Community Banks Remain Resilient Amid Industry Consolidation

Analysts agree that consolidation is a long-term trend that has significantly reshaped the banking industry over the past 30 years.[1] There has recently been renewed debate as to the future pace of industry consolidation and what implications this trend holds for community banks. This paper presents an analysis of long-term consolidation and its effects on community banks. We conclude that the recent uptick in the rate of consolidation is attributable to factors that are likely to subside once the effects of the crisis are fully behind us. We also find that consolidation has had much less impact on the community banking sector than is commonly believed.

The key finding of this study is that institutions with assets between $100 million and $10 billion—most of which can be considered community banks—have increased in both number and in total assets since 1985. The number of banks with assets between $100 million and $1 billion increased by 7 percent between 1985 and 2013, while the number of banks with assets between $1 billion and $10 billion increased by 5 percent. These groups of institutions also experienced growth in terms of total assets. The assets of banks between $100 million and $1 billion increased by 27 percent between 1985 and 2013, while the assets of banks between $1 billion and $10 billion grew by 4 percent.

Consolidation has had its biggest net effect on the very smallest and the largest banks. The number of institutions with assets less than $100 million declined by 85 percent between 1985 and 2013. Meanwhile, institutions with assets greater than $10 billion have seen their number almost triple, while their total assets have increased more than ten-fold.

Because of the limitations of applying fixed asset-size thresholds over such a long period of time, we also analyze the effects of consolidation using the functional definition of community banks that was introduced in the 2012 *FDIC Community Banking Study*.[2] Seen through this lens, consolidation has had a much less pronounced effect on the community banking sector. More than 90 percent of FDIC-insured institutions operate as community banks, a share that has steadily increased since the mid-1980s. Moreover, the rate of total attrition through failure or merger has been far lower among community banks than among noncommunity banks since 1985—a disparity that has become even more pronounced over the past decade. When community banks do fail or close voluntarily, almost two-thirds of the time the acquirer is another community bank. So while today's community banks may be somewhat larger, on average, than those of 30 years ago, they continue to meet the definition of institutions providing traditional banking services to their local markets.

These conclusions are somewhat at odds with the often expressed view that the post-crisis period will be characterized by heightened consolidation, which will increasingly marginalize the community banking sector. Our analysis shows that the projected decline of the community banking sector has been significantly overstated. Community banks have, in fact, remained highly resilient amid the long-term trend of banking industry consolidation. While their share of industry assets has declined over time, they are disproportionately important providers of credit to small businesses and serve hundreds of counties and thousands of communities that are overlooked by larger noncommunity institutions. While the overall trend of consolidation may well continue, it appears unlikely to diminish the importance of community banks or the role they play in our financial system.

A Closer Look at the Process of Consolidation

Before specifically evaluating the effects of consolidation on community banks, it may be useful to examine the process of consolidation itself. Consolidation is by no means a new development; in fact, it has been a defining trend in the U.S. banking industry since around 1980. After remaining fairly steady for more than three decades, the total number of banking and thrift charters declined from around 20,000 in 1980 to 6,812 at the end of 2013 (Chart 1). While the top-line figures in Chart 1 appear to depict a disappearance of banking charters over time, it is more useful to consider this trend in terms of the three main components of structural change in banking.

[1] For a previous FDIC study of long-term consolidation in banking, see Jones and Critchfield (2004).

[2] The 2012 FDIC *Study* defined "community banks" in terms of balance-sheet characteristics that reflected a focus on lending and deposit-gathering activities, and on a limited geographic scope of operations. For more details, see: http://www.fdic.gov/regulations/resources/cbi/report/CBSI-1.pdf.

Chart 1

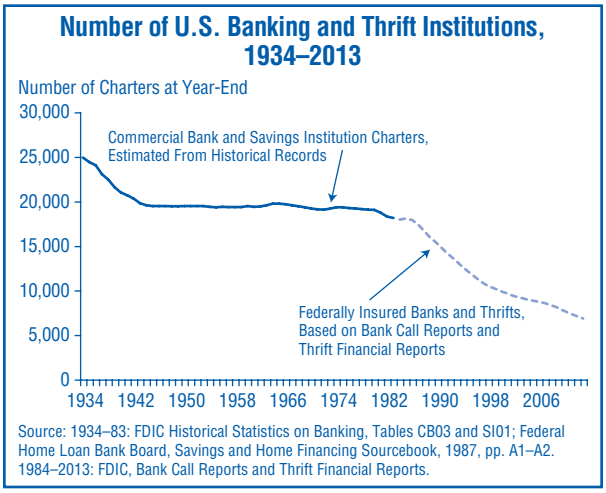
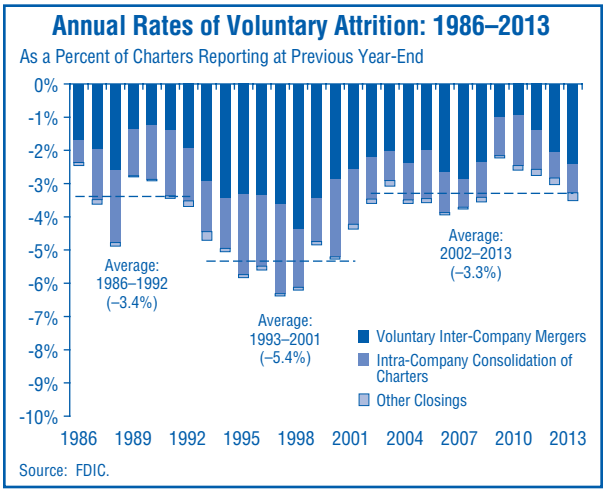


Chart 2



Voluntary closures have slowed since 2001. The most important component of long-term consolidation in banking is the voluntary closure of bank charters, which has accounted for around 80 percent of the total attrition in charters that has taken place since 1985. Voluntary closures of charters occur through *intra-company consolidation* of commonly owned charters, *inter-company mergers*, and, occasionally, through *self-liquidation*. It is useful to think about intra-company consolidation as a means by which an existing bank holding company can rationalize its internal structure by combining charters. These consolidations reduce the number of charters, but have no effect on the total number of banking organizations. In contrast, inter-company mergers are a means by which banking organizations can expand their size and geographic reach by merging with or acquiring charters operating under separate ownership.

