Economic Review

Considering Bank Age and Performance for De Novo Status

by: Stephen Jones, Forest Myers and Jim Wilkinson

June 02, 2022

Newly formed banks perform similarly to established banks after three years, suggesting the current three-year period of enhanced supervision is appropriate.

Newly formed or "de novo" banks provide important benefits to banking markets, but they are also considered more financially fragile than established banks and are thus subject to a period of enhanced supervision. Currently, federal banking agencies impose more stringent supervision on de novo banks for at least three years, during which de novos may have more frequent examinations, more intensive surveillance, higher standards for capital levels, and limits on capital distributions. However, whether this three-year period effectively balances risk mitigation with regulatory burden is an open question.

Stephen Jones, Forest Myers, and Jim Wilkinson evaluate the appropriate length of the enhanced supervisory period by analyzing de novo bank financial performance over time. They find that the typical de novo bank's financial performance differs substantially from that of established banks during their first three years; by the end of three years, the financial performance of de novo banks more closely resembles older and more mature banks. Their results suggest that the three-year enhanced supervisory period is likely appropriate for mitigating risk without excessively burdening new banks.

Publication information: Vol. 107, no. 2
DOI: 10.18651/ER/v107n2JonesMyersWilkinson