

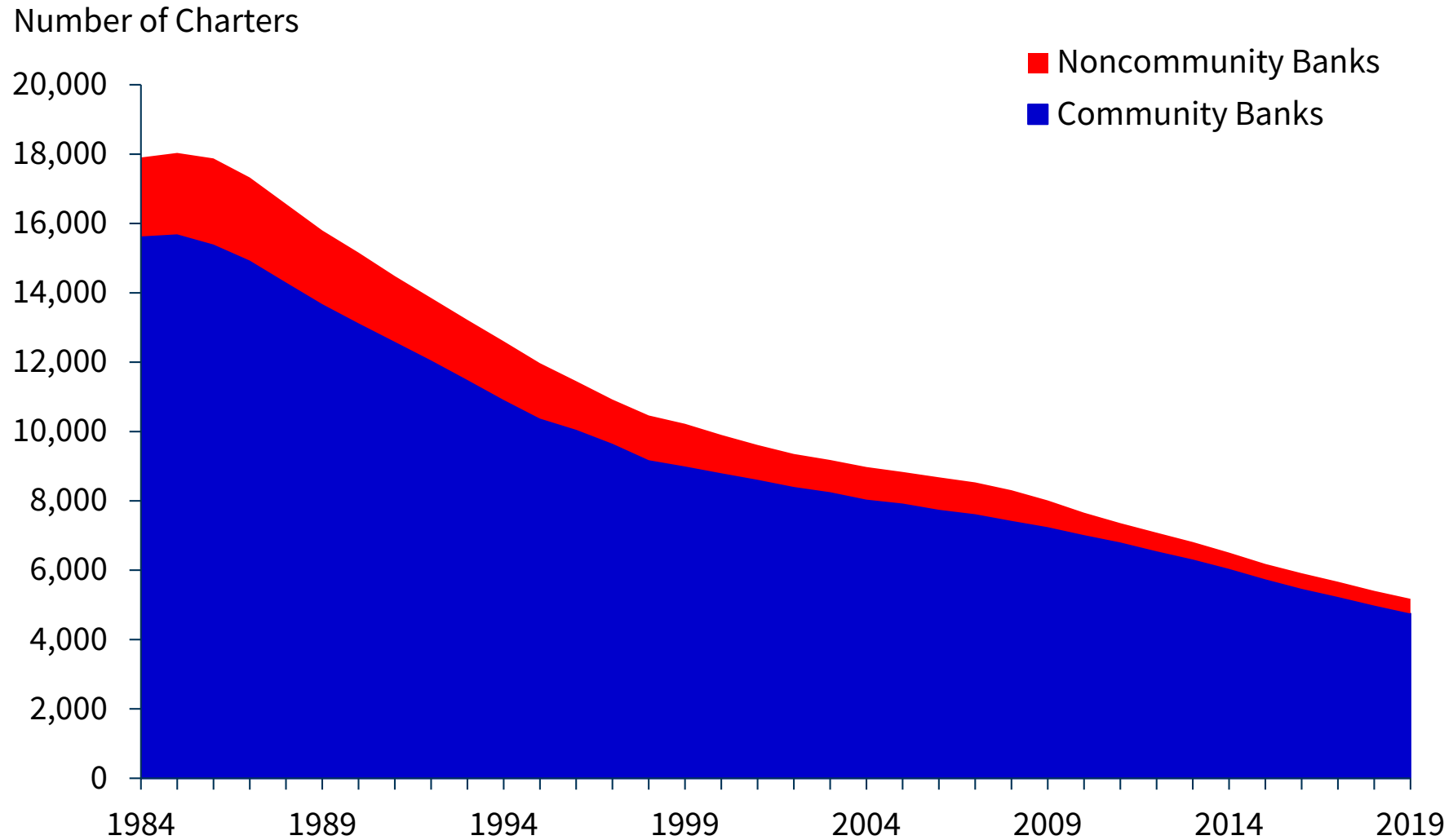
FDIC Advisory Committee of State Regulators

October 14, 2020

Community Bank Consolidation



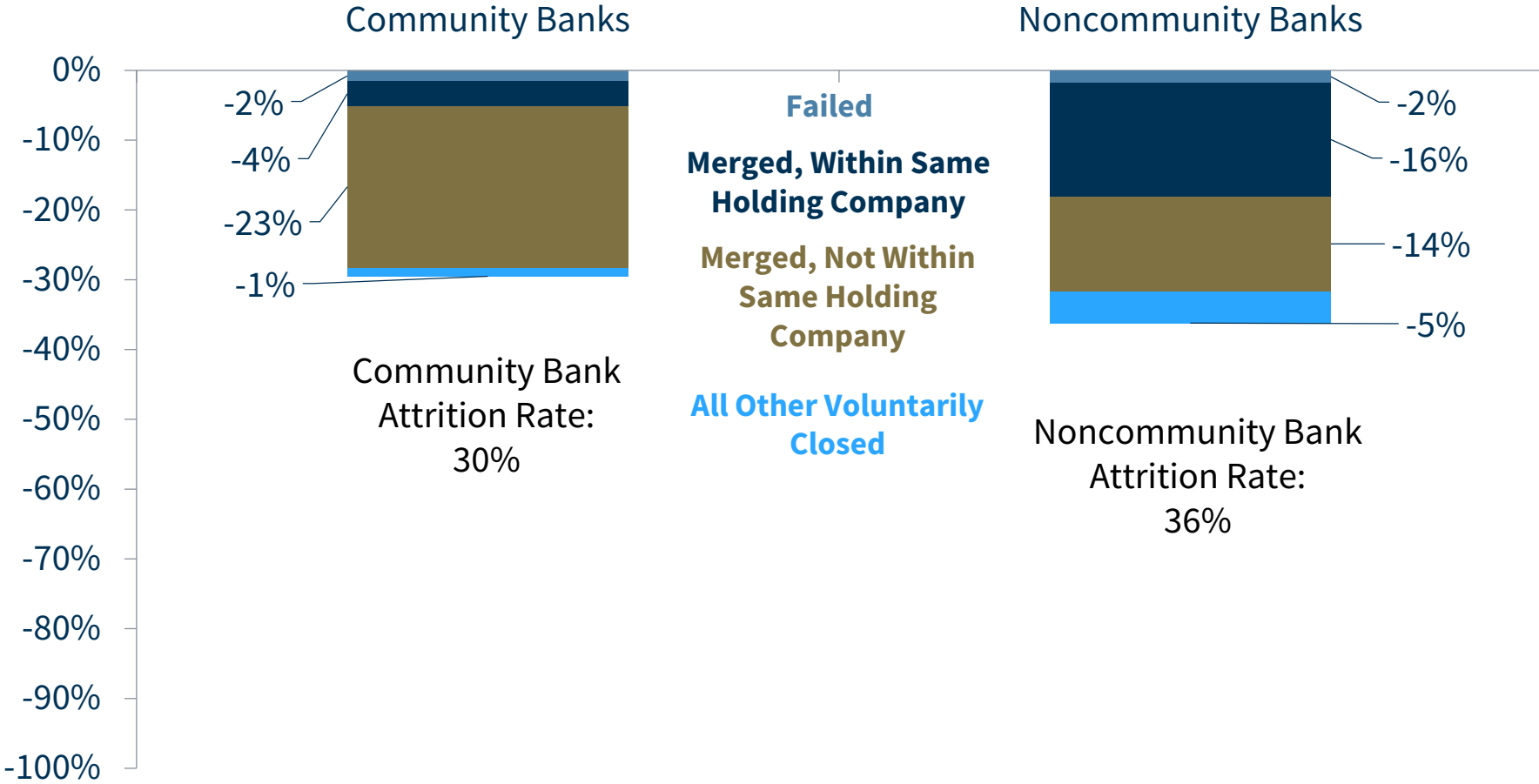
Banking Industry Consolidation Is a Long-Term Trend



