# Defying economic gravity

*The big Texas banks planned to dominate the South, but now they're all gone.*

Just a few years ago, the big Texas banks saw themselves poised on the verge of becoming national powerhouses. Having conquered Texas, they cast their eyes longingly on their neighboring states, seeking new markets to dominate. What we need, they decided, is interstate banking.

These banks, working hand in hand with their cousins, the huge Houston law firms, set about to make interstate banking a reality. They began a massive political mobilization to convince the Texas state legislature that interstate banking would be good for the state. The legislature, which had always been opposed to such things in the past, was won over.

The bankers and lawyers also launched an attack on federal interstate banking laws, via the federal courts. When the Houston law firm of Bracewell & Patterson won the right for a Texas bank to enjoy the same rights as Mississippi S&Ls, it marked the beginning of the end for federal restrictions against interstate banking.

With Washington, D.C. full of Texans, the local boys thought that they had adequate protection against political counterattacks. After all, Vice President George Bush, Treasury Secretary James Baker, Comptroller of the Currency Robert Clarke, and Federal Reserve Board member Ed Kelly were all from Houston. Baker and Clarke were from big firms (Clarke was from Bracewell and Patterson), and Baker owned a substantial chunk of Texas Commerce Bancshares. What could possibly go wrong?

Unfortunately for them, plenty.

The Texas boom was due primarily to the rapid rise in oil prices in the late 1970s. When oil hit $40 per barrel, Houston became a true boomtown. The city was awash in capital, and speculators from all over the world converged on the city to cash in. Small energy companies popped up right and left, and existing companies expanded as fast as they could. The local banks, naturally, were ready to lend money to finance all this growth. Their energy loan portfolios swelled with lucrative transactions.

The rapid growth of the energy industry triggered a similar rate of growth in the real estate market. Office buildings sprang up all over Houston, such that the construction crane became the unofficial city "bird." Giant apartment complexes were built, and outlying prairies were turned into sprawling, single-family-home subdivisions. Naturally, the banks financed a great deal of this real estate expansion.

The Texas banks, like the Texas economy as a whole, rode the crest of the oil price boom to new highs, but, as such artificial booms are wont to do, the oil boom eventually played out.

The first crack appeared in the mid-1980s, when the price of oil declined and the oil industry entered into a slump. Many of the energy companies began losing money, and began having problems paying off their bank loans.

To compensate for their losses, the bankers made what would prove to be a fatal mistake: They shifted their loan portfolio from energy loans to real estate. During the 1982 to 1986 period, nearly one out of every two dollars lent by the big Texas banks was for some sort of real estate transaction.

However, in their zeal to maintain profits, the banks overlooked the obvious—that the collapse of energy would detonate a much larger blowout in the real estate market. Energy loans weakened the banks, but real estate loans killed them.

By the time interstate banking came to pass, the Texas banks were in no position to take over anyone, and were in fact struggling just to survive.

Chemical Bank of New York was the first outside bank to move in, buying up Texas Commerce Bancshares of Houston in early 1987. Months later, First Interstate of Los Angeles took over Allied Bancshares.

But that was it. The condition of the Texas banks had deteriorated to the point that no one else was willing to take the risk. Instead, like vultures, the money center banks waited for the inevitable failures, hoping to buy the remains with generous assistance from the Federal Deposit Insurance Corporation.

That is precisely what happened. During 1988 and 1989, one after another, the major Texas banks admitted their real estate losses and were seized by the FDIC. First City, First RepublicBank, and MCorp all folded, and were taken over by out-of-state interests.

On July 20, 1989, the FDIC closed all 24 banks of Texas American Bancshares of Fort Worth, the last of the big six Texas bank companies still alive, marking the end of an era.

The Texans, who thought they had everything under control, had been wiped out, and the state was reduced to the status of financial colony. How quickly the mighty fall, when they defy the laws of physical economy.