“Any fool can make something complicated. It takes a genius to make it simple.”

— Woody Guthrie, passed away on this day in 1967

In This Issue...

This week, the seventh annual Community Bank Research Conference was held in St. Louis. The Examiner will cover the biggest highlights of the conference. More information on the research papers, speakers, and conference recordings can be found on the official conference website.

- Sentiment Index: Banker Optimism Remains Strong
- Community Banker Concerns Shift to Funding
- Podcast - Community Banks as the Pulse of Our Economy
- Highlights From Speeches at the 2019 Community Bank Research Conference

Banker Optimism Remains Strong

By CSBS Senior Executive Vice President Michael L. Stevens
The September CSBS Community Bank Sentiment Index came in at 121. This is a very small decline from the very strong initial reading of 122 in the last quarter. An index rating of 100 is neutral.

The index is calculated based on community banker expectations in seven key areas:

- Business conditions
- Monetary policy
- Regulatory burden
- Capital expenditures
- Operations expansion
- Profitability
- Franchise value

Bankers lowered their expectations for future profits and overall business conditions. In both areas, there was a shift from expecting “better” to expecting “the same.” Given the generally positive economic environment and performance of community banks, even being the same is good news.

Community bankers expect monetary policy to continue to be more accommodative. Comments in the press started suggesting a cut in the federal funds rate during the survey period for the national survey, which includes the index questions. The first-rate
cut occurred after the survey closed, with a second cut during the data collection for the current index. Overall, bankers expect this environment to continue.

Even as the September index is being released, there seems to be growing concern that contraction in economies outside the United States are now impacting the United States. Our hope is the data collected from community bankers to calculate this index will provide insight to what is actually happening at the local level as bankers talk to consumers, farmers and business people who live and work in the real economy. Currently, their optimism remains. Let’s see if that holds.

The next data collection will kick-off on December 2. Any bankers interested in participating in this five-minute survey should email index@csbs.org.

Community Banker Concerns Shift to Funding

Funding and cybersecurity top the concerns for community banks, according to the sixth annual community bank survey conducted by the Conference of State Bank Supervisors (CSBS). It is a marked shift from previous years, when regulatory compliance costs were found to be the chief issue for community banks.

This year’s survey showed 36% of banks said funding costs were the most likely factor to influence future profitability, up from 11% in 2016. More than 70% of respondents ranked cybersecurity as their most important risk. Only four percent of surveyed banks said that regulation was most likely to influence profitability, compared to the 60% of respondents who named it as a top concern two years prior.

In its sixth annual survey, CSBS canvassed 571 community banks in 37 states. Other key findings from the 2019 survey include:
Compliance-related costs increased 4% in 2018, in contrast to the 13% drop reported the prior year; however, with a total of $4.9 billion, those costs are much lower than the peak of $5.4 billion set in 2016.

Nearly 30% of bankers considered depopulation an important limitation to retaining core deposits.

While last year’s survey showed community banks were embracing technology, the actual number of those offering digital and online services remains largely unchanged due to cost.

An additional section called “Five Questions for Five Bankers” accompanied the survey, providing context for the national survey results at the state level during the same three-month period. State bank commissioners asked five questions to five community bankers in 30 states.

The questions addressed the effectiveness of the Economic Growth, Regulatory Relief and Consumer Protection Act, S. 2155 and the community bank business model, funding and liquidity concerns, technology and cybersecurity.

To access the survey report, click here.

Podcast - Community Banks as the Pulse of Our Economy

Learn More about the Sentiment Index

Economists, investors, policymakers, and reporters use all sorts of different “indicators” as guideposts to assessing the health of the economy. Some are purely informational
and numeric, like job growth numbers and changes in GDP. But others are based on feeling, like consumer sentiment. They’re basically asking someone “how’s it going?” and compiling all those feelings into a single indicator.

Getting a comprehensive picture across the country can be tough. But, there is one group that is connected to consumers and businesses alike that could provide us this valuable information. Community bankers are some of the most connected individuals in a wide cross-section of society, whose very livelihood relies on the success of neighbors and local businesses – rural, urban and in between.

In this podcast, we talk with Mike Stevens, Senior Executive VP at CSBS, who has examined, worked with, and promoted research on these community bankers.

Also discussed: a new economic guidepost six years in the making, designed to use community bankers nationwide to take the pulse of America’s economy. It’s called The Community Bank Sentiment Index.

Follow Simply Stated on your favorite podcast service:

- SoundCloud
- iTunes
- Stitcher
- PocketCasts
- PodBean
- TuneIn
Highlights From Speeches at the 2019 Community Bank Research Conference

Below are highlights of major speeches given at the 2019 Community Bank Research Conference, as well as links to the full remarks for each.

