

Current state of banking in Louisiana:

Louisiana Bankers Association

New Orleans, Louisiana

April 7, 1989

Good morning, ladies and gentlemen. Its a real pleasure for me to join a group that Charles Worsham, your Association's Executive Vice President, called "the survivors of Louisiana banking.

There is no question that we are in an era of significant change for our nation's economic system. With those changes will come subsidiary changes to the banking industry and other financial institutions. It is going to take survival-oriented leadership to succeed in this environment, and you are to be congratulated for the measure of success you have thus far obtained.

That reminds me of a story a friend told me about a college reunion he recently attended. While there, my friend stopped by to visit an old economics professor still actively teaching well into his eighties.

During the visit he idly picked up some examination papers on the professor's desk. To my friend's surprise, he noticed that the questions were essentially the same as when he'd taken the course decades earlier.

My friend mentioned this to the professor, saying that he expected the questions would have been very different after such a long period.

"No", the professor explained, "the questions actually change very little. Over the years only the answers seem to change"...

I believe we are dealing with that phenomena right now -- in Washington -- and right here in Louisiana. And we have no choice but to have to find new answers to those old questions.

Let me begin this morning with a discussion of the current state of Louisiana banking, as seen through the eyes of a deposit insurer. I'll then turn to several other related issues I believe are important to the future of U. S. banking.

This is not a report card of how Louisiana banks have done, per se. It is my attempt to provide you with a straightforward assessment of what I see in both results and trends -- both the good and bad news -- in your state's banking industry.

It is understood, of course, that banking in any area follows underlying business and economic trends. There are few places where this connection is more obvious than Louisiana. In the 1980s your State's strong dependency on oil-related industries has provided both a boom -- and a bust. You've been on a roller coaster ride -- and its not over yet!

Despite a modest recovery in late 1987 and 1988, Louisiana's relatively undiversified economic base, high unemployment, and low rate of income growth have given your banks a very substantial challenge.

I recently heard a story about two experts arguing about the financial condition of the oil patch states. One man insisted there was a money shortage. The other scoffed at this statement. "There's no shortage of money," he said, "Go to the bank and ask them to show you all the money stored in vaults. Money by the millions. And in every bank too. But ask them to lend you some of it, and they ask you what collateral you have. That's where the trouble is. There is plenty of money, but a very serious shortage of collateral"!

[pause]

The problem in Louisiana has been that much of your collateral is not worth what it used to be -- and that has taken a heavy toll. Louisiana has had six banks fail so far in 1989, in addition to 13 in 1988, 15 in 1987, and 9 in 1986.

Unfortunately, you do not appear fully out of the woods yet, but certainly you are no longer in the deepest depths of the jungle either. Small favors, as they say.

On a more positive note, we are pleased at the FDIC to see that your State now authorizes statewide branching. We hope this will mean fewer bank failures in the future.

Another bright spot is that, overall, Louisiana's banking sector registered a modest profit for 1988, indicating a light at the end of the tunnel.

Your banks' broke even last year, as reflected in the third quarter numbers I will be using throughout this report. Last year's income is certainly not a record to be satisfied with, but it is a significant improvement over the previous two years of losses. It also compares favorably with the overall record of Southwest banks that posted a negative 0.78 percent return.

At the FDIC we are especially heartened by the fact that the number of your banks with full-year losses was considerably lower in 1988. This bodes well for a lower bank failure rate in Louisiana in the future, and for the fiscal health of the FDIC fund.

Key factors in this improving earnings picture were lower loan losses and smaller provisioning for future losses. Better control of overhead costs also contributed to this development.

Another positive in the earnings area is that Louisiana banks reporting operating losses have fallen sharply -- from 41.3 percent in 1987, to 26.7 percent through third quarter 1988.

For your 203 commercial banks with less than \$100 million in assets -- losses continued, but at a significantly reduced rate.

The average annualized return on assets showed substantial improvement, increasing to a negative 0.02 percent, up from a negative 0.51 percent. These losses still reflect very high levels of nonperforming assets, net charge-offs and loan-loss provisions.

After giving you a look at your smaller banks, it seems only fair to take a look at the earnings of your 55 largest banks with assets over \$100 million.

On average, these larger banks reported an annualized return on assets of 0.01 percent in the first nine months of 1988.

Unfortunately, this is a decline from the 0.13 percent realized in 1987. Like the smaller banks, these banks are also heavily burdened by very high levels of nonperforming assets, net charge-offs and loan-loss provision.

Turning from the earnings story, another area of general improvement is the average asset quality found in your banks.

Aggregate nonperforming assets declined to 7.43 percent in 1988, down from 1987's mark of 7.97 percent. The most troubled loan types continue to be real estate and commercial loans.

It is also encouraging that nonperforming assets declined despite lower net charge-offs, which were down to 2.07 percent. However, we need to look to even further improvements in asset quality so that Louisiana's banks can return to their traditional levels of profitability.

Capitalization is an area that also experienced modest improvement. Your bank's average equity capital grew slightly in 1988, climbing over twenty basis points to 7.19 percent. That reverses two years of declining capitalization. And the extra cushion your banks are developing is good news for the FDIC, as it is for you.

But that cushion is not as plump as we might hope. Loan loss reserves were down last year, and that despite the fact that reserve coverage of nonperforming assets was less than half the national average. The lack of a substantial reserve cushion to absorb future losses probably means that Louisiana banks' earnings will continue to be held down by future loan charge-offs.

So how does all this add up on my neon scoreboard? Things are looking up for Louisiana banking -- but only modestly. There are plenty of problems and challenges left for you survivors.

In many ways, the answer to the question of how good 1989 will be for your banks depends on the answer to another question -- Will oil prices rise? Not being clairvoyant in all areas -- even as a federal official -- we will have to wait and see.

In any case, the key to Louisiana's long-term health requires substantial diversification of your State's economy so that your future is not forever tied to what happens at oil rigs thousands of miles away.

I'd like to now turn quickly to a few other issues facing the banking industry and the FDIC today that I thought might be of interest to this group.

[Insert discussion on short capsule issues.]

[Conclusion]

Well, that brings me almost to the end of my talk, and to the beginning of what I'm certain will be an interesting question period.

In conclusion, it seems to me that the situation facing Louisiana's bankers can be summed up in a litany of cliché's I recently heard that seemed as numerous as the gallons of water in Lake Ponchatrain.

It went like this:

The difficulties of today's Louisiana banking industry are such that bankers like yourselves must keep your backs to the wall -- your ears to the ground -- your shoulders to the wheel -- your noses to the grindstone -- your heads level -- and your feet on the ground!

At the same time, however, you must have your heads in the clouds so that you can look for the silver lining!

It won't be easy -- and you know that better than I -- but I'm betting that you survivors are, by and large, going to be successful. Good luck.

Thank you for your attention. I'll be pleased now to take your questions.