

DOING WHAT YOU CAN

Presented by

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to

The Alabama Bankers Association

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Several years ago, Alabama bankers were giving me more than the normal share of headaches that go with a Federal Reserve Bank President's job. More recently, though, you bankers from Alabama have gone about your business in such a competent fashion that we have heard very little from you. So, I am pleased to see you today, to praise you, and to offer some comments and suggestions which I hope may be useful.

Only five years ago, some of us in the Federal Reserve System were concerned with conjectures that banking in Alabama was showing signs of an inability to serve the public adequately. Moreover, Alabama banks were generally smaller than those in surrounding states. The state's largest banks were really only medium sized, and they were indeed few in number. Even those few, with one exception, could operate only in a single county.

Today, however, banking in your state is vastly different. As a whole, Alabama banks have more than twice the assets they had five years ago. The average bank has also doubled in deposit size; employs about 25 percent more personnel; and has one and a half times as many offices. Further, there are more than twenty new banks in the state, and several banking organizations there are comparable in size to the large organizations in neighboring states. Four of these operate state-wide, and the four largest each have assets well in excess of one billion dollars.

An increase in quality accompanied these increased quantities. Nonpar banking has been abolished. You apparently operate more conveniently for your customers than before, because relatively the number of banking offices in your state has increased considerably faster than the state's population.

Deposits are more equally spread among banks in most of your local markets than five years ago, despite the growth of large statewide organizations.

Your capital-asset ratios have fallen by less than those of banks in the United States as a whole or the rest of the Sixth Federal Reserve District.

More than other banks in the United States or the rest of the Sixth District, you have shifted assets from U. S. Government securities to loans and to state and local government securities. Yet, your loan losses have remained moderate, and your loan portfolios, as our examiners express it, are very "clean."

Alabama banking has not wholly changed, though, and you are to be congratulated for that. Bankers in your state, on the whole, kept their heads during the swing to "go-go" banking in the early 1970's. Your growth demonstrates that you took advantage of your opportunities, but you did not press your luck or overreach your skill. While in most of your neighboring states the proportion of assets committed by banks

to real estate loans was rising, this proportion in your banks remained nearly constant.

Your loan losses also rose less than those of your neighbors. Further, you depended less on Federal funds and large CD's for loanable funds. Clearly, all the evidence we have indicates that while you followed prudent banking practices, you kept alert to opportunities for advancement.

Some could say that because you had fewer opportunities in your state, your good record is a result of a perverse kind of good fortune. We do not agree entirely with that point of view. We do know that even the larger Alabama banks concentrated on banking expansion in their own backyards, so to speak; while those banks in states where opportunities abounded ranged far afield in terms of geography and nonbanking activities. The records of these banks speak for themselves. It may be that a lack of opportunity played a minor part in your good record; but it's major cause was prudent and sound judgment.

The results are here for all to see. Along with advancement, you have maintained relative stability. Alabama's banks have not staggered under the spectacular difficulties that have been the lot of a few banks in other states. Although there have been problems, you have been able to cope with them.

Here, let me say that we are aware that activities at the Federal Reserve Bank of Atlanta and in the Federal Reserve System, in general, directly influence some of you. Consequently, a few words about our

stance may be helpful.

In most matters of supervision and regulation, Federal Reserve Banks act within a general framework of goals, procedures, and oversight established by the Congress and the Board of Governors. We attempt to make most decisions at the Reserve Bank level without recourse to the administrative machinery at the Board of Governors.

In supervising banks and bank holding companies, we follow principles similar to those many of you have followed in recent years: approval of actions prudent and beneficial to the public and disapproval of actions that might lessen competition and endanger banking stability. Our efforts are directed toward balancing these objectives when they are in conflict.

In processing applications for expansion of banks, we take a close look at financial performance. Maintenance of sound, adequately capitalized banking subsidiaries is fundamental to holding company and bank management. Capitalization is still a prominent topic in the published opinions of the Board of Governors. Therefore, any applications for additional subsidiaries or activities are studied to determine their impact on the strength and flexibility of the parent company or bank.

Adequate equity capital support is required for future expansion. Loan losses, non-earning assets, and weak loan demand have eroded

and continue to erode the capital bases of many banks. Capital markets and possibly earnings will have to be tapped not only to replenish capital but to provide support for expanding operations. The issue of capital will become increasingly important in future applications for expansion.