Source: FDIC.

Community Banks Were Less Likely Than Noncommunity Banks to Close Between 2012 and 2019

Closings by Type of Closure, as Percentages of Institutions Reporting at Year-End 2011

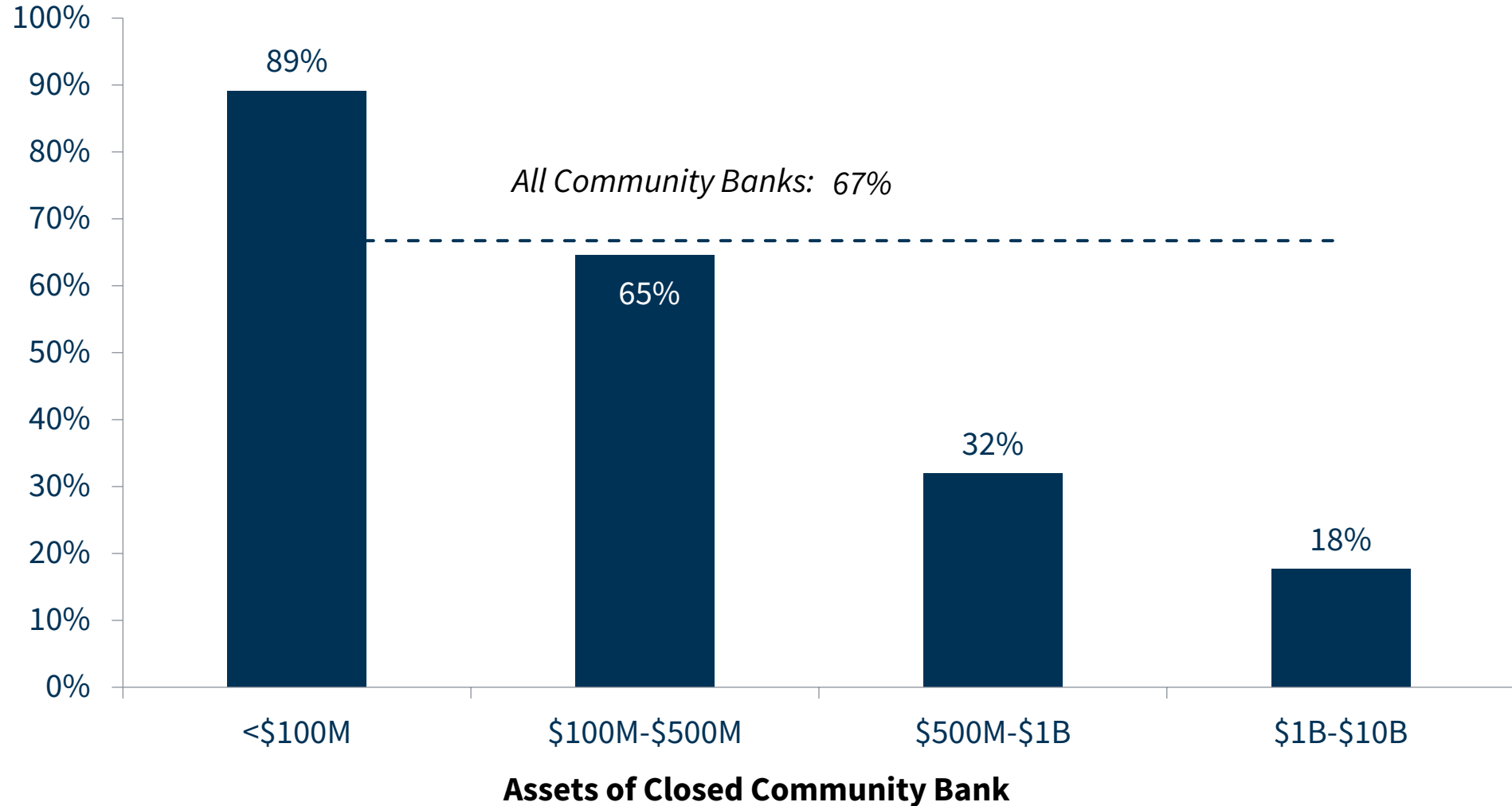


Source: FDIC.

Note: Summation of the percentages by type of closure may not equal the attrition rate due to rounding.

Community Banks Are Overwhelmingly Acquired by Other Community Banks

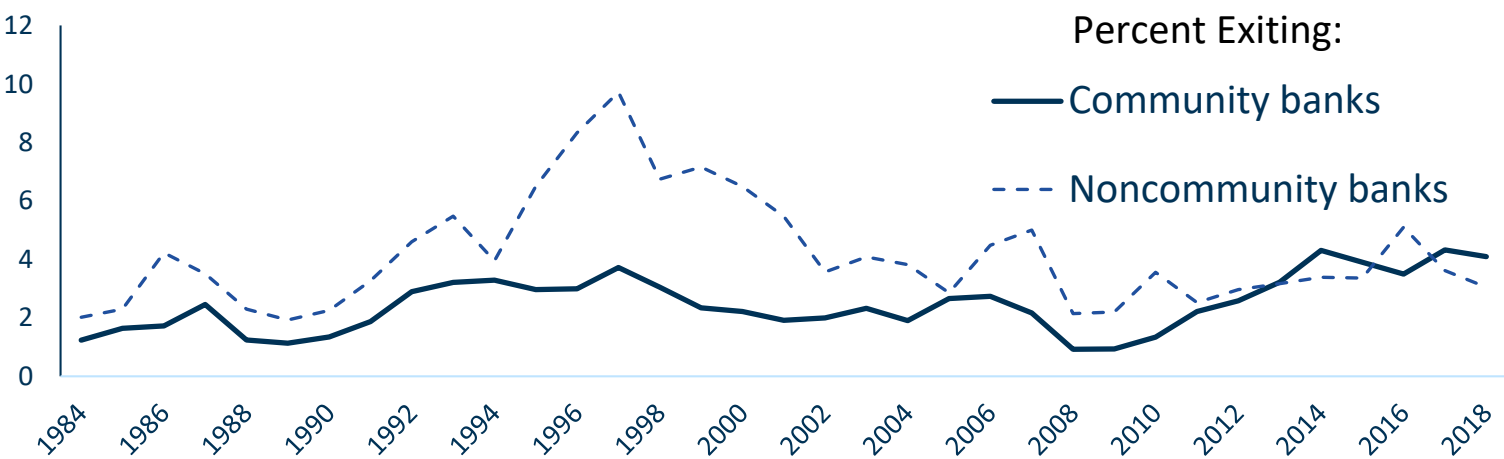
Percent of Closed Community Banks Acquired by Other Community Banks Between 2012 and 2019, by Closed Bank Assets



