FDIC
FEDERAL DEPOSIT INSURANCE CORPORATION

NEWS RELEASE

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Statement on

FDIC SURVEYS TO DATE ON IMPACT OF NYC DEFAULT ON NONMEMBER BANKS

Submitted to the

Subcommittee on Commerce, Consumer and Monetary Affairs
of the
Committee on Government Operations
House of Representatives

by

Frank Wille, Chairman
Federal Deposit Insurance Corporation

October 8, 1975

The Federal Deposit Insurance Corporation is pleased to respond to the Subcommittee's request for information as to the surveys it has been making of the potential impact on the banking system of a New York City default in the payment of its outstanding bonds and notes.

At the outset, I should note that the FDIC surveys have been limited to the nation's 8,889 nonmember banks which the FDIC examines on a regular basis, i.e. those insured banks which do not belong to the Federal Reserve System. An accurate overall view of the banking system's exposure must, therefore, include an aggregation of the information developed by the Comptroller of the Currency and the Federal Reserve System for member banks in addition to the FDIC's results for nonmember banks.

Secondly, the FDIC has sought to obtain factual information as to the holdings of various types of State and local obligations by nonmember banks. This information, to the extent we presently have it, will be detailed in later portions of this statement. Partly because this information is incomplete but mainly because the FDIC has no background of expertise with which to evaluate likely market reactions in the event of a New York City default, the FDIC itself has reached no judgment as to the likely impact such a default would have on the nation's nonmember banks, nor has it authorized any such predictions to be made on its behalf.

A prediction as to likely impact requires at least two basic assumptions which the FDIC itself is in no position to make: One relates to the extent market values of State and local government obligations, particularly those issued by New York City, will drop if a default occurs, and the other relates to whether or not issuers of State and local obligations other than New York City will also be forced to default because market developments make it impossible for them to roll over existing debt in a timely manner. Even if such assumptions can be made, a prediction would require a bank-by-bank analysis of each bank holding such securities, since the impact may differ considerably depending on a great many factors peculiar to each bank. As will be described later in this statement (see Page 8) such analysis is now underway by the FDIC for State nonmember banks, but it is not yet complete.

The FDIC has viewed its function as one of developing a background of factual information relating to nonmember banks so that the full range of potential impact can be foreseen both by the Administration and by the Congress. One's judgment as to actual impact will then depend on the market assumptions one is willing to make or on the market developments that actually occur subsequent to a New York City default.

Thirdly, the FDIC has viewed the potential effects on the banking sytstem to be serious enough to warrant contingency planning on a joint basis with the other bank regulatory agencies in three areas which relate to the safety and solvency of individual institutions: (i) the examination treatment of defaulted obligations held by an insured bank, (ii) the liquidity needs of particular banks whose holdings of affected State and local obligations may result in adverse depositor reaction, and (iii) the capital needs of particular banks which suffer a loss of public confidence because of such holdings. Although this hearing appears not to have been called to discuss such contingency plans, I would be glad to respond to any questions members of the Subcommittee may have concerning them at the conclusion of this statement.

The FDIC surveys of nonmember bank holdings of selected State and local obligations have been conducted in three stages. The first effort, which began in late July, was a review of the most recent FDIC examination workpapers for a selected sample of approximately 540 nonmember commercial banks, including all of the 44 nonmember commercial banks located in New York State, in order to estimate the relative percentages which each bank's holdings of New York City and New York State Housing Finance Agency obligations bore to that bank's total capital and reserves. The sample of nonmember banks used in this initial survey (other than those in New York State) consisted of those nonmember banks which had been supplying weekly money supply data during a recent ten-month period ending in May, the purpose of which was to assist the Federal Reserve System to estimate more accurately the nonmember component of the nation's money supply. For that purpose, the sample had been reasonably representative of all nonmember banks in the country, but we recognized that its use for estimating nonmember holdings of the two types of issues in question might not produce estimates with the same degree of reliability. In addition, the data derived would reflect different dates of examination, some of them more than six months before. Nonetheless, this type of survey was manageable in numbers and could be made without undue publicity at a delicate time for New York City and the Municipal Assistance Corporation in their refinancing efforts. This survey, which we recognized would result in a rough approximation only, of the holdings of the nation's 8,559 nonmember commercial banks, showed the following:

-- In New York State, there were only 8 nonmember banks, smaller than $100 million in total deposits, which held New York City obligations representing 25% or more of total capital and reserves, and only one nonmember over $100 million in deposit size with a comparable exposure.

