Good evening. I am so happy to be here in St. Louis. It has been many years since I have been here. I hope all of you will be able to taste a little bit of what St. Louis has to offer while you are here.

I have been really gratified by the warm welcome I have received, despite the fact that I am a self-confessed Red Sox fan. So let me congratulate the St. Louis Cardinals on winning the National League Central Division and being the other team with the best record in baseball. As we are poised to go into the post season, I just want to point out that since the Cardinals beat us in heartbreaking games in the World Series in 1946 and 1967, although we pulled out a win in the 2004 series, we are still down one in our matchup and would just be evening things up if we were to win this year.

I want to commend the leadership of the Federal Reserve, in particular the St. Louis Fed, and the Conference of State Bank Supervisors for visioning, mapping out and executing all of the efforts and events leading up to today’s conference on community banking. To the many policy makers and regulators who have come to participate - Thank you for being willing to engage with us. And please pass along our appreciation to all those who have been watching the live stream and reading the materials. I also want to extend appreciation for the work of the researchers. We’ve been told that the Fed is a research organization, and an issue doesn’t exist without research, so thank you for making these issues a reality. Finally, I want to recognize the participation of scores of community bankers, and industry representatives, both those who are attending today as well as those who participated in the town hall sessions. They represent thousands of their community banking colleagues from all across the country who work day in and day out to meet the needs of their customers and communities. On their behalf, I am very honored to be part of this important conference.

I want to begin with a disclaimer, which is that my comments tonight don’t reflect the position of any company, organization or government agency – they are just my own thoughts. They’re drawn from my experience as a community banker, my interaction with my peers around the country and my reactions to the materials prepared for this conference. So everyone has plausible deniability. But I credit the organizers with insuring that the voices of the community bankers are heard in this process.

Tonight, we’ll spend some time together reflecting on what we’ve shared today and look ahead to tomorrow. I am hoping, whether you are a policy maker, regulator, industry representative, banker or researcher, that each of you is not just absorbing as you go through this conference, but listening with an inquiring mind, open to possibilities and new ideas and asking yourself – what am I supposed to do with this? I will have thoughts on that in the latter part of my comments.

But before that, I want to begin with what brought us here and set some context for today’s findings. This process began with a question: *In this post financial crisis time, with dizzying changes in technology and financial services offerings, are community banks important or even relevant?* The macro statistics are daunting, and some have said that community banks are going the way of record stores and video rental companies. We can read in a variety of Federal Reserve and FDIC reports that community banks hold a smaller proportion of assets and deposits in the U.S. than their share of banking organizations. That point becomes starkly evident if you divide the banks into three groups: the megabanks, the large regional and superregional and the community banks.
A Federal Reserve reports note that the megabanks—with assets of between $250 billion and $2.3 trillion—consist of a mere 12 institutions. These banks, which accounted for roughly 0.2 percent of all banks, held 69 percent of industry assets. Another group numbering nearly 70 banking organizations—the large regionals and superregionals—with assets of between $10 billion and $250 billion—accounted for 1.2 percent of banks, while controlling 19 percent of industry assets. Whereas banks under $10 Billion, the community banks, accounted for 98.6 percent of all banks but only 12 percent of total industry assets. So there are a lot of community banks, but they control only a minority of assets and deposits. Also, as you can see in the latest FDIC summary of deposits report, they only hold a minority of the nation’s deposits.

Consolidation continues and the overall number of financial institutions is shrinking, which is exacerbating this trend. Questions about scale arise, and I know a number of community bankers who have posed the counter question to “Too Big to Fail” and that is, is there a level at which they are “Too small to succeed”? But this is where good research and input from “boots on the ground” is so important.

The research that was reviewed today, as well as the report of the town hall meetings, and other studies by the Federal Reserve and the FDIC, probed the fundamental question: Are community banks important? The picture that is developing is that yes, in fact they are very important.

We saw in today’s research that community banks play a critical and disproportionately large role in small business and farm lending, in access to credit, in residential lending and in community building and stabilization. We heard that the involvement of community banks enhances the chances of a startup and its associated jobs, to survive. We learned more about the deleterious impact that bank failures have on local economies. We heard about the concept of social capital and the lower default rates in lending community banks achieve because of their intimacy with the community.