CSBS Chairman Bret Afdahl: How We Regulate Just As Important As What We Regulate

On the value of the conference:

In its short history, this conference has strengthened partnerships. Oftentimes, regulators speak to one another in a moment of crisis. This conference has brought together federal and state regulators, industry leaders and academics, to thoughtfully discuss current and future policy related to community banks. I would like to add that I hope it makes us think outside of our usual parameters to improve the way we regulate community banks so they can do what they do best – serve their communities.

This conference has a real impact on policy, and in turn, the communities in which these banks serve. And that is important. It underscores the need for all of us to give more thought to not only what we regulate, but how we regulate.

On major conference findings:
The research generated here has shown that leverage capital is an effective measure of capital adequacy for noncomplex banks. It has pointed out the limitations of the Herfindahl-Hirschman Index to gauge competitiveness. The research has identified areas where the federal appeals process of material supervisory issues could be improved. It also has shown the importance of the proximity of regulators to the banks they supervise. Likewise, the community bank survey has been a reference point for lawmakers, influencing legislation on important matters such as qualified mortgages and capital simplification.

CSBS President & CEO John Ryan: Applying Research to Supervision

On the impact of supervision:

We regulators need to own that supervision has an impact – and not just on the financial institutions we regulate. A paper presented yesterday proposed that regulatory relief for small bank holding companies has a real impact on local economies because it can boost their small business lending without affecting risk-taking or transparency.

On facilitating a level playing field in fintech and banking:

I think this is a great opportunity to further delve into how community banks can retain customers in a high-tech/fintech world. What type of consumer is going to be attracted to brick and mortar
banking operations that have embraced technology? Our panel of students yesterday gave us a very useful tool to test out these ideas. Banks – what is the sweet spot where your customer want to do business with you in the future? Who are these customers? How do you retain them? As regulators - what is our impact on competition? Are we facilitating on a level playing field, or one that advantages fintech? I do think we need to understand this as a network of regulators.

Federal Reserve Governor Michelle Bowman: Advancing Our Understanding of Community Banking

On the economic importance of community banks:

From my perspective, the Federal Reserve supports community banks as a central component of a strong, resilient, and stable financial system. Our system is made more resilient through a broad and varied range of institutions serving different types of customers, with community banks providing access to credit and other financial services in towns and cities across America. With the support of community bankers, these investments are the building blocks of a strong community and help support a vibrant economy across the country—from here in the Midwest to the coasts on either side.

On consolidation and profitability:

To better understand what is happening with these institutions, we
looked at several potential differences between small community banks that have been acquired and those that were not. Was it the smallest community banks, or those with the smallest markets, that were most likely to be acquired? It turns out that the key difference between these banks was not their geographic reach or their size, but rather their profitability. We find that small banks that were acquired by another institution were, on average, about the same size and geographic scope as other small banks but they were less profitable. This fact challenges the notion held by some that small scale or operating in a very limited geographic area is a disadvantage and it shows that many small, locally focused banks are performing well in a changing and challenging marketplace.

On the challenges of consolidation:

It is important to point out that many of the changes to community banking through consolidation that I have described, in a general sense, are a natural and often desirable consequence of competition in a vibrant market economy. However, consolidation is less desirable when it limits access and choice for customers without other benefits, or when it is an unintended effect of government regulation and the cost of that regulation rather than a result of vigorous competition. This isn't news to community bankers or to community banking researchers. It is not news to many people who live in small towns or urban areas who have lost access to community banks with deep roots in the community. And it is a major challenge for those who live in areas that lack access to service from any bank.
On how community banks must continue to adapt:

The adoption of mobile banking is a great start, but consumer expectations for a truly digital experience continue to grow. Banks must evolve with these expectations, and their technology service providers must evolve, as well. Existing core processing systems typically provide a number of different platforms for lending and deposit-taking activities. These platforms may use differing data standards and may not interact with one another, let alone solutions from other companies.

On the battle between data and security:

Data is the new capital. Financial service providers are using data and technology to develop new services for consumers. These providers often rely on data aggregators to consolidate a customer's financial information from one or more institutions. The data aggregator can then present the consolidated information in a user-friendly format to these service providers. Consumers clearly benefit from the innovation and competition that 'open banking' fosters. But these benefits do not come without some costs. Customer-permissioned data sharing raises a number of questions regarding data ownership, privacy, security, liability, and consumer control.

Discussing a new tech lab:
Broad adoption of technology – both at the FDIC and within the banking system – was one of the driving factors behind our decision to establish a new office of innovation within the FDIC. The FDIC Tech Lab (FDiTech) will collaborate with community banks on how to deploy technology in delivery channels and back office operations to better serve customers. Many of the institutions we supervise are already innovating, but a broader adoption of new technologies across this sector will allow community banks to stay relevant in the increasingly competitive marketplace.

Back to Top