Source: FDIC.

Community Banks are Exiting Banking Faster than Before

Acquired by Unaffiliated Bank or Self-Liquidating
Percent of Existing Institutions

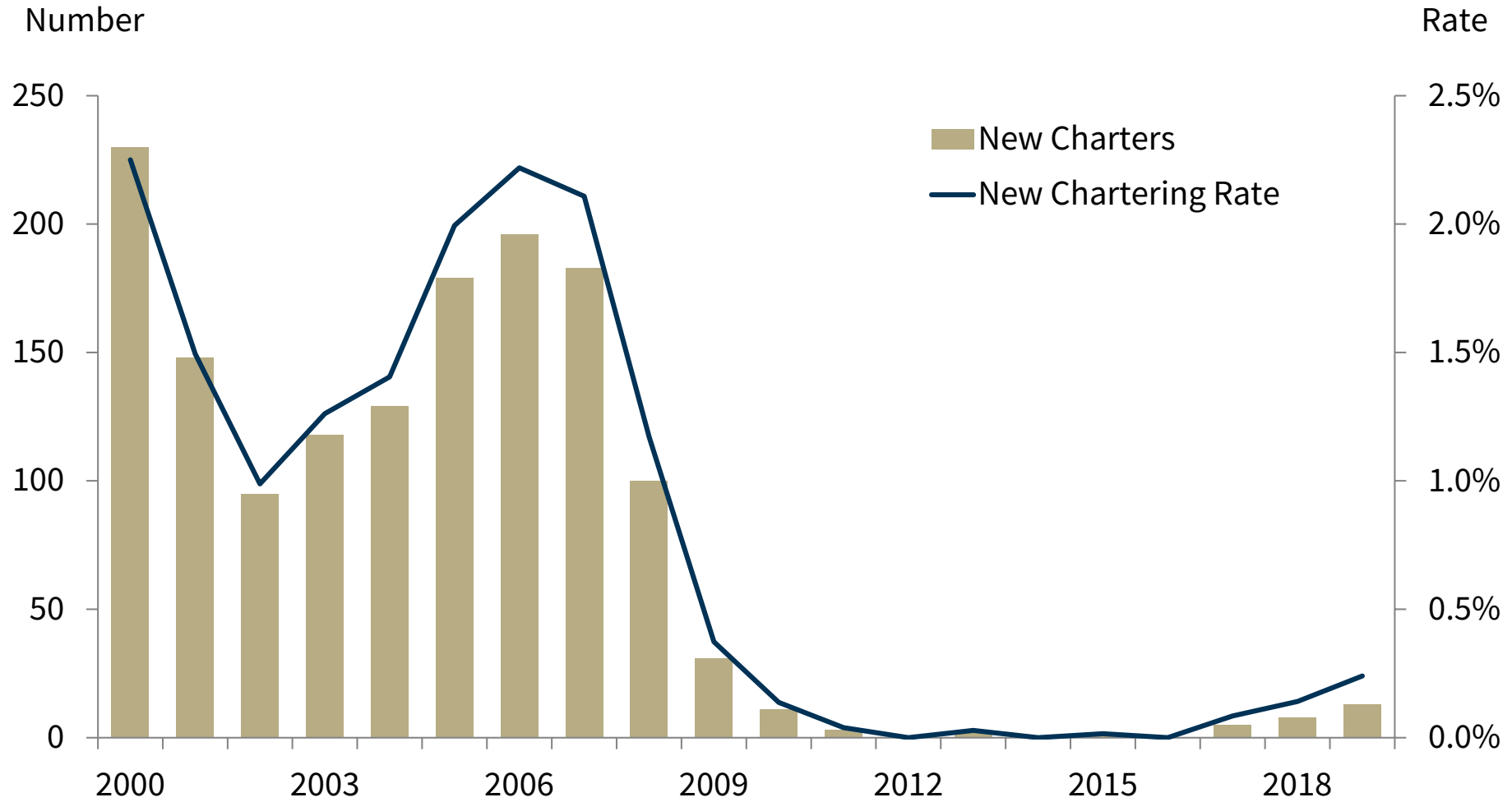


Source: FDIC.

Note: Percent of banks existing at yearend that were acquired by an unaffiliated institution or self-liquidated within one year.

