

Outline for Jerry Jordan's presentation
to Leadership Cleveland
1/12/93

I INTRODUCTION

Thank you, Peter, for that kind introduction. It is a pleasure to take part in today's program.

It is especially important for a city that is at the heart of one of the nation's great metropolitan regions to have well informed leaders who are committed to improving the quality of life for area residents.

Despite our problems, it's worth noting that compared to other parts of the country, both Ohio and the Cleveland region remain rich and prosperous. Between 1986 and the second quarter of 1992, personal income in Ohio grew by 6.1 percent, fastest in the Great Lakes region and well above the national increase of 4.7 percent. Per capita personal income for the Cleveland area is five percent greater than the national average. The area ranks 45th nationally in total personal income, and first in the state.

We have restored the competitiveness of manufacturing by cutting costs and investing in new equipment and technology. Consequently, we are no longer in decline relative to the rest of the country.

What I would like to talk about today is the important role banking plays in the region's economy, and discuss what sources of capital are available for future economic growth in northeast Ohio.

II Banking and the regional economy.

A) Before starting, it may be helpful to clarify the links between banking strength and a region's economy.

B) A bank's primary function is intermediation, that is, pooling funds and channeling them from savers to borrowers. Banks have developed a comparative advantage in evaluating and monitoring loans to certain categories of borrowers, especially households and small businesses. Sound and efficient banks are able to perform this intermediation function and thereby bolster regional prosperity by providing credit to creditworthy borrowers for sensible projects and purchases.

C) Put another way, banks which are on solid financial footing are better able to finance growth in their home region.

1) By the same token, weakened banks often are reluctant to lend, even to borrowers formerly deemed creditworthy, thereby crippling a region's economy.

2) We've seen this interaction at work recently in areas such as New England, where the weakness of banks has slowed the region's recovery.

III Strength of our region's banks.

A) With that as background, let's take a look at this area's banks.

B) I'm pleased to say that we in the Fourth Federal Reserve District, which encompasses all of Ohio, the western portion of Pennsylvania including Pittsburgh, the eastern portion of Kentucky including Lexington, and the panhandle of West Virginia, have headquartered here some of the strongest banks in the country.

1) If I may interject a personal note, one of the reasons I accepted this position as president of the Fourth District was the strength of banks in the District.

C) Let me share with you a few statistics:

1) Return On Assets -- considered one of most important measurements of a bank's strength, since it measures its earnings as a percentage of its assets.

a) Through first nine months of 1992, ROA for banks nationwide averaged 1.18 percent. For Fourth District banks was 1.37 percent.

b) For banks in Cleveland metropolitan area, ratio was even better. Through first three quarters of 1992 they reported a 1.77 percent ROA, versus for the nation.

2) Asset quality -- measured by what percentage of a bank's

loans have been written off as uncollectible, and what percentage are overdue.

a) Nationally, through the first ^{five} ~~nine~~ months of last year, banks had written off ^{1.11} percent of their loan portfolios, while another ^{3.45} percent of their loans were overdue.

b) In the Cleveland metropolitan region, through September 30, banks had written off only .96 percent of their loans, while 2.63 percent of their loans were delinquent.

3) Market capitalization -- how much a bank is worth as measured by the market value of its shares outstanding.

a) Through the third quarter of 1992, two of the top 20 banks in country were based in Cleveland, three were

headquartered in Ohio, and four are in the Fourth District, as were seven out of the top 50.

4) The aggregate capital of Bank Holding Companies headquartered in Ohio was approximately \$17 billion, and for the Fourth District was \$30 billion, second highest in the nation.

5) Capital ratio -- ratio of banks capital to its total assets, an internationally agreed upon measurement of banking strength.

a) For Ohio banks is 7.85 percent, versus 7.23% for nation.

IV Geographic expansion.

A) The strength of the area's banks has enabled them to expand their

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B) Being a financial center is something new to this region, which traditionally has been better known for its manufacturing capabilities.

1) The change has not gone unnoticed. I'd like to share with you something I came across in The Wall Street Journal. An

article in the December 22nd edition was discussing banking in the midwest. It contained this quote from a financial analyst with the New York investment bank Morgan Stanley: "If anybody

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would have postulated 20 years ago that Ohio would be the center of where banks would expand from they'd have been laughed at."

C) Today, no one is laughing.

1) The Fourth District is home to several so-called superregional banks -- banks with at least \$20 billion in assets and significant operations outside their home state.

a) Among them are two Cleveland banks, Society and National City Bank.

2) About 10 percent of all banking assets in the country are controlled by institutions headquartered in the Fourth District, up from six percent just five years ago.

a) Included in that figure are more than 40 percent of Indiana's assets, about 34 percent of Arizona's and 11 percent of Texas's and Wisconsin's.

V Reasons for strength of area banks.

A) No magic to it.

1) Continued adherence to sound banking principles.

2) Fewer loans for real estate development, or collateralized by commercial real estate, so when that

market slumped, banks here were not faced with same degree of nonperforming loans or loan writeoffs.

B) Whatever the reason, there seems little doubt that banks here are well positioned to be sources of capital for fueling economic growth.

VI Other sources of capital

A) Banks are not the only sources of capital available, however.

B) In fact, banks have been declining as a source of financing.

1) Nationwide, commercial banks' share of nonfinancial credit fell from 32.8 percent in 1980 to 25.1 percent in mid-1992.

a) No specific data for northeastern Ohio or Fourth District, but no reason to assume pattern is different here than elsewhere.

2) Banks role as intermediators for pooling and channeling funds being replaced by a wide variety of institutions, financing instruments.

a) So-called nonbanks, such as financing divisions of large corporations.

(1)GE Financial Services' commercial loan portfolio is second in size only to Citibank's.

b) Securitization -- the process of creating tradable assets by bundling together smaller loans, such as car loans or home mortgage loans.

c) Commercial paper -- corporations issuing their own IOU's.

3) Start-up and fledgling companies can turn to venture capital funds for financing.

a) Northeast Ohio home to several, including Primus Fund, an offshoot of Cleveland Tomorrow, and Morgenthaler Ventures.

4) Finally, there are financial institutions and instruments which have been in existence for a long time, but in recent years have become important sources of business capital.

a) Finance companies, insurance companies, private placements.

VII Conclusion

A) Ohio and the Fourth District are fortunate to be home to some of the nation's strongest and best-managed banks.

B) Capital availability is a necessary but not sufficient condition for regional growth. Other attributes, such as strong, imaginative leadership in both the public and private sectors, high quality schools, colleges, and universities, and a skilled labor force are also important.

C) Using these criteria, I believe northeast Ohio's prospects are bright indeed.