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Remarks by Secretary Tim Geithner Before the Independent Community Bankers of America Annual Washington Policy Summit

Timothy F. Geithner

U.S. DEPARTMENT OF THE TREASURY

Press Center

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As Prepared for Delivery

WASHINGTON – Thank you, Mike and Cam Fine, for your leadership of the ICBA and for your work on behalf of community banks.

Everyone here should know that three days after I was sworn in as Treasury Secretary, Cam Fine was in my office talking about the ICBA.

Community banks play a vital role in our financial system and a central role in our economy.

Yours are the banks where children open their first savings accounts and then come back years later to get a small business loan or to get help buying their first home.

In a time when financial innovation has put more and more distance between borrower and ultimate lender or investor, yours are the banks where staff and customers greet each other by first name, and where relationships still define the business of banking.

Of the over 8,300 banks in America, 92% are small or mid-sized banks, with assets below $1 billion.

And as a group, you entered this crisis on average with strong capital positions, and that has allowed many of you to be a source of credit during a period of enormous challenge for businesses and families across America.

Lending by small banks held up better last year than lending did overall, or by large institutions.

Community banks have accounted for more than one third of the dollar volume of loans to small businesses – the businesses which in turn have accounted for the majority of new jobs created annually over the past decade.

And your banks provide financial services to communities that would otherwise not have them. Of the 9,800 banking offices located in communities with populations under 10,000, more than two-thirds are community banks. In these markets, the local bank is the essential and the indispensible provider of banking services and credit.

At a time when many Americans have lost faith in the financial system as a whole, a Gallup poll conducted in just the past week found that 69% of customers have a lot of confidence in small and medium size banks.

Collectively, you are a source of strength and resilience for the U.S. financial system. And you will play a critical role in laying the foundation for economic recovery.

When President Obama took office, the country was facing a deep recession and a damaged financial system.

In the months immediately preceding our arrival, American employers were shedding jobs at an average of 700,000 a month, auto sales were plunging at a 38% annual pace, and new single-family home sales had fallen from their 2005 peak by three-quarters.

Facing these extraordinary challenges, this Administration and the Congress responded with extraordinary action. We enacted a historic economic recovery plan that is giving 95% of American households a tax cut, creating or saving 3.5 million jobs, and helping 1.4 million Americans purchase their first home by providing $6.5 billion in tax credits.

We have taken action to stabilize our housing market and avoid foreclosures; to boost new consumer and business lending by re-starting the market for securities; and to create a market for old mortgage loans and securities that are keeping banks from lending by weighing down their finances.

And we just concluded an unprecedented regulatory review of the nation's largest banks to bring greater transparency and new capital into the financial system.

On the strength of these efforts, the financial system is starting to heal. Concern about systemic risk has diminished. And overall lending conditions have started to improve.

- Spreads for investment grade corporate bonds have fallen about 210 basis points and spreads on high yield corporate bonds are down about 800 basis points since the end of November.
- Risk premiums in short-term inter-bank markets have fallen 275 basis points over roughly the same period, and the cost of credit protection for the largest U.S. banks has fallen by about 150 basis points just since early April.
- With the help of our lending facility with the Fed, new securities issuance has started to revive. Spreads for AAA credit card receivables ABS have fallen about 300 basis points from their peak.
- There has been more issuance of consumer asset-backed securities in the past two months than in the preceding five months combined.
- In our housing market, interest rates on 30-year mortgages have dropped to an historic low of 4.8%, and refinancing has surged. These are all welcome signs, but the process of financial recovery and repair is going to take time.

We have already seen a substantial amount of adjustment in our financial system. Leverage has declined. The more vulnerable parts of the non-bank financial system no longer exist. Banks are funding themselves more conservatively. These are necessary changes, and there is more restructuring ahead for the financial industry as a whole. But a substantial part of the adjustment process is now behind us.

This has been challenging period for community banks, even though, on average, you were better positioned to withstand the pressures of recession.

That is why Treasury, working closely with the FDIC and the Federal Reserve, has worked hard to provide support for community banks.

The Capital Purchase Program, established last October, provides viable financial institutions of all sizes an optional extra layer of capital for to help support lending.

These programs have benefitted communities across the country. Treasury has invested capital in the form of preferred stock in 579 institutions, of which over 300 are small banks. We have made investments of $1 million or less in 17 banks, $5 million or less in 147 banks and $10 million or less in 258 banks. We have also invested in 15 community development financial institutions.