New Chartering Remains Near Historic Lows

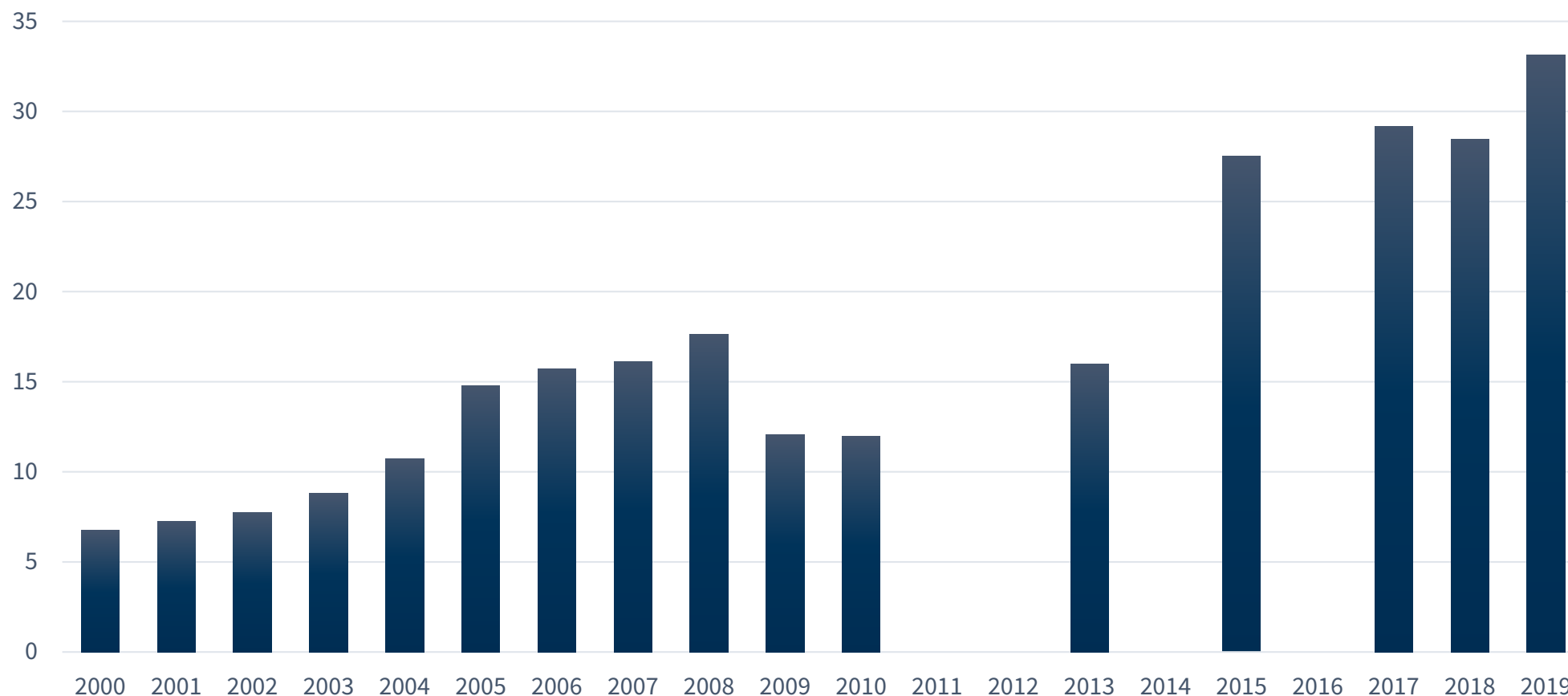
Annual Number of New Charters and New Chartering Rate as a Percentage of Charters Reporting at Previous Year-End, 2000 to 2019



Source: FDIC.

The Cost of Chartering a Small Bank Has Increased

Mean Initial Equity of De Novo Small Banks
\$ Millions

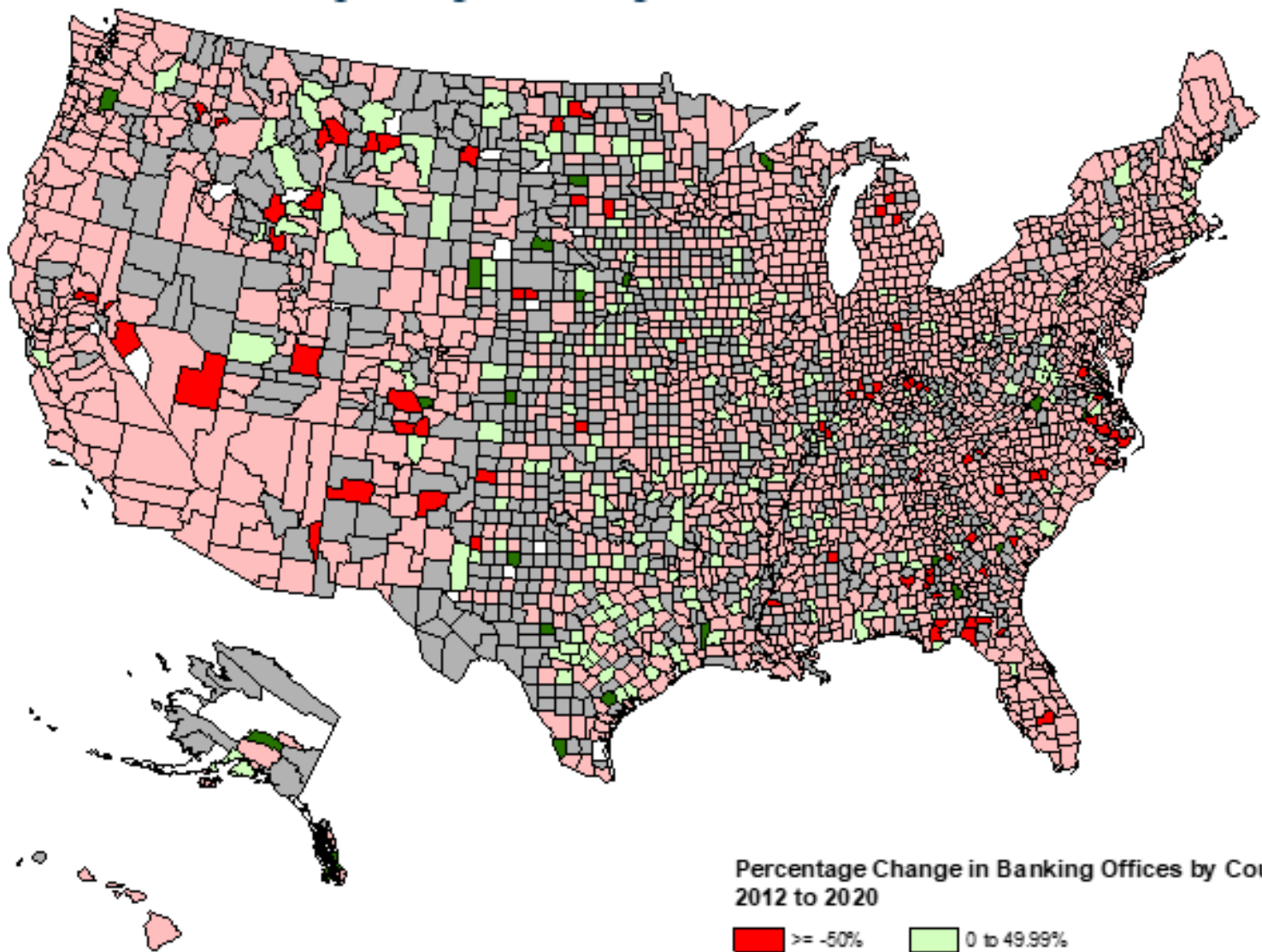


Source: FDIC.

Notes: Equity capital reported as of banks' first Call Report filing. Analysis limited to de novo banks with initially reported equity capital less than \$100 million.

Declines in the Number of Banking Offices Have Been Widespread

Percentage Change in Banking Offices by County, 2012 to 2020



Source: FDIC.

