

SPEAKING FRANKLY

SPEAKING FRANKLY

---

By  
Edison H. Cramer, Chief,  
Division of Research and Statistics,  
Federal Deposit Insurance Corporation.

Georgia Bankers Association  
Savannah, Georgia  
April 19-20,  
1950

## SPEAKING FRANKLY

May 1, 1950  
Revision for proceedings

Some of you may recognize in the title of my address a steal from the title of a book written by an eminent son of your neighboring state of South Carolina. "Speaking Frankly" is the way friends speak to each other. It is the method by which they cement and consecrate their friendship. When a friend prefaces his remarks with the statement that he is going to speak frankly, he is ordinarily expected to say something that might give offense, something that he doesn't like to say but nevertheless regards as for his friends' good. So if I say anything of that character you will understand that it is as a friend among friends.

With all the attention given to such national issues as monetary and fiscal policies, bank holding company legislation, revision of the FDIC law, and reorganization of bank supervisory agencies, banking developments of a local character tend to be neglected. But that does not mean that they are unimportant. They are the raw material which prescribe the nature and the limits of the broader issues. Today I want to talk with you about certain features of the banking scene in Georgia, features whose details you know more intimately than I do. If we can look at these features from the viewpoint of how they compare with the banking situation in other states, we shall have a better idea of where we stand and where we are going.

Like everyone else, we in the Federal Deposit Insurance Corporation are frequently confronted with unhappy alternatives. We're damned if we do, and we're damned if we don't. A most typical example of this occurs in connection with applications for deposit insurance. These

applications are of two kinds - the proposed new bank which desires to open for business with deposit insurance protection, and the operating noninsured bank which desires to accord its depositors the benefits of deposit insurance. While these two situations differ slightly, the factors prescribed by law which our Board of Directors is required to take into consideration are identical in both instances. They are: the financial history and condition of the bank, the adequacy of its capital structure, its future earnings prospects, the general character of its management, the convenience and needs of the community, and the consistency of its corporate powers with the purpose of deposit insurance.

The intent of this provision of the law was to prevent the needless establishment of uneconomic banking units - which was partially to blame for the banking collapse of 1933 - but at the same time to safeguard communities against monopolistic practices and thereby preserve the spirit of healthful competition in our banking system. The frequent presumption that a bank is eligible for deposit insurance, simply because it has met the statutory chartering requirements of the state, often places the Corporation in an unenviable position. On the one hand we are liable to be charged with obstructionist tactics designed to protect a banking monopoly in a certain community and, on the other hand, we are constantly faced with the necessity of being able at all times to give satisfactory evidence that we have not contributed to excessive chartering of banks.

To meet this situation our Board has set up a well defined procedure. It begins with an "on the spot" examination and investigation by a well-seasoned field examiner. The proposal is then carefully screened by our district office. Upon receipt of the field examiner's detailed report, accompanied by the Supervising Examiner's recommendation, which may include information he has been able to develop independently, the proposal is then screened by our Division of Examination, which makes its recommendation to the Board of Review. The Board of Review is comprised of one of our Directors and his Assistant, the deputy to the Chairman, and the chiefs of the Divisions charged with the primary responsibility of carrying on the day to day administrative functions of the Corporation. After careful consideration, the Board of Review submits its recommendation to the Board of Directors for final decision.

From what I have just said, you may gather the idea that we operate under a complicated system of Government red tape. I would like to try to assure you that this is not true. All of the members of the Board of Review started out with their bare feet on the soil. Almost every member of this committee has had more or less extensive banking experience. Without mentioning names, I would like to say that the present committee consists of a country boy and small town banker from Ohio, a Nebraska farm boy, a short shoreman from the east shore of Maryland, a North Dakotan, a Tennessean, an Arkansan, and a farmer and banker from Colorado.

The factors relevant to determining the adequacy of banking facilities in a given area have endless ramifications. And the things

to be considered in approving or disapproving an application for a bank charter extend beyond certain statutory requirements. It has been necessary for our Board to implement our own statutory requirements by formalizing standards intended to carry out the legislative intent of the Congress. Since these standards have been reflected to some extent in actions actually taken with respect to certain applications from Georgia you may be interested to know something about these Georgia situations.

During the last five years, 1945 to 1949, the Corporation has granted insurance to some 50 Georgia banks. About half of these were banks, or successors to banks, which had been in operation for some time. The other half were newly organized institutions; by that I mean entirely new banks which provide new or additional banking facilities in their particular community. It is with these 26 new nonmember banks, where the problems encountered in obtaining deposit insurance are intensified, that we are presently concerned.