One example is Farmers National Bank in Emlenton, Pennsylvania. Farmers National has around $400 million in assets and 12 offices throughout rural Western Pennsylvania. In 4 of those locations, they are the only bank in town.

Bill Marsh, the President of Farmers National, told us that he took a Treasury investment last fall because he wanted to make his viable bank even stronger and ensure that it could lend more aggressively.

With the $7.5 million investment, he has been able to expand lending to small businesses in his area. Since January Farmers National has provided $18.2 million in commercial and small business loans, an increase from the last quarter of 2008, despite a worsening economy.

The bank helped two real estate investors purchase older properties and turn them into affordable single family housing units. That means contractors, plumbers, electricians, and roofers are all getting work. And they helped an aspiring small business owner buy a small furniture store which he is now expanding. That means new hires.

Another example is the Bank of Commerce in Charlotte, North Carolina, which has around $170 million in assets. As the economy started to contract, their president, Wes Sturgis, wanted to make sure he had enough capital to generate growth going forward and capital from the Treasury allowed him to do that.

The $3 million Treasury invested through CPP meant Mr. Sturgis could lend more actively. In the 1st quarter Bank of Commerce issued $5 million in loans helping an insurance agency purchase an office building and enabling a local printer to expand his business and workforce.

The Administration fully supports the FDIC's request to increase its permanent statutory borrowing authority from $30 billion to $100 billion under its line of credit with the Treasury Department. This could prove an important step towards decreasing the FDIC assessment fees that your banks now face and that we know you are deeply concerned about.

We have also sought to ensure that small businesses can continue to grow and borrow from small banks such as yours. Beginning with our Recovery and Reinvestment Act we put in place a strategy for small businesses that increases loan guarantees and temporarily eliminates fees on SBA loans.

On March 16 the President, alongside Cynthia Blankenship and myself, announced a new $15 billion initiative of direct purchases to restart the secondary lending market. Together these measures are designed to give banks the confidence to lend and since March 16th, SBA weekly loan volume is up 25%.

And today I want to announce additional action we are taking to ensure your banks have the capital you need.

Using the proceeds of the repayments we expect to receive from some of the largest banks, we plan to re-open the application window for banks with total assets under $500 million under the Capital Purchase Program, and raise from 3% of risk-weighted assets to 5% the amount for which qualifying institutions can apply. This applies to all term sheets – public and private corporations, Subchapter S corporations, and mutual institutions. Current CPP participants will be allowed to reapply, and will have an expedited approval process.

In addition, we will extend the deadline for small banks to form a holding company for the purposes of CPP. Both the window to form a holding company and the window to apply or re-apply for CPP will be open for six months.

I want to close with a look ahead to the comprehensive regulatory reform efforts this Administration will propose in the coming weeks.

We have focused initially on addressing systemic risk, making sure those risks that arise are less threatening to stability and that the government has tools necessary to contain the damage they pose to the American economy. As in any financial crisis, this damage has been brutally indiscriminate. Ordinary Americans, small business owners, and community banks who did the right thing and played by the rules are suffering from the actions of those who took on too much risk.

Our goal is to limit the extent to which community banks and tax payers are forced to bear the burden of those institutions that take irresponsible risks. Capital, liquidity and risk management requirements must be more exacting for the largest, most interconnected institutions. They must be applied with a view not just to ensure the soundness of the individual institution, but to maintain the stability of the system as a whole. They need to be strong enough so that the system can withstand the impact of the failure of large institutions. As part of this we need to bring the markets where institutions come together, such as the derivatives markets, under a strong framework of oversight.

These changes will help prevent future crises and limit their severity. They will have to be accompanied by stronger tools for resolving crises when they happen, including the ability for the government to act more quickly to contain the potential damage cause by the potential failure of a large complex financial institution.

We have proposed resolution authority to help fill that gap. The proposal is structured as an extraordinary mechanism for extraordinary situations, and will be kept strictly separate from the existing FDIC deposit insurance fund. With this authority, the financial costs of intervention would no longer fall to those institutions that played by the rules and made conservative and prudent choices.

We believe that the combination of smarter, tougher regulatory standards to mitigate risks and resolution authority to manage risks when they arise will create a system that is more stable and resilient.

These steps will help level the playing field. They will help ensure that we preserve one of the most important strengths of the U.S. financial system, the thousands of community banks.

Thank you.

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