The Number of Counties With Only One Bank Office, or No Bank Offices, Is Increasing

	2020	2012
Number of Counties with One Bank Office:	134	107
<i>Community Bank</i>	94	76
<i>Noncommunity Bank</i>	40	31
Number of Counties with No Bank Offices:	34	33

Of the 34 counties without bank offices, 26 also did not have any bank offices in 2012. Six of them had one office in 2012, and one had two offices in 2012.

Of the 134 counties with only one bank office, 95 also had only one bank office in 2012. Four of them did not have any bank offices in 2012, 28 had two bank offices in 2012, and seven had either three, four, or five offices in 2012.

Shared Destinies? Small Banks and Small Business Consolidation

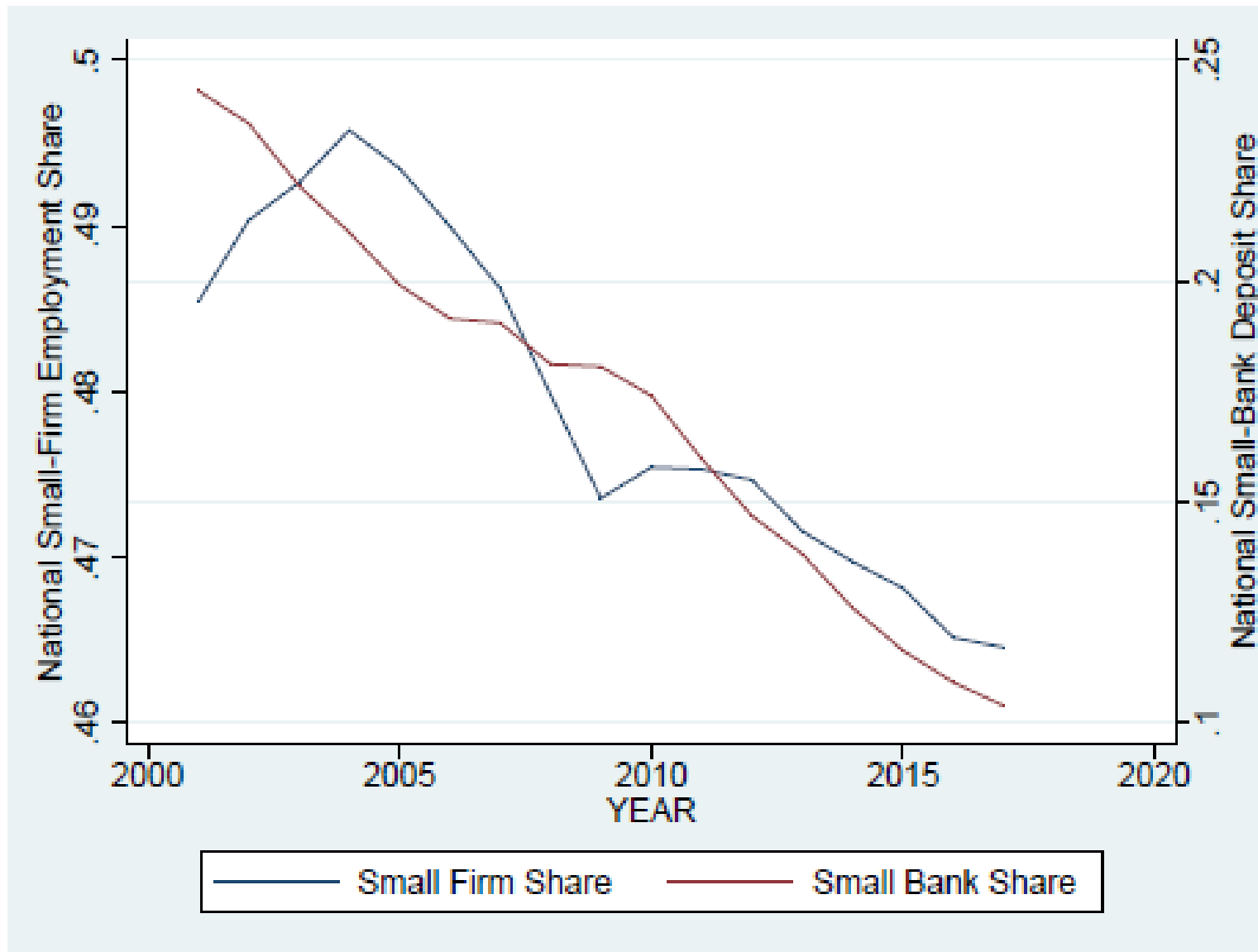
A Working Paper by:
Claire Brennecke (CFPB)
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Disclaimer

Views and opinions expressed in this presentation reflect those of the authors and do not necessarily reflect those of the FDIC, CFPB, or the United States.

Decline in Small Banks and Small Firms



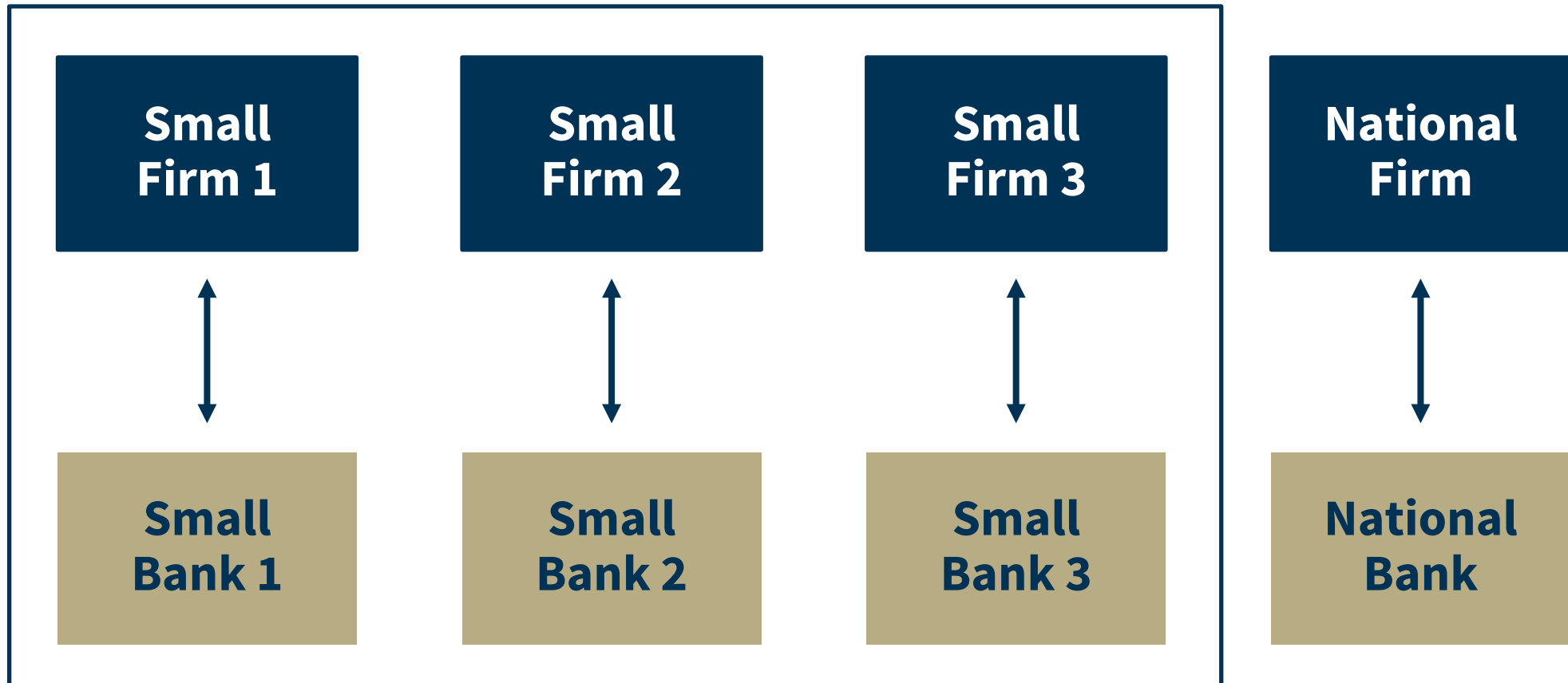
Source: Quarterly Workforce Indicators (Firm Shares). Summary of Deposits (Deposit Shares).
Small Firms <250 employees
Small Banks < \$1 bn assets