Chart 2 depicts the annual rate of voluntary attrition, and divides the period since 1985 into three distinct periods. These include two periods of relatively slow voluntary attrition—the first between 1986 and 1992 when the annual voluntary attrition averaged 3.4 percent, and the second between 2002 and 2013 when the annual rate averaged 3.3 percent. During these 19 years of relatively slow voluntary attrition, the annual rate exceeded 4.5 percent in only one year. These periods were divided by a period of more rapid voluntary attrition between 1993 and 2001 when voluntary closings exceeded 4.5 percent of existing charters in *every* year.

The period of highest rates of voluntary attrition immediately followed a period of changes in federal and state law, during which geographic barriers to banking activities were significantly relaxed. Before the 1980s, depository institutions were subject to a range of geographic restrictions, interest rate ceilings, and other limitations that had been introduced in response to the banking crisis that accompanied the Great Depression. Around 1980, however, increasing disintermediation from traditional banks, and especially thrifts, prompted a series of legislative measures to enable depository institutions to more effectively compete with nonbank providers.[3]

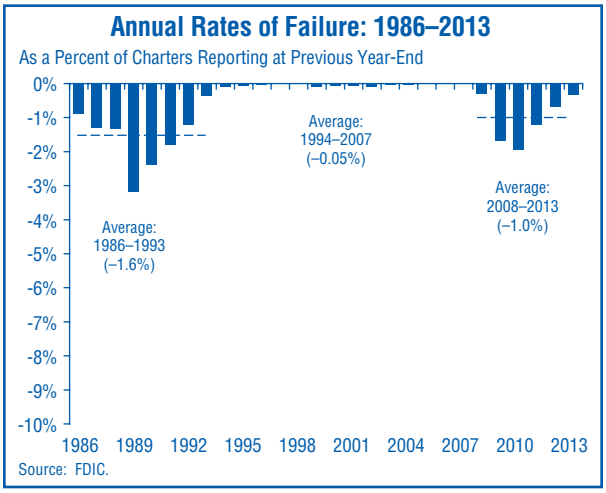
These regulatory changes at the state and federal levels virtually eliminated the geographic restrictions on banking activities that applied to many states prior to 1980. While only 16 states permitted unrestricted intrastate branching in 1984, by 1994 the number had risen to 40.[4] Similarly, while 42 states restricted interstate combinations of banking charters in 1984, by 1994 only Hawaii retained this restriction.[5] The Interstate Banking and Branching Efficiency Act of 1994 (Riegle-Neal) introduced full interstate branching, which further facilitated the consolidation of charters within banking companies. It was in the immediate aftermath of this liberalization of geographic restrictions that the industry

[3] The Depository Institutions Deregulation and Monetary Control Act of 1980 (DIDMCA) and the Garn-St. Germain Depository Institutions Act of 1982 (Garn-St. Germain) lowered net worth requirements and expanded investment powers for savings institutions, eliminated the Regulation Q interest-rate ceilings on bank and thrift deposits, and increased federal deposit insurance coverage from $40,000 to $100,000. Also around this time, state usury laws that placed interest-rate ceilings on consumer loans were being superseded by a 1978 U.S. Supreme Court ruling that permitted banks to follow the usury ceiling in place in their home state.

[4] Strahan (2002). The District of Columbia is not included in these state counts.

[5] Strahan (2002).

Chart 3



experienced its highest annual rates of voluntary consolidation. This relaxation of these geographic restrictions was conducive to both the consolidation of charters within existing organizations and the acquisition of charters operated under different ownership.[6] However, in some sense this represents a one-time historical factor that by now, some 20 years or more after the fact, has diminished in importance as a driver of industry consolidation.

Failures rose during the recent crisis, but are now abating. The second most important factor contributing to consolidation since 1985 has been *bank and thrift failures*. Between 1985 and 2013, a total of 2,580 federally insured banks and thrifts failed. Failures have accounted for slightly less than 17 percent of all charter attrition since 1985. The vast majority of those failures have taken place within two concentrated waves: one during the 1980s and early 1990s, and the other beginning in 2008.

Chart 3 depicts annual percentage rates of failure for federally insured banks and thrifts. The chart divides the period since 1985 into distinct eras that coincide with two crisis periods. The annual rate of failure ranged between 0.3 percent and 3.2 percent in every year between 1986 and 1993, as the banking and thrift industries were experiencing credit losses associated with commercial real estate and construction lending and a series of regional economic downturns.[7] After 1993, the annual rate of failure never exceeded 0.1 percent in any year until 2008, when the industry experienced a second wave of failures associated with the recent financial crisis. The annual rate of failure once again equaled or exceeded 0.3 percent in every year between 2008 and 2013, peaking in 2010 at 2 percent. In all, 97 percent of the failures that have taken place since 1985 have occurred during these two crisis periods.

While failures have been an important factor contributing to the banking industry consolidation since 1985, it is by no means assured that they will continue to contribute to consolidation to the same degree in the years ahead. Substantial reforms put in place since the recent crisis, including the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (Dodd-Frank) and the Basel III capital standards, are designed to contribute to a more stable banking environment in the years ahead. To the extent that bank risk managers and bank supervisors are successful in creating a more stable banking environment in the years ahead, failures may contribute much less to consolidation than they have since 1985.

