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Remarks by

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Good morning and welcome to the Conference on Antitrust and Banking. The Office of the Comptroller of the Currency is pleased to host this timely reexamination of the role of antitrust in banking.

The wave of bank mergers we've experienced the past several years has generally been hailed on Wall Street, where analysts applaud the prospect of economies of scale and scope created by consolidation. On Main Street, the same phenomenon is viewed with some trepidation. Americans' traditional distrust of all things big raises concerns about how smaller markets and small business customers will be served in a future with fewer, and considerably larger, banks.

Here in Washington, regulators and policy makers have the responsibility to examine the public policy issues raised by 1995's bank mergers: What are the overall competitive effects? Are there significant consumer benefits? What are the safety and soundness implications?

Different groups have different ways of raising these basic concerns. Bank customers are asking "Are these new banking behemoths going to be too big to serve me in the way I want?" Consumer advocates ask, "Are they getting so big as to stifle competition in the local markets in which they operate?" And regulators must ask, "How do we supervise these larger institutions -- with their new and sometimes different risks -- to ensure safety and soundness?"

Are the public's concerns are justified? Certainly they are nothing new. Throughout the history of our country, Americans have expressed reservations whenever they've seen a concentration of resources in the hands of a few large businesses within an industry. Because we all know the benefits of competition, we can understand why the public fears the power of a dominant market player with unbridled economic and political prowess.

The Sherman Act of 1890 and the Clayton Act of 1914 are evidence of a national commitment -- a quintessentially American commitment -- to a policy of preventing monopoly and

fostering competition. As Emanuel Celler, Chairman of the Antitrust Subcommittee of the House Judiciary Committee, wrote in 1965, "Antitrust principles are a peculiarly American instrument for the promotion and preservation of competition in free markets."

In the banking area, the Bank Holding Company Act of 1956 and the Bank Merger Act of 1960 gave federal bank regulatory agencies power to restrict anticompetitive mergers. Three years after the Bank Merger Act -- in 1963 -- the Supreme Court held in the Philadelphia National Bank decision that, contrary to the prevailing conventional wisdom, bank mergers were subject to Section 7 of the Clayton Act. The Court went on to argue that preventing concentration was even more critical in regulated industries such as banking where entry was more controlled than it is in other industries. While making it clear that banking was subject to the antitrust laws, the decision failed to anticipate the evolution of financial services and the fact that banking would be increasingly confronted with nonbank competitors who enjoyed relatively unrestrained access to the market and could develop specialized expertise in one or two areas of the financial services universe.

Unlike 35 years ago, there are now nonbank competitors for nearly all commercial bank services. Today, it is hard to identify market segments where banks maintain a clear competitive advantage, except, perhaps in small business lending -- in the form of lower information costs -- and in retail deposits -- in the form of federal deposit insurance. And the latter advantage is shared with other depository institutions. Indeed, one could argue that only bank innovativeness in entering new markets such as those for derivatives and various financial guarantees such as standby letters of credit has allowed them to remain major players in financial markets.

I believe that the lowering of geographical barriers -- which, by broadening local markets, has given the country a less balkanized banking system -- together with increased nonbank competition means that mergers are less anticompetitive today than they would have been in the past. Perhaps the larger question -- but one largely unasked in the wake of merger announcements -- is whether, given the reach of modern technology, disappearing barriers to interstate banking, and the explosion of nonbank financial services providers, it is even possible for a single bank to gain monopoly control of financial services in a given market?

Despite the common confusion of absolute size with size relative to the market, high concentration that leads to anticompetitive effects is more likely to result from mergers in small towns and rural areas -- where the number and average size of competitors is small -- than from megamergers of institutions serving large metropolitan markets or diverse regional economies. And in those instances, the market for small business lending is likely to be most damaged by a merger

that eliminates a bank competitor. So attention should be paid to the competitive effects of mergers in highly concentrated local markets. But while the focus in judging the effects of potential mergers has been on the "most damaged market," it is not clear that a merger that strengthens competition in most of the markets in which a bank competes should be denied because of anticompetitive effects in a single market. At the very least, the issue should be revisited. Particularly in light of recent studies that have suggested that large banks and banks headquartered in other states are as willing as local banks to lend to small business.

Let's now consider the consumer benefits touted when bank mergers are announced and Wall Street weighs in with its seal of approval.

The basic justification of mergers has been economies of scale or improvement in efficiency. In these cases, we're told that consumers, shareholders, and employees will reap across-the-board benefits from the lower operating costs. Consumers are promised benefits in the form of better service at lower prices. Shareholders hope to see higher profits and garner larger dividends. And the spin for employees is that although bank mergers may result in some layoffs -- as is true of most organizational changes that improve efficiency -- remaining employees may find greater career opportunities in a stronger and more stable institution.

