

Remarks by
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I've been Comptroller for about ten weeks now, and I must say that it's been an enlightening and humbling experience. The OCC is blessed with an impressive staff of professionals, and, as I listen to their presentations on various regulatory issues, I can't help but recall words attributed to the great historian Will Durant when he was well into his eighties. "Sixty years ago," he said, "I knew everything, but now I know nothing."

Durant viewed education as "the progressive discovery of our own ignorance." With that in mind, I've always recognized that it was better to listen first and figure out how much I had to learn before venturing out to speak and letting the world in on it. But, although my education is by no means complete -- and never will be -- I believe that it's important to speak out now on issues of concern to us all.

As many of you know, I don't come to the job of Comptroller as a novice to the banking business. I've spent more years than I care to count as a banking lawyer, law school professor, bank regulator, and, most recently, as a senior member of Secretary Rubin's team at the Treasury Department, with special responsibility for domestic issues. Over these many years, a number of banking subjects have been particularly near and dear to me -- and none more so than what brings you here to Orlando: your role -- your critical role -- as the community bankers of America.

The basic role that you play hasn't changed appreciably since I was a boy. I clearly remember walking into a bank in my home town on Long Island to open my first Christmas Club account with my earnings from shoveling snow. They seemed genuinely happy to have me as a customer.

That experience was the start of my education in banking. It continued through three decades of law practice that involved both large and small banks. And the lesson I learned over time was that banks are not just about loans and deposits. They're crucial to the social fabric of a community as well as its economy. They help transmit shared values: the values of thrift and industry, permanence and stability, and service to the community. They teach us through example that doing the best we can for ourselves and our families requires the financial and moral support of the community behind us.

Many things have changed in my old home town. When I was growing up, three or four banks, all locally-owned, served a population of around 25,000. The executives who ran the banks were the leaders of our community.

After leaving the bank for the day, they assumed many other important roles -- as library board members or church trustees, Scoutmasters or community fund raisers. Home office protection and

restrictive branching laws preserved the local character of banking. Our corner of the world was safe and secure.

Today, this town is still home to 25,000 people. Now, ten banks do business there. But none of these banks is locally owned. One is a subsidiary of a holding company located in Rhode Island, three states away. Five others are branches of banks headquartered in New York City -- only 25 miles distant, but a world apart in many respects.

I'm sure that these banks compete vigorously with one another, offering their customers all sorts of new products and services. I'm sure that the bank's managers and employees give generously of themselves to the community after hours. But I wonder whether my Christmas Club account would be welcomed as warmly today as it was 50 years ago.

Analysts used to scoff at the large number of independent banks in the United States compared to other industrialized countries. The difference ran literally into the tens of thousands during the heyday of unit banking back in the 1920s. It wasn't unheard of for towns of 200 or 300 people to be home to two or more locally-owned banks.

Certainly, from a purely economic standpoint, that structure left a lot to be desired in terms of efficiency and often stability. Many of these small, thinly-capitalized institutions proved unable to withstand even minor economic shocks. That's when some people really came to appreciate their banks and the importance of their contributions -- when they were gone. Some of these towns never did recover.

We've come a long way since then. The U.S. banking system has become more rational and coherent -- or so some would say. From more than 22,000 commercial banks in 1922, we're down to perhaps 9,000 today, despite our vast gains in population, geographic dispersion, and economic output over that period.

Not many people predicted how rapidly this consolidation would occur, especially in recent years. I certainly didn't. Still, despite this rapid consolidation, the United States still boasts many more banks than the second-place country, Germany. This is not the result of the size of our economy or population. Rather, it's the outgrowth of our communities' enduring dependence on the tangible -- and intangible -- products and services that independent banks have traditionally excelled at providing.

And, by all accounts, you're doing a better job of providing those services than ever before. If community banks were once a source of vulnerability in our financial structure, that couldn't be less true today. You've turned your natural advantages into assets.

You -- who know your customers by their first names -- are well positioned to satisfy their financial needs and wants. You -- who have your ear to the ground -- are in a position to respond to changing local business conditions before the news has flashed on your competitors' computer screens perhaps hundreds of miles away. No cumbersome, impersonal banking bureaucracy can compare with what you can do when it comes to delivering the products and services your customers want, when they want it.

