M&T's CEO Says Dodd-Frank Won't Prevent Another Financial Crisis

Wilmers says regulations fail to address major causes of mortgage meltdown; Cites inaction on credit rating agencies, Fannie and Freddie and "Too Big to Fail" Banks

WASHINGTON, Sept. 22, 2011 /PRNewswire/ -- In a keynote address at the American Banker Regulatory Symposium this week, M&T Bank Chairman and CEO Robert G. Wilmers said that the Dodd-Frank Wall Street Reform and Consumer Protection Act failed to address key causes of the recent financial crisis.

"One devoutly wishes to be able to say that this new law has done that which it was passed to do: prevent the recurrence of a financial crisis like the one we have experienced. I fear very much, however, that it will likely fall short," said Wilmers.

Read Wilmers' entire speech on M&T Bank's website at http://mtb.mediaroom.com/american_banker_symposium

"I am concerned that the actual law has neither resolved nor seriously addressed a number of significant problems implicated in the financial crisis," Wilmers explained. "In particular, I think of those posed by three major types of institutions and their activities: first, credit rating agencies, key enablers of the transactions which sparked the crisis; second, the government-sponsored enterprises, Fannie Mae and Freddie Mac, whose indeterminate status continues to impede recovery in the housing market; and third, large bank holding companies which continue to avail themselves of the ill-advised protection offered by government taxpayers for risky activities not traditionally associated with banking."

Said Wilmers, "all were key contributors to the financial crisis from which the American economy has yet to recover; all were too big to overlook."

Credit ratings agencies, rather than sounding a timely alarm, were part of the problem

Wilmers said that, "in the years leading up to the recent financial crisis, rating agency assessments were poor to the point of inaccuracy -- creating a false sense of confidence on the part of investors and regulators alike and in turn, contributing to the crisis."

Standard & Poor's rated 17,000 asset-backed security issues with a face amount of almost $10 trillion between 1985 and 2011. Of those, M&T Bank studied a sample of 2,679 residential mortgage-backed issues totaling $564 billion in face value: 2,670 or 99% were rated triple-A at origination, but today, 90% are rated non-investment grade by both count and dollar balances. "The magnitude of this miscalculation is staggering," said Wilmers.

"Despite this poor record, the rating agency oligopoly, which government has helped to install, amounts to a near gold mine. For 2008 through 2010, the pretax profit margin from the ratings business at both Moody's and Standard and Poor's exceeded 45%. In 2006, it exceeded 60% at Moody's. From 2000 to 2007, Moody's profits quadrupled, and for five years in a row, the firm had the highest profit margin of any company in the S&P 500."

Wilmers also said that, "the financial crisis from which we are still trying to recover is not the first major crisis in which the rating agencies, rather than sounding a timely alarm, were, instead, part of the problem. We cannot allow a group of organizations which have gotten so many important things so wrong for so long -- including assessments of municipal debt, the likelihood of major corporate bankruptcies and, of course, the value of subprime mortgage-backed securities -- to continue unchallenged."

Nonetheless, Wilmers said, Dodd-Frank does little to cause "an oligopoly which government has, over the past generation, helped to establish and embed, to be replaced with what we need: an open, competitive, effective and accurate ratings system. As a practical matter, the rating agency oligopoly remains in place and will not be dislodged quickly or easily."

Dodd-Frank leaves untouched the GSE giants who buy three-quarters of the mortgages originated

Wilmers also said that Dodd-Frank ignored the government-sponsored housing finance enterprises, Fannie Mae and Freddie Mac, which "were not only central to the financial crisis, but continue to play a critical role in the economy today -- even as they require ongoing taxpayer assistance at high levels.

"In the last 20 years, Fannie and Freddie have underwritten $13.5 trillion in mortgages, of which $5.3 trillion are still outstanding." But, "the losses with which Fannie and Freddie have saddled taxpayers have been nothing less than staggering," explained Wilmers.

"Since 2007, they have lost $246.5 billion and have been taken over by the government, as the illusion of their being bona fide private stock corporations has melted away. Consensus projections have them losing another $90 billion by the end of 2013. Such projections reflect the fact that, as of June 30, the two GSEs had $54 billion or four percent of their portfolios either in foreclosure proceedings or more than 90 days delinquent. Seventeen percent of their mortgagees had loans worth more than the value of their homes," Wilmers said.

"Despite the astronomical costs to which Fannie and Freddie's activity have led, the percentage of American households owning their own homes did not, on net, increase as the housing bubble inflated and then burst between 2000 and 2009. Notwithstanding our collective investment in their operations, such countries as Sweden, Spain, Poland, Greece, Ireland and Italy actually have higher homeownership rates than the U.S., as do the United Kingdom and Canada."

Yet, "what are, for all practical purposes, agencies of the federal government, today are led by CEOs each of whose total compensation exceeded $5 million in 2010. In other words, these CEOs of what amount to government bureaucracies are paid nearly 14 times more than the salary of the President of the United States," said Wilmers.

"Despite the enormity of the problem, no action has been taken to resolve the question of how to restructure Fannie Mae and Freddie Mac so as best to serve the private housing market without exposing taxpayers to yet more risk," he continued. "While Dodd-Frank calls for myriad changes in reporting and oversight on the part of community banks, it leaves untouched these GSE giants who are currently the buyers of almost three-quarters of the single family mortgages originated in 2011. Like the big six private banks, they are deeply embedded in our economy -- and too big to overlook."

Dodd-Frank allows the continuation of a business model driven by trading in speculative investment vehicles

"A flurry of new requirements and regulations affecting banks can be found in the bill. Unfortunately, a great deal about banking which actually helped create the financial crisis has been left unchanged," said Wilmers. Dodd-Frank allows both, "increased concentration in the financial services sector and the emergence of a business model driven not by the prudent extension of credit that furthers commerce but by trading in speculative investment vehicles."

Trading revenue at the six largest U.S. banks represented 91% of such revenues of all American banks in 2010, said Wilmers. "Looked at in a different way, revenues represented 23% of the total non-interest income at these six institutions, compared to 2.6% for the rest of the American banks. In turn, the big six have a different set of global competitors than typical U.S. banks -- and their resultant risk profiles are also uniquely different from traditional banks."

Nonetheless, Wilmers said, "the major bank holding companies who engage in and rely on trading revenue can continue to do so with the protection of the FDIC system -- established to protect depositors, not speculators. This FDIC protection both encourages risk-taking and increases the likelihood that banks who do not engage in trading -- in other words, the vast majority of U.S. banks -- will need to increase their FDIC contributions, as has already happened because of excessive risk taking related to the housing bubble." Wilmers pointed out that FDIC contributions have risen from $32 million in 2006 to more than $13 billion in 2010.

"Simply put, Dodd-Frank, rather than beginning the necessary process of changing the model for bank holding companies said to be too big to fail, has acquiesced in the perpetuation of their problematic business model and linked the fortune of traditional banks with their fate," concluded Wilmers.

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