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Editors' Note on the Special Issue of the 10th FDIC/JFSR Bank Research Conference

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This special issue of the *Journal of Financial Services Research* includes a selection of papers originally presented at the Tenth Annual FDIC-JFSR Fall Banking Research Conference in October 2010. The papers in this special issue were invited by the editors of the JFSR but were subjected to the regular JFSR referee process. We also invited the conference paper discussants to draft their comments for publication in this special issue.

In the first article of this special issue, "Dèjá Vu All Over Again: The Causes of U.S. Commercial Bank Failures This Time Around," Cole and White (2012) use a logistic regression framework to identify factors associated with more than 300 bank failures since 2009. This paper was presented in the "Reflections of the Financial Crisis" session of the Conference. The authors find that many failing banks tended to have loan exposures to real estate construction and development, commercial real estate and multifamily residential mortgages. Unlike many of the largest banks that were negatively impacted by their exposures to wholesale subprime mortgage securitization activities, residential mortgage exposures in smaller community banks tended to reduce the probability that these banks failed.

The discussant for the session was Pete Kyle and his discussion underscores the importance of capital especially for small banks. Kyle (2012) also differentiates short-term and long-term effects of capital where capital is more important in the short-term but volatility of asset returns dominates in the long term. For large banks the prescription is heightened supervision, which should be geared toward understanding new risky business lines, especially those that may pose systemic risk.

Three of the papers in this special issue, presented in the "Measuring Systemic Risk" session of the program, focus on the measurement of systemic risk. Robert DeYoung provides a unified discussion of systemic risk and the contributions made by each of these papers. As DeYoung (2012) points out, the profession has yet to decide on a single focused

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definition of systemic risk and consequently papers on systemic risk can discuss a wide variety of issues and phenomenon.

In “Forward-Looking Tail Risk Exposures at U.S. Bank Holding Companies,” Knaup and Wagner (2012) propose a new method for identifying institutions with underlying systemic risk exposure. Many BHCs that appear safe and solvent under normal condition may pose a solvency risk under more extreme market conditions. Knaup and Wagner (2012) propose a method to identify when a bank’s performance and solvency is a nonlinear function of general market conditions. The authors find that banks with the potential for enhanced solvency risk during downturns often are banks with relatively modest market model betas and banks with extensive non-traditional bank activities.

In “Systemic Risk Contributions,” Huang et al. (2012) propose a measure of systemic risk, which is the hypothetical price of insuring all banks liabilities against default losses above a specified threshold. The authors track each of the 19 SCAP institution’s estimated contribution to overall systemic risk throughout the financial crisis and argue that the systemic risk attributions are reasonable for the most part.

In the final paper on systemic risk, “Credit Derivatives and the Default Risk of Large Complex Financial Institutions,” Calice, Ioannidis, and Williams (2012) modify the stock return factor models that are used to calibrate bank default correlations to include changes in the values of two CDS indices, the North American CDX index and the European iTraxx index. They find that many of their sample 16-large complex financial institutions would have required substantial capital injections during the crisis if they had been required to meet a capital standard that includes CDS indices as common market factors.

The final paper was presented in the “Consumer Loan Defaults” session. Black et al. (2012) article titled “Differences Across Originators in CMBS Underwriting,” examine the performance of over 30,000 commercial mortgages that are included in commercial mortgage-backed securities during 1999–2007. Black et. al. find that the CRE mortgages originated by on-balance sheet lenders (commercial banks, investment banks, insurance and finance companies) had better performance (lower delinquency rates) compared to those originated by foreign entities and domestic conduits. They argue that their results may be explained by differences in originators funding risk exposures where on-balance sheet originators typically bear loan warehousing risks and conduit originators do not.

In his discussion of the paper, David Musto elaborates on the importance of the “hot potato” warehouse risk issue and how it relates to the negative “vintage” effects observed by Black et al. (2012) for CRE mortgages originated between 2005 and 2007. This period, characterized by reduced warehousing risk, was also characterized by mortgage originations with observable deteriorations in underwriting standards including reduced capitalization rates, lower debt-service coverage ratios, gains in the use of interest-only and shorter maturity CRE loans terms and increased use of “seconds” or “mezzanine debt”. Musto (2012) points out that while causality is not established, there seems to be a link between the risk that an originator may be forced to own a commercial mortgage long-term and the diligence with which the loan is underwritten.

Overall, the published articles, the papers presented in the conference, and the discussions reflect the high quality and timely research presented at the FDIC-JFSR Conferences over the last ten years. We thank the many authors, discussants, and participants who have contributed to the quality of the FDIC/JFSR Conferences through their paper submissions, presentations and thought provoking discussions. Finally, we thank the FDIC for its continuing commitment to support academic research on issues that help to promote informed public policy debate on issues related to banking and the financial services sector.

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