New charters represent a highly cyclical component of consolidation. The other main component of consolidation is *new banking charters*. The rate at which new charters have been added to the industry has proven to be highly cyclical. Since year-end 1985, the industry has established new federally insured institutions at an average annual rate of 1.3 percent (Chart 4). The establishment of new institutions has been strongest during periods of economic expansion and strong financial performance on the part of the banking industry. The pace of chartering activity has undergone three distinct lulls that have occurred during and immediately after the recessions of 1990-91, 2001, and 2008-09. The most recent crisis period has taken a particularly severe toll on the pace of chartering activity. Only 15 new charters were established between the end of 2009 and the end of 2013. The highly cyclical nature of chartering activity suggests that, in the wake of the worst financial crisis since the Great Depression, a significant drop-off in chartering activity should not have been wholly unexpected.

If the experience of the last banking crisis is any guide, chartering activity can be expected to recover over the next few years as the effects of the crisis recede. As depicted in Chart 4, the lowest levels of industry-wide chartering activity before 2008 were registered in 1993 and 1994, when new charters amounted to fewer than

[6] See Berger, Demsetz and Strahan (1999), p. 150.

[7] For a detailed analysis of the complex combination of causes that led to the extraordinary number of bank failures in the 1980s and early 1990s, see FDIC (1997).

Chart 4

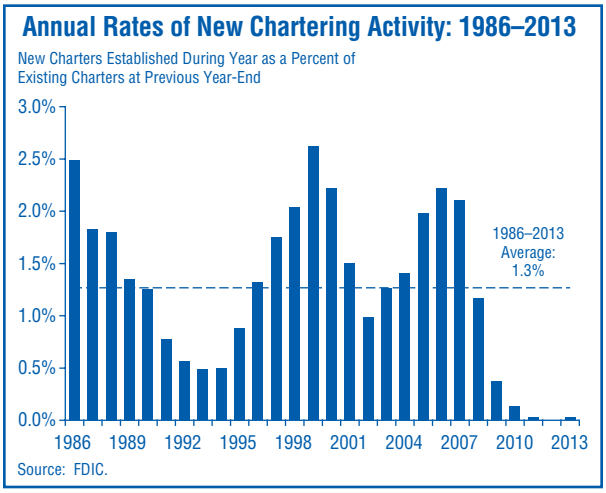
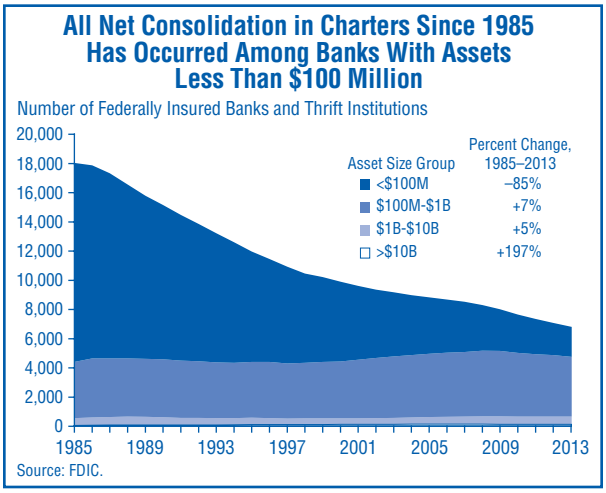


Chart 5



0.5 percent of existing institutions. By 1999, however, the pace of chartering activity had risen to 2.6 percent—the fastest of any year since 1985 and twice the annual average for the past 28 years. There are certainly reasons to think that chartering activity in this cycle might not recover as quickly or to the same degree in this recovery. However, to the extent that the pace of chartering activity does increase, we can expect the rate of net consolidation to slow in coming years.

Effects of Consolidation on the Size Distribution of Banks

Consolidation has mainly affected the smallest and the largest institutions. Consolidation since 1985 has had two main effects on the size distribution of the banking industry. It has dramatically reduced the number of institutions with assets less than $100 million, while greatly increasing the size and share of assets held by the largest institutions. Notably however, consolidation has had much less effect on institutions operating in the size categories between $100 million and $10 billion, which currently encompass most community banks.

All of the net reduction in the number of bank and thrift charters between 1985 and 2013 can be accounted for by the decline in the number of institutions with assets less than $100 million, which fell by 85 percent over this period (Chart 5). The number of institutions with assets less than $25 million declined by 96 percent during this period, from 5,717 to just 205. While the number of institutions with assets between $25 million and $100 million also declined by 77 percent during this period, some 1,851 institutions continued to operate in this size category in 2013.

It is important not to misread the net decline in the number of small charters as an indicator of their relative success or longevity. Among charters operating at the end of 1985, the rates of failure, voluntary closure, and overall attrition through year-end 2013 were lower for institutions that started out with assets less than $100 million than for those in any other size group (Chart 6). Equivalently, the proportion of institutions starting out with less than $100 million in assets in 1985 that were still operating in 2013 was greater than that of any other size group.[8]

The second way that consolidation has reshaped the size distribution of the banking industry is by generating tremendous growth in the size and share of industry assets held by the largest banking companies. The share of industry assets held by the top 10 banking organizations rose from 19 percent as late as 1990 to 56 percent at the end of 2013. In all, the total assets of institutions with assets greater than $10 billion grew from $1.1 trillion (28 percent of industry assets) in 1985 to $11.9 trillion (81 percent of industry assets) in 2013 (Chart 7).

Institutions with assets between $100 million and $10 billion have increased in number and total assets. Somewhat overlooked amid these large changes at either end of the size distribution is the relative stability

[8] The reason institutions in this smallest size group could experience the lowest rate of attrition and yet see their numbers decline the most in percentage terms was that so many of them managed to grow into one of the larger size categories. In all, some 2,777 of the institutions that started out in 1985 with assets less than $100 million were still reporting at year-end 2013 in one of the larger size categories. In fact, 12 of them reported total assets of more than $10 billion in 2013.