Banking Consolidation

- Consolidation of banking system, driven by:
 - Regulatory changes (Riegle Neal 1994, Gramm Leach Bliley 1999, Dodd Frank 2010)
 - Technological changes (ATMs, credit scoring)
- Small banks have comparative advantage in lending to small businesses
 - Boot (1999), Petersen and Rajan (2002), Chakraborty and Hu (2006)
- Common narrative: Banking consolidation → loss of small businesses
 - Cetorelli and Strahan (2006), Sapienza (2002)

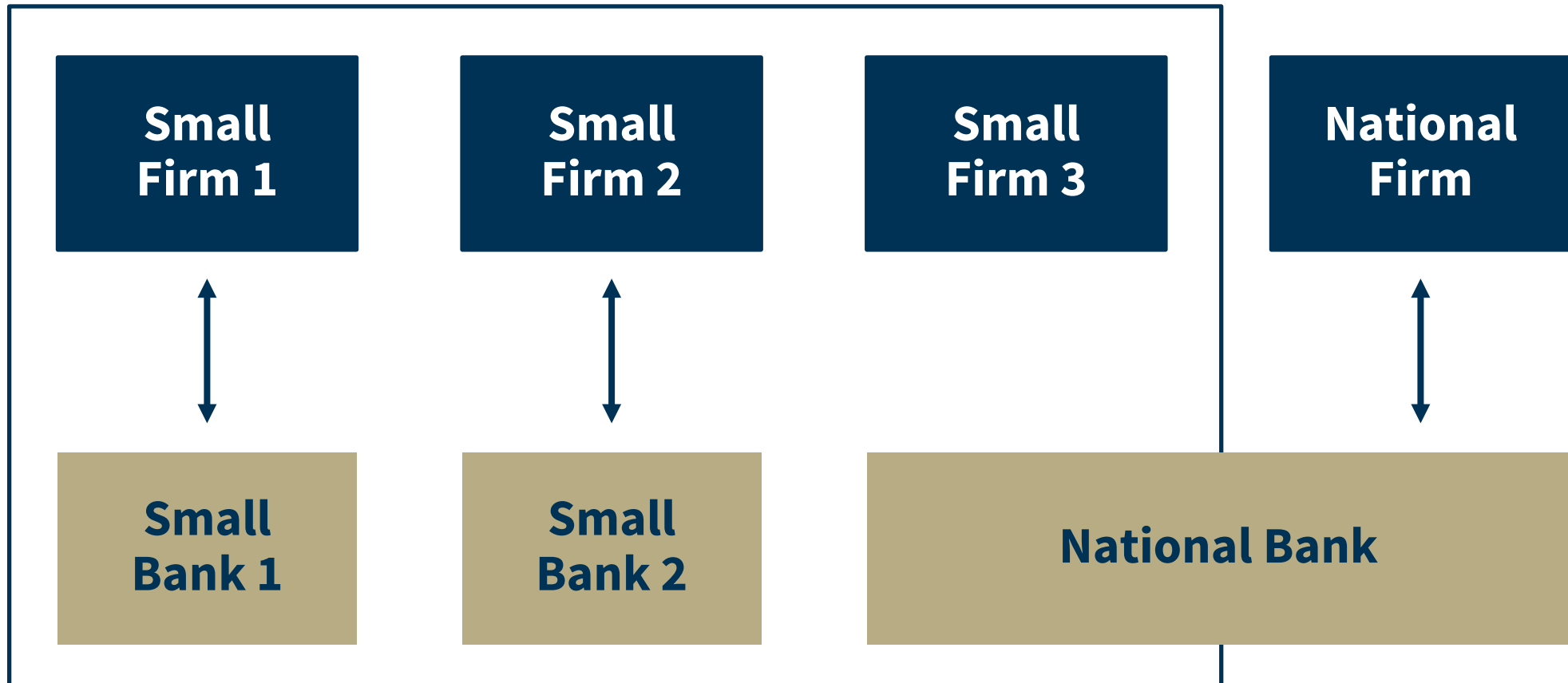
Literature in a Picture

County C



Literature in a Picture

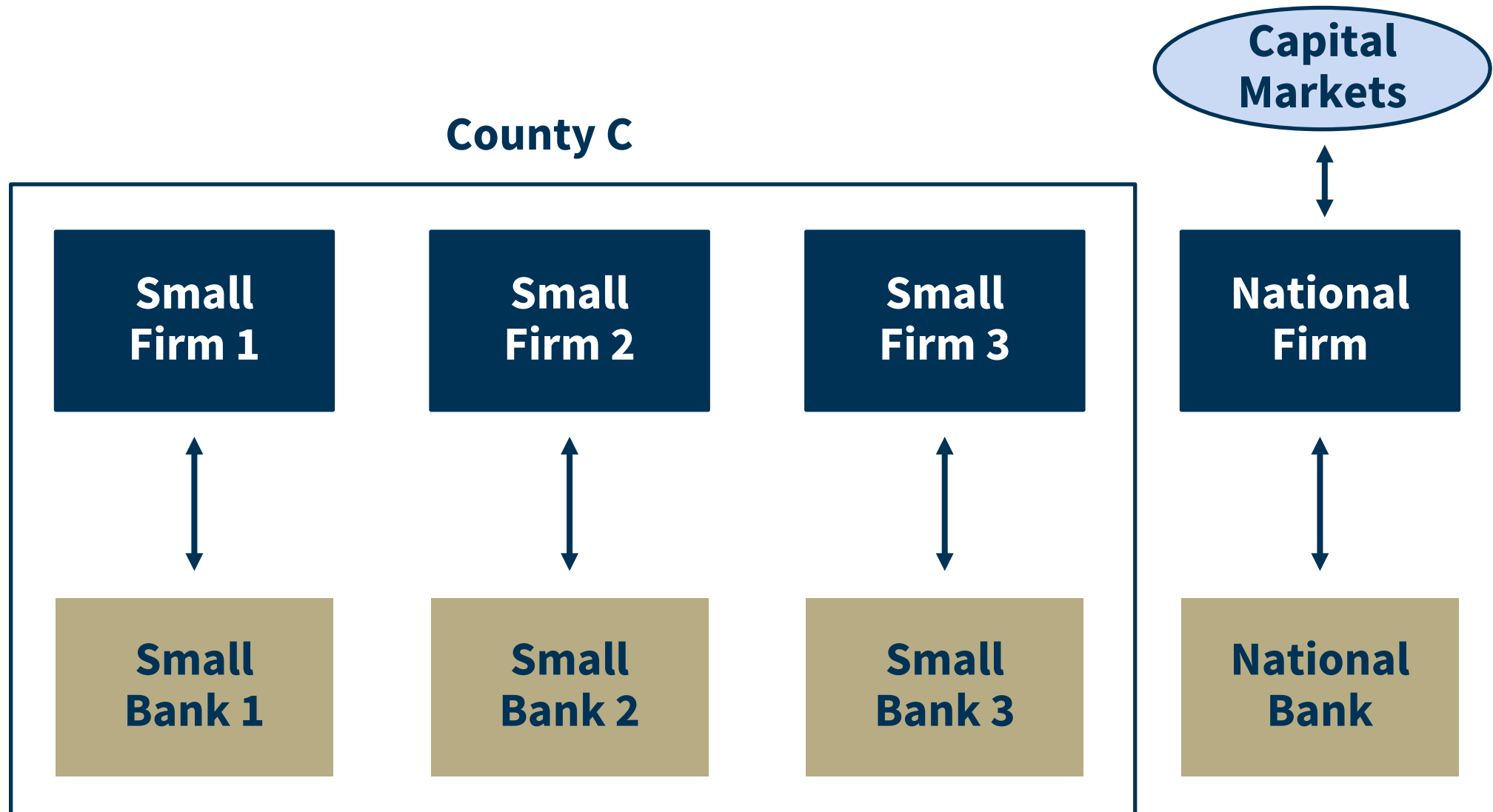