-- In New York State, if holdings of New York State Housing Finance Agency obligations were added to those of New York City, there were only 12 nonmember banks, smaller than $100 million total deposits, which had 25% or more of their total capital and reserves exposed, and only 4 nonmember banks over $100 million in deposit size similarly exposed.

-- In New York State, less than one-third of the nonmember banks appeared to have capital exposures between 10% and 25%, based on their holdings of similar obligations.

-- Nationwide, it appeared that approximately two and a half percent of all nonmember banks below $100 million in deposit size would have holdings of New York City obligations in excess of 25% or more of their total capital and reserves, while only about 1% of the nonmember banks larger than that would be similarly exposed. If New York State Housing Finance Agency obligations were added to their holdings of New York City obligations, about three and one-half percent of the nonmember banks in both size categories appeared to be similarly exposed.

The FDIC moved to the second stage of its fact-finding in late August when it appeared that the marketing difficulties of the Municipal Assistance Corporation made a New York City default sometime in September or October a more immediate prospect than it had been up to that point in time. On August 25, I asked each of the nation's 8,889 nonmember banks -- including the 330 FDIC-insured mutual savings banks -- to report to the FDIC within ten days of receipt its holdings of New York City bonds and notes as of any convenient date in August 1975. This survey, although limited to New York City obligations, had the two advantages of reflecting current information and the holdings of all nonmember banks. The form of this survey, together with my transmittal letters, are attached as Exhibits A and B to this statement. New York City notes were to be reported separately from bonds and the maturity schedules for both were to be reflected. Such detail was requested only of nonmember banks with more than 20% of their total net worth exposed (i.e. about 1.5% of total assets for the typical nonmember bank) -- the 20% figure reflecting an interagency judgment that most banks below that cutoff would probably not experience significant adverse consequences if New York City were to default.

As of the close of business Monday, October 6, the reports of 8,606 nonmember banks had been received -- about a 97% response. Of the 8,606 reporting banks, 271 indicated holdings of New York City obligations as of August 1975 amounting to 20% or more of their total net worth. Their holdings of such obligations approximated only $265 million of New York City's total outstanding debt, and was distributed as follows:

New York City Obligations
(dollar amounts in thousands)

	Number of Banks	Notes	Bonds	Total
Current book value as % of Net Worth:				
20% to 30%	125	$24,550	$53,325	$77,875
30% to 40%	54	3,120	22,223	25,343
40% to 50%	36	5,837	18,357	24,094
50% to 70%	36	19,007	16,589	35,596
Over 70%	20	69,101	32,629	101,730
	271	$121,615	$143,123	$264,638

The 271 nonmember banks reflected in the above table are located in 34 States, with ten or more located in Alabama, Arkansas, Florida, Illinois, Louisiana, Missouri, New York, Tennessee and Texas. The 56 nonmember banks reporting the largest concentrations of New York City obligations, i.e. 50% or more of their net worth, are located in 18 States, with only 5 States having 4 or more such nonmembers (Arkansas, Florida, Illinois, Missouri and New York).

The size distribution of these 271 banks is as follows, with all but 5 of them below $100 million in total deposits (as of June 30, 1975):

Holdings of New York City Obligations, by Size of Bank

Deposit Size (millions)	Insured Banks Having NYC Obligations as Percent of Capital and Reserves of: 20-50%	50-70%	Over 70%	Totals
Less than $1.	-	-	-	-
1 - 2	2	-	-	2
2 - 5	27	5	4	36
5 - 10	66	18	2	86
10 - 25	76	7	8	91
25 - 50	29	3	2	34
50 - 100	12	2	3	17
100 - 500	2	1	1	4
$500 - $1,000	1	-	-	1
Over $1 billion	-	-	-	0
Totals	215	36	20	271

The largest bank reflected on the above list is a mutual savings bank headquartered in New York City which has total holdings of New York City obligations equal to less than 30% of its net worth. The two banks in the $100-$500 million category having 50% or more of their net worth exposed are actually in the $200 - $300 million size range and both are headquartered in New York State.

