Testimony of

H. Douglas Chaffin

On Behalf of the

Michigan Bankers Association

Before the

Subcommittee on Oversight and Investigations

Of the

Committee on Financial Services

United State House of Representatives

November 30, 2009

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Chairman Moore, Ranking Member Biggert, Congressman Peters and members of the Subcommittee, I am Doug Chaffin, president and CEO of Monroe Bank and Trust (MBT). MBT is a community bank headquartered in Monroe Michigan with $1.4 billion in assets. We serve the southernmost portion of southeast Michigan. I am immediate past chairman of the Michigan Bankers Association (MBA) and I am here on behalf of the MBA which is the voice of the banking industry in Michigan representing virtually all the banks in the state.

We are pleased to share Michigan's unique perspective on the challenges of extending credit in a severely distressed economy and offer our thoughts on capital assistance and improving business lending.

A total of 182 banks are currently doing business in Michigan and a full 93 percent or 169 of those banks are MBA members. Banks of every size from the smallest one-branch community bank to large institutions share membership in the MBA. Approximately 40,000 Michigan residents are employed by the industry and the Michigan banking industry provides more than $200 billion in loans to consumers and businesses.

Michigan Challenges:

The state of Michigan has been challenged with an economic downturn and continued job loss for the past nine years. It consistently ranks highest in unemployment rates across the country topping 15 percent statewide with some significantly impacted counties reaching well over 20 percent unemployment. The last time Michigan had an unemployment rate below the national average was November of 2002. In 2007, the state saw its highest average annual rate since 1993. Unemployment is expected to soar to 15.8 percent next year according to the University of Michigan Research Seminar in Quantitative Economics (RSQE) annual forecast.

As far back as 2005, southeast Michigan was taking a beating in the job market. Between September 2004 and September 2005 the Detroit area lost more jobs than any other metropolitan area in the nation recording a loss of 21,600 jobs, nine times more jobs than second place Baton Rouge, Louisiana according the U.S. Bureau of Labor Statistics.

Michigan's decline has been deep and broad. According to the Mackinac Center's James Hohman, between 2002 and 2008, Michigan lost 19 percent of its manufacturing jobs, 17 percent of its construction jobs, 12 percent of its natural resources and mining jobs, 11 percent of its information jobs, and lesser losses in financial activities, professional and business services and government. The manufacturing sector will account for 36 percent (91,000) of the state's job losses in 2009. Michigan is predicted to lose another 24,000 manufacturing jobs in 2010 and 16,000 more in 2011 says the RSQE forecast.

The whole country knows that unemployment is very high in Michigan, and most people also know that the automotive manufacturing industry has taken a nose dive in the past five years. During this recession almost 75 percent of auto jobs that existed in mid-2000 were wiped out according to the RSQE.

The U.S. Bureau of Labor statistics indicate that between October 2008 and October 2009 Michigan lost 262,700 jobs. Total job loss in Michigan for 2009 is projected at 283,000, the worst loss in any given calendar year for the past 70 years. One out of five jobs in Michigan has disappeared since 2000.

Michigan suffered from both the highest unemployment rate in the country at more than 15.3 percent in September 2009, and one of the nation's worst mortgage foreclosure rates. According to research done by The PEW Center on the States 2009, projections are that by the end of this decade, Michigan will have lost one million jobs, more than a third of those in 2009 and more than 268,000 in the auto industry. The RSQE outlook calls 2009 one of the worst economic years of our modern history, maybe the worst, and job losses in Michigan are projected to continue through much of 2011.

In addition, Michigan ranks last among the states in economic momentum, according to an analysis published in the State Policy Reports newsletter, a project co-sponsored by the National Governors Association and the National Conference of State Legislatures. Michigan received a -1.45 on the index placing it a full 1.5 percent behind the 49th worst state.

Even replicating the rapid growth rates of the 1990s, it would be 2025 or 2030 before all of the jobs lost this decade would be replaced. Economic forecasters from Moody's Economy.com said they do not expect to see another peak in Michigan's business cycle during their entire 30-year forecasting horizon. The jobless rate for the fourth quarter of 2009 will average out to 15.6 percent and is predicted to drop modestly in 2011 to 15.4 percent, the third-highest rate in four decades.

