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Comptroller Hawke Highlights Strong Commitment
Community Banks Have Made to Risk Management

WASHINGTON -- Comptroller of the Currency John D. Hawke, Jr. today highlighted the strong commitment community banks have made to risk management, citing examples of practices that he said exemplify risk management at its best.

"What we see -- encouragingly -- is that community bankers are working hard to manage risk by educating their customers in better ways to manage theirs," he said in a speech to a risk-management conference sponsored by the Federal Financial Institutions Examination Council.

"For example, some agricultural banks are working with borrowers to help them manage the risk associated with volatile commodity prices -- long the farmer's bane," he added. Community bankers have helped their farm borrowers adapt techniques, such as forward sale and marketing arrangements, that have made the difference between a farm loan in default and one that remained current, Mr. Hawke said.

Some community bankers have taken advantage of government guarantee programs to limit risk, he said, while others have established relationships with banks in nearby communities to help mitigate the risk of loan concentration.

"Some big city bankers could learn something from some of their smaller counterparts' innovative approach to managing risk," he added.

In his speech, Mr. Hawke said that risk management cannot be reduced to a tool or a technique. Instead, he said, "It is a philosophy -- a consciousness -- that permeates every aspect of a bank's operations."

The Office of the Comptroller of the Currency, he said, takes a more comprehensive view of the loan portfolio than ever before. While the underwriting and administration of loans remains a key concern, the agency's philosophy also recognizes that the interrelationships among portfolio segments can be just as important in determining a bank's credit risk profile.

Consequently, OCC examiners look for qualities that define a sound risk management culture, including:

clear objectives and risk tolerance limits, management information systems capable of monitoring loan performance, diversification policies, policies on exceptions, stress testing procedures, and independent audit, loan review and control functions.

These elements, Mr. Hawke said, must be supplemented by appropriate risk measurement tools.

The OCC, he said, looks to ensure that "these and other risk management functions work in harmony with one another. The failure of any one can render the others ineffective."

He cited two examples of how banks might have all the right risk management techniques and procedures in place, but still not have an adequate risk management strategy "if management's heart is not truly in it."

If a bank's audit department is well staffed and trained, and it is dogged in pursuit of irregularities, that might not be enough if the bank's culture encourages these problems to be resolved without addressing them at their source.

And if a bank's compensation plan rewards loan production and loan growth and does not hold its people accountable for the quality and performance of those loans, that too is not effective risk management.

"When OCC examiners find that banks have effective credit risk procedures in place," Mr. Hawke said, "it tells them a great deal about a bank's overall attitude toward risk."

Calling attention to bank capital, Mr. Hawke said a banker might consider his or her institution adequately capitalized because it meets or exceeds all statutory standards. "But how long would that capital last in the event of a downturn in your local economy? As we know, minimum capital and adequate capital are hardly synonymous."

Mr. Hawke encouraged community banks to diversify their portfolios and to take other steps, such as opportunities to securitize and sell parts of the loan portfolio, as ways to reduce credit risk.

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The OCC charters, regulates and examines approximately 2,400 national banks and 59 federal branches and agencies of foreign banks in the United States, accounting for 58 percent of the nation's banking assets.

Its mission is to ensure a safe, sound and competitive national banking system that supports the citizens, communities and economy of the United States.