County C



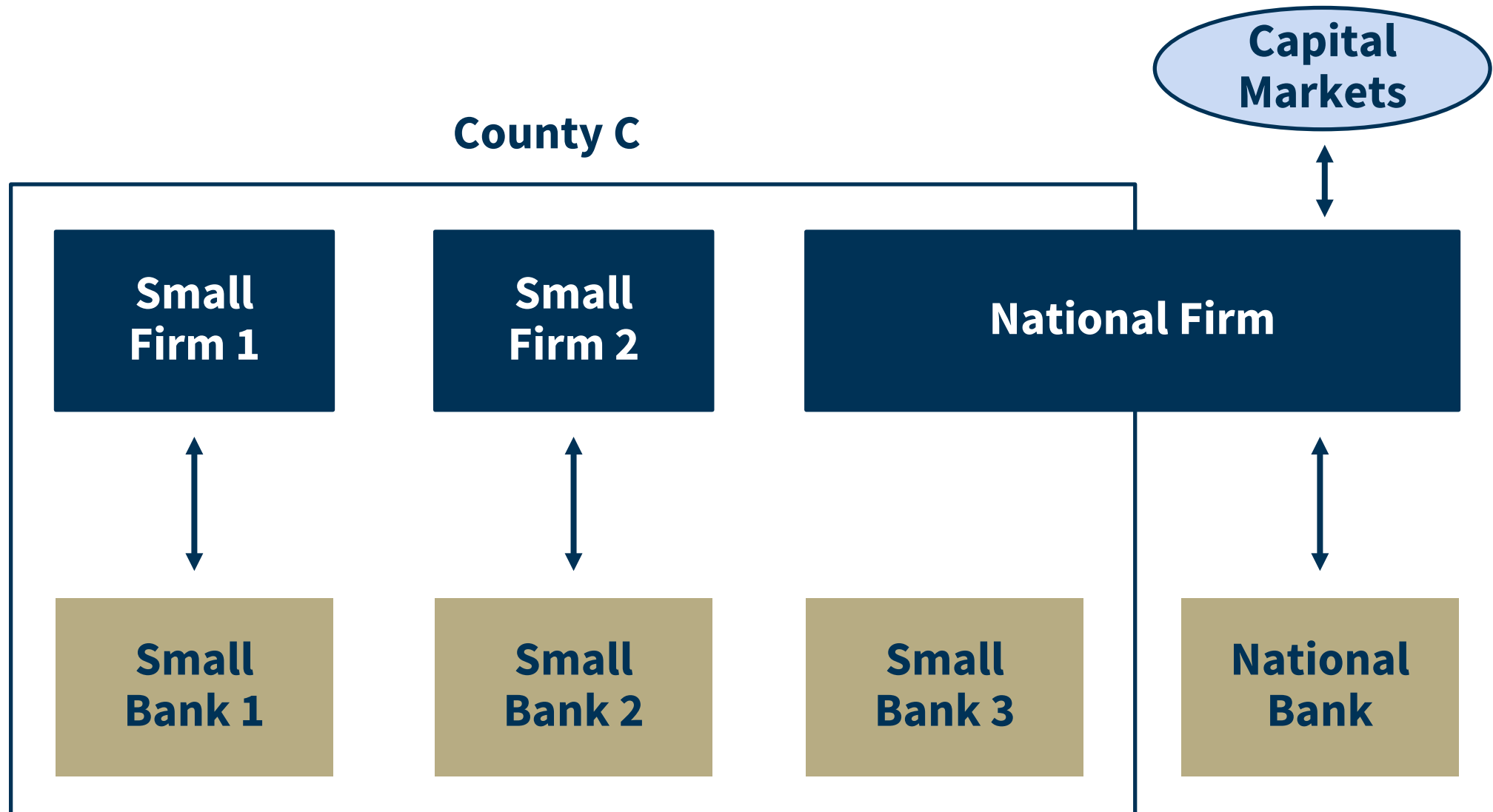
Real-Side Consolidation

- Consolidation of real industry (Grullon et al. 2019, CEA 2016, Jia 2008)
 - Technological changes (e.g., supply chain management (Holmes 2008), e-commerce (Goldmanis et al. 2010))
 - Regulatory (e.g., antitrust (Gutierrez and Philippon 2017))
- Small banks have comparative advantage in lending to small business
- **Our narrative: Loss of small business → changes to viability of small banks**
- Not mutually exclusive, but helps us weigh efficacy of policies
- COVID recession and government response → SmBus → Small Banks