A further concern which grows out of our responsibilities to the public is competition. Directions from Congress in the Bank Holding Company and Bank Merger Acts make it clear that we should not allow the diminution of competition through holding company acquisitions or bank mergers. The only instances in which the Federal Reserve may approve acquisitions or mergers that diminish competition are those that will avoid large costs to the public, such as in the saving of a failing bank.

Here, there are two related problems that concern us greatly. First, we allow little latitude for direct competitors interested in combining. The Board of Governors has denied only four applications for bank holding company acquisition in Alabama. A major concern of the Board in each of these cases was loss of direct competition if the applications were approved.

Second, we are mindful of our influence on the longer-term development of a state's banking structure. Our attention to this aspect of expansion has grown over the years. Thus, larger organizations that are likely to become competitors will have difficulty combining even if they do not compete now.

Almost fifteen years ago, a majority of the members of the Board of Governors expressed concern with state banking structure in a Florida case, and a similar concern about cases in Tennessee, Maryland, and Texas surfaced more recently. Too, on more than one occasion, a minority of Board members have voiced concern about Alabama's banking structure.

On the positive side, the Federal Reserve has favored combinations of noncompetitors and the extension of bank activities that strengthen banks or add to the quality and variety of banking services offered to the public. Over the past five years, the Federal Reserve has approved more than fifty Alabama holding company acquisitions in which these aspects were dominant.

We realize that you have not always agreed with every one of these approvals. Nevertheless, the evidence is clear that Alabama's smaller independent banks have remained competitive with the larger banks and bank holding companies.

I think it is likely that independent bankers make up the majority of this audience today. And I am sure that all of you--in holding companies and out--have had to work harder in recent years to satisfy your customers. You will have to keep on working hard if you are to keep your customers contented and meet your competition. Let me say that competition will come probably more and more from outside the

banking industry. Nonbank thrift institutions are moving through their regulators and through legislatures to add demand deposits and a broader potential assortment of assets.

Recent securities market innovations such as money market mutual funds and small-transactions markets for Government securities are competing for funds of medium-and large-sized depositors. Large nonbank lenders, particularly commercial finance mortgage, leasing, and factoring companies, are expanding the range of their services. Several of these have the backing of large banks. Some are already operating in Alabama.

Economic recovery came to Alabama earlier and has advanced further than in other Southeastern states. Only one state other than Alabama in the Southeast presently has more people employed than were employed before the recession began. With your sound condition, you are in an excellent position to help your state sustain this lead.

But you will not be able to stand pat. As an ex-country banker turned Federal Reserve Bank President, let me speak of some of the decisions you face. When you design lending policies, include objectives of soundness and liquidity, but do not neglect flexibility to meet the needs of your community, state, and nation. Lending for commercial and industrial development must be supported by consumer lending.

When you plan goals for asset mix, emphasize activities that can enhance economic development in your area. Participations in loans to national concerns and Federal funds sales have their attractions in maintaining liquidity or producing high yields. But some of these investments provide little stimulus for growth in your own region. On the other hand, dependence on Federal funds purchases and large CD's for loanable resources can be treacherous in certain circumstances.

Short- and long-term planning should fully consider the alternative strategies available to you. Planned growth enables an entire organization to react in support of the plan. For example, capital planning must include consideration of future positions required to support an expanded level of operations. Agricultural lending demands accompanying liquidity management to meet cyclical demands. Industrial needs for capacity expansion often require innovative bank financing if growth is to occur. Reforms of traditional lending practices for construction and mortgage loans should be considered as a response to recent experience with construction lending and to the impact of economic pressures on consumers.

Do not overlook technological advances in the transfer of funds. Development of electronic payments mechanisms is moving us toward a "less-checks" society if not a checkless society. Change has been slow, but the days are numbered when market expansion is synonymous

with buying bricks and mortar. A commitment to the development of electronics funds transfer systems is vital if a bank is to serve its customers and maintain its place among financial institutions.

These days, many bankers are acting as if "slow-slow" banking is the only alternative to "go-go" banking. Perhaps Federal regulators must share the blame for this. The regulators have emphasized prudence, urging that present operations be put into order. Their purpose is not to stifle but to remind bankers who may have gone out on a limb that they should turn cautious and get an overall view of their opportunities, responsibilities, and abilities.

Over the years, changes in banking have caused businesses, consumers, and governments to place increasing reliance on banks. Bankers have a vital role in financing the economic recovery now in process. We must not neglect this role, nor must we miss opportunities for the extension of new services to our communities. Fail in this and the recovery will be slower and the public will be poorly served.

In the future, we should act as bankers, on the whole, have acted in the past: practice prudence but welcome acceptable opportunities for advancement.