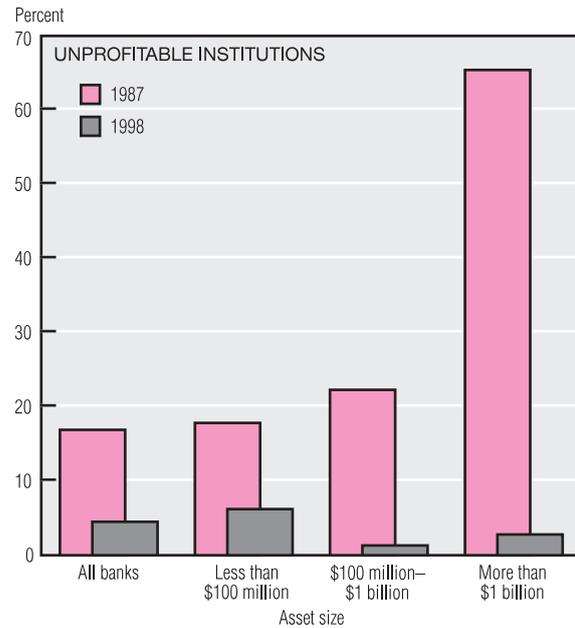
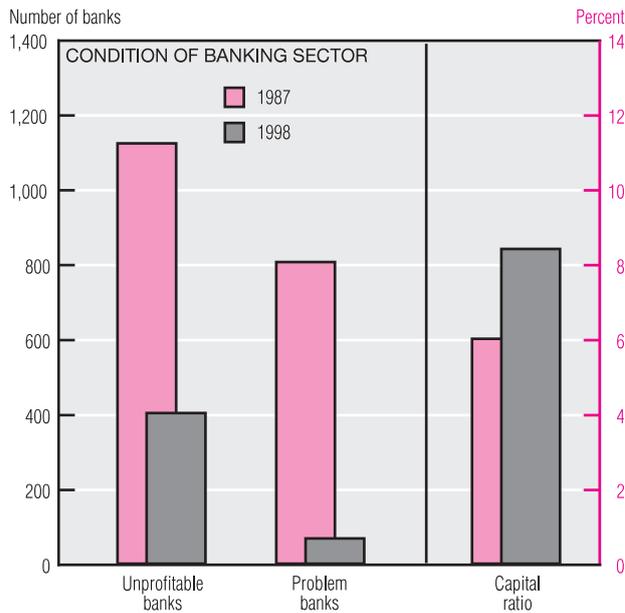
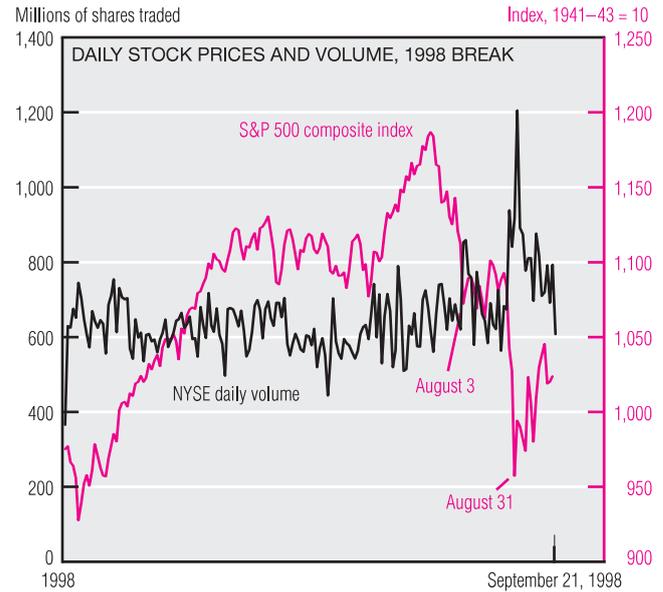
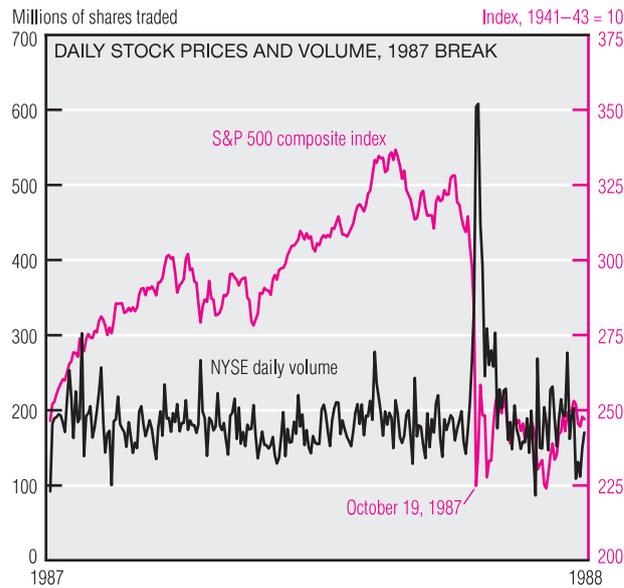


Banking and the Stock Market



SOURCES: Federal Deposit Insurance Corporation, *Quarterly Banking Profile*, 1987:IIQ and 1998:IIQ; New York Stock Exchange, <http://www.nyse.com/public/market/2c/2cix.htm>; and Standard and Poor's Corporation.

The Dow industrial average dropped 512.61 points on August 31 and has been volatile since then. Setting aside speculation regarding motivations for the sell-off, people quickly drew comparisons between this episode and the stock-market crash of October 19, 1987, when the Standard and Poor's (S&P) 500 composite index dropped 25%, and the New York Stock Exchange (NYSE) reported roughly triple the usual daily trade volume.

This time around, the same measures show a somewhat less severe drop. On August 31, the S&P 500

composite index fell 15%, while the NYSE reported about double the usual daily trade volume.

One difference between the two market breaks is that healthier conditions prevail in the banking sector now than in 1987. The earlier break occurred in a banking environment that may have contributed to a more general nervousness about whether financial stability could be sustained. For example, there were almost three times as many unprofitable banks in 1987 as there are today, and more than 12 times as many problem banks. Banks' capital ratios

were more than two percentage points lower than now. Questions were being raised about the condition of several large money-center banks. In fact, over 65% of banks with more than \$1 billion in assets were unprofitable.

Today, however, far fewer unprofitable institutions can be found in every asset class than in 1987. The current health of financial institutions may have prevented a more serious erosion of confidence in the equities market.