Chart 6

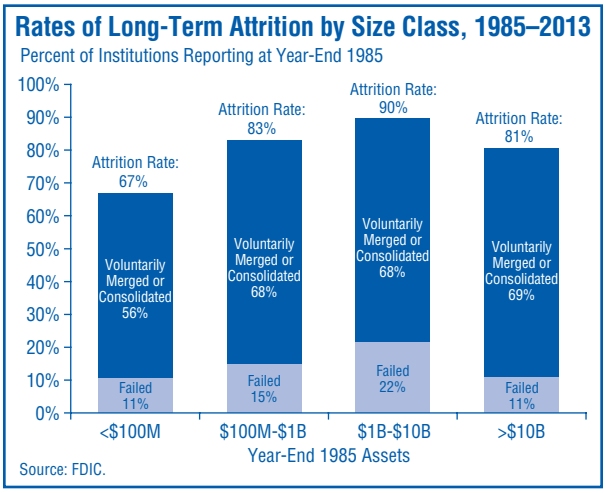
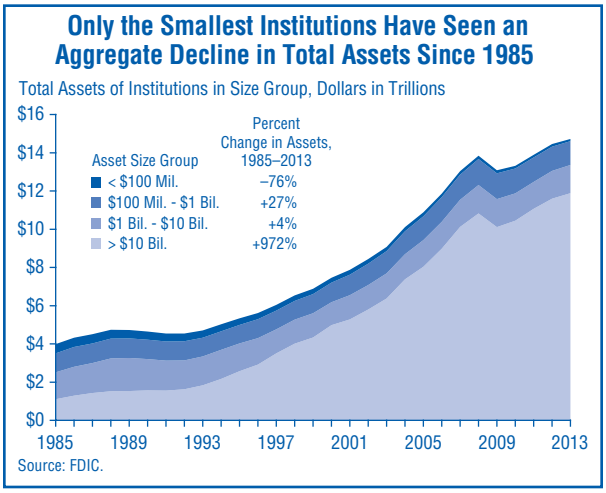


Chart 7



that has been observed among banks between $100 million and $10 billion in assets. As depicted in Chart 5, the number of banks with assets between $100 million and $1 billion increased by 7 percent between 1985 and 2013, while the number of banks with assets between $1 billion and $10 billion increased by 5 percent. These groups of institutions also experienced growth in terms of total assets. The assets of banks between $100 million and $1 billion increased by 27 percent between 1985 and 2013, while banks with assets between $1 billion and $10 billion grew by 4 percent (Chart 7).

One reason why this stability in the $100 million to $10 billion size category is so important for this study is that it is in these size groups where most community banks currently operate. At year-end 2013, some 68 percent of community bank charters held assets between $100 million and $10 billion.[9] Another reason not to overlook the relative stability of these institutions is the research that has recently been done on economies of scale in banking.[10] A recent FDIC study explored the issue of economies of scale in community banking and the extent to which the presence of economies of scale may have induced mergers and acquisitions that contributed to banking industry consolidation over time.[11] While the magnitude of economies of scale among community banks was found to vary according to lending specialization, most of the cost benefits from scale appear to be achieved for community banks with as little as $100 million in assets (Charts 8 and 9). What this implies is that while economies of scale may help to explain the large declines that have occurred over time in the number of banks with assets less than $100 million, they do not appear to have had nearly the same effect on banks bigger than $100 million. As such, economies of scale do not appear to be working against the majority of community banks.

Community Banks Have Been Highly Resilient Amid Consolidation

By focusing strictly on size group definitions, the previous discussion provides only a limited account of the effect of consolidation on community banks. In part, these shifts in the asset size distribution reflect the limitations of relying on fixed asset-size categories, as any yardstick measured in nominal dollars is likely to shrink over such a long period of time.[12] A more robust analysis of how consolidation affects community banks requires a functional definition of the community bank that is not strictly based on asset size. This is precisely

[9] The term "community bank" here refers to institutions meeting the definition established in the 2012 *FDIC Community Banking Study*.

[10] The term economies of scale refers to the relationship between the cost of producing a unit of output and the level of output. To the extent that average costs fall with the level of output, then a firm can be said to experience economies of scale. The existence of economies of scale is important to understanding consolidation in banking. To the extent that they exist, economies of scale can render smaller institutions uncompetitive, making them more likely to exit the industry over time. Improved operational efficiency has been posited as one of three main motivations behind bank mergers, with the other two being increased market power and increased access to the regulatory safety net. See Berger, Demsetz and Strahan (1999).

[11] Jacewitz and Kupiec (2012).

[12] Between 1985 and 2013 the consumer price index increased by 2.2 times, the total assets held by federally insured banks and thrifts rose by 2.7 times, and the nominal size of U.S. Gross Domestic Product (GDP) rose by 3.9 times.

Chart 8

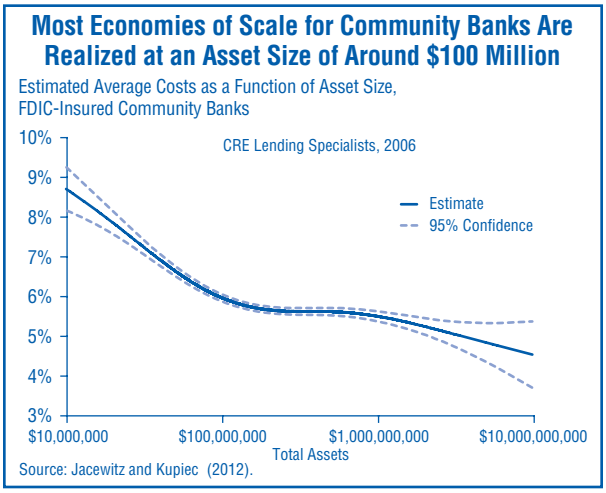
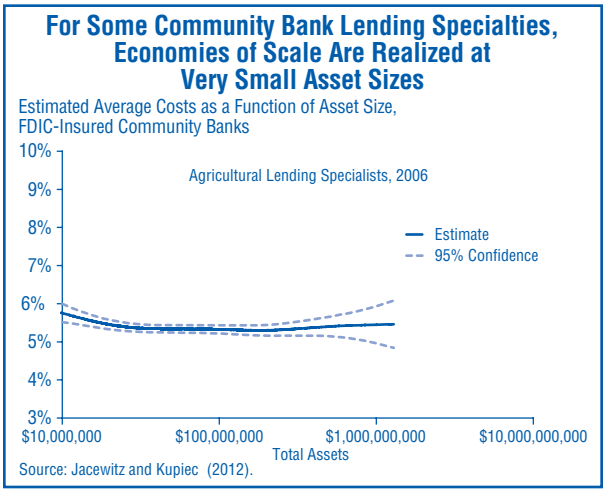


Chart 9



the type of definition that was introduced in the 2012 *FDIC Community Banking Study*.

