

The New CRA: Sustaining Our Communities  
Mark Hopkins Hotel, San Francisco  
For delivery December 1, 1995, 8:15 AM PST

I. Good morning. I'm Bob Parry, President of the Federal Reserve Bank of San Francisco.

A. Before I begin my remarks this morning, I'd like to take a moment to welcome all of you here on behalf of the Bank.

1. We're delighted to be co-sponsoring this conference with the Federal Home Loan Bank of San Francisco,

2. and we're very pleased to have so many people of national prominence come to speak to us over these three days.

II. I know you had some very interesting sessions yesterday, and I want to kick things off today with a slight variation on the conference theme of "sustaining our communities."

A. Instead of discussing changes in the new CRA,

1. I want to consider another change in banking\_

2. \_one that could have a substantial impact on our communities\_

3. \_and that's the trend toward consolidation in banking.

B. Since the mid-1980s, we've seen the number of banks in the U.S. drop by almost 30 percent.

C. Now here we are in the mid-1990s, and this trend still has plenty of momentum.

1. In the first half of this year alone, there were some 156 mergers.

2. As for the future, I think we can look to California for some insight,

a. since it's such a large state and since it has statewide branching.

b. Extrapolating from California's experience suggests that eventually we could see the number of banks nationally drop by another 50 percent or so.

c. Of course, this would still leave us with thousands of institutions, including a large number of small and mid-size independent banks.

D. In large part, consolidation has meant that small and mid-size banks get absorbed into larger institutions.

1. But more and more, so-called "mega-mergers" have grabbed the headlines.

2. We've all seen the names of banking giants splashed across the business pages\_

a. \_Chemical merges with Chase\_

b. \_First Union with First Fidelity\_

c. \_Wells Fargo and First Bank vie to acquire First Interstate.

III. What's behind this consolidation trend?

A. One factor clearly is deregulation.

1. It has removed many of the artificial barriers to geographic expansion that banks used to face.

B. Another factor is technological change.

1. In addition to re-enforcing the consolidation trend, it also underlies the innovations in bank delivery systems.

C. For example,

1. not only are we seeing fewer banks,

a. but we're also seeing less emphasis on "brick-and-mortar."

2. Instead, what we're seeing more of is

a. limited service offices,

b. automated tellers,

c. and other dimensions of electronic banking.

IV. All of this is the predictable adjustment to a more natural banking structure.

A. One advantage of this new structure is that it holds the promise of greater diversification of risk.

1. For example, there's ample opportunity for banks to reduce the variability of their earnings by operating across state lines.

a. And, according to research done at our Bank, that's true, even if the state lines they cross are all out here in the West.

2. From a public policy perspective, this could mean less risk exposure for the deposit insurance system and ultimately the taxpayer.

B. Another advantage of this more natural banking structure is that allowing banks to operate over broader geographic areas should lead to a more efficient distribution of banking services.

C. The advantages in terms of costs, interestingly enough, aren't all that clear from the research that's been done so far.

1. For example, empirical studies find a wide variation in cost efficiency among banks.

a. So that means that mergers of the right banks—that is, high-cost banks with low-cost banks—could mean substantial cost savings.

b. But while some studies show that a large number of mergers have led to lower costs for the consolidated bank,

c. others have resulted in higher costs.

d. So, on balance, the evidence has turned out to be inconclusive.

2. Other studies, though, point out that the effects on costs may be only half the story.

a. Mergers may be a way for consolidated institutions to alter their mix of services, dropping less profitable services and focusing resources on what they do best.

b. They also may allow consolidated institutions to offer a wider variety of services to a broader customer base.

D. In short, bank consolidation appears to be market-driven,

1. and that should mean a more efficient banking system.

V. While further consolidation in the industry as a whole appears to be inevitable, individual bank merger applications still need to be scrutinized carefully.

A. And we take this responsibility very seriously.

1. For example, in every merger application we handle, we conduct a careful analysis of the impact on competition.

a. This involves calculating the combined institution's market share in every community it serves.

b. And on the basis of this analysis, you should know that we sometimes require banks to divest branches.

c. So far, our efforts have been effective in maintaining competition in local banking markets, and this will continue to be a top priority.

2. In addition, we analyze the institutions' financial and managerial factors, as well as any legal issues.

B. Of course, the most germane issue for this conference is our review in terms of "convenience and needs" of the affected communities.

VI. So I want to give you some flavor for how this issue comes into play when the Fed evaluates applications for bank mergers and acquisitions.

A. When reviewing the "convenience and needs" issues, we look at both

1. the CRA performance of the institutions involved in the application

2. and at all comments received from other parties.

B. Sometimes, as in the case of the Bank of America/Security Pacific merger in 1992, the Fed holds a public meeting to collect comments on the CRA performance of the institutions.

1. Another example is the Fleet-Shawmut merger.

a. In this case, the Fed responded to community concerns by requiring Fleet to report quarterly on the economic impact of any planned branch closings.

C. In some other cases, the applicant bank has given us statements indicating

1. how it intends to improve its performance,

2. or how it intends to meet specific banking needs,

3. or how it plans to serve its new market effectively.

D. These statements often have become conditions for approval of merger applications.

1. When that happens, the Fed plays an ongoing role by monitoring the bank's performance in meeting those commitments or conditions.

E. This is all to let you know

1. that we're very careful in our analysis,
2. that we're concerned about the impact of bank mergers on communities,
3. and that we do take all of the comments we receive very seriously.

VII. Now let me turn to the new CRA regulation. I believe this new approach will result in some positive changes.

A. To begin with, the focus on lending performance, instead of on process, holds promise.

1. It will help ease some of the burdensome features of the regulation,
2. and it keeps the focus on getting safe and sound loans into the communities.

B. In addition, the new regulation is beneficial for the smaller banks, which will be subject only to a streamlined examination.

1. I understand the specifics of the small bank exam were covered in detail in a breakout session yesterday.

C. And the larger banks will find the strategic plan option in the regulation very helpful. It affords them an opportunity

1. to define their own CRA policies and performance level
2. and to know exactly how their performance will be measured.

3. The strategic plan option will be covered in detail in a breakout session later this morning.

D. In general, I think the regulation will result in banks focusing more on the lending, service, and investment needs of their markets,

1. and that, in turn, will benefit the communities.

VIII. Turning to today's agenda, it looks like we have quite a line-up for you.

A. We have a panel of regulators up next to answer all your CRA questions.

1. Our moderator for the panel is John Taylor, Executive Director of the National Community Reinvestment Coalition.

B. Following the panel are more breakout sessions.

C. Immediately after lunch you'll have a chance to hear from Dave Coulter, the new Chairman of BankAmerica Corporation\_

1. \_I'm sure we're all very interested in hearing about his vision for the future.

D. Following Dave, we have Assistant Attorney General Deval Patrick to talk about the Justice Department's stance on fair lending issues.

1. \_All in all, a very stimulating day.

IX. Before I go, let me just say welcome once again, and thank you for being here.

A. And let me give thanks also to Jim Yacenda and all our friends at the Federal Home Loan Bank for co-sponsoring the conference.