That's why community banks have been particularly successful in the small business loan market -- more successful, apparently, than big banks or, indeed, any other class of financial provider. You bring the attributes small business people seek in a financial provider: local ownership, quick decision-making, accessible senior management, outstanding service, and intimate understanding of their business and their markets. And you continue to build on these attributes to create important new growth markets in agricultural, commercial, and residential real estate lending.

The numbers reflect your success. Last year, community banks earned a higher return on assets than either megabanks or the commercial banking industry as a whole. The average capital ratio for community banks was over 11 percent, compared to eight and a half percent for the industry at large.

Non-interest income -- a safeguard against over-dependence on loans -- has increased significantly, as new fee-generating products and services are introduced. And community banks are making tremendous strides in improving their efficiency ratios, so that you can keep more of the income you earn and continue to compete effectively against larger financial institutions. These performance measures speak volumes about your skill and acumen.

Still, you face major hurdles today and into the foreseeable future. Some of these are common to the industry, others unique to community banks. For example, while I know the value that you add to your customers and communities, and you know it, some of them may not know.

But they should. It's vitally important that you get the recognition you deserve for all that you do. Customer service -- which really means being sensitive to the way your institution is perceived by your customers -- is an area where community banks have a natural and strong advantage over their multimarket competitors.

Some of the challenges you face are the offspring of your own success. You can't take too much for granted: your best customers can very easily become someone else's. That's especially true in the small business market, where nonbanks are aggressive competitors.

Accordingly, some analysts are predicting lagging earnings growth for community banks, as competition for new loans erodes margins and market share, and more loans find their way into the problem loan category. And it's a creative and dextrous banker indeed who can achieve continued savings in overhead without also undermining the service quality so important to your customers.

I know that liquidity and a dwindling deposit base are concerns that keep you up at night. They should. To sustain current loan volume, new funding sources must be identified as traditional sources increasingly dry up. That's why the Administration has supported broader access for community banks to the resources of the Federal Home Loan Bank System, as part of a broader reform of the system.

Technology poses challenges all its own: what's the right mix of automation and personal service? How best to cope with competition over the Internet? And, most urgent of all, will you and your information systems be ready for the century date change -- Y2K?

As if the marketplace weren't making your lives interesting enough, Washington keeps throwing new complications at you. One bright idea that recently came out of D.C. is the proposed Federal requirement that you adopt policies and programs to Know Your Customer. The banking agencies are still in the process of receiving comments on this proposal. But I ask you: Do the community bankers of America really need new Federal regulations telling you to know who your customers are -- something you already do better than anyone else in the business?

I also suspect that doubt has crossed your minds as to whether the financial modernization debate in Congress last year and the debate already underway again this year is really worth getting exercised about. I know how strong the temptation must be to write off the whole show as just another piece of political theater, of little serious consequence to your institution's day-to-day health and the financial welfare of your customers.

It would be easy to ignore this debate. But it would also be a major mistake. Once in a blue moon, Congress has an opportunity to fundamentally reshape key sections of our national landscape. This is one of those rare occasions. Today's financial marketplace is governed by laws written more than 60 years ago. It might be another 60 before the occasion for fundamental reform arises again. I think you'll agree that, for that reason alone, it behooves everyone with a stake in the outcome to follow the debate carefully. And no one has a bigger stake in the outcome than the community bankers of America.

It's no exaggeration to say that the legislation now under consideration in Congress could profoundly affect your future, one way or the other. Much has been said about specific provisions of that legislation, and, in a moment, I'll add a few words of my own. But it's imperative that we not lose sight of what the broader impact of the proposed legislation could be if it were enacted.

In my view, it could really mark a turning point in the way financial services are provided in this country. It holds the potential that banks will be diminished as financial services providers and replaced with holding companies made up of separate, specialized product providers. It could signal the end of the era of the full-service, integrated financial provider.

In particular, if the legislation mandates a rigid, "one size fits all" format in order to take advantage of new opportunities, banks would be denied the flexibility they need -- today more than ever -- to compete successfully in the financial marketplace. Such constraints would inevitably weaken our banks, as bank resources were upstreamed to fund holding company ventures and bank earnings opportunities were diverted to holding company affiliates.

