“SMILING THROUGH THE APOCALYPSE: THE SEQUEL”

REMARKS OF COMMISSIONER JOSEPH A. SMITH, JR.

TO THE NORTH CAROLINA BANKERS ASSOCIATION DIRECTORS ASSEMBLY

GREENSBORO, NORTH CAROLINA

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I appreciate, as always, the chance to be with you. Whether in my office’s Bank Directors’ College or at this event, it is always gratifying to be with the directors of our State’s banks and to discuss matters of common interest. Your willingness to serve and your commitment to continued learning are among the most valuable assets your institutions have.

As I was preparing these remarks, I looked back over some prior speeches at NCBA events and ran across one from almost three years ago, June 2008 to be precise, entitled, “Smiling Through the Apocalypse.” The speech -- whose title was based on a collection of essays from *Esquire* magazine about the *last* Apocalypse (the ‘60s) -- included an assessment of the “subprime meltdown,” the debate over bank regulatory reform, and some ideas about what we should do in response. Given the passage of time, I thought it would be well to review what has actually happened and to discuss what we should do now. If sequels are good enough for Hollywood, they are good enough for us, no?

In 2008, I discussed with you the “subprime meltdown,” lamenting its projected losses to financial institutions and investors of $400 billion, and subtly needling the large national and international banks that were its victims. Regrettably, the damage has ultimately proven to be much larger and more widespread than I anticipated, with total losses to all stakeholders in the trillions and an ongoing tide of foreclosures and bank failures. And, I fear, we are not through with the aftershocks of the crisis and the attendant damage to our financial system and economy.

In 2008, I was concerned about the Paulson Plan for regulatory reform, including creation of a single federal bank regulator. I argued that such an approach would lead to further consolidation of the industry as a result of increased regulatory burden on community and regional banks. The good news is that the Paulson Plan was not enacted; the other news is that Dodd-Frank Act was, bringing with it a substantial amount of regulatory activity, some of which is applicable to most North Carolina banks, much of which is not. Consolidation of the industry is continuing.

On the basis of my analysis of our circumstances in 2008, I suggested that we should: make the case for a diverse banking system; advocate for two-tiered regulation of banks, based on size and complexity; broaden the asset mix of North Carolina banks, away from commercial real estate; and address issues of equity and access to financial services. While all of these were, and are, worthy ideas, our current circumstances require a new approach.

As I noted above, the consequences of the financial meltdown have been severe: significant reductions in national and state GDPs, increases in all measures of unemployment to very high and persistent levels, reductions in real estate values, and stress on state, local and personal budgets. While I am hearing some "green shoots" stories about recovery in our markets, the most credible analysis that I have seen suggests that you and I should plan for a long, slow recovery with above average unemployment.

While my view of our circumstances is sober, please know that it is far from hopeless. Our banks are, as a rule, well capitalized and well led. While it won't be easy, your banks are capable of surviving and prospering in the future. Further, I know from personal experience, that investors from around the country view North Carolina as a desirable place to put money to work. The beaches, the mountains, the Sand Hills, the Research Triangle, and our colleges and universities haven't suddenly ceased to exist and are attractive to them. Charlotte is still the capital of both Carolinas. We have a good climate for business and a shared objective of welcoming new investment and supporting it. Can we work our way out of this recession? To coin a phrase: Yes we can!

To get our economy back on track, we -- and I mean your institutions and my agency – need to reinvent ourselves to meet the needs of North Carolina today. From the beginning, in 1805, banks have had a special status under North Carolina law in order to provide the financial architecture necessary to support commerce, trade and a healthy economy. The Office of Commissioner of Banks, from its establishment during the Great Depression of the Twentieth Century, has had as it primary goal the safe and sound operation of banks so that they could perform their very important services to our State. The question for each of us to answer is, "How do we perform these important functions in 2011 and beyond?"

To start, we should seriously review the financial needs of North Carolina and its various regional and local markets. By "seriously," I mean more than collection of anecdotal evidence; I mean pulling together all the information we can get from universities, trade groups, state and federal governments, and other sources and then deriving from it as clear a picture as we can about what North Carolina needs.

We should then assess the capacity of the banks and other financial services providers to meet these needs. I include other financial services providers because banks alone may not be able to fulfill some needs. For example, there is clearly a need to restructure or refinance a number of commercial real estate loans that are currently on our banks' books. Given regulatory restrictions on CRE concentrations and the current levels of such loans on your balance sheets, the analysis may reveal a need to attract additional capital either to capitalize banks sufficiently to allow restructurings or take the loans off the banks' books or both. In such a situation, the best available solution may be to attract third parties to bring the needed capital. While this isn't exactly textbook bank or bank regulatory strategy, these aren't textbook times. We need to have a clear view of where we are and work together to address our common problems.

It is likely that in analyzing North Carolina's financial services needs, services to businesses, particularly small businesses, will be at the forefront. I am proud to be a member of a working group -- including representatives of NCBA -- that has done a great deal to provide you with resources to enhance your small business lending efforts and to provide small businesses with the assistance necessary to get a loan from you when they need and deserve one. I hope very much that we can continue this good work, so that there will be a fully developed infrastructure to support economic recovery by effectively meeting businesses' credit needs.

I also hope that our efforts will include services to the assets of businesses that don't show up on the balance sheet: their employees. Many of our businesses, particularly small businesses, employ low-wage workers. The financial well-being of these workers materially and directly affects the success of their employers, so services to them can materially and directly support the success of your business customers. I know that providing such services is not easy and may not be very profitable, at least when viewed in isolation. However, nothing worth doing is easy and, to reiterate, enhancing the financial health of our low-wage working population supports the success of our businesses and economic recovery. At the very least, I hope we can discuss how banks can profitably provide such services or agree that we should allow third parties other than banks to do so. This is a reprise from the 2008 speech; it's unfinished business we need to do.

We also need to address legal and regulatory infrastructure. On the state level, I hope you will support efforts this year and next to revise the North Carolina banking law to bring it up to date with current corporate, accounting and regulatory standards. Such a revision can make life easier for you and for me and, if we do the job right, can help in the search for needed capital. Additionally, we must continue to engage with the FDIC and Fed in a constructive way to right size the regulatory costs borne by each of you and, ultimately, by your customers, employees and shareholders. While I understand your concerns regarding Dodd-Frank, I must tell you (as a friend) that that statute was a response to breathtaking irresponsibility in the management of major financial firms and has to be understood in that context. Like it or not, it is the law. It is in your best interest and mine to make it work.

In closing, I would like to say how honored I am to be Commissioner of Banks and how much I hope to continue to do the important work of my office with you in the future. While we do not always agree, I hope you know that everything my colleagues and I do is intended to make your bank stronger and our economy more prosperous and fair. Working together, I know we can strengthen our industry and economy and get the Tar Heel State back on track to growth and opportunity for all our citizens.

Thank you.