

ILLINOIS BANKERS ASSOCIATION

Chicago, Illinois  
June 13, 1995



**I. Introduction**

- A. Thank you, President Robert Wallace for the opportunity to speak today.
- B. Full schedule, interesting, important topics.
- C. As new president of Fed, I welcome opportunity. You probably won't believe me if I said I'm from the Fed and I'm here to help you. (smile) But it is true that I'm from the Fed and I'm asking for your help. I plan to meet with bankers on regular basis. Intend to continue contact to share ideas and concerns. We're all in very challenging industry and I feel we can all benefit from this kind of interaction.
- D. Early impressions of Fed, unique institution, part government, private sector and academia, good fit for me.
- E. As you know, the Fed has three principal responsibilities — financial services, economic research and monetary policy, and supervision and regulation.
  - 1. All work together toward the broad goal of maintaining a safe, flexible, and stable monetary and financial system.
  - 2. I would like briefly to discuss three topics that fall into each of the Fed's responsibilities:
    - a. New check facility we will open in Peoria
    - b. State of banking in Midwest and some changes taking place
    - c. Economic research initiatives we are undertaking that may be relevant to this audience

## II. New Check Processing Facility in Peoria

- A. Our mutual challenges are probably most evident in providing financial services. While the competition for providing these services presents a challenge for all of us, it also helps promote a sound, efficient payments system.
- B. A sound, efficient payments system is an important responsibility that complements our supervisory and monetary policy responsibilities.
- C. As provider of services, we're facing same problem as other providers: increased competition as a result of mergers and consolidations and the emergence of new providers.
- D. We're responding to these challenges as you are — with innovation and a focus on customer service.
- E. We're committed to high quality service and are providing it, as evidenced from a survey of our customers.
- F. We're excited about opening new facility in Peoria at the Regional Airport in September — the first Federal Reserve office to open in some twenty years.
  - 1. Represents our commitment to providing and improving services to customers in central Illinois.
  - 2. We worked closely with an advisory group of bankers to make sure products at the new office will meet the needs of our customers.
  - 3. High-tech check sorters and printer in Peoria driven by computers in Chicago help streamline operation and make more efficient.
  - 4. With state-of-the-art technology, close to your operations, we expect to maintain and even improve our high quality service at very competitive prices — in some cases as low as a penny a check.

## III. State of Banking and New CRA

- A. At Chicago Fed another of our responsibilities is to help foster a sound, stable, and effective banking system. To this end, we naturally monitor closely the state of banking in Seventh District, which includes northern two-thirds of Illinois. I would like to share some of this information with you this morning.
- B. Midwest as well as Illinois banks are doing well. Lending continues to rise; loan quality continues to improve, although some signs of relaxation in underwriting standards. For Illinois banks, nonperforming loans as a percentage of total loans first quarter 1995 was 1.80 percent, up from 1.12 percent at end-of-year 1994.
- C. Mergers and consolidations are continuing, reducing number of banks in five-states of Seventh District by about 100 last year. In Illinois the number of banks fell to 898 first quarter 1995 from 905 end-of-year 1994.

- D. Midwest banks' ROA declined in 1994 to 1.05, slightly below national average of 1.13. For Illinois banks, first quarter 1995 ROA was 0.98, up slightly from 0.82 end-of-year 1994. ROE for Illinois banks first quarter was 11.54 percent, again showing improvement from 10 percent end-of-year 1994.
- E. With continued concentration on asset growth, consolidation, quality lending, and new technological innovations, Illinois banks well positioned to thrive in an uncertain future filled with lots of change.
- F. One change that is of interest to all of us here is the new CRA regulations. I would like to comment briefly on the regulatory changes.
- G. With my experience at HUD, economic development important to me. From beginning Fed concerned about credit availability, then for rural areas. Now for low-and moderate-income neighborhoods in urban areas.
- H. New CRA not ideal, but is reasonable compromise. We share the same goal: results, not reports; loans, not lip service. CRA compliance should become less cumbersome, but CRA activity should not be seen as less important.
- I. CRA activity is not only the right thing to do, it can also be a safe, sound, and profitable business when conducted properly by banks knowledgeable about local markets.
- J. For CRA to succeed, it has to be profitable. Banks are not philanthropic institutions. CRA must meet test of market for long-term benefit desired. Therefore, CRA activities to meet credit needs in low-and moderate-income neighborhoods should be well-planned and thoughtfully implemented within an institution's overall business plan.

#### IV. Research Interests

- A. Changes taking place in the financial system leads directly to my third topic this morning — some of our emerging areas of emphasis in economic research at the Chicago Fed.
- B. In addition to research on current economic and banking conditions in our District, and monetary policy issues, we have for many years placed special emphasis on researching specific and timely issues related to the financial industry. We intend to continue this special focus and expand upon it.
- C. As many of you know, the Chicago Fed sponsors an internationally-renowned Conference on Bank Structure and Competition each year. This unique Conference brings together academics, regulators, and, importantly, practitioners to help promote research and dialogue about those issues that affect our industry.
- D. Some of the important issues we will emphasize include credit access, and risk control, specifically the use of financial derivatives.
- E. Regarding credit access, our research focuses on how best to assure that all communities have access to credit.

1. While fair lending obviously is a concern within the context of credit availability, the issue goes beyond questions related to discrimination.
    - a. We have already talked about CRA and community development.
  2. From our perspective a crucial question is — What role, if any, should the public sector play?
  3. Other important questions include: How do we achieve community development goals? Should a carrot or a stick approach be used? Perhaps a more fundamental question is — Are banks the appropriate medium to achieve these goals or might they better be achieved in less regulate bank subsidiaries (e.g. SBICs)?
  4. In general, the question comes to — What are the factors that contribute to successful community development within the context of sound and profitable lending?
  5. The research we are undertaking in these areas complements our community outreach efforts designed to foster strong partnerships among lenders, community groups, and other organizations interested in community development
- F. Regarding risk control and derivatives, there has been so much publicity, much of it emphasizing the riskiness of derivatives, that I hope we do not respond in a knee-jerk fashion and eliminate many of the benefits generated by these markets.
1. Instead, I hope we can arrive at an effective, workable solution for managing risk in financial markets.
  2. Worth noting that Chicago exchanges have arrangements to manage risk which have proven to be successful.
    - a. Exchanges are providing leadership.
    - b. Exchange process stresses self-regulation.
- G. In both credit access and risk control, the Chicago Fed intends to play a prominent role and hopefully provide information and analysis of use and interest to you.

## V. Conclusion

- A. Thank you for opportunity to meet with you today. We're all involved in dynamic industry facing many of the same challenges.
- B. One of the great strengths of the decentralized Fed System is that it facilitates the flow of information and ideas. I look forward to many more opportunities to meet with you, exchange ideas, and discuss some of our mutual challenges.