BK Dir|Stat
Spch
FDIC
Chrm
W

FDIC

FEDERAL DEPOSIT INSURANCE CORPORATION, Washington, D.C. 20429

OFFICE OF THE CHAIRMAN

FDIC AND THE NATION'S LARGER BANKS

Excerpted from the Remarks of

Frank Wille, Chairman
Federal Deposit Insurance Corporation

before the

Association of Reserve City Bankers

Boca Raton, Florida

April 7, 1975

The FDIC carries out three basic roles in the American banking system: (i) it is a supervisory agency for insured State banks which do not belong to the Federal Reserve System, (ii) it is the insurer of deposits in both member and nonmember banks, and (iii) it acts as receiver of closed insured banks. In each capacity we have not, until recently, been an agency with significant or regular contact with the nation's larger banks. That is changing, in all three capacities, as the following information demonstrates.

-- As a supervisory agency, we are today examining, along with state banking departments, about 8,450 nonmember commercial banks, most but not all of which are relatively small. These nonmember commercial banks range in size from under $1 million in deposits to about $1.2 billion in deposits. The total number of nonmember banks is increasing by about 200 banks annually, largely as a result of newly chartered State banks in the unit banking states of Florida, Illinois and Texas. In addition, FDIC examines about 320 mutual savings banks, the average size of which is considerably larger than the average nonmember commercial bank. The largest of these mutual savings banks is The Bowery Savings Bank in New York, which has $3.5 billion in deposits. Since the membership of your Association is drawn from the larger banks of the country, let's talk this morning primarily about them.

At year-end 1974, there were 812 banks inclusive of national banks and State member banks that exceeded $100 MM in domestic deposits. In the aggregate these banks held about 70 percent of all the commercial bank assets of the country. Eighty-three of these banks had over $1 billion in domestic deposits. About 60 percent of these 812 larger banks are national banks, but it may surprise you to learn that 202 are nonmember banks and only 123 are State-chartered member banks. Actually, the division of State banks between members and nonmembers varies by size group over $100 MM. At the lower end of the spectrum, between $100 MM and $500 MM, where there are 636 of these banks, nonmember banks outnumber State member banks by about 2 to 1. Between $500 MM and $1 billion, the two categories claim about an equal number of banks, with nonmembers slightly outnumbering State member banks. Above $1 billion, there are only 3 nonmembers, as compared with 24 State member banks and 56 national banks. While member banks clearly predominate among $1 billion banks, as you might expect, we at FDIC are examining on a regular basis a growing number of large commercial banks, and as we do, our familiarity as an agency with the problems they face is growing commensurately.

-- As the insurer of bank deposits for almost all of the nation's banks, we are naturally concerned with the risks within the banking system as a whole and with that particular group of national, State member and nonmember banks we regulators refer to generally as "distressed" or "problem banks." Since that list hardly ever contains more than two or three mutual savings banks, we are talking almost exclusively about risks within the commercial banking system. A number of factors have combined over the last few years to shake public confidence in banking, but high on anyone's list has to be the well-publicized failure of two billion-dollar banks and the near failure of two others, specifically: Bank of the Commonwealth in Detroit in 1972, United States National Bank in San Diego in 1973, Franklin National Bank in 1974, and Security National Bank of Long Island this past January. Whatever aberrations these four banks represented, their downfall stripped away for the public, for bank investors and for bank regulators, the unspoken assumption that large banks are somehow immune to mismanagement, mistake and misconduct. I regret to say we will all be living for some time with the climate of uncertainty, disbelief and suspicion engendered by the relatively rapid succession of these four, well-publicized incidents in American banking history. Many of us, both bankers and regulators, have tried to place in perspective the basic stability and strength of the 98 percent of all American banks which present no significant cause for concern to the public or the supervisory agencies, but it is an uphill battle. None of us in the future can afford the luxury of believing that a large bank in difficulty is somebody else's problem -- that bell tolls for all of us.

I can and have gone around the country seeking to quiet some of the alarm expressed largely but not, I regret to say, exclusively, by the "instant" bank specialists of the press. Speaking of the commercial banking industry as a whole, I can point out that neither the rate of bank failure, nor the number of problem banks, is out of line with past experience. One insured bank failed in 1972, six in 1973 and four last year. With 183 problem banks at year-end 1974, we are well within the range of 150 to 250 banks that has prevailed each quarter over the last fifteen years. Despite tight money, disintermediation and recession last year, charged-off domestic loans net of recoveries came in for all of 1974 at almost precisely the $2 billion predicted -- $1,957,000,000 to be exact -- or 36/100ths of 1 percent of the domestic loans held by all of the nation's commercial banks. In dollar terms, this was about 69 percent greater than 1973 but it remains a very low figure when related to the total domestic loan exposure of the commercial banking system. Loan loss reserves already set aside and still remaining for future use are more than four times the net charge-offs of 1974, while retained earnings after current provision for new loan loss reserves increased the capital accounts of all insured commercial banks by almost $5.7 billion during the year.