We know that community banks play a critical role in communities that are not served or are underserved by other financial services institutions. We know that these banks themselves are important employers and job creators in their communities. They provide corporate leadership, and are a great source of philanthropy and volunteerism. And these banks, committed to their communities, are there in good times and bad.

In 2011, The Massachusetts Bankers Association reported on a study they had commissioned which showed that during and after the financial crisis, the larger institutions retreated from lending to small businesses, and community banks stepped into the breach and increased small business loans, which helped many businesses get through those difficult times. Although there is clearly more to know, there is empirical evidence that the issue of supporting the survival of community banks is not for the banks’ sake, but as David Cotney, the Commissioner of Banks of Massachusetts has said, “this is about jobs, small business and local economies.”

This recognition has brought us together. Because if community banks are important, and will continue to be, then we all have a common agenda — to understand the threats and challenges that face them, to identify successful evolving models, to craft a legislative and regulatory framework that provides for safety and soundness and yet does not threaten their viability. There is much to research. Tomorrow, we will look at some studies of bank performance and learn about the feedback from the town hall meetings conducted jointly by the Fed, the CSBS and the State Commissioners which will provide some insight into these questions.
So at the risk of focusing on the headwinds facing community banks, I do think it is important to level set as to the context in which they are operating. They are facing challenges in this rapidly changing world including the economy, customer expectations, competition, technology, legislation and regulation.

In terms of the economy, community banks are creatures of their customers and communities. The prolonged downturn and concomitant economic uncertainty have created a strain on both. Community banks have been more significantly impacted by the economic hardships faced by many rural communities.

I know I should be circumspect about talking about the impact of the interest rate environment in this setting, but the low rates and flat yield curve have created margin compression, which has particularly hurt community banks earnings, which rely to a great extent on interest income. The financial crisis also led to a negative perception of the banking industry, and this has impacted many financial institutions who had no involvement in the dynamics that contributed to the downfall.

The world around us is changing quickly, and that means that bank customers are changing in terms of their lives and their expectations. There has been, for example, a significant outmigration of population (especially young people) from non-urban areas, which has far reaching implications for these communities and the banks that serve them from the perspective of economic viability, workforce and succession planning.

Rapid adoption of technology has:
- Changed customer expectations and habits
- Unleashed new and rapidly evolving competition including many competitors outside the traditional banking industry
- And increased the cost structure for Banks to in order to try to keep up

For example, community banks are in a disproportionate bargaining relationship with vendors and core system technology providers which makes it hard for them to negotiate advantageously or change providers rapidly. Keeping up not only involves providing the latest in products and services, but also staying on top of and mitigating threats to information security. Other threats arise from Patent trolls and DDOS attacks.

In terms of competition, Community Banks face changing competition from:
- Too big to fail banks that have only gotten larger after the financial crisis
- The alternate providers of payment systems that pose an enormous threat to the regulated banking industry and particularly to community banks.
- Monoline non-bank providers like online Mortgage Lenders
- Credit Unions and government agencies like Farm Credit that compete for same customers but pay no taxes

Again, I say with only a modest degree of trepidation in this setting that changing and increasing regulatory expectations have presented significant challenges to community banks. When asked about it, bankers cite the significant difficulty of anticipating and complying with the changing regulatory landscape. This uncertainty from all the changes has made it difficult to plan and execute effectively.
When one particular regulation was introduced last year, my bank received conflicting guidance from three different sources: consultants, trade associations and the government. We took the most conservative and costly approach because of that uncertainty.

In some cases, as noted in a recent ABA survey, the strategic technology partners whom the community banks employ are not prepared to support the banks’ compliance with new regulations. The cost of compliance has skyrocketed, adding to the overhead cost of community banks. We have quality control and a system of checks and balances for compliance. We have internal checkers who check the checkers, and then we frequently have multiple layers of consultants to check the people who are checking the checkers.

All this adds up. Sometimes I feel our mortgage operation is a compliance shop that does a few loans on the side. Economies of scale are not available to the smaller institutions; therefore the community banks bear a disproportionate burden. And this regulatory burden is not only at the federal level, State and Local ordinances are springing up that are creating a patchwork of divergent restrictions and expectations. And finally, regulatory tightening has inhibited lending.

If we were on Cape Cod, the marine forecast for community banks would be for a N’oreaster with heavy swells.