While they are frequently thought of strictly in terms of asset size, community banks are more accurately described in terms of how and where they conduct business. Community banks tend to focus on providing essential banking services in their local communities. They obtain most of their core deposits locally and make many of their loans to local businesses. For this reason, they are often considered to be "relationship" bankers as opposed to "transactional" bankers. This means that they have specialized knowledge of their local community and their customers. Because of this expertise, community banks tend to base credit decisions on local knowledge and nonstandard data obtained through long-term relationships and are less likely to rely on the models-based underwriting used by larger banks.

The 2012 FDIC *Study* incorporated a number of these considerations into a new research definition of the community bank based on publicly available data that describe banking activities and the institution's geographic scope of operations.[13] Because this definition is not strictly based on a fixed asset-size threshold, it does not automatically "define away" community banks as smaller institutions grow, merge, or acquire other banks. An implementation of this definition using year-end 2012 data resulted in the identification of 6,544 community banking charters operating within 6,141 community banking organizations.[14] Based on this more robust definition, we are better able to analyze the effects of consolidation on institutions engaged in community banking, as opposed to institutions operating within arbitrary, fixed asset-size thresholds.

The vast majority of FDIC-insured institutions operate as community banks. The most obvious indicator of the resilience of community banks in the face of industry consolidation is the fact that some 93 percent of FDIC-insured banking charters met the community bank definition at year-end 2013, up from 87 percent at the end of 1985 (Chart 10). While the total number of federally insured institutions declined by 62 percent over this period, the decline among noncommunity banks (78 percent) was actually greater than that among community banks (60 percent).

Notwithstanding the relative stability in the community bank share of banking charters, the community bank shares of offices and assets have steadily declined since 1985. As a share of total banking offices, community banks have experienced a gradually declining share over time, from 53 percent in 1985 to 35 percent in 2013 (Chart 11). In large part, this trend reflects the large increases in geographic scope seen among

[13] Appendix A of the 2012 FDIC *Study* details the implantation of this definition using publicly available data. See: http://www.fdic.gov/regulations/resources/cbi/report/CBSI-A.pdf. Listings of FDIC-insured institutions according to whether they meet this definition are provided on the FDIC website at: http://www.fdic.gov/regulations/resources/cbi/data.html

[14] The community bank analysis conducted in this paper generally follows the convention established in FDIC (2012) and Backup (2013) of defining community banks as of the end of each calendar year. The exception in this paper is our analysis of calendar-year 2013, which is based on community bank definitions as of year-end 2012.

Chart 10

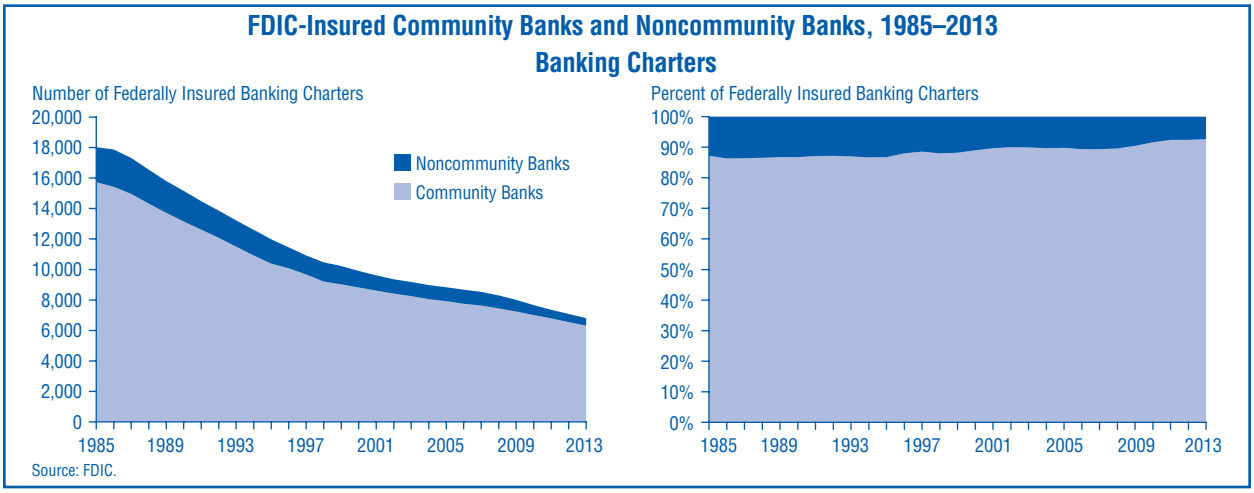
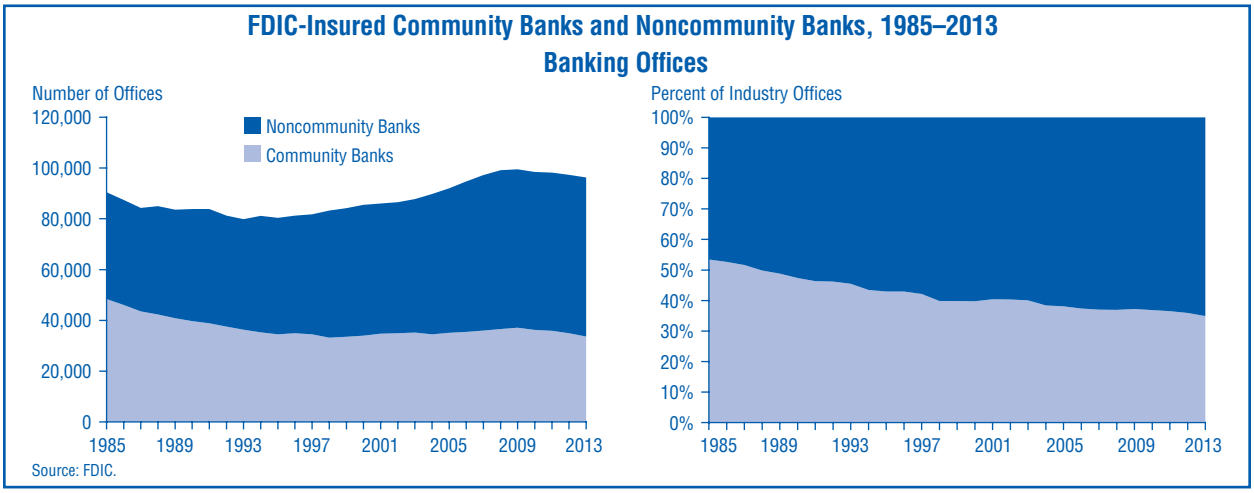