About two-thirds of the new banks were opened in communities whose economic life rested upon agriculture. Cotton was the main farm crop in these areas, and lumbering was a leading activity in several of them; the increasing attention to peanuts, livestock and corn also was in evidence in some areas, and in others tobacco was an important cash crop. Of the other one-third of the banks, 7 were located in industrial areas and 2 in residential areas. The industrial areas were mostly centered around the larger cities, with textile and clothing manufacture, auto assembly, railroad shops, and canneries comprising the main activities.

Most of these new banks, as might be expected, were relatively small. Only six of them had initial capital and surplus in excess of \$100,000, and none of the others started with capital funds sufficient to warrant a million dollars in deposits. Nine of the banks had capital and surplus of less than \$50,000 at the time they opened their doors.

Over one-half of the new banks were located in centers of between 2,000 and 10,000 population. Only two of the banks were in cities of over 10,000 while 10 of the banks were in towns of less than 1,000 population. It was in the latter communities that convenience of the local residents played such an important part in obtaining a new bank. In the larger cities the growth of the area and the attendant ability to support another bank were major factors. There were elements of local dissatisfaction with the services of the existing bank fostering the establishment of six of the new banks. In at least two cases the opportunity to realize high earnings appeared to be the over-riding purpose of the proponents of the new bank.

The importance attached to providing local banking facilities is indicated by the fact that half of the new banks were located in towns that lacked banking facilities at the time. Only two of these communities, however - both growing suburbs of cities - had never had a local bank; and seven of them, at one time or another in the past, had had two or more banks. Thus it is evident that most of the recent increase in the number of banks is simply a replacement of banks that had gone out of existence; many of the communities obtaining new banks had been without local banking facilities for 15 to 20 years.

What we have accomplished in granting insurance to these 26 new banks has not, of course, gotten us off the hook. There are doubtless some people who think we have been too generous in approving applications for insurance; and there are certainly others who think we have been too severe. These differences of opinion come in the main from the differences in the statutes and the standards under which banks are chartered and insured. These disagreements are bound to arise, and our dilemma is certain to continue, as long as there are differences in banking standards among the chartering and insuring agencies.

A special committee of your national association has done a monumental work in the field of promoting uniform standards. One of the members of your own Georgia Association, Mr. R. E. Gornley of the Georgia Savings Bank, was a member of the Special ABA Committee on Model State Banking Code. The proposed state banking code drafted by this Committee has aroused wide interest and stimulated the legislatures and banking authorities in various states to consider anew their banking statutes. We have made certain minor criticisms of the proposed model code. In most part these have been intended, however, to clarify rather than qualify the code. We believe the model code to be a landmark in the effort to promote more uniform and higher standards of banking. And without presuming to advise on how it may be adapted to your own situation in Georgia, we commend it to your earnest attention.

The model code offers no guidance, however, on one of the basic problems of banking in your state. It refers only to banks duly chartered by state authorities. Thus it omits from its scope all reference to that unique Georgia institution - the private bank. I say "unique" not because



Georgia is the only state to have private banks, for there are some in other states. However, Georgia is unique in that it is the only state which now permits the establishment of private banks; furthermore, almost half of all private banks in the country are located in Georgia.

During the last ten years the number of private banks in Georgia has ranged between 50 and 60. Considerable change has occurred, of course, in the identity of these banks, as new ones open up and some in operation go out of existence. The picture did not change much during the war. But in the last five years, 1945 to 1949, 28 new private banks opened their doors for business in your state. This number was exactly offset by discontinuances of private banks, in one way or another, during the same period. During the period 19 private banks - some new and some old - took out a state charter to do a regular commercial banking business; six went into voluntary liquidation; and three failed. If one simply compares the figures of the number of private banks in operation in Georgia now and at the end of the war, he gets an impression of no change. Actually, however, beneath this surface stability, there has been an almost constant stir, much of it of a disturbing character.

During the last few years the Corporation has become involved to a considerable degree in the kaleidoscopic private bank picture. A well-defined pattern of evolution from private bank to insured bank has developed. The first step in the process, the opening of a private bank, requires little more than individual initiative. One can open a private bank in Georgia as easy as he can open a grocery store. In

fact, it's probably easier, for there are no outlays for inventory, and other costs are similarly low. Sooner or later the private bank may decide to apply for a state charter to do a regular commercial banking business. If the state bank commissioner rules against granting a charter, the bank may then appeal to the Court of the County in which the bank is to be located and may secure a mandamus requiring the commissioner to grant the charter. At this point, or anytime after it receives its state charter, it may apply for deposit insurance. That is where we come into the picture.

