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Abstract

Focusing on the recent oxies for the Federal Deposit Insurance Corporation’s proprietary CAMELS measurement system effectively predict the likelihood of failure for most regulated, depository institutions with U.S. operations (in and out of sample testing). This article also utilizes regulatory enforcement actions as both an explanatory and predicted variable. The CAMELS ratings from bank examinations are not released to the public because of regulatory concerns over potential bank runs. To the extent that such ratings provide timely information to banks, our lagged proxies are less likely to be effective predictors of bank failure. However, we find that proxies for each of the six categories of CAMELS—capital adequacy, asset quality, management, earnings, liquidity, and sensitivity to interest rates—are significantly associated with the probability of bank failure when examined individually. Nearly all measures maintain their significance when examined collectively. These results should aid investors, customers of commercial banks, and also regulators to better assess the risk of bank distress in the future.

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