The conclusion we can draw from the research presented so far is that community banks are a unique model that contributes to the economic and social fabric of our country, especially in underserved areas. So if there are all these challenges, but Community Banks are so critical, what can be done to help them mitigate threats and evolve to succeed in a changing landscape?

I would propose that it takes a commitment on the part of all stakeholders to the goal of supporting the existence and vitality of community banks, and to employ creativity and innovation on the part of all stakeholders to achieve that goal. I’d like to address each of you separately with thoughts about what each of you can do. And I think it is important that you understand the changing roles of each stakeholder, because that will impact your collaboration and coordination.

I’ll start with the community banks themselves. Do they have any strengths they could leverage to survive and thrive? What is their competitive differentiation? Community Banks have demonstrated strengths that can be leveraged. The research documents their intense local knowledge and the advantage that provides in the lending arena.
What else has the research demonstrated? They have a smaller size, flatter organizations and management logistics that can enable them to be more nimble. They tend to have customers based on strong relationships, especially small business. They are closer to their customers, and can get a sense of changing needs in real time, which helps them tailor their offerings to niches and local needs, such as agribusiness, energy, or fishing. They are usually more involved in communities in a very localized way. Community banks tend to hold high levels of customers’ trust, because people know local management. Customers see them at the grocery store and their children play soccer together.

What will they need in order to leverage their strengths? Leading up to this conference, many community bankers from across the US participated in town hall meetings with their state commissioners. I’ve had a chance to preview some of the comments from my community bank colleagues and was struck by the insights that came out of these meetings. For example, a community banker in West Virginia said that, “management teams and board members must be visionaries, strategists and problem solvers.” I’d like to elaborate on that thought a little bit and then add some thoughts of my own about what community banks need to leverage their strengths.

Community Banks need forward thinking management teams engaged in ongoing dialogue and divergent thinking about what is new and promising to create opportunities that could be capitalized upon. They need engaged boards with complementary skill sets to insure broad discussion of issues and they need to insure that dissenting viewpoints are heard and addressed. They need to dream and imagine new business models or their banks will quickly become irrelevant.

This can’t just be done around the margins. They need to look for uncontested space in how they do what they do, in what they offer, and to whom they offer it. They need to look for pockets of opportunity and niches they can fill. And take all the possibilities afforded by new technology and create the kind of customer experience that sustains and evolves the deep relationship they have with their customers. And use that technology to create effective process improvement.

They need to draw on some great current management thinking from people like Gary Hamel, David Rock and Daryl R. Connor about culture and people, about the necessity to:

- Engage in strong talent management focused on “creating a mind-set of discovery and openness”.
- Focus on “potential versus limitations to use the knowledge we have in different ways”.
- And to develop organizational cultural adaptation to “absorb and build resilience to the unexpected implications of discontinuous change occurring”.

They must embrace a focus on developing their younger employees. And speaking of younger people, they need understand the frames of reference of the new generations of customers in order to develop new ways of attracting and serving them.

Tomorrow we will see some examples of successful, adaptive banks. But, they can’t do it all on their own. They will need support from the Industry. And they need an appropriate legislative, policy and regulatory framework in which to operate, one which recognizes and adapts to the changes the banks need to make.

What kind of support from the industry? Undertake a separate approach to supporting community banks. Work with policy makers and regulators on a rational, coherent tiered Legislative and regulatory
framework that recognizes that community banks are different larger institutions. Keep community banks updated with information on legislation, regulation, innovation and best practices, and threats.

Take measures to address scale issues through shared services such as technology or professional services like compliance. Provide training and education. Help address the image issues. Help attract people (particularly young) to the industry. Help insure that Community Banks have equal and competitive access to the reformed secondary market in order to have access to market liquidity, insuring a competitive mortgage market, allowing them to retain their customers and not be required to sell the servicing and their customers to large bank aggregators.

Turning now to Policy Makers and Regulators, - what is their role? First of all, begin with the premise that small banks are very different than large ones. As I said before, community bankers have a closeness to their customers that is unique. We bump into the people to whom we lend money and who use our other products and services every day. We have to look them in the eye. It brings a different level of social responsibility. When our customers talk about our bank, despite the fact that we are a mutual, they say, “Cape Cod Five, that’s my bank”. They are vested in us and we are in them.

