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BANK RESERVES

Address Of

JESSE P. WOLCOTT, CHAIRMAN

FEDERAL DEPOSIT INSURANCE CORPORATION

Before The

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NORTH CAROLINA BANKERS ASSOCIATION

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BANK RESERVES

If you expect from the title of my address to hear a disquisition on the finances of banks, you are doomed to disappointment. Reference to bank reserves ordinarily conjures up visions of money stowed away for some specific purpose. The kind of reserves I have in mind today, however, is less measurable, less mobile, and less manageable, but no less important. I refer to human reserves, an indispensable element in any undertaking, and one that banks have tended to neglect in their preoccupation with financial matters.

Several years ago a professor of sociology at Northwestern University made a survey to determine typical attitudes toward different types of occupations and professions. On the basis of his findings, he classified different jobs in the order of the prestige they carried. At that time the profession of banker rated close to the top, just below that of college professor and above that of minister -- and, incidentally, far above that of Government employee.

A similar survey made within the last year, again by a noted sociologist and covering the Chicago area, revealed somewhat different ratings. This study classified various occupations into seven status groups; the job of bank cashier was ranked in the third status group from the top, and that of bank clerk in the fourth group.

To a business such as banking which has long relied on its prestige presumptions as a major attraction in obtaining and keeping personnel, this deterioration in the status of the banking profession provides both explanation and warning: Explanation of the frequent complaints about banks' difficulties in attracting and keeping able people and in arranging for competent management succession; and warning that the situation is likely to get worse unless banks take effective measures to meet the competition for talent.

Some aspects of this problem come up at practically every meeting of the Board of Directors of the Federal Deposit Insurance Corporation. Let me tell you about a case which concerned us not long ago. It involved a bank which had gotten into some temporary difficulties because of bad loans -- bad because of depressed prices for a local commodity which bulked large in the community's economy and in which the bank understandably had a considerable stake. The loan problem, however, was not insuperable, and a virile and aggressive management would undoubtedly have found a way around the problem. But the management of the bank was no longer imaginative, and lacked both the will and the vigor to dig itself out. Instead, it meekly and almost plaintively begged the Corporation's assistance, which was given by arranging for another bank to take it over with our financial help.

In working out that situation, it became clear that the bank's management had allowed itself to drift, growing old as it drifted, and making no provision for that inevitable day when it would no longer be able to carry on. The management could not be rated incompetent, unless lack of vision is itself a dimension of incompetence. In its day-to-day operation it had done a respectable job. In fact, as things look now, when the Corporation closes its books on this case it will have recovered more than it paid out, an indication that the bank might well have licked its problem had it possessed alert and competent management in its time of trial.

Relatively few banks reach the extremity that this bank did. However, an unhappily large number of cases which reach our Board have the self-same symptoms of a weak or improvident management dragging down an otherwise promising situation. I recall one case recently where we reviewed an application of a bank to take over another bank which seemed to be a most unlikely candidate for absorption. The latter bank had a strong capital position; its earnings were well above average; it was in a growing area and occupied a strong competitive position. The most recent examination had revealed no blemishes of moment, unless such be inferred from the listed ages of its active management. And, as it turned out, that was why it was open to a bid from another bank. The otherwise successful management, having neglected to provide for its own succession, opened the way to a bank which was alert to seize this promising opportunity to extend its own operations.

Intrigued by the recurrence of similar situations in applications coming before our Board, we recently made an analysis of the reasons behind applications from absorbing banks which required the action of the Board in the four years 1955 to 1958. Perhaps I should explain that the Corporation's approval is required in the case of only certain bank absorptions; specifically, whenever a noninsured bank is absorbed by an insured bank, or whenever the resulting bank is not a member of the Federal Reserve System and the absorption involves a diminution of capital or surplus. Also, there are absorptions not requiring consent of the Corporation which nevertheless give rise to applications to us to convert the head office of the absorbed bank into a branch.