Chart 11



noncommunity banks over this period. The average number of offices operated by noncommunity banking organizations grew from 83 offices in 1985 to 154 offices in 2013, while the average number of offices operated by community banking organizations grew from 3 to 6.

The community bank share of banking industry assets also underwent a secular decline over this period (Chart 12). While community banks held 37 percent of industry assets in 1985, their share declined to just 14 percent by 2013. However, most of the gain in the share of industry assets held by noncommunity banks was concentrated in just a handful of institutions. Excluding the ten largest banking organizations, the community bank share of industry assets would have been 45 percent in 1985 and 31 percent in 2013.

The rate of long-term charter attrition has been far lower for community banks than for noncommunity banks—particularly over the past decade. As described earlier in the case of banks with assets under $100 million, simply tracking the net number of institutions in a group over time does not necessarily provide the clearest picture of their relative success or longevity. It is also instructive to look to their rate of total attrition over time as a measure of their long-term staying power. Among institutions operating at year-end 1985, some 68 percent of the community banks had failed, merged or otherwise consolidated by 2013, compared to 94 percent of noncommunity banks (Chart 13). This disparity in rates of total attrition is even more startling when measured during the period of relatively slow voluntary attrition since 2003. Between year-end 2003 and year-end 2013, the total

Chart 12

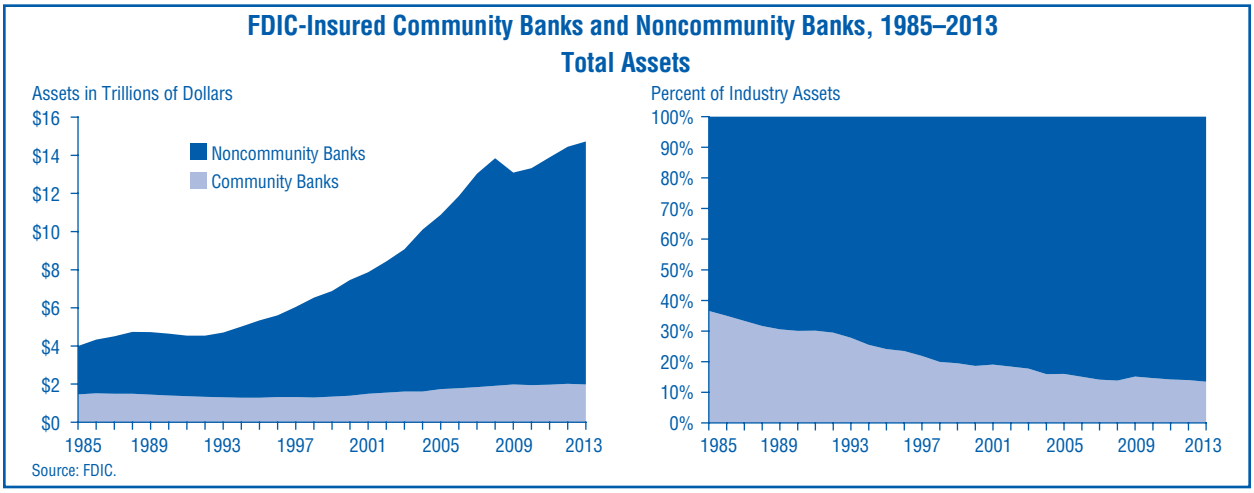
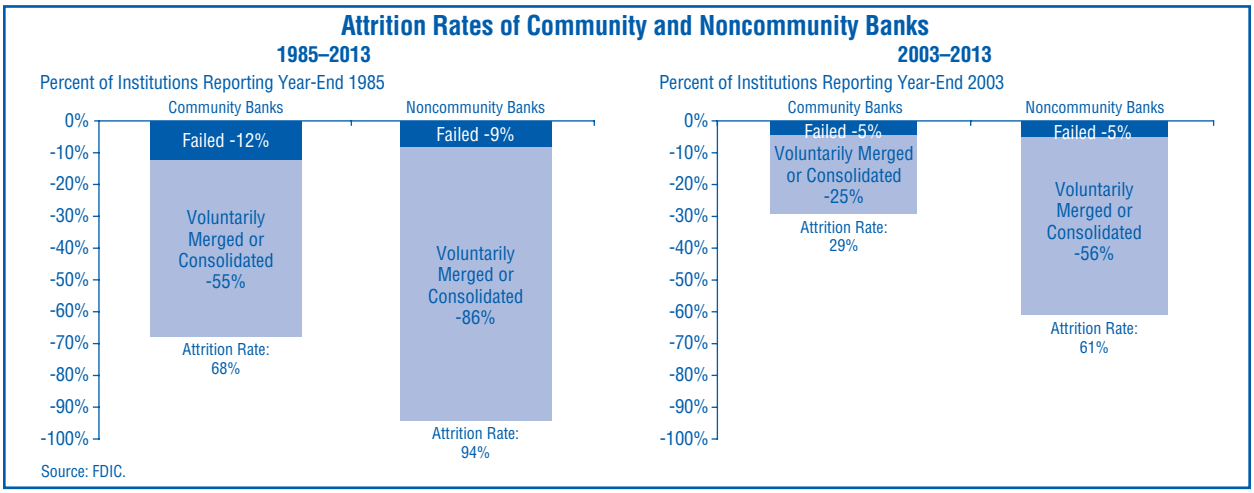


Chart 13



attrition rate for community banks was 29 percent, compared to 61 percent for noncommunity banks. The failure rate was identical for the two groups, rounding to 5 percent.