With respect to the 56 nonmember banks having holdings of NYC obligations equal to 50% or more of their net worth, a bank-by-bank review by the FDIC's Division of Bank Supervision indicates that the seriousness of their exposure is considerably less than the numbers alone might suggest. A good number are exceptionally well capitalized, so that even a 50% mark-down in the value of their NYC holdings in the event of a default would still leave them with a healthy and respectable capital to assets ratio. Others are members of large multibank holding companies or have access to obvious sources of additional capital, so that any significant write-down of their New York City obligations because of a New York City default would not necessarily lead to supervisory concern. Many of the 56 turn out to be so conservatively managed, with such a low level of classified assets, that a significant write-down of capital because of a New York City default would similarly not lead to supervisory concern. A few hold NYC obligations maturing in the very near future so that any successful refinancing by New York City or the Municipal Assistance Corporation would remove them from the list altogether. Only one of the 56 banks is on the FDIC's current problem bank list.

While some of this information is reassuring as to the potential impact of a New York City default on the nation's 8,889 nonmember banks, our factual analysis has not yet taken fully into account the additional complications of possible default by issuers of State and local obligations other than New York City. To develop this information, FDIC examiners during the past ten days have been obtaining from approximately 950 nonmember banks detailed information as to their holdings of State and local obligations other than New York City bonds and notes, including maturity distributions and issue by issue information for agency issuers like the New York State Housing Finance Agency which finance many different categories of construction through separate financing programs. The nonmember banks presently being surveyed in this third stage of the FDIC fact-finding effort consist of the 271 banks whose holdings of New York City obligations exceed 20% or more of their net worth, all nonmember banks on the current FDIC "problem bank" list, all 245 nonmember banks with total assets in excess of $100 million as of June 30, 1975, and the approximately 200 nonmember banks which reported the largest percentage of asset holdings in State and local obligations as of June 30, 1975.

When this third phase of our survey effort is completed, probably within the next two weeks, I shall be glad to forward to the Subcommittee a detailed summary of our review which may help to quantify the dimensions of the write-down of assets and capital by nonmember banks which may be required in due course if issuers other than New York City default. It should be noted, in the event of a default by New York City or any other issuer, however, that the supervisory requirements for a write-down would not necessarily result in a permanent write-down if the defaulting issuer manages to remedy the default and to restore the marketability of its outstanding issues.

Based on the information as to nonmember banks presently at hand, we believe that with the contingency plans being developed by the Federal Reserve as to liquidity needs and by the FDIC as to write-down requirements and capital assistance, the effect of a New York City default would be limited if the following assumptions are made: (i) that market developments do not permanently erode more than 50% of the book value of New York City obligations, and (ii) that default is limited to New York City. To the extent that market depreciation over several months exceeds 50% of book value and to the extent other issuers are forced to default on their obligations because of market developments following a New York City default, the potential impact on nonmember banks could become significantly more serious. We expect the bank-by-bank data we are currently collecting to be extremely important in determining the full range of potential fallout on nonmember banks which may be caused by a New York City default. Before that information is in and analyzed, I would consider it premature to predict, under varying assumptions as to market developments, the potential impact of a New York City default on the nonmember banks in the nation's banking system.

EXHIBIT A

FDIC

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

OFFICE OF THE CHAIRMAN

BL-20(c)
August 25, 1975

TO THE CHIEF EXECUTIVE OFFICER OF THE BANK ADDRESSED:

Subject: **Holdings of New York City Obligations**

The FDIC would appreciate your assistance in developing accurate and current information of the extent of nonmember bank holdings of bonds and notes of the City of New York, so that in conjunction with information supplied by the Comptroller of the Currency and the Federal Reserve System for member banks the exposure of all insured banks in the event of a default by New York City may be known. This information is being developed as a precautionary measure, and should not be construed as any indication that the Federal bank agencies are either expecting or predicting such a default. The survey, moreover, is being undertaken to confirm our preliminary estimate, based largely on a sampling of 1974 reports of examination, that only a limited number of nonmember banks has any significant amount of New York City obligations.

Please complete and return the form on the reverse side of this memorandum within ten days of receipt, furnishing information as to your bank's holdings of such obligations as of any convenient date in August 1975. A simple checkmark in the space provided will suffice if your bank's aggregate holdings of New York City obligations are less than 20% of the bank's total capital and reserves. If your bank's holdings are 20% or more of total capital and reserves, please fill in the more detailed information requested.