Analyzing the applications received under these circumstances during the four years, we discovered that in just about half the cases a management problem was the prime or proximate reason why the owners of the absorbed bank were willing to sell. In fact, of 97 cases in which it was possible to identify the reasons behind the banks' absorption, in 38 cases the principal one was the problem of management succession; and in 9 additional cases, poor or incompetent management.

It is significant, I think, that in only 11 cases was an unfavorable earnings situation the principal reason for the absorption, although of course it was a factor of importance in a large number of cases. In 9 additional cases the indicated principal reason was competition from larger banks, and in 9 others the owners could not resist an attractive price. In the other cases a variety of reasons were given, including sale as an alternative to voluntary liquidation, inadequate capital, and control of the banks involved by the same interests. It took all these varied reasons together, however, to equal in importance the sole factor of management as the principal element in the banks' decisions to sell.

The shortage of management indicated by our analysis of reasons underlying bank absorptions is no isolated finding, but simply confirms other studies that have been made of the problem. The State Bankers Association of your neighboring State of Virginia made a survey of its member banks two or three years ago, and found that four out of ten Virginia banks, on their own admission, had no satisfactory replacement for their top operating executive. The situation, as might be expected, was more acute among country banks than among urban banks.

A recent survey of banks in another State revealed a similar situation. This study, which was prepared by one of our examiners and, incidentally, accepted as a library thesis at the Graduate School of Banking at Rutgers University, covered 50 selected rural banks in the State. In only 7 of the 50 banks were there qualified successors employed by the bank. That the problem of preparing successors could not be prudently deferred much longer is indicated by the further fact that the average age of the managing officers in the 50 banks was 61 years. Let me hasten to tell you that I don't consider 61 old, but I wouldn't object to having an under-study at that age.

What has caused this problem of officer deficiency to come about? The aforementioned study concludes, after analysis of the matter, that

> "the managerial shortage stems largely from small salaries coupled with a lack of advancement opportunity in the general sense...Also pertinent to the problem are aptly named one-man banks, apathetic directorates, inadequate and haphazard training of possible managerial successors, declining economic conditions in rural areas, personal considerations of bank officers and their families, (and) the rapid post-war expansion of banking facilities..."

At the beginning of my remarks I referred to the high regard in which bankers were once held, and implied that the decline in prestige of their office called for compensating increases in wages and salaries. If man does not live by bread alone, neither can he live without it. It is an unfortunate but undeniable fact that banks, on the whole, have not shown the disposition or the ability to meet their competition for top-drawer talent. This is particularly true in the recruiting of college graduates. Is it unreasonable for a fledgling banker to expect the same starting salary as a graduate engineer? Salary-wise he must do as well as his colleagues or the bank will not be able to hire him. Work-wise he must deliver and continue to learn, or the bank will not keep him. Banks must pay the going rate to attract and keep the high caliber of personnel which at one time and to an extraordinary degree gravitated in their direction.

The larger banks have, in fact, been doing pretty well. In a survey made two years ago of some 8,000 banks there was a striking direct relationship between size of bank and amount of salary of the bank's top officers. In banks with deposits of $20-25 million, the largest size group in the survey, the average compensation of the highest paid officer was $20,300. Such compensation decreased directly with declining size of bank, and averaged $3,800 for banks having less than one-half million dollars in deposits. It is, indeed, in the smaller banks that the salary problem is most crucial. This same survey showed that of 800 banks with less than $1 million in deposits, about 600 had at least two officers, and the average compensation of the second highest paid officers was around $3,000.

There are, of course, compensations in banking other than salary. Banks rank near, if not actually at the top, in the extent of fringe benefits provided, and in the degree of employment security so highly prized today. The most recent of the series of surveys on fringe benefits made by the Chamber of Commerce of the United States revealed that such benefits averaged almost a third of the payroll of banks included in the survey, the highest percentage of any of the industry groups. Again, however, it must be pointed out that such generous fringe benefits are pretty much unknown in the smaller banks. A recent survey of private pension plans, pensions being one of the most esteemed fringe benefits, showed that of 189 national banks with deposits of less than $1 million, only 3 of the banks had a pension plan. At the other extreme, all but 9 of the 137 banks with deposits of more than $100 million had such plans.