Despite the perception that community banks are losing their place in the banking industry as a result of consolidation, the data show that over the past decade they have failed just as often as noncommunity banks, while their rate of total attrition was less than half that of noncommunity banks.

When community banks are closed through failure or voluntary merger, nearly two-thirds of the time the acquirer is another community bank. The attrition of charters over the past decade, depicted on the right hand side of Chart 13, resulted in the acquisition of over 2,500 community bank charters by other institutions. While this could be interpreted as a net loss to the community banking sector, this would not necessarily be the case if the acquirer were also a community bank. In that event, the resulting institution would likely continue to carry out traditional lending and deposit gathering activities within a fairly limited geographic area, with relatively little impact on the nature of banking services provided to the customers of the bank or the communities it serves.

Analysis of the 2,579 community bank charters that were acquired between year-end 2003 and year-end 2013 shows that 65 percent were acquired by other community banks (Chart 14). Among community banks with assets less than $100 million, the share acquired by other community banks was 85 percent, and among those with assets between $100 million and

Chart 14

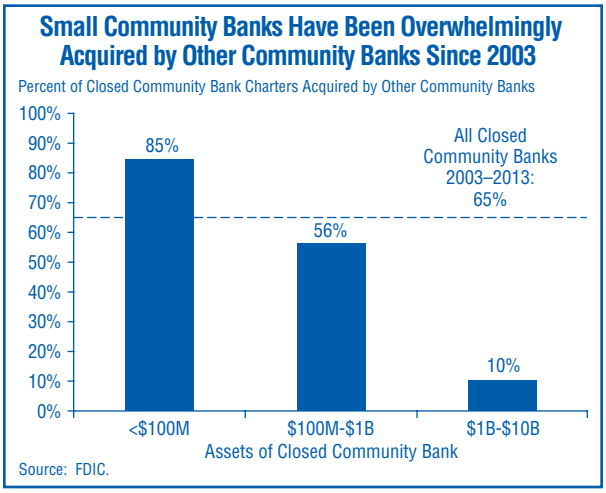
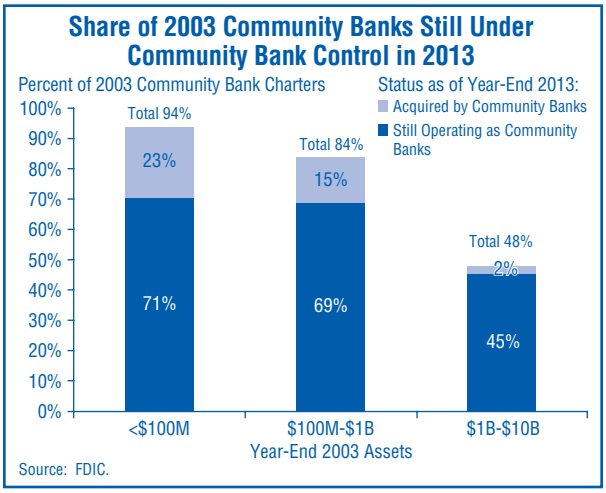


Chart 15



$1 billion, the share acquired by community banks was 56 percent.[15]

There may be two reasons why the percentage of community banks acquired by other community banks declines as asset size increases. One is that in most mergers the substantially larger institution acquires the smaller institution. Of the 1,668 community bank charters acquired as part of voluntary inter-company mergers between year-end 2003 and year-end 2013, the acquiring banking organization was larger than the target organization in 83 percent of the cases. This means that the ranks of potential community bank acquirers diminish rather quickly as the size of a potential merger target increases. While 62 percent of institutions with assets between $1 billion and $10 billion met the community bank definition at year-end 2013, only 2 percent of banks over $10 billion did so.

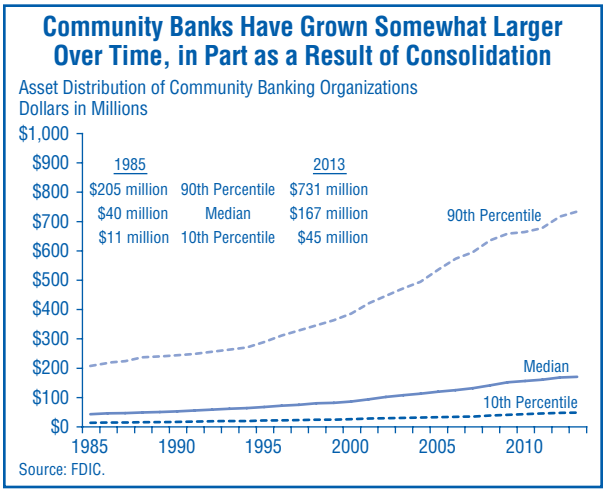
In addition, small community banks have proven to be far more likely than larger institutions to be acquired through voluntary transactions. Of community banks acquired between 2003 and 2013, only 9 percent of those with assets less than $100 million were failed institutions, compared to 21 percent of banks with assets between $100 million and $1 billion and 23 percent of those with assets between $1 billion and $10 billion. A higher share of "forced sales" among these larger acquisition targets may reduce the odds of finding a suitable community bank acquirer at the time of failure.

[15] Only 158 (6 percent) of the 2,579 community banks that were acquired between 2003 and 2013 held total assets of more than $1 billion at the time of acquisition.