But while mergers create opportunities for economies, they don't guarantee them. In fact, the evidence on benefits in this regard is extremely mixed. Some studies suggest only weak support for mergers, and little research has been done on the effects of prices and services to consumers. Further, experience has shown that economies of scale top out at about $100 million in assets for retail banks.

Consumer benefits are inversely related -- in many cases -- to the level of concentration in the markets in which the merged bank competes. Mergers between banks in the same local market may simultaneously enable banks to improve productive efficiency and, by increasing concentration and facilitating tacit collusion in the market, prevent consumers from enjoying the benefits of that improved efficiency. Indeed, those mergers promising the most efficiency are arguably the most anticompetitive because they involve banks in the same local markets. The resulting increases in bank concentration tend to raise prices to customers, and the closing of overlapping branches, while lowering the merged bank's costs, also reduces customer convenience and eliminates alternatives. Again, the negative effects would be greatest in areas that have experienced less penetration by nonbank providers of financial services.

To date, at least, the ongoing consolidation movement in U.S. banking does not seem to have led to dangerous levels of concentration. Some data assembled recently by Dan Nolle of the OCC's Bank Research Division tell what has been happening

at the national level.

It is true that nationwide concentration has increased considerably over the past decade -- the percentage of total assets accounted for by the largest 100 banking organizations rose from 63 percent in 1985 to 75 percent in early 1995 -- and the number of banking organizations declined from nearly 11,000 to around 7,900 over the same period. But these numbers also show that the U.S. banking system still remains by far the least concentrated in the world. In any case, it is generally recognized that concentration at the national level provides little information on the competitiveness of local markets, which are most relevant to consumers and small businesses.

Some data from a recent paper by Stephen Rhoades at the Federal Reserve Board may help to put the effects of the recent mergers on local markets in better perspective. Measured by the share of deposits held by the three largest banks in the market, average concentration in Metropolitan Statistical Areas barely increased between 1985 and 1994, from 67.4 percent to 68.3 percent; by some measures it actually declined. Nonmetropolitan counties experienced declines in concentration by both measures. Despite the newsworthiness of the recent megamergers, this is hardly the picture of a banking system becoming highly concentrated overnight.

Nonetheless, in assessing the impact of these mergers on competition and their realized and potential benefits to consumers, it is worth noting the regional interstate banking compacts of the early 1980s, which initially permitted interstate acquisitions only within a particular region. The result was to encourage mergers of the largest banks within each region of the country, resulting in increased concentration at the regional level. Although few studies have looked at this question, it is conceivable that the benefits to consumers may have been smaller than if we had moved directly to nationwide banking.

Conceptually at least, one would expect greater benefits when banking organizations acquire banks in other regions -- facilitating the interpenetration of markets -- than when they merge with other large institutions in the same region. At the very least, it is worth investigating the impact of mergers on customers who are large enough not to be entirely dependent on banks in the local market but not large enough to enjoy nationwide alternatives.

I have never counted myself among those who feel that mergers spell the end of community banking and the benefits consumers enjoy from dealing with a small bank around the corner. The survival and continued chartering of small banks suggest they are serving special niches and can compete effectively with their larger brethren. While the future probably will bring more large, complex multistate companies to banking, we must continue to support America's tradition of small entrepreneurial financial institutions and make sure this segment of the financial services sector remains a vigorous

one.

And finally, what are the supervisory implications of bank mergers? I want to emphasize that the thought of a financial services system with larger institutions does not trouble me from a safety and soundness standpoint -- so long as we are able to regulate them effectively. In general, mergers produce larger and more diversified organizations that are less vulnerable to failure. But critics have suggested that mergers also create more banks that might be seen as being too-big-to-fail, despite the restrictions on that policy in FDICIA, because there is always strong pressure for government intervention to keep large banks afloat. Again -- while I may not personally agree with this suggestion -- this is a topic worthy of further discussion.

With few exceptions, the merger applications filed with the OCC over the last several years have raised neither substantive competitive nor supervisory concerns. In keeping with our continuing quest to reduce the unnecessary regulatory burden on banks, we've developed a simplified application tool for assessing the competitive effects of bank mergers, which we recently clarified in collaboration with the Department of Justice.

Today's conference gives us the opportunity to explore the issues raised by bank mergers from a variety of angles and in greater depth than I've covered this morning. Gary Whalen, with the help of other members of the Bank Research Division, has done an outstanding job of organizing the conference. I am also grateful to our current Visiting Scholar, Bernie Shull -- an economist at the OCC under James Saxon in the early 1960s who spent a number of years at the Federal Reserve Board and built a distinguished career as an academic before coming home for a visit this year -- for his help in planning the conference.

They've been instrumental in assembling a high-powered lineup of industry leaders, key policy makers and renowned scholars who have offered to share their insight and whose presentations will -- I'm certain -- stimulate lively discussion and much for us to consider. I'll be back later to moderate the day's final panel discussion. Until then, I encourage you to take advantage of this conference and I thank you again for joining us today.

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