Volume 1
Number 2

Quarterly Banking Profile

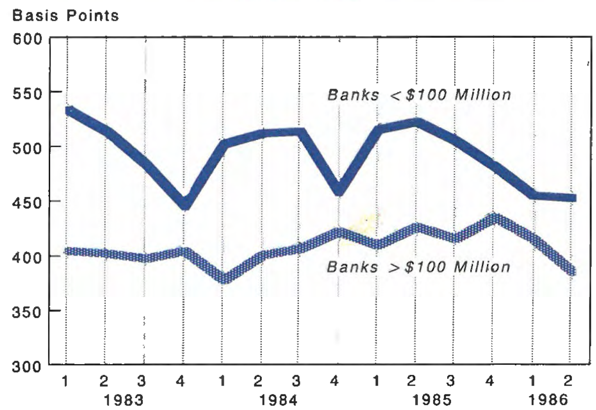
FEDERAL DEPOSIT INSURANCE CORPORATION

Second Quarter 1986

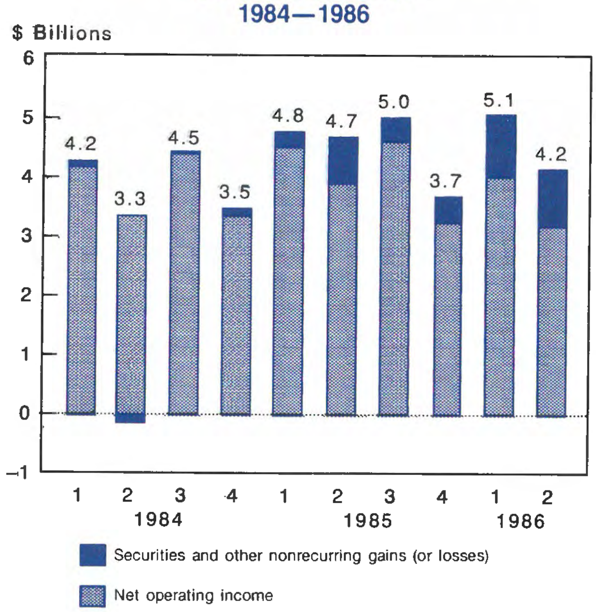
COMMERCIAL BANKING PERFORMANCE — SECOND QUARTER, 1986

Aggregate net income and overall profitability of insured commercial banks declined in the second quarter of 1986. Net income was down 11 percent from the level of a year ago, and down 18 percent from the first quarter of this year. Net income for the first half of 1986 was $9.25 billion, down 2.4 percent from the first half of 1985. The magnitude of these declines was limited by sizable gains from sales of securities and from nonrecurring items. Absent these gains, which have remained significant over the past several quarters, income would have been 18.4 percent lower than the second quarter a year earlier, despite asset growth of nearly 8 percent.

Commercial Bank Net Interest Margins 1983—1986



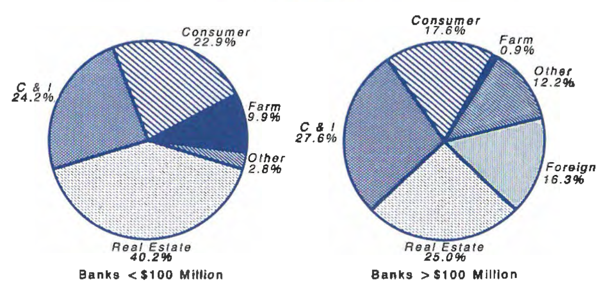
Quarterly Net Income of FDIC-Insured Commercial Banks 1984—1986



Banks' loan-loss provisions increased by 36.4 percent over year-earlier levels, as asset-quality problems accounted for most of the downward pressure on bank earnings. The number of banks with earnings losses (net income less than zero) in the second quarter was 2,384, up from 1,876 in the same period of 1985. The FDIC's "problem" list increased by 128 commercial banks during the quarter, to 1,321 as of June 30. Through the first six months of 1986, 64 insured commercial banks failed. The smallest commercial banks continue to exhibit the most severe earnings erosion of any segment of the industry, reflecting pressures from credit problems in agriculture and real estate portfolios.

Falling interest rates contributed to year-to-year reductions in both total interest income and expense. Net interest margins contracted slightly, as earning assets growth of 8.5 percent outstripped net interest income expansion.

Composition of Bank Loan Portfolios June 30, 1986



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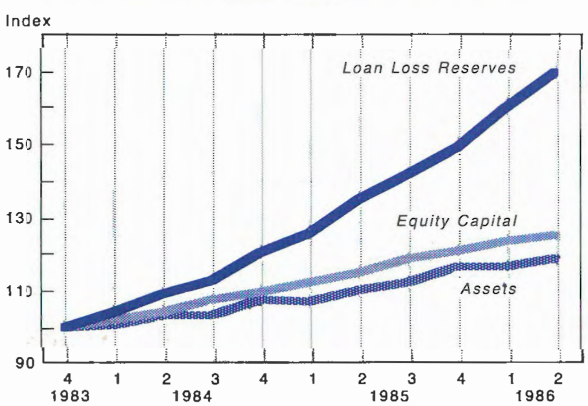
Small banks' level of problem loans remained highest and showed the most pronounced deterioration of any size group in the second quarter. Banks in the Midwest still show the highest regional level of loan charge-offs, but Southwestern banks experienced the sharpest growth in charge-offs during the quarter.