The net result of community bank attrition and acquisitions over the past decade is depicted in Chart 15. The chart compares the percent of 2003 community banks, in three size classes, that either continued to report as community banks in 2013 or that had been acquired by another community bank sometime during the decade. Ninety-four percent of the community banks that started out in 2003 with assets less than $100 million either continued to report as a community bank in 2013 or had been acquired by another community bank sometime during the decade. For community banks that started out with assets between $100 million and $1 billion, the share was 84 percent. By contrast, fewer than 50 percent of community banks that started out with assets between $1 billion and $10 billion continued to operate as community banks at the end of the decade.

These results suggest a significant degree of underlying stability in the structure of the community banking sector overall, and especially among the smaller size classes of community banks. While attrition has led to consolidation among these institutions over the past decade, the vast majority have remained part of the community banking sector. It is in the largest size class of community banks—those with assets over $1 billion—that we see more institutions leaving the community banking sector either by changing their business model (and thereby no longer meeting the community bank definition) or by being acquired by a noncommunity bank. For perspective, it is useful to note that fewer than 5 percent of community banks held assets greater than $1 billion at year-end 2013.

Chart 16



Compared to the mid-1980s, today's community banking sector is composed of somewhat larger institutions that continue to provide essential banking services to a limited geographic market. We have shown that community banks have experienced relatively low rates of attrition and, when they do exit the industry, are usually acquired by other community banks. After nearly 30 years of industry consolidation, the median community bank in 2013 had grown to $167 million, more than four times the median size in 1985 (Chart 16).

This increase in the median size of community banks is consistent with both the large declines that have been observed in the number of very small charters (especially those with assets less than $25 million) and the existence of economies of scale at these very small asset sizes. It does not comport with claims that only community banks with assets of $1 billion or more could be considered viable.[16] In fact, almost 90 percent of community banks operating at the end of 2013 held total assets of less than $730 million.

Many of today's community banks have survived two episodes of bank failures and a long-term process of consolidation that has reduced their total number by around one-half. What they do have in common with community banks from previous eras is a focus on providing essential banking services in their local communities. Amid the changes associated with consolidation, community banks continue to serve this core function in our economy much as they always have.

As defined in the 2012 FDIC *Study*, community banks are vitally important sources of small loans to U.S. farms and businesses and as providers of mainstream banking services to rural communities, small towns, and urban neighborhoods that are frequently overlooked by larger banks. At year-end 2012, community banks held just 14 percent of banking industry assets, but held 46 percent of the industry's small loans to farms and businesses.[17] While they held just 18 percent of banking industry deposits in 2012, they held the majority of deposits in banking offices located in both rural counties and micropolitan counties. In addition, there are more than 600 U.S. counties (almost one fifth of all U.S. counties) that would not have had any physical banking offices operated by FDIC-insured institutions if not for those operated by community banks.

Conclusion

The post-crisis period has brought renewed debate as to the future pace of banking industry consolidation and the possible implications for community banks. Despite the concerns of some that a period of heightened consolidation could diminish the prospects of community banks, there are several reasons to think that these concerns may be significantly overstated.

Consolidation is by no means a recent development. Instead, it is a long-term trend that has been reshaping the banking industry since around 1980. About 80 percent of the charter attrition that has been observed since 1985 has taken the form of voluntary closings, mainly consolidations within holding companies or voluntary mergers between banking organizations. The period when the pace of voluntary consolidation was most rapid was between 1993 and 2001, shortly after geographic restrictions on banking activities were virtually eliminated. To the extent that these one-time regulatory changes took place 20 years or more in the past, their impact on future consolidation is likely to be limited.

Another 20 percent of charter attrition since 1985 has taken place through bank failures, mainly during the crisis periods of the late 1980s and early 1990s and since 2007. To the extent that regulatory reforms, prudential supervision and bank risk management can ward off a repeat of these episodes, failures also figure to contribute less to charter attrition going forward.

[16] See "Small Banks Look to Sell as Rules Bite," *Wall Street Journal*, April 3, 2014, p. C-1.

[17] These year-end 2012 calculations for community banks are found in Backup (2013).

New chartering activity has brought new resources into the banking sector over time, replenishing the number of charters amid ongoing attrition. Chartering has proven to be highly cyclical over time, and never more so than during and after the recent crisis. If the experience of the last banking crisis is any guide, chartering activity can be expected to recover over the next few years as the effects of the crisis recede. To the extent that this turns out to be the case, we can expect the rate of net consolidation to slow in coming years.

Much attention has been focused on the effects that consolidation has had on the smallest and the largest institutions. While all of the net reduction in the number of banking charters can be explained by the decline in the number of banks with assets less than $100 million, the largest institutions have seen tremendous increases in their size and share of industry assets. Too often overlooked is the relative stability among institutions with assets between $100 million and $10 billion, which have seen their number and their total assets grow amid industry consolidation since 1985. The disparity between the decline in very small charters and growth among charters between $100 million and $10 billion suggests that economies of scale offer only a limited explanation for consolidation, and that community banks have been much less affected by consolidation than is commonly thought to be the case.

Conducting analysis using the FDIC's functional definition of the community bank further demonstrates the resilience of community banks in the face of long-term consolidation. After more than 30 years of industry consolidation, well more than 90 percent of banking charters met the FDIC's community bank definition at the end of 2013. Second, the rate of long-term charter attrition has been far lower for community banks than for noncommunity banks, particularly over the past decade. In addition, when community banks are closed through failure or voluntary merger, almost two-thirds of the time the acquirer has been another community bank. In these cases, the nature of banking services provided to the customers and communities served by these institutions can be expected to remain relatively unaffected by consolidation.

The net result is a community banking sector made up of institutions that tend to be somewhat larger than was the case in 1985, but that otherwise continue, as before, to make loans and take deposits within a fairly limited geographic area. After more than 30 years of industry consolidation, community banks still serve as vital sources of credit for small businesses and providers of banking services to communities that might not be served by noncommunity banks. The available evidence strongly suggests that they will continue to carry out these important functions for the foreseeable future.

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