FDIC NEWS RELEASE

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FDIC STUDY OF BANK FAILURES SHOWS DANGERS OF LENDING CONCENTRATIONS, INFREQUENT ON-SITE EXAMINATIONS

A combination of a volatile economy, lending concentrations by banks and fewer on-site examinations by regulators largely explain the high failure rates among Texas commercial banks, according to an FDIC study released today.

The staff study said failed Texas banks concentrated loans in real estate, and the concentration caused failures when the real estate markets weakened. The study also faulted the reduced frequency of examinations, due in part to hiring freezes and increased workloads at government agencies.

FDIC Chairman L. William Seidman said: "The failed banks we studied were among the best-capitalized institutions in the United States. To me, this says two things. First, capital alone is not the answer to safe and sound banking. Second, adequate government supervision is preventive medicine worth the price. It is clear that supervision levels were reduced to historically low levels just when Texas banks were undergoing tremendous growth, at tremendous cost to the FDIC."

Mr. Seidman noted that the bank regulatory agencies in Washington are considering various measures to enhance supervision, including increasing the number of examiners nationwide and expanding the list of large banks with on-site government examiners on a full-time basis. Chairman Seidman ordered the staff study of the high Texas failure rate several months ago to gain insights that could be applied nationwide.

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Texas failures have become increasingly frequent and costly. In 1983, only three Texas banks failed. In 1989, that number increased to 133, with one more requiring FDIC assistance to keep from failing. In the 1980s, a total of 389 Texas banks failed and 76 others required FDIC assistance.

Also, the FDIC's losses on the 12 Texas banks that failed in 1985 were $80.9 million, or about nine percent of the FDIC's losses on failed banks that year. In 1988, FDIC losses on Texas banks that failed or required assistance jumped to $4.7 billion, or 88 percent of the agency's insurance expenses. In 1989, losses in Texas totalled $4.6 billion, or 81 percent of the FDIC's expenses.

The major findings of the staff study released today include:

- Most Texas banks that failed were heavily concentrated in loans to oil companies, gas producers and other commercial firms when oil prices began dropping in mid-1981.
- To replace lost opportunities in energy loans, Texas banks that later failed appeared to increase concentrations in construction and land development loans and continued to do so long after commercial real estate markets showed signs of being overbuilt.
- At the same time the banks were building up their real estate lending activities, examinations of Texas banks were cut in half. During a crucial two year period, examinations of Texas banks fell from about 300 per quarter in 1983 to about 150 per quarter in 1985.

The principal author of the study was John O'Keefe, a financial economist in the FDIC's Division of Research and Statistics.

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