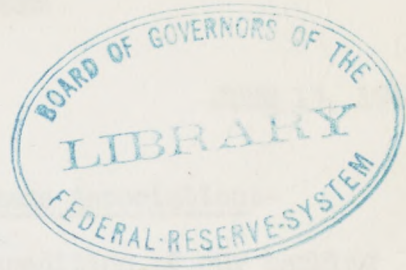




FEDERAL DEPOSIT INSURANCE CORPORATION
WASHINGTON



FOR RELEASE AFTER 12:00 NOON E.S.T., FRIDAY, JUNE 13, 1941

EXCERPTS FROM THE ADDRESS OF
HONORABLE LEO T. CROWLEY
CHAIRMAN, FEDERAL DEPOSIT INSURANCE CORPORATION
BEFORE THE
WEST VIRGINIA BANKERS ASSOCIATION

WHITE SULPHUR SPRINGS, W. VA.

JUNE 13, 1941

ADDRESS OF HONORABLE LEO T. CROWLEY, CHAIRMAN,
FEDERAL DEPOSIT INSURANCE CORPORATION, BEFORE
THE ANNUAL CONVENTION OF THE WEST VIRGINIA BANKERS
ASSOCIATION

WHITE SULPHUR SPRINGS, WEST VIRGINIA

JUNE 13, 1941

Mr. Chairman, members of the West Virginia Bankers Association:-

I should like today to appraise the condition of our banking system as we prepare to throw its full resources behind the defense efforts and the program of aid to the democracies that now occupy our attention. I should like also to suggest a few considerations that should govern our decisions during the months to come. Finally, I shall look briefly at the prospects for successful readjustment of the banking business at the conclusion of the present period of extraordinary activity.

Banking System in Good Condition

In my judgment, the banking system is in excellent condition to undertake successfully the task that lies before it. The breathing spell of the last seven or eight years, though it had some real disadvantages and worked some irksome hardships, at least gave us time to gird up our loins, clean out our banks, and gather strength for the task that lies ahead.

Structurally, the banking system is on an eminently sound footing. We find the national system and the State systems working harmoniously together, their independence preserved despite the threat of unification that came with the 1933 banking holiday. We see a system greatly invigorated by the severe pruning of its weaker units during past years through failures, mergers, and voluntary liquidations - its individual units given new life and rehabilitated through the injection of new capital funds and in many cases by FDIC financial aid, so that their millstones of worthless assets could be thrown off, and their depositors be given again real protection

in the form of valuable assets and reasonable capital accounts.

From the structural point of view we can say today of the country as a whole that it has few banks whose immediate futures are in jeopardy or whose place in the system seems unjustified, though there do remain some institutions which need careful supervision and management to put them on a proper footing. The tendency, I believe, will continue to be for the number of operating banks to decrease each year, but this reduction under present conditions cannot possibly be interpreted as a disintegration of the system. It represents, rather, a material strengthening of the system when earning power has become so important and when improved accessibility of larger communities has made it unnecessary to have banks in many localities.

The banks certainly do not lack available resources for the financing job they have ahead. In fact, so swollen are their vaults that the authorities responsible for control of the volume of bank credit already are asking for additional powers to prevent a runaway expansion of such credit. The assets of insured commercial banks increased from \$63 billion at the end of 1939 to nearly \$71 billion at December 31, 1940, a jump of 12 percent. A tremendous volume, and under present conditions there can be little doubt about the availability of a great part of it.

The examinations of insured commercial banks during 1940 showed an improvement in quality of each of their major types of assets, extending a trend that has been in evidence during the seven years of deposit insurance and supporting our belief that the banks are ready for the emergency. The assets of 13,347 insured commercial banks examined during 1940 were appraised at 99.7 percent of their book value, only three-tenths of one percent being set up as net deductions by examiners. Approximately 96 percent of the assets were free from any criticism, as compared with 94 percent in 1939 and 92 percent in 1938.

Our year-end figures for 1940 show that even then the banks were well launched on their financial support of the nation's new programs. We find that for insured commercial banks during the past calendar year commercial and industrial loans increased \$837 million, or about 14 percent; agricultural loans went up about \$200 million or nearly 20 percent; and real estate loans of all kinds increased, loans on residential properties alone going up \$286 million, or more than 11 percent.

But it has been so long since most of us in this business of banking were caught up in a rush of enthusiasm, activity, and business opportunity, that it might be well for us to take stock of our situation and to set up a few standards and objectives to guide us during the months to come.

Under the program that is now laid out for us, cash will be required in huge quantities both by the Federal Government, which is biggest buyer under the program, and by the producing, distributing, and utilities industries, which must greatly increase and speed up their facilities in order to meet their Government's urgent needs and to supply its continuing requirements under the unsettled international order that promises to prevail for several years.