Frank Wille

Frank Wille
Chairman

FEDERAL DEPOSIT INSURANCE CORPORATION

SPECIAL SURVEY OF NEW YORK CITY OBLIGATIONS

INSTRUCTIONS: Complete all applicable items below and return within 10 days to **Director of Research, Room 3008 G, Federal Deposit Insurance Corporation, Washington, D.C. 20429.** *Report obligations of New York City* **only.** *Do not include obligations of New York State or any of its agencies or obligations of the Municipal Assistance Corporation.*

ITEM 1. If current book value holdings of New York City issues are less than 20 percent of the bank's total capital and reserves as of June 30, 1975, check the block at right and return the form in the enclosed envelope. ☐

ITEM 2. If current book value holdings of New York City issues are 20 percent or more of the bank's total capital and reserves as of June 30, 1975, complete **A** and **B** below.

A. BOOK VALUE OF HOLDINGS BY MATURITY

Express figures in thousands of dollars as of any convenient day in August. **Enter date in block at right.**

DATE (As of) August , 1975

DESCRIPTION	MATURITY PERIOD							TOTAL
	1975	Jan.-June 1976	July-Dec. 1976	1977-1979	1980-1985	1986-1995	After 1995	
Notes								
Bonds								
TOTAL								

B. Total Capital and Reserves as of June 30, 1975

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NAME AND BUSINESS PHONE NUMBER OF PERSON FILLING IN REPORT

EXHIBIT B

FDIC

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

OFFICE OF THE CHAIRMAN

BL-20(m)
August 25, 1975

TO THE CHIEF EXECUTIVE OFFICER OF THE MUTUAL SAVINGS BANK ADDRESSED:

Subject: Holdings of New York City Obligations

The FDIC would appreciate your assistance in developing accurate and current information of the extent of nonmember bank holdings of bonds and notes of the City of New York, so that in conjunction with information supplied by the Comptroller of the Currency and the Federal Reserve System for member banks the exposure of all insured banks in the event of a default by New York City may be known. This information is being developed as a precautionary measure, and should not be construed as any indication that the Federal bank agencies are either expecting or predicting such a default. The survey, moreover, is being undertaken to confirm our preliminary estimate, based largely on a sampling of 1974 reports of examination, that only a limited number of nonmember banks has any significant amount of New York City obligations.

Please complete and return the form on the reverse side of this memorandum within ten days of receipt, furnishing information as to your bank's holdings of such obligations as of any convenient date in August 1975. A simple checkmark in the space provided will suffice if your bank's aggregate holdings of New York City obligations are less than 20% of the bank's total surplus and reserves. If your bank's holdings are 20% or more of total surplus and reserves, please fill in the more detailed information requested.

Frank Wille

Frank Wille
Chairman

FEDERAL DEPOSIT INSURANCE CORPORATION

SPECIAL SURVEY OF NEW YORK CITY OBLIGATIONS

INSTRUCTIONS: Complete all applicable items below and return within 10 days to **Director of Research, Room 3008 G, Federal Deposit Insurance Corporation, Washington, D.C. 20429.** *Report obligations of New York City only. Do not include obligations of New York State or any of its agencies or obligations of the Municipal Assistance Corporation.*

ITEM 1. If current book value holdings of New York City issues are less than 20 percent of the bank's total surplus accounts as of June 30, 1975, check the block at right and return the form in the enclosed envelope. ☐

ITEM 2. If current book value holdings of New York City issues are 20 percent or more of the bank's total surplus accounts as of June 30, 1975, complete **A and B** below.

A. BOOK VALUE OF HOLDINGS BY MATURITY

Express figures in thousands of dollars as of any convenient day in August. **Enter date in block at right.**

DATE (As of) *August* , 1975

DESCRIPTION	MATURITY PERIOD							TOTAL
	1975	Jan. - June 1976	July - Dec. 1976	1977 - 1979	1980 - 1985	1986 - 1995	After 1995	
Notes								
Bonds								
TOTAL								

B. Total Surplus Accounts as of June 30, 1975

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NAME AND BUSINESS PHONE NUMBER OF PERSON FILLING IN REPORT