I must say, I find it inexplicable that any agency charged with safeguarding the safety and soundness of banks, would insist on a rigid, holding-company-only format, that would deprive banks of the opportunity to diversify their earnings and would force resources out of banks to fund new activities in holding companies.

In short, depending on how it's structured, financial modernization could usher in a new era of prosperity -- or one of prolonged marginalization -- for community banks. All this -- and more -- is riding on the outcome of this debate.

Unfortunately, in my view, this year's version of H.R. 10 contains many of the defects that were present in last year's legislation. If the current version is enacted into law in anything like its present form, I'm convinced that the results will not be helpful to community banks.

Let me give you an example of what I mean. One reason banks are relatively healthy these days is that they have eagerly embraced new techniques for controlling risk and diversifying income. In general, loan portfolios are better balanced among types of loan products and some whole categories of loans have been pushed off the books entirely through securitization.

Just as important, as I mentioned earlier, non-interest income has been rising steadily as a percentage of total revenues over the past 15 years, with especially dramatic gains registered over the past five. Banks today derive significant revenues from selling various types of financial products and from such activities as investment advice, asset management, and data processing. This fact reflects the clear recognition on the part of bank managers of the importance of diversifying earnings flows.

One of the products that all customers need and want is insurance. The opportunity to sell insurance is frequently a natural outgrowth of a bank's day-to-day banking activity. And you should be able to offer those products without unreasonable burdens. The sale of insurance as an agent has little or no financial risk attached to it and does not require significant capital. Few analysts doubt that insurance sales can make an important contribution to a bank's revenue stream and thereby advance the industry's general safety and soundness.

Community banks particularly stand to benefit. So do your customers. Studies show that most Americans are seriously underinsured. Lowering the cost of insurance through increased competition in the sale of insurance products is one of the best ways I can think of to help American families obtain the coverage they need. Moreover, using modern and efficient delivery techniques, banks can improve access to insurance products for segments of the market that have long been underserved or even ignored in the past by the traditional, labor-intensive system of independent agent delivery.

Of course, none of these advantages will come to pass unless banks are permitted to compete freely and fairly with other insurance providers. But H.R. 10 raises so many obstacles, and presents so many opportunities for controversy and litigation, that it's hard to see how these provisions square with any reasonable concept of financial modernization.

Let me give you just a few examples.

H.R. 10 would permanently restrict the ability of banks and bank subsidiaries to offer insurance in a principal capacity to those products already approved by the OCC prior to January 1, 1997. This means not only that banks could never become innovators of insurance products, but it also means that their ability to offer innovative banking products that may have some insurance elements in them could be severely curtailed. Indeed, under this provision, banks could not

even take advantage of innovations introduced by others.

Some of you work with banks in communities of fewer than 5000 people. If you do, and yours is a national bank, H.R. 10 would not take away the right you have under present law to sell insurance products directly to your customers. But if you're in a community larger than 5,000, then all bets are off: H.R. 10 would require you to form a holding company or subsidiary to conduct insurance activities.

Is that really financial modernization? I don't think so.

Finally, there is this item. While H.R. 10 upholds the right of banks to sell insurance without interference from the states in principle, it then proceeds to undermine that principle by setting out 13 areas in which states may discriminate with impunity against bank insurance sales. They include advertising, licensing, disclosure, and much more. Any state that was intent on burdening insurance sales by banks in order to preserve competitive advantages for nonbank sellers of insurance would be given virtually free rein to do so if H.R. 10 were to become law. That would be bad for competition, bad for communities, and bad for consumers.

While the handful of very large banks who negotiated this language may have the resources to defend their positions in lengthy and costly litigation, community banks clearly don't. No bill with such potential to impede the fulfillment of your historic responsibilities can be good for America.

How well you would fare under its provisions should be an important test of any financial modernization legislation. In its present incarnation, H.R. 10 does not pass the test. It's time to put our heads together and our parochial interests aside to come up with one that does.

By taking these steps now, we can ensure that community banks continue to play their critical role in our nation's economic and social life. Genuine financial modernization legislation will safeguard a more secure future for you and your customers. I look forward to working with all concerned parties to that end.

Thank you.□