Total capital accounts and reserves for losses now aggregate almost $72 billion for the commercial banking industry as a whole, some 36 times the net charge-off experience of last year. Obviously, even greater charge-offs this year than last -- which I am not predicting -- would not affect the fundamental safety or soundness of the system. In addition, the rate of growth in domestic assets has moderated, from 12.9 percent in 1973 to 9.6 percent in 1974 -- again for the system as a whole. I could cite other figures, as well as easing monetary conditions, but they add up to the same conclusion: that the admitted risks in our commercial banks are within tolerable limits for the system as a whole and that the nationwide statistics give little justification for the widespread uneasiness about the commercial banking system which we see on all sides today.

Having said this, I must point out at least to this group what I refrain from saying elsewhere: that there are a number of factors which currently give the supervisory authorities more concern about banks over $100 MM in deposits as a group than about the banks below that cutoff.

First of all, I think we share a belief based on our experience of the last four years, that public confidence is more easily and thoroughly shaken by the failure of one large bank than several smaller ones. For about 25 years prior to 1965, the largest bank to fail involved only $17 MM in deposits. Since that time, at least ten banks over $100 MM have required disbursements from the FDIC trust fund, or an emergency merger to prevent failure.

Secondly, the number of larger banks appearing on the watch lists of the three Federal agencies has increased steadily over the past ten years, and their classification on these lists has been increasing in severity. Whereas ten years ago, it was rare to see a bank over $100 MM on any agency's watch list, there were a disproportionately high number of them on our respective watch lists at year-end 1974, with more than just a few between $100 MM and $1 billion listed as "serious" problems. Two reasons for this -- and there are others in every instance -- were the tighter monetary policies of last fall and the impact of the deepening recession on bank borrowers. Suffice it to say, as Deputy Secretary Gardner pointed out last night, the unthinkable has clearly become thinkable.

Thirdly, although mathematical ratios based on average performance are clearly unfair to particular banks, there are some figures for the larger banks as a group which compel closer supervisory inspection and analysis. Last year, despite tight money and widespread efforts to control growth, the rate of growth in domestic assets of banks over $100 MM was almost twice the rate of growth of banks below $100 MM, and significantly higher for the banks over

$1 billion than for banks between $100 and $500 MM. Moreover, even without taking into account foreign loans and deposits for the larger banks with overseas branches, loan to deposit ratios for banks over $100 MM were 15-25 percent higher than for banks under $100 MM, while 1974 charge-offs net of recoveries as a percentage of net operating earnings were about 70 percent higher for these larger banks than for the banks under $100 MM. Bank loans to REITS may be only about 2 percent of the total loan portfolios of all commercial banks, but they are known to be concentrated in the largest size group we are discussing. Total capital accounts to total domestic assets were about 7.9 percent for banks under $100 MM but 6.6 percent for banks over $100 MM. If we include foreign assets, the same capital ratio for the larger banks was slightly less than 5 percent. Moreover, as a percentage of total assets, net current operating income after taxes of banks over $100 MM tended to be 20 percent lower on average than the comparable figure for banks under $100 MM. There are many reasons why these figures, even on average, are so different for the larger banks than for the smaller banks, but I think you can see why the supervisory agencies today are concentrating their attention on these 812 banks in the system with more than $100 MM in deposits. It is, I believe, to your interest and the interest of the public at large that we do so so long as we resist the usual supervisory instinct to paint everything in black and white terms for all banks in a particular group. The quality of a bank's management remains the key factor in any supervisory analysis, and we are fortunate that it is so high in most of our larger banks.

-- As a receiver of closed banks regardless of charter, the Corporation has different responsibilities than it has either as a supervisory or insurance agency. Basically, we act as a fiduciary for the creditors and security holders of a failed bank, with a legal duty to do the best we can in realizing the highest price and the maximum collections on the bank's assets. This duty obviously colors the way in which we respond in distressed or failing bank situations where there appears to be a lively possibility FDIC may become receiver. I mention it here, not merely because it helps to explain how we arrived at the transactions by which Crocker took over the deposits of United States National Bank and European-American the deposits of Franklin National Bank, but to point out that in the receiverships of both banks the FDIC is participating in asset workouts with an increasing number of the larger banks of the country, a number of which also have a creditor's interest in the success of our collection efforts.