It would be illusory to believe that inducements of the kind just mentioned -- better compensation, fringe benefits, security and opportunities for advancement -- can solve all the management problems of banks. For it is patent that banks which most need to provide such inducements are often least able to afford them. It is impossible to divorce the deficiencies in bank management from the economics of banking, for if money were no object, many if not most of the deficiencies could readily be corrected. Banks on the brink of survival, suffering perhaps from both low earnings and improvident management, can hardly be expected to adopt warm-heartedly a suggestion that what they need is a higher salary schedule and a more enlightened promotion policy.

What happens in such cases? Usually, stronger banks buy out the marginal ones, often converting them into branches. Thus the community continues to be served by a banking office, which may well be able to offer better services, its efficiency and operations being strengthened by the new management which is now feasible through the economies of spreading the overhead.

This development, which has been going on for a number of years, is strikingly reflected in the growth of bank branches. In the past six years the number of branches has increased by almost a third; only a small part of this growth, of course, has resulted from the conversion of absorbed banks, but the general development of the techniques of branch banking has provided a ready, though not always desirable, solution to the shortage of bank management.

There may be some individuals who, looking at this phenomenon and the accompanying decline in the number of banks, fear for the vitality of our banking system. I do not. Far from being an indication of weakness, this rejuvenation of management is evidence of flexibility and strength. Not all mergers, of course, serve a constructive purpose, and we must be alert to those which unduly reduce competition. But this is a matter which the bank supervisory agencies have long dealt with, and I have no fear of their continued ability to make reasoned and reasonable determinations.

Meanwhile, individual banks themselves can do something toward preserving the balance in our system between unit and branch banks. After all, our banking system is still predominantly comprised of individual units; of the 14,000 banks in the nation, almost 12,000 are separate units without any operating branches. The question of management succession is probably no problem to most of them. In other banks where low earnings or unrealistic attitudes hinder the employment of more competent management, relatively small and inexpensive changes in practices can often-times work wonders.

In the study that I mentioned earlier, it was brought out that several of the banks which paid low salaries also paid relatively substantial income taxes, suggesting that lack of earning power was not an obstacle in those cases. Such situations indicate short-sighted attitudes, and offer the possibility of giving management a better break.

Another area in which banks can do something is in encouraging employees to take training courses. There is no business in the country which has a better in-training program than that provided through the American Institute of Banking, the several regional banking schools, and the graduate school of Rutgers University. Where local classes are not feasible, as in rural banks, correspondence courses are available. When I say banks should encourage employees to take such courses, I mean more than give their permission. It would not be out of line to pay whatever expenses are involved, and possibly make it understood that completion of a course or courses will be followed by appropriate promotional recognition. Investment in training and managerial proficiency is the best investment a business can make if it wants to grow and prosper.

It is easier to enumerate other areas for improvement than to prescribe what might be done. Certainly the area of fringe benefits, almost completely neglected in many banks, should be improved. It may seem pretentious to speak of a promotion policy for banks whose employees number five or fewer; yet the absence of one is in fact a policy which is certain to keep prospects away. The lack of opportunity, not only within an individual bank but in the area which it serves, is a drawback which forces many banks to rely solely upon the local talent remaining after the best has been attracted elsewhere. Many of these short-comings of a banking vocation might be overcome if a banking career had the fascination of rocketeering or the allure of other pursuits now socially and economically attractive. Instead, a banking job has come to be regarded as promising, at best, respectability, but offering little outlet for individual initiative or socially significant service.

As a business with great opportunity, banking has been sold short. It is a business assured of an expanding and challenging future. Better appreciation of its prospects and of its key role in our economy should themselves help to ameliorate the management problems which confront it today. Managerial needs and the depth in human reserves vary from bank to bank. Some banks desperately need back-stopping to fill imminent gaps; other banks would benefit from an infusion of new managerial talent; and all banks would gain if they could find as spokesmen leaders of stature and vision to demonstrate that opportunities do exist, never content until the banking profession regains the prestige it once enjoyed.

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