

NR 98-35
March 31, 1998

OCC Issues Loan Portfolio Management Guidance

WASHINGTON, DC -- With the goals of improving overall portfolio management, reducing potentially dangerous credit concentrations, and enhancing the quality of bank lending decisions, the Office of the Comptroller of the Currency (OCC) today issued its first comprehensive loan portfolio management guidance.

"It's as crucial for banks to manage their portfolios as a whole as it is to review the quality of each individual loan," said Comptroller of the Currency Eugene A. Ludwig. "Loan concentrations -- whether energy loans in the Southwest, real estate loans in the Northeast, or too many loans in one geographic area -- have been a major factor in bank failures for the past two decades."

Mr. Ludwig said that while studies have consistently cited poor management as the cause of bank failures, deeper analysis points to poor credit risk management as the specific culprit in the vast majority of cases.

"Credit risk and credit risk management issues account for approximately 70 percent of the banks with which we have concerns," he said.

"The Loan Portfolio Management' section of the Comptroller's Handbook that we're issuing today will raise the bar with bankers and examiners alike in the face of deteriorating underwriting standards and control cutbacks," said Wayne Rushton, the OCC's senior deputy comptroller for supervision policy. "It does so in a considered and comprehensive manner."

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Mr. Ludwig has been warning bankers since 1996 that declining underwriting standards and loosened credit controls need to be addressed while the economy remains robust. His latest warning came last month when he expressed continuing concerns with underwriting and portfolio management problems.

The handbook, which is being sent to national banks and OCC examiners, provides an extensive discussion of the "credit culture" -- the combination of policies and practices that shape a bank's lending activities. The handbook is intended to promote more sophisticated loan portfolio management efforts by banks.

In drawing up strategic objectives, the handbook suggests that bank management and the board should consider these twelve issues:

- o What proportion of the balance sheet the loan portfolio should comprise.
- o Goals for loan quality.
- o Goals for portfolio diversification.
- o How much the portfolio should contribute to the bank's financial objectives.
- o Loan product mix.
- o Loan growth targets by product, market, and portfolio segment.
- o Product specialization.
- o What the bank's geographic markets should be.
- o Targeted industries.
- o Targeted market share.
- o Community needs and service.
- o General financial objectives.

The OCC advises banks that they should have systems in place to analyze and control exceptions to their lending policies whether they apply to documentation or underwriting. And if an exception could have a material impact on the bank, it should be brought to the attention of the bank's senior management and board. The handbook advises banks to track the aggregate level of exceptions to help detect shifts in the risk characteristics of loan portfolios. "In consumer lending, where such tracking is common, it has facilitated risk evaluation, strengthened portfolio liquidity, and helped management to identify new business opportunities," said Dave Gibbons, the OCC's deputy comptroller for credit risk. He led the team that drafted the handbook.

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Copies of the "Loan Portfolio Management" section of the Comptroller's Handbook are being mailed to national banks, OCC examiners and subscribers to the Comptroller's Handbook. To order copies of this handbook section, please send your request and a \$15 check for each booklet to: Comptroller of the Currency, P.O. Box 70004, Chicago, IL 60673-0004.

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The OCC charters, regulates and examines approximately 2,800 national banks and 66 federal branches of foreign banks in the U.S., accounting for more than half the nation's banking assets. Its mission is to ensure a safe and sound and competitive national banking system that supports the citizens, communities and economy of the United States.