Impact on Bank Lending

In addition to record high unemployment rates, housing values have dropped causing both residential and commercial properties to lose their collateral value. The condition of Michigan borrowers is dismal and forward looking income projections are equally dire since the condition of borrowers drives loan qualification. It is important to understand that credit follows recovery, it does not lead it. Borrowers must be credit worthy and employed, business must have collateral and sufficient earning projections to qualify for credit. Both of these are severely strained in the state of Michigan.

Hard hit by the demise of the auto industry and manufacturing, Michigan banks, like all Michigan businesses, are working hard to serve their communities, support their customers' needs and support their employees.

Unfortunately, our State's nine straight years of job losses are taking a huge toll on our citizens and our businesses. These job losses make it difficult for many to meet current obligations or to qualify for new credit. In addition, the value of homes and business properties has declined, which again affects credit lines. So, it's not surprising that loan demand is down and qualifying for credit can be challenging. Every Michigan bank is going to great lengths to keep people in their homes, but no amount of credit adjustment can replace a lost job and lost income. For those still employed, personal income is expected to drop 3.4 percent this year.

In spite of a declining economy, Michigan Banks continued to find ways to lend to their customers. Loan balances at Michigan banks reflected respectable rates of growth as compared to other banks in the nation through 2006. As Michigan's unemployment rate increased to levels significantly above the national average, bank profitability declined, capital ratios fell and loan growth rates were reduced in 2007 and 2008 to 4.9 percent and 2.7 percent respectively. While still positive, these rates of growth paled by comparison to national peers which posted an average loan growth of 9.5 percent over those two periods. For the first nine months of 2009, loan balances at Michigan banks declined by .67 percent as a result of capital levels falling significantly below that of national peers.

Credit standards are tighter today than they were two years ago. Collateral values, the value of the homes and businesses used to secure lending, are down. Business performance is diminished and for many, income is down. When banks lend, they are legally and ethically obligated to expect that these loans are repaid. The no-income, no-down payment, no-problem loans made popular by those who promised "low-monthly-payments-please-do-not-bother-to-read-the-documents" loans with low teasers rates have proven a disaster for the borrowers and everyone else.

Virtually none of these "exotic" loans were made by banks. They were made by brokers who took their full commission at closing and have no financial interest whatsoever in whether the loan is repaid. They were made by an industry that never saw a regulatory exam, unlike banks who ALL have their loan files examined at least every 18 months by both federal and state examiners.

In accordance with bank regulators who are cautioning banks to only make good solid secure loans, banks are carefully looking for the capacity of borrows to pay back the loans and provide sufficient collateral if the unforeseen happens.

Capital is being frozen due to uncertainty of real estate value, the proliferation of empty production facilities and the value of the equipment within. If the auto industry continues to shed jobs in 2010, lending options can only continue to grow more challenging. Without some kind of federal support, banks will be unable to provide the credit needed to stem Michigan's recession. Changes in banking regulations are expected to further hamper banks' ability to lend as additional regulatory burdens add to costs and inhibit options.

The biggest issue for the Michigan banking industry is access to capital and its impact on business lending. Any programs the government can offer to increase lending, especially those targeting business lending, will help shore up the credit available to Michigan industry and commerce as well as boost the state's struggling economy.

Conclusion

Thank you, Chairman Moore, Ranking Member Biggert and Congressman Peters for the opportunity to present the views of MBA on the challenges ahead for Michigan banks and their communities.

First and foremost, now is not the time to saddle an already heavily regulated industry with new regulations. The Michigan banking industry supports consumer protection but adding the burdens of the CFPA will quite possibly strangle community banks. Overly restrictive efforts to attack banks on interchange and overdraft fees at this time could further damage community bank revenue.

However, we do support: extending similar standards to the relatively unregulated lending community; curing the too big to fail doctrine and systemic risk controls; and the committee's actions to address damaging procyclicle accounting standards as outlined in Rep. Perlmutter's amendment to the Financial Stability Improvement Act.

Faced with an economy reeling from a nine-year recession and the collapse of the auto industry in Michigan, our banks are making monumental efforts to provide for the credit needs of our residents.