at a later date. We refer to such areas as the World Bank, foreign aid activities of the U.S. State Department, Saudi Arabia, etc.

We have also contacted appropriate officials in the Province of British Columbia to investigate any such development funds they may have created. We were informed that no such funds have been created or are presently contemplated. The Provincial Government has been subsidizing some public and private ventures from general fund revenues. These have been mainly railroads, ferrys and high-ways.

This summary of White, Weld's efforts to date in reviewing existing funds and development authorities which may be of interest to the Alaska State Investment Advisory Committee with regard to the creation of the Alaska Permanent Fund is not intended to be a complete and final analysis of all possible areas of interest. It is presented to inform the Committee of our progress to date and to stimulate comment and discussion. We would expect to proceed with further investigations into other possible areas of interest and to investigate in more depth some of the areas already discussed.

We look forward to working closely with the Committee on this important and interesting assignment in whatever capacities we agree would be mutually beneficial.

Sincerely,

KR Butler

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This memorandum is a summary of significant concepts brought out during a meeting requested by White, Weld & Co. with Moody's Investors Services held on Monday, August 23, 1976, at White, Weld & Co. offices in New York.

The purpose of the meeting was to discuss the proposed creation of an Alaska Permanent Fund and the impact of creating such a fund on the rating agencies perceptions of Alaska.

In attendance from Moody's were Claire Cohen, Vice President and permanent member of the rating committee and Bill Bunce, oil company analyst.

Summary of Concepts Discussed:

- (1) Permanent Fund vs. Development Fund. Is the name properly descriptive? The investment community has prior definitions of these terms.
- (2) Financing of General Fund deficits from non-renewable resource revenues is of strong concern to them.
- (3) Alaska has large capital needs. Formation of Development Fund to coordinate and direct the raising of this capital looked on as positive step.
- (4) Heavy demands and pressure for immediate assistance from Permanent Fund almost a certainty. Assigning priorities and criteria will be difficult but crucial as far as Moody's is concerned.
- (5) Cannot comment specifically on effect of Permanent Fund on ratings, borrowing capacity, etc. until more details of structure and operation are known.
- (6) Would like to work closely and be kept informed in timely manner concerning developments.

Kenneth R. Butler
August 23, 1976

Alaska State Legislature

file

SPECIAL COMMITTEE ON
THE ALASKA PERMANENT FUND
(907) 276-3433
528 W. 5TH, SUITE 270
ANCHORAGE, AK. 99501
[POUCH V, JUNEAU, AK. 99811]
(907) 465-3873



MEMBERS
REP. CLARK GRUENING, CHMN.
REP. TERRY GARDINER, V. CHMN.
REP. E. J. HAUGEN
REP. RUSS MEEKINS
REP. BILL MILES
REP. LEO SCHAEFFER
REP. RICK URION

House of Representatives

May 3, 1978

Mr. Ted Swick
Senior Vice-President
White, Weld & Co.
One Liberty Plaza
91 Liberty Street
New York, New York 10006

Dear Ted:

Good to see you and Sam again last week. In line with our conversation of April 28, would you please supply our Committee with a memorandum covering the questions we discussed concerning SB 429. Hopefully, you can send us your comments as soon as possible on the following topics:

- 1) The legality and/or workability of the arbitrage mechanism envisioned in SB 429, i.e. the one percent "service fee for administrative costs" over the cost of borrowing to the Alaska Loan Program.
- 2) The legality of the use of tax-exempt borrowing under present statutory and Treasury restrictions for the purposes of the Alaska Loan Program in SB 429.
- 3) The likely reaction of bond market investors to packages of tax exempt bonds which aggregate mixed purpose issues as envisioned in the Alaska Loan Program. (Sec.45.96.030 of SB 429).
- 4) The likely impact on the credit rating of the State of Alaska of aggregating the various existing public purpose issuing agencies into one blanket issuer, the Alaska Loan Program.

Mr. Ted Swick

-2-

May 3, 1978

5) The relative strengths or weaknesses of CSHB 596 (Finance) and SB 429 in insuring the safety of the Permanent Fund principal.

6) Any other matters in your area of expertise relating to the two bills which you would like to bring to the attention of the Committee.

At the moment I am unable to say when hearings of the free conference committee on the Permanent Fund will begin but testimony on these issues may be required sometime during the week of May 15, 1978. I would like to arrange a conference call with you for sometime between May 11 and May 15 to discuss your response to these issues. Any expenses you incur in responding to this inquiry will be approved from the Committee's funds.

Cordially,

Representative Clark Gruening

CG:jl

A BILL

For an act entitled: An Act providing for guarantees payable from certain income derived from the Alaska Permanent Fund of indebtedness issued by governmental agencies of the State for power projects.