Government Financing From Private Savings

As much as possible of the defense financing of the Government should be absorbed by existing pools of savings and by the increased savings which should result from our rising national income. It will be necessary, too, to convert for defense production some plants now engaged in consumer industries. We hope that this change can be effected without undue hardship upon the thousands of small businesses engaged in the distribution of consumers' goods. One sure effect of the change, however, will be to increase individual savings as the purchase of consumer goods becomes difficult or uneconomic. By promoting investment in Defense Bonds among your customers, each of you can give the

defense program a big boost.

Commercial Banks To Care For Business Needs

It is desirable also to leave both the resources of commercial banks and the energies of their managers free to satisfy the legitimate financial needs of business under today's accelerated demands. Here definitely, is a job at which a community's banker can excel and at which a community's active funds should be put to work. This is an all-out effort, requiring skill in its planning and speed in its execution. It is a nationwide effort, best promoted by action on thousands of local fronts.

In meeting our responsibility for financing the increasing activity of business it is imperative, I believe, that we bankers not lose sight of major credit principles in a welter of lesser considerations. Our responsibility is two-fold. We must care for the legitimate credit needs of our communities, and our loans must be repaid so that stockholders and especially depositors will not suffer loss. The business of credit extension is an art, not bound by artificial restrictions based on terms of loans or size of borrowers, but resting on the basic fact that any loan that will be repaid at maturity is a good loan. It is in the application of this art that you men exert your greatest usefulness to our economy and to the welfare of our people.

Despite the skill with which we exercise the art of credit extension, there are bound to be some losses arise in the loans we make. Before embarking on expanded lending programs, therefore, it would be well for each of us to survey the ability of his institution to absorb such losses without endangering his depositors.

Bank Capital Ratios Down As Assets Grow

The improvement in asset quality that I mentioned earlier is very encouraging to those charged with supervision of banks. The Federal Deposit Insurance Corporation, however, is concerned by the continued increase in the number of banks with small capital cushions. Since 1936 the growth of assets at a rate much more rapid than the growth of capital has caused a general lowering of the capital ratios of banks.

Examinations of insured banks made during 1940 revealed an aggregate net sound capital amounting to 9.7 percent of the appraised value of total assets, as compared with 10.6 percent in the preceding year. The further rapid increase of assets during 1940 and the first quarter of 1941 had caused a continued decline to less than 9.0 percent on May 1 of this year. The capital ratios of banks probably average lower now than at any other time in our history. Examinations made during 1940 showed that more than one-fifth of the banks had a net sound capital of less than 10 percent of the appraised value of their assets. These banks held almost two-thirds of the deposits in all insured banks.

It is true that a considerable part of the increase in bank assets has been in the form of cash and balances due from banks, the so-called 'riskless' assets. Any subsequent shift to business loans and securities, however, will leave many of the banks in a vulnerable position. As business demands increase, supervisory authorities cannot take action against a large proportion of the banks to enforce capital standards without appearing to retard business activity. Steps should be taken to improve the capital position of these marginal banks before increased business requirements further narrow their capital cushions.

Retention of Earnings For Safety

I mention this widespread capital deficiency because now, if ever, is the time we should be planning to do something about it. As lending activity increases, bank income is rising substantially. Gross income of insured banks rose \$25 million during 1940 to a total of \$1,631 million. Income on loans for these banks was up over \$40 million to aggregate \$769 million.

The budgeting of net earnings should receive our careful attention. Stockholders will expect some participation in the bank's improved income. Primary consideration, however, should be given to the fact that the increased income results from the assumption of increased risks. Loans mean income, but they also mean potential losses. Income on loans is not all rental paid for use of funds; it is partly a premium to insure the lender against loss. It is both logical and necessary, therefore, that a substantial portion of banks' earnings be retained in their capital accounts and reserves. If they are needed to absorb losses, they will be there; if not, they still will be there representing additional equity for stockholders. Meanwhile, bank stockholders have not been faring so badly as might be supposed. Cash dividends paid to common stockholders by all insured banks during 1940 amounted to nine percent of the aggregate par value of the common stock of those banks.

