IT WAS THE BEST OF TIMES; IT WAS THE WORST OF TIMES. (WHICH IS IT?)

It's time to peep out of the fox holes and see what's really out there
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It was Charles Dickens who made this statement in the opening lines of his classic novel A Tale of Two Cities. There are many who disagree on which part of the statement aptly describes our situation as commercial bankers today, especially those of us who are working as community bankers.

Over the course of many years as a commercial banker, I've experienced the ebbs and flows of attitudes and practices that are considered "the norm" in the industry. There is no shortage of personal foibles or misjudgments by practitioners--though today the stakes seem higher and the scrutiny greater.

In the larger sense, the context of the discussion has changed and that's worth considering today.

Looking back at an industry that's only a memory

In the 1960s, the banking industry looked a lot different. There were many more banks and many fewer branches, due to the slow demise of unit banking laws that severely limited branching powers of banks on a state by state basis. Almost no state was the same and it was a confusing time for customers who didn't understand why in California there were branches on most every urban corner while in Illinois and Florida, to cite two examples, there was no branching permitted, period.

As an industry, we found our "work arounds." But the overall landscape was inconsistent and senseless. The clear advantage, though, seemed to be with the smaller players, as the large banks were prohibited from applying economies of scale in some obvious and cost-effective ways.

This eventually changed, of course, and community bankers were nearly overwhelmed in the next years by the "convenience" that the very largest players were able to offer their customers.

By the late 1960s we were suffering through a very real systemic liquidity scare. Banking law and regulation prohibited market forces from operating freely for a time. The results were upside-down loan-to-deposit ratios and sometimes upside-down net interest margins. The playing field got releveled, but more in favor--it seemed--of the very large banks rather than the very small.

As we entered and progressed through the 1970s, all of us active as bankers in those days remember the inflationary distortions in our economy. These included the very real fears of our customers who were forced to manage their way through an uncertain economy and the distortions and stresses of inflation on their balance sheets and income statements.

The 1970s were also a period of legislative "activism," where we saw significant changes in the way we were forced to deal with our customers. Truth in Lending (Regulation B), the Community Reinvestment Act, and the substantial rollback of limitations on what banks could pay on deposits (Regulation Q) come most quickly to mind. Many bankers, probably myself included, considered the changes in Reg B and Reg Q as existential threats to our business models, almost regardless of our individual bank size.

Regulation begins to bite

Regulation (or perhaps a peculiar selective absence of it) took other forms starting during that time. I remember my boss saying to anyone who would listen that the way you could tell what business lines in a commercial bank were unprofitable were to identify those not offered by Merrill Lynch.

I remember vividly how we felt hamstrung by limitations on what we could do while Merrill Lynch and others went after our business-line customers with vigor and not without considerable success. These were also that days of "sox and stocks" when Sears Roebuck began to offer business lines dealing with consumer financial needs. In other words, our competition could pretty well do as it pleased but we were forced to conform to "obsolete" and "unfair" regulatory requirements.

The 1970s and 1980s finally faded away as did the pain and difficulty of a prime rate of 18% deemed necessary early in that period by then-Chairman Volker and his colleagues on the Federal Reserve Board of Governors. What we experienced next was an unsettled period of economic growth and pronounced distortions of the commodity prices of oil and natural gas internationally that worked their way into our domestic economy. These strains produced turmoil and loss for many oil field banks. I was there and experienced difficulty and pain I'd never expected to see as a commercial banker.

Those bankers a thousand miles away were hardly aware of our distress in Texas and Oklahoma. But they did see firsthand, sometimes with direct experience in their own portfolios, how net interest margins could go upside down when current rates rose to levels considerably above rates of outstanding residential mortgages held in their portfolios. Today, these difficult days are most often referred to as those of the "S&L crisis," but I can assure you that the pain was not limited to thrift institutions.

The 1990s gearshift that didn't last

The 1990s were relatively quiet compared to earlier years but there were regional difficulties for banks. I was in New Mexico by then and the community and small regional banks experienced a significant commercial real estate recession for part of that decade. We also witnessed the merger of Citibank and Travelers Insurance that marked the end of the Glass-Steagall Act and a whole different view and emphasis of banking regulation.

Seemingly gone was the dead hand of regulation and in its place dawned an era of self-policing. While the larger banks responded less well than most of their community cousins, the entire industry struggled in that brave new world and no one emerged unscathed and without at least some level of blame for the pain of what was to come by 2008.

The first decade of the new century brought evidence of enormous debt bubbles including those of Silicon Valley and commercial and residential real estate.

By 2007 when the economic ground shook, everyone felt it and we were all frankly scared and bewildered. Do any of you recall those days of only three or four years ago fondly with any serious wish to relive them?

Dickens and banking in 2013

This brings me back to Charles Dickens and I'll call the question.

Is today, February 2013, among the best of times or the worst of times?

Do you really yearn for a return of the protective cloak of Regulations B and Q?

Do you think that there was absolutely NO need for CRA?

Do you want to return a patchwork quilt of state regulation on branching?

Let me say it in even plainer language. When have community bankers had so favorable an outlook for the next few years over the span of almost the last two generations?

Let's take inventory.

We are several months into an economic recovery. We have a new regulatory landscape not exactly of our choosing, but certainly probably less draconian than our then view of Truth in Lending or the complete deregulation of interest rates payable on deposits. The examiners, who share a degree of blame for the recent tumult, have made their points and have now backed off somewhat.

But perhaps most significantly, even the big banks regularly validate the worth of our business models. They fail to offer personal service to smaller-sized business borrowers while routinely offending their customers by being in their faces with endless sales promotions and solicitations of products and services designed primarily to benefit themselves rather to whom they are sold.

Community bankers should peer out of their fox holes and realize that the next few years could have more opportunity and success than any we've experienced in decades. It's we who have what the banking public really wants--service, concern, convenience, a willing ear and attitude and a grass roots connection to local business conditions.

Have the next few years ever looked this good?

About Ed O'Leary

Veteran lender and workout expert O'Leary spent more than 40 years in bank commercial credit and related functio working with both major banks as well as community banking institutions. He earned his workout spurs in the dark days of the 1980s and early 1990s in both oil patch and commercial real estate lending.

York in 1964, and worked at banks in Florida, Texas, Oklahoma, and New Mexico. He served as a faculty member and thesis advisor at ABA's Stonier Graduate School of Banking for more than two decades, and served as long as a faculty member for ABA's undergraduate and graduate commercial lending schools.

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