Remarks
Ricki Helfer
Chairman
Federal Deposit Insurance Corporation

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I would like to discuss briefly with you who we are at the FDIC, what we do, and where we are going.

In the early nineteenth century, two experiments in maintaining the presence of the national government in the U.S. banking system ended in disaster. We finally succeeded in establishing a lasting national banking authority in 1863. Before the federal government entered the banking system that year to create a uniform currency and a reliable system of money, there were in circulation some 10,000 currencies issued by 1,600 private banks. Some analysts have said that only the necessities of financing armies in the field during our Civil War could overcome opposition to the presence of the national government in banking. Indeed, our central bank -- the Federal Reserve -- was not founded until 1913. We came to our senses late.

In one regard, however, we have led in banking, not followed. The FDIC today manages the oldest national deposit insurance fund in the world.

Our birth was painful. Nine thousand banks failed in the four years before the FDIC was created in 1933 -- almost half in the first few months of that year. Those 9,000 failures resulted in losses to depositors of about $1.3 billion. The failure of one bank would set off a chain reaction, bringing about other failures. Sound banks frequently failed when large numbers of depositors panicked and demanded to withdraw their deposits -- leading to a "run" on a bank.

The U.S. banking system lay dormant. The U.S. economy was suffering the worst economic depression in modern history. With the U.S. financial system on the verge of collapse, both the manufacturing and agricultural sectors were operating at a fraction of capacity.

Between 1886 and 1933, at least 150 proposals for national deposit insurance or a national guaranty of deposits were made in Congress. Many of these proposals came in response to financial crises, although none were as severe as that of the early 1930s. Despite conditions at that time, President Franklin D. Roosevelt, the Chairman of the Senate Banking Committee and the American Bankers Association voiced opposition to a government guarantee of bank deposits. They believed that such a guarantee would subsidize poorly managed banks at the expense of well managed banks. The bankers association, in fact, led the opposition, holding deposit insurance to be, and I quote, "unsound, unscientific, unjust and dangerous."

Public opinion, however, demanded action, and action was taken. A government insurance fund was set up to back deposits. The year after the FDIC was created, nine insured banks failed.

One economist summed up the birth of the FDIC in this way: it was the obscure and unwanted Federal Deposit Insurance Corporation that brought the anarchy of unmanaged bank failures in the United States to an end.

Over three generations, deposit insurance has brought peace of mind to tens of millions of depositors, who no longer had reason to fear the failure of their banks. More important, by insulating banks from runs and panics, deposit insurance stabilized the U.S. financial system and helped facilitate the Federal Reserve's effort to manage the money supply.

Deposit insurance was so successful in stabilizing the U.S. financial markets that stability -- in the sense of maintaining equilibrium -- began to be taken for granted. A small but vocal group of critics began to question the need for deposit insurance at all. They asked: in a global financial marketplace linked by instant communication, have we not gotten beyond the idea of guaranteeing household savings?

No one, however, repealed the business cycle. The failures of nearly 1,400 U.S. banks from 1982 through 1992 reminded us that stabilizing can also mean keeping a deteriorating situation from worsening. Those failures reminded us that guaranteeing savings is not only an end in itself but a means of stabilizing the banking system in times of stress. Those failures reminded us that stability is always a goal, not a given.

I would not argue, however, that there are not legitimate questions that can be raised about deposit insurance.

One area to which we have given a great deal of attention -- and to which we will give more -- is the element of moral hazard presented by our deposit insurance system. In banking, deposit insurance gives bank managers -- whose job it is to maximize shareholder value -- the incentive to increase risk, both by investing in riskier projects than would otherwise be undertaken and by increasing leverage.

Deposit insurance shifts these risks onto the deposit insurer, and in our case, potentially onto the American taxpayer. In other words, it creates a situation where if a bet -- a loan -- comes up heads, the insured institution wins, and if it comes up tails, the insurer loses.

In the last few years, we have instituted risk-related deposit insurance premiums, higher minimum capital standards, and other reforms to address the problem of moral hazard.

It is difficult, however, to eliminate moral hazard altogether from any deposit insurance system.

In the end, the U.S. government's guarantee of the deposit insurance fund stabilizes our banking system. A similar guarantee would probably be prohibitively expensive for a private, non-governmental insurer.

In the final analysis, I believe the benefits in terms of stability that flow from our deposit insurance system have outweighed its potential costs and effects.