It should hardly be necessary, in view of the recent experience which all of us shared, to warn good bankers against allowing worthless and risky assets to accumulate in their institutions. When the pressure of a period of Widespread liquidation hits the banking system, banks with clean houses have a hard enough time to survive. Those stocked with the debris and dead cats of a lifetime are doomed to early extinction. The time to prepare for a squeeze is before it hits us. I urge, therefore, that those institutions which still have some housecleaning to do take advantage of improved earnings to adjust all their assets to proper carrying values

and to write off those they know to be worthless. Let them also take advantage of the improved condition of the real estate market to get rid of the other real estate they have acquired and still hold. The banks as a whole have done an excellent job along these lines during the past seven years, but there still remain many institutions that have problems to surmount. As of the close of 1940 there were about 750 insured banks which on the basis of their latest examinations had fixed and substandard assets amounting to 20 percent or more of their total assets. Most of these banks are following constructive programs which bring steady improvement to their positions.

First, then, let us sweep out or properly price the substandard assets we now hold. And henceforth, let us eliminate known losses currently and provide amply for losses that are likely to occur in the future.

Deposit Insurance Will Aid Readjustment

Any discussion of the probable future of our banking system after the present period of intense activity dwindles off must center around the history of deposit insurance or deposit guaranty. It is my own belief that the existence of a strong and vigilant Federal Deposit Insurance Corporation is our best guarantee that this future will find the banking system readjusting itself smoothly and without disturbance.

The seven and a half successful years of operation of Federal deposit insurance have contributed immeasurably to the health of our banking system. The Corporation has been able to care for what emergency situations arose without financial strain and practically without loss to the depositors of insured banks; it has moved into about 350 banks that failed or that were deteriorating rapidly; it has expended more than \$230 million for protection of the 1,200,000 depositors in these banks, whose deposits totalled \$445 million and

of whom fewer than one-quarter of one percent were not fully protected; it has encouraged supervisory activities that have helped eliminate the problem assets of thousands of other banks; and meanwhile, it has built up reserves that bring its total assets today to more than \$500 million. Most important of all, it has instilled in the people of the country a knowledge that their funds are safe and liquid under the protection of Federal deposit insurance, has convinced them that their banks are carefully supervised and that bad and unsafe banking will not be tolerated, and has developed in them a sense of calm and security that will be a splendid factor for good during the next period of readjustment.

Federal deposit insurance is succeeding where earlier State plans failed primarily, I believe, because it has an adequate income and a degree of authority over its risks which the State plans lacked. So long as the Corporation is responsible for the safety of depositors' funds, it must have the power to control its membership and to supervise the activities within banks which affect the risk the Corporation assumes.

FDIC To Continue Realistic Supervision

I have heard it said that Federal Deposit Insurance Corporation is too exacting in its application of supervisory standards. That occasionally may be true, but I believe that the good banker would rather have us err on the side of strictness than on the side of leniency, and that these bankers support our policies individually, if not collectively. Further, the record shows that though our examiners may be strict they still stop short of appraising on a liquidating basis. In the insured banks placed in receivership or merged with financial aid from FDIC during the first seven years of its existence, the losses we expect to suffer in liquidation of our outlay are more than two and a half times as great as those set up by examiners shortly before

the banks were closed or merged. On the average, examiners estimated that losses would approximate 9 percent of total assets in the banks involved. Actually, losses will amount to 23 percent of total assets on the basis of current appraisals.

We would be remiss, indeed, if we did not call them as we see them. Those bankers are remiss who fail to realize that we are working for the preservation and prosperity of their institutions as well as for the protection of depositors. Security can be achieved only through vigilance and through prompt remedial attention to what weak spots are found. We propose to continue to examine insured banks fearlessly and fairly. We ask that you bankers help us make yours stronger banks by expediting what corrective measures are found necessary.

Despite the best efforts of bankers and bank supervisors, there probably always will be occasional bank failures from factors beyond our control. In these enlightened days, when bank failures no longer mean losses to depositors, the supervisor who hesitates to close an insolvent or hazardous bank not only is shirking his duty and defying the law but is also being unfair to FDIC. The longer such situations drag along, the greater will be the Corporation's eventual loss. We urge prompt action by supervisors in each such case, and we stand ready promptly to meet our financial responsibility for protection of the depositors of those banks. Nothing contributes quite so much to a depositor's sense of safety and security as seeing deposit insurance actually work when a bank has to close. The growth of this sense of safety and security is the best non-book asset of every sound, well managed bank in the land. Only doubt and uncertainty are engendered by the continued operation of banks which generally are known to be in unsound condition.

By these means, then, do I hope to see our banking system play its full part in the present national emergency and smoothly make the readjustment when the emergency is over. Let's keep the system structurally clean, let's manage each of its units according to sound and well proved principles. Let's demonstrate to depositors that behind the safety they get from deposit insurance lies the even greater bulwark of sound, progressive bank management. Let's show by our record during the years ahead that the millions who today are 'buying a share in America' will have a banking system without peer in the world.