Section 1. Subject to the approval by the legislature as provided in Section 4 hereof, the board of trustees of the Alaska Permanent Fund is hereby authorized to enter into agreements with any public authority of this State or any borough or other governmental agencies of this State, providing for a guarantee, payable solely from the income derived from the Alaska Permanent Fund established by AS (other than income derived from the Alaska Enterprise Development Fund established by AS) of the payment when due, whether at maturity or by sinking fund redemption but not by acceleration of maturity, of the principal of and interest on bonds, notes or other indebtedness of such governmental agencies issued to finance a project or projects for construction of electric generating and related transmission facilities. Such agreements shall contain such terms, provisions and covenants in furtherance of the purposes of this act as said board of trustees shall determine.

Section 2. No bonds, notes or other indebtedness shall be guaranteed pursuant to this act unless said board of trustees shall determine that the debt service for any year with respect to all such bonds, notes and other indebtedness will not exceed the amount of annual income estimated by such board of trustees to be derived during such year from said Alaska Permanent Fund (other than income from said Alaska Enterprise Development Fund). Such determination shall be made by resolution of said board of trustees prior to the execution of any guarantee agreement pursuant to this act.

Section 3. Any bonds, notes or other indebtedness guaranteed pursuant to the act shall have on the face thereof an endorsement of such guarantee by the chairman of said board of trustees or any designee of such officer.

Section 4. No bonds, notes or other indebtedness shall be guaranteed by said board of trustees pursuant to the act until the facilities to be financed with the proceeds of such bonds, notes or other indebtedness have been approved by a joint resolution of the legislature.

Section 5. If any term or provision of this act shall be declared unconstitutional or ineffective in whole or in part by a court of competent jurisdiction, then to the extent that it is not unconstitutional or ineffective such term or provision shall be enforced and effectuated, nor shall such determination be deemed to invalidate the remaining terms or provisions hereof.

Section 6. This act shall take effect immediately.

49

Alaska State Legislature

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WHITE, WELD & CO.
INCORPORATED

ONE LIBERTY PLAZA
11 LIBERTY STREET, NEW YORK, N. Y. 10006

CHARLES J. FUHRMANN II
FIRST VICE PRESIDENT
212 / 285-2388

CABLE ADDRESS: "WHITEWELD"

October 1, 1976

Alaska State Investment Advisory Committee
State of Alaska

Dear Committee Member:

In accordance with your request, we have undertaken a survey of domestic, foreign and international development banks, funds and development programs for your use in determining the future structure and objectives of the Alaska Permanent Fund. In performing our survey, we have selected those banks, funds or development programs which are of major importance, as well as those which are particularly relevant to Alaska's situation in that they are either based upon natural resource revenues or confined to a limited geographic area.

Our analysis of domestic permanent funds focused on those states which received income from a finite natural resource and the manner in which that income was expended. The majority of states receiving income from finite natural resources spend that income on a current basis. Those states and the application of income are set forth in tabulation form. States which accumulate natural resource income in a trust fund are set forth individually.

Each state has created programs to assist and encourage economic developments. A description of the Government Development Bank of Puerto Rico and the Pennsylvania Industrial Development Authority has been included in this study. A summary of state general assistance, incentives and special services to industry has also been included. In depth information on each particular economic development program has been requested from each state's development agency and will be sent along, as received, to Mr. Edenso for inclusion in the source file of all background information we are putting together for the Committee.

Substantially all of the less developed nations of the world, and a certain number of the more developed nations, have government owned or controlled entities whose purpose is to participate in the financing of local economic development projects. In most of the small nations, these entities

Alaska State Development
Advisory Committee

October 1, 1976

function principally as the vehicle through which development funds are dispersed to the economy by the government and are consequently heavily involved in the internal political process. In many cases, these entities also act as the conduit through which development funds provided by the larger international development banks and funds are invested in smaller projects in the country concerned. One of the advantages of the latter process is that the use of the local bank as a vehicle permits the larger institution's loan to receive a government guarantee, which is commonly a prerequisite for the extension, or the initial extension, of credit to the country. In most countries, the development banks and funds that perform the above functions also serve as the means through which internal economic growth is directed and channeled in accordance with national economic policies and are, in effect, extensions of the local economic ministry.

The institutions covered by our survey which fall into this category are the Swedish Investment Bank, Japan Development Bank and National Financiera S. A. (Mexico). All of these entities are government owned institutions which both borrow funds in various capital markets and lend domestically for development purposes. In each case, the institutions are responsible for carrying out national economic policy through their activities and enjoy various degrees of autonomy from the national political process. The most independent is the Swedish Investment Bank and the least is National Financiera S. A. Both National Financiera and Japan Development Bank appear to be heavily involved in the political process in their respective countries, and the former has acted as a conduit for World Bank lending in Mexico.

The larger development banks and funds are international institutions whose memberships consist of several countries and whose purpose is to foster the economic growth and development of a particular region or its members. In general, these entities represent potent world-scale economic forces and tend to be both non-political and commercial in their operations. The financial strength of these entities is typically based on the uncalled capital subscriptions of their members, and virtually all of them borrow heavily, both locally and in the international capital markets. Substantially all of the activities of these institutions consist of direct lending for specific projects in the various countries, and lending policies appear to be determined on social benefit as well as economic grounds. As a result, and to the extent that many major industrial nations are commonly among the larger contributing members of these institutions and receive no benefits, they can be viewed as quasi "foreign aid" banks.