We in the Corporation are, of course, happy to facilitate the evolution of a private bank into an insured bank, provided it can meet our standards. Right there, however, lies a major difficulty. The possession of a state charter, as I have said before, does not always provide assurance that the bank is able to meet the factors prescribed by the FDIC law. Can we, for example, justify insuring a new bank on the ground that it is necessary for the convenience and needs of the community when there is one or more banks already serving a small rural community?

We must face the fact that the private bank is a 19th Century institution in a 20th Century economy. As holders and creators of part of the money supply they perform a distinctly public function. There is no reason why they should not be required to submit to the public supervision exercised over other segments of the banking system. You in the Georgia Bankers' Association have been alert to this situation, as evidenced by the Commission which you set up last summer, headed by

John R. Hines. True to the GBA tradition of cooperation, I understand you have made good progress in your talks with representatives of the Private Bankers' Association of Georgia.

The effort to secure prohibition of the opening of new private banks would, if successful, eliminate the most risky aspects of the situation. You do not need to be told that many private banks, here as elsewhere, have a long and honorable history, and are capably managed by men of high esteem. Particularly in communities lacking other banking facilities they have performed a real service. We need not be fearful of these banks; nor need they be fearful of public supervision, if and when it comes. It is to prevent the abuses of unrestricted establishment of new private banks that remedial legislation should especially be directed.

Abuse of the banking privilege can easily lead to trouble. In confirmation of this, one small statistic speaks louder than a volume of argument. During the past year there were four bank failures, all of noninsured banks, in the whole United States; two of these, both of private banks, were in Georgia. The impact of these failures is much greater than its injury to the depositors who suffered. A bank failure communicates its perverse effects to other parts of the banking system, eroding the confidence so fundamental to the maintenance of a sound banking system.

Now I know that the significance of bank failures is a somewhat controverted matter. There are a few people who look upon failure as a

normal and desirable method of ridding the banking system of unhealthy banks, a way of purging the system of its weak sisters.

We in the Corporation have a somewhat different view of the matter. We recognize that failures cannot always be avoided, and that conditions in individual banks may reach such a state that the filing of bankruptcy papers is the only feasible course. We are not happy, however, to see a bank fail. We do not expect sufficient compensating benefits in its cathartic effects upon the banking system as a whole. Our whole philosophy is one of prevention rather than of cure.

In ordinary businesses where entry is easy it is reasonable to expect a high rate of failure. But banking is not an ordinary business. It is so clothed with functions of a public character that no one questions its amenability to public regulation. The grant of authority to Banking Departments or supervisory agencies demands results in keeping with this public responsibility. The particular result demanded of the FDIC is the maximum protection of depositors, within the statutory limitations. To that end we have used our examining powers in the best manner we know how; we have been careful in admitting new banks to insurance; and we have stood ready to aid mergers of banks that get into difficulties. As a result of these practices, and of good business conditions, no insured bank has gone into receivership and no depositor in an insured bank has suffered a loss in the last six years. This record of solvency and stability is without parallel in the nation's history, and we in the Corporation are very proud of it. With your continued cooperation and the cooperation of the other supervisory agencies, State and National, this record will, we trust, be extended.

What has happened to banking in Georgia since the war reflects one phase of the rapid economic growth that is still going on in your state. The dawn of a new day in the economic life of the South is no longer mere platitude. It is a reality, taking the form of new agricultural crops and methods, new industries, and an awakened public spirit that not only invites but incites new ideas. Georgia has been in the forefront of these exciting developments.

The growth in the number of banks in the state has resulted in part from the economic stimulus of new opportunities for service and profit. The increase in bank deposits is not merely a manifestation of inflationary forces; it reflects the real growth of the economy. The average account in Georgia banks has doubled since 1941; and the number of accounts has increased by nearly one third. The wartime and early postwar growth in banking aggregates has stabilized at a high level. Private deposits in insured commercial banks in Georgia fell a nominal 3 percent during 1949, but still were over 3 times greater than 10 years ago. Last year loans in Georgia banks increased 5 percent, a greater rate of increase than experienced by the country as a whole. When the figures now being assembled by the Census takers are finally tabulated Georgians shall doubtless have further and varied confirmation of their economic growth and strength.

You bankers, accustomed to giving credit, can take a good bit of credit for these developments. You are one of the many vital links in the chain of business and industrial progress, providing a spark of civic leadership in addition to your regular financing activities. Your

name has acquired a distinctive meaning in the common phrase "someone you can bank on", and I am sure you will continue to justify that compliment.