Let me give you an idea of the magnitude of our work. As you probably know, we insure deposits of up to $100,000 at banks and savings and loan associations. Last year insured banks in the United States held approximately $2.5 trillion in deposits. We insured $1.9 trillion of those deposits -- about 77 percent of the total.

The savings and loans that we insured held $720 billion in deposits. The Savings Association Insurance Fund coverage represented $693 billion of those deposits -- about 96 percent. In addition, in 1994 we examined more than 4,300 institutions for safety and soundness, and we still have about $13 billion in assets to liquidate from banks that failed, mostly from the banking crisis in the late 1980s and early 1990s.

Our Bank Insurance Fund has a balance of just over $25 billion and our Savings Association Insurance Fund has a balance of just above $3 billion. The FDIC has been lauded as the most successful program of the New Deal. More recently, it received credit for preventing the savings and loan and bank crises of the late 1980s and early 1990s from chain reacting into catastrophe.

Throughout those crises, it did what Congress intended it to do: maintain confidence in the financial system. It insured the public's confidence in banks -- no one lost a single penny of an FDIC-insured deposit -- and this protection cost the taxpayer nothing whatsoever. It also established an orderly process to liquidate tens of billions of dollars of failed bank assets.

To do its job, the FDIC's staff ballooned from 846 in 1934 to 3,500 in 1982 to 15,611 in 1993. Aside from size, however, the agency has not changed much since Congress created it. It faces the new millennium doing much of what it did during the New Deal: examining

banks, liquidating the assets of failed banks, and providing insurance coverage for bank depositors.

Before I became FDIC Chairman a year ago, I asked myself if it would be better -- for the public, for the financial system, for the economy -- if we put our efforts into helping banks stay open to serve their customers and communities rather than into liquidating them after they failed? And would it be better if we took more advantage of technological and managerial developments to do our job more effectively? The answers were clear: yes and yes. We had to take on new and growing demands.

Fortunately we had a model to follow in making this transition: the private sector. Successful companies simply do not do the same thing in the same way year after year. Companies must respond to changing market demands by altering what they produce and how they produce it.

It was obvious to me that the FDIC had to be repositioned by altering what we do -- in short, by identifying, monitoring and addressing risks to depository institutions before they failed. We had to retool the FDIC to increase efficiency, reduce bureaucracy, and cut costs. We had to run the FDIC the way a business operates -- by striving for greater productivity and enhanced performance, by using rigorous cost/benefit analysis, by relying on up-to-date management concepts and technology.

In business, this kind of thinking is conventional management.

To succeed, we had to articulate a new direction for the organization and to undertake specific initiatives to move the organization in that new direction. In business, these objectives are often achieved through the use of a strategic plan, an operating plan, and a reorganization, which together form a foundation for change.

We developed and implemented a strategic plan -- the first in the history of the organization -- which focuses our efforts on identifying, monitoring, and addressing risks to banks and savings associations.

We developed an operating plan -- 151 specific initiatives -- some devoted to shifting our emphasis from examining banks and liquidating them when they fail to our need to focus on risk in advance. One of those projects was to determine the number of people we will need once we have cleared the remaining debris from the thrift and bank crises and made the managerial reforms we need to make.

Our staff now numbers about 10,500. In three years, we could be down to 7,000. As I noted before, we have already reduced staff from a high of 15,611 in 1993 -- that is, about a third in total. The scale and speed of the downsizing in which we are engaged are unprecedented for a government agency -- or almost anywhere else, I believe.

Finally, we reorganized the FDIC, first by establishing a management team to supervise the projects in the operating plan and to assure that all the parts of the organization work together and, second, by creating a Division of Insurance to monitor risks and recommend responses to problems so that something is done about them before banks fail.

I have been told that the saying, "it's good enough for government work," harkens back to the early industrial era. At that time, government was an innovator and a research resource. It was also -- as it is today -- a customer of private enterprise. Government's purchasing standards then were as high or higher than those of business. When contractors produced products that met the government's standards, they would say that the products were "good enough for government work."

The story may be apocryphal, but it suggests an important point. There is nothing inherently inferior in government work, although that phrase has taken on a somewhat derogatory meaning. I believe that nothing but the best is good enough for government work. We taxpayers deserve that. With proper management, government can be a low cost provider of high quality services. That is my aim for the FDIC.

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