Among such international and regional development institutions covered by our survey, the most significant is the International Bank for Reconstruction and Development (World Bank), both in terms of its worldwide membership and the international scope and significance of its lending activities. Importantly, all of the other international institutions included in our review (Inter-American Development Bank, Asian Development Bank and African Development Bank)

Alaska State Development
Advisory Committee

October 1, 1976

have been created with the assistance of, or modeled after, the World Bank, both operationally and in financial structure. Of these three derivative institutions, only the African Development Bank is not a significant international borrower and depends heavily on loans from other institutions, such as the World Bank. This characteristic results from the fact that its uncalled capital funds are to be provided by countries that are not viewed as being particularly strong by the world capital markets and that a significant private capital market in black Africa does not exist. Two other institutions which fall somewhat into this category in that their activities are regionalized are the European Investment Bank and the European Coal and Steel Community, both of which are related to the European Economic Community (Common Market). Significantly, while both borrow in various capital markets and re-lend for projects consistent with their purpose, the credit strength of the European Coal and Steel Community is based fundamentally on the strength of the private steel industry in Europe. European Investment Bank is modeled along the lines of the World Bank and depends on the credit of the various EEC member states.

The remaining type of institution is one which functions in a limited geographic area or within a particular industry to promote economic growth and development or to achieve a social objective and is based on local or regional resources. Of the three basic groups of international development institutions, this group contains the smallest number of entities and is, perhaps, the most analogous to the situation in Alaska. These development institutions or funds are new and, to a large degree, based on natural resource revenue. Significantly, only two are international in scope; others are modeled after the World Bank but limited in their activities to a defined geographic region, ethnic grouping or social purpose. The remainder are "national" investment funds. The majority of these funds are based in the Middle East and dependent upon oil related revenues. Those that have an international scope are the Saudi Development Fund and the Arab Bank for Economic Development in Africa, both of which were created after the increase in world oil prices in recognition of the balance of payments and development problems created in the developing states by such increase. The remaining funds (Arab Fund for Economic and Social Development, Abu Dhabi Fund for Arab Economic Development, the Islamic Development Bank and the Kuwait Fund for Arab Economic Development), although created at approximately the same time, reflect in both the source of their capital (member states' subscriptions or allocation of national revenues) and their purposes the Arab nationalism which emerged after the Mid-East wars. Importantly, most of these funds have yet to become fully operational, and it is too early to judge their potential significance. The two "national" investment funds, the two which you may find are the most directly related to the proposed Alaska Permanent Fund, are the Fondo de Inversiones de Venezuela and the Alberta Heritage Savings Trust Fund. The similarities extend to both source and purpose, as can be seen in the studies included herewith.

Alaska State Development
Advisory Committee

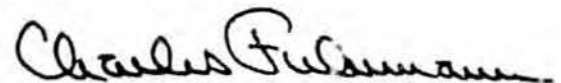
October 1, 1976

It is premature to recommend to the Committee certain key features of any one of these banks, funds or development programs over the others until it has had a chance to digest the information in our survey and to review the source file we are also providing. We are available to detail the differences as we see them and to discuss other alternatives available to Alaska.

Following the Committee's meeting on October 13, which we will be attending, we will want to sponsor visits by Committee members at least to Alberta to meet with their Heritage Savings Trust Fund counterparts. Visits to New Mexico and to New York would also appear advisable.

We look forward to our next meeting in Anchorage.

Sincerely yours,



Charles J. Fuhrmann II
First Vice President

CJF:yu
Attachment

TABLE OF CONTENTS

- I Domestic Permanent Funds
 - Montana Resource Indemnity Fund
 - New Mexico State Permanent Fund
 - New Mexico Severance Tax Bonding Fund
 - New Mexico Severance Tax Permanent Fund
 - New Mexico Severance Tax Income Fund
 - Texas Permanent University Fund
 - Wyoming University Permanent Land Fund
 - Wyoming Permanent Mineral Trust Fund
 - Wyoming Government Royalties Fund
 - Summary of Certain Other States

- II Domestic Economic Development Programs
 - The Government Development Bank of Puerto Rico
 - The Pennsylvania Industrial Development Authority
 - Summary of States' General Assistance, Incentives and Special Service to Industry

- III National Institutions
 - Swedish Investment Bank Ltd.
 - Japan Development Bank
 - National Financiera S.A.

- IV International and Regional Development Institutions
 - International Bank for Reconstruction and Development (World Bank)
 - Inter-American Development Bank
 - Asian Development Bank
 - African Development Bank
 - European Investment Bank
 - European Coal and Steel Community

- V Natural Resource Related Institutions
 - Saudi Development Fund
 - Arab Bank for Economic Development in Africa
 - Arab Fund for Economic and Social Development
 - Abu Dhabi Fund for Arab Economic Development
 - Islamic Development Bank
 - Kuwait Fund for Arab Economic Development
 - Fondo de Inversiones de Venezuela
 - Alberta Heritage Savings Trust Fund

Exhibit I