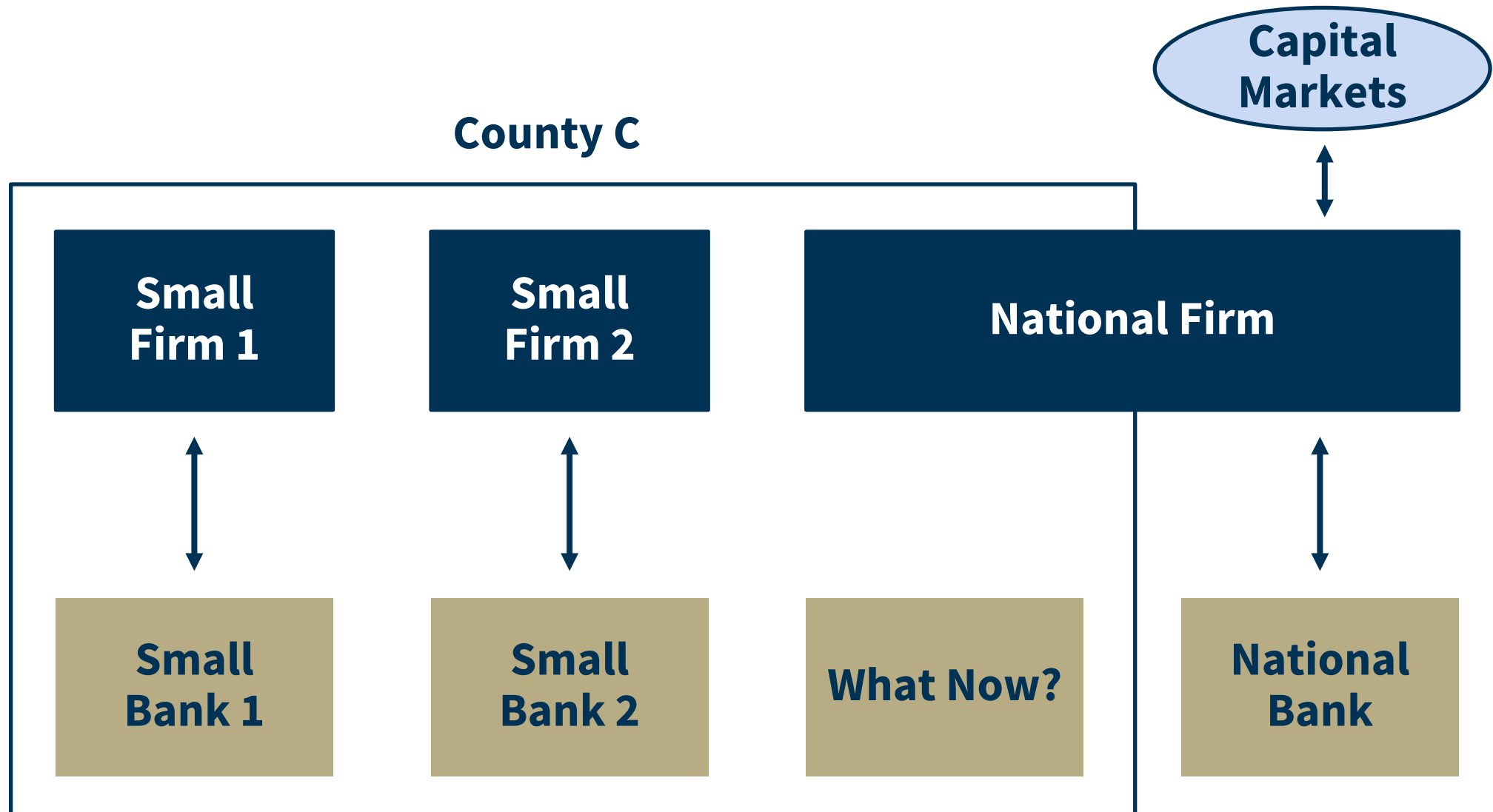
Literature in a Picture



Literature in a Picture



Literature in a Picture



What We Do

- Estimate effect of small business performance on small bank performance using:
 - Census Quarterly Workforce Indicators (QWI) data on county employment by firm size
 - FDIC Summary of Deposits (SOD) data on bank deposits by bank size
- To establish a causality direction
 - Rely upon 2000 county-industry shares as differential exposures to national trends by industry and firm size

To Show That Effects Are Demand-Driven

Healthcare: 35
Transportation: 25
Retail: 15
Manufacturing: 25

Jon's Home County, 2000

Healthcare: 25
Transportation: 15
Retail: 30
Manufacturing: 30

Stefan's Home County, 2000

National Small Business
Employee Trends:
2002 to 2017

Healthcare: +31%
Transportation: +8%
Retail: -16%
Manufacturing: -20%



Expected Demand in
Small Business
Financial Service

Main Findings

- 1 percent decrease in small-firm employment growth → 0.9 percent decrease in small-bank deposit growth
 - Decrease small-bank income
 - Decrease small-bank small-CI lending, less robust/smaller decrease in RE lending
 - Increase provisions
 - No change in large-bank deposit growth
- Large-firm employment growth → no change in small-bank deposit growth

What Drives Our Findings?

- Small firm employment drops associated with decreased small bank deposit growth
- Possible explanations: Small firm employment decreases makes small bank business model less profitable
 - More likely to be acquired?
 - More likely to look to acquire?
 - More likely to fail?
- Examine small-bank county deposits and headquarters associated with acquisition, failure

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Conclusions

- The composition of the banking industry depends, at least in part, on the composition of the real economy
- Combined with existing literature, there is a feedback loop between small-bank and small-business consolidation
- Evolution of the organizational structure of banking will depend, in part, on the evolution of the American small business
- Policies affecting small banks are interdependent with policies and trends affecting small business

2020 Academic Challenge:

The Effects of Community Banks on Local Economic Development

- Bring real-world banking policy questions into the classroom
- Nationwide competition for teams of four to five undergraduate students
- Two rounds:
 - Written component, six pages, November 20, 2020
 - Finalist presentation component, April 16, 2021
- Provide question prompts and datasets that may be used by students to engage the material