In addition, the level of complexity of community banks is different. Most community bankers are involved in the the most straightforward of financial products and services. This reduces many risks and should be incorporated into how they are examined and regulated. Their scale is very different. The financial impact to the bottom line of adding an FTE of a top 20 bank probably has a lot of zeros before the number in terms of percentage, whereas with a community bank, it is a very meaningful number. The need to add FTEs or engage consultants to keep up with increasing regulation has been a significant burden for community banks.

So the challenge to policy makers and regulators is to step back and ask:

- What is the policy or regulation really trying to address?
- What has been the involvement of community banks in this matter?
- Has actual harm occurred in a significant way with community banks?
- Are there other, less burdensome ways of effectuating the desired outcome?
- Working collaboratively with other regulators, are there creative or innovative ways of addressing this?
- Can technology and modern methodologies be brought to bear by the regulators that would minimize manual entry and recordkeeping on the part of banks?
- Is a tiered approach, which recognizes the unique nature of community banks, possible?

Basel III and some of the CFPB rulemaking are examples of beginning to break new ground with tiers of regulation. Are there other ways in which this can happen?

I would also suggest that policy makers and regulators recognize that the genius of community banks is meeting local needs. Regulation and oversight should be flexible enough to support that. For example, in the markets we serve, my bank has number one deposit and lending market share in our market on Cape Cod and significant share on Nantucket and in the surrounding areas. It is not because the large institutions aren’t there – in most of the communities we serve, they are and have been for years. It is because the wonderful people at my institution know how to lend to and support businesses and individuals in a highly seasonal economy where most people need to make a full year’s earnings in 13 weeks and a rainy August can spell disaster.
So whether it is a seasonal or rural or other unique community – support the community banks in delivering their highly localized solutions. Be aware of challenges that are faced and help address them. Be proactive, for example, about addressing the unlevel playing field created by the tax exempt status of credit unions and the competition posed by agencies like Farm Credit. So in terms of the policy and regulatory role, this conference and all that has gone along with it is a good an encouraging step in the right direction, as have been Chairman Gruenberg’s community bank initiatives at the FDIC and Comptroller Curry’s at the OCC.

You researchers have been patient as I have addressed the other stakeholders, but you knew your time would come. We have just scratched the surface on the questions to be asked regarding the impact of community banks on their communities, especially rural America, consumers, small businesses, and the creation and sustainability of jobs.

There is a need for research on the impact and cost to community banks of current and proposed policy and regulation, national, state and local. The potential impact and implications of a tiered system should be probed. One of the things that could be researched is the number of community bank “Good” loans that fall outside of QM. An analysis of our loans falling outside of QM show that, by and large, due to careful underwriting, they did not contribute to any meaningful increases in delinquency or foreclosure activity. Something that was raised at several town halls was the possibility of tax credits or incentives for “investments” in communities - could this be researched?

There is not sufficient current data on the impact of Non-Bank Competition on Community Banks from the Payments System, Mobile Wallets, Non-Bank Mortgage Providers, and from competitors which operate outside the regulated banking industry and are lightly or unregulated. We’ll begin looking at this tomorrow, but what have been Successful Strategies? What is working and why? What are opportunities? Are these reproducible? With your research, you will make these issues real. You will open possibilities. You will generate the right energy and conversation. Your research will support policies, regulations and strategies of action to provide for an appropriate regulatory framework and will serve as a catalyst for survival and growth.

However, I will also challenge the Fed and the researchers to work thoughtfully together with the industry in the framing up and dissemination of this research. I encourage the Fed, the CSBS, the researchers and all the stakeholders: the other regulators and policy makers and the industry to work together to prioritize, to help put findings in appropriate context and to explore the ramifications.

We are beginning to get a greater understanding of the fact that the survival of community banks has broad implications for our country. We are seeing that what is critical is a diverse banking landscape that supports its economic vitality. And we are beginning to gain insight into what our country would look like if there were no community banks. That should be our call to action. Tomorrow we will look at Bank performance and community banks that have been successful in these stressed and changing times. We’ll review the feedback from Town Hall meetings.

Tonight I encourage you to continue the dialogue. Let’s make this conference a springboard for creating the conditions from which sustainable strategies can emerge and to stimulate the creativity and innovation on the part of all stakeholders to take on this important matter. Let’s organize ourselves around our common goals and work together to support businesses, jobs and communities across the country by supporting the viability of community banks. Thank you for your time, your efforts and your interest.