Banks in the Southwest region have the highest proportion of nonperforming assets, and this level rose further in the second quarter.

Net loan-loss levels increased more rapidly than loan-loss reserves at commercial banks in the second quarter, as small banks' aggregate loss provisioning fell short of actual losses. Most larger banks continued to bolster their reserve levels. Banks in the largest asset-size group maintained the highest ratio of loss reserves to loans outstanding of any size group—1.67 percent. Equity capital and assets have grown at roughly comparable rates at commercial banks, while reserve growth has been much more rapid.

Commercial Bank Loan Loss Reserve, Equity Capital and Asset Growth Index 1984—1986

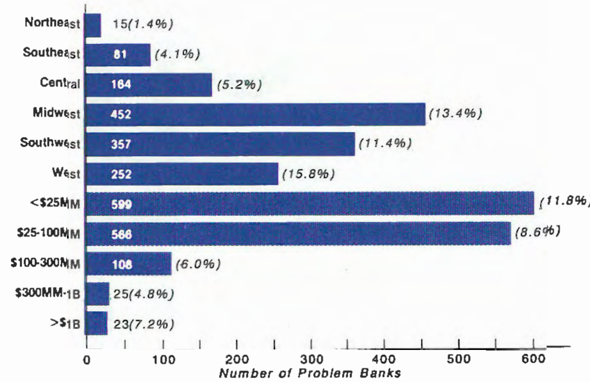


Note: Year-end 1983 = 100

The Southwest region had the highest proportion of unprofitable banks in the second quarter—27 percent—while the Western region had the largest share of banks on the "problem" list. These results reflected a continuation of the deteriorating trends in both regions. The Southeast, Northeast and Central regions had the fewest troubled institutions, and showed improving trends in this area. Nonperforming asset levels stabilized, and growth in overall reserve coverage of loan portfolios improved at Western banks in the second quarter.

Through the first half of 1986, the Mississippi River has continued to represent a dividing line for commercial bank performance. Banks in the East have had fewer credit-quality problems and stronger asset growth than their Western

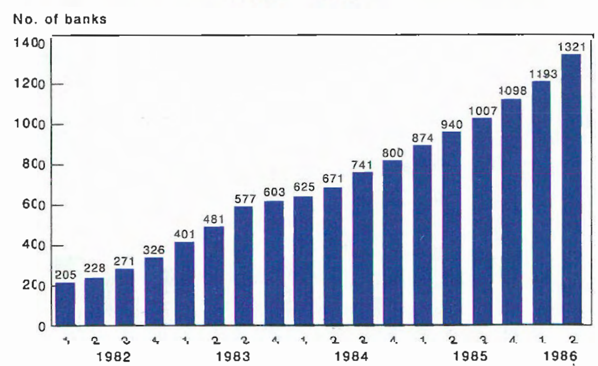
Problem Banks, By Region and By Asset Size June 30, 1986



Number of banks on FDIC "Problem List" and percent of all banks in each region/asset-size group.

counterparts. Problems in the agricultural and energy sectors have been the principal difference. Continuing growth in the number of "problem" banks portends no respite during the rest of 1986 from the high level of bank failures.

Commercial Banks on FDIC "Problem" List 1982—1986



For the banking industry as a whole, recent trends of slowing GNP growth, lower industrial production and capacity utilization levels, and fewer housing starts all point to slack loan demand in the months ahead. The remainder of the year is likely to be marked by continued credit-quality problems among commercial and real estate loans stemming from the plunge in oil prices and lingering weakness in the agricultural sector. Continued growth in subquality asset levels may mean further increases in the number of problem banks. Slow economic growth and lower interest rates make lackluster year-to-year earnings comparisons likely for the second half of 1986. Net interest margins may remain under pressure with loan growth lagging behind last year's pace and lending spreads remaining narrow. The growth of nonperforming assets — up 10.8 percent in the first six months of 1986 — will almost certainly lead to higher charge-off rates in the second half.

U.S. COMMERCIAL BANKING INDUSTRY QUARTERLY PROFILE
Aggregate Condition and Income Data, FDIC-Insured Commercial Banks
(dollar figures in millions)

	Preliminary 2nd Qtr 1986	1st Qtr 1986	2nd Qtr 1985	% Change 85:2-86:2
Number of banks reporting	14,311	14,382	14,467	-1.1
Total employees (full-time equivalent)	1,582,203	1,565,503	1,550,987	2.0
CONDITION DATA				
Total Assets	$2,774,592	$2,729,950	$2,570,936	7.9
Real estate loans	467,262	451,378	407,596	14.6
Commercial & industrial loans	581,208	580,390	570,905	1.8
Loans to individuals	317,889	308,826	285,197	11.5
Farm loans	34,737	34,383	40,474	-14.2
Other loans and leases	269,867	266,393	249,110	8.3
Total loans and leases	1,670,964	1,641,370	1,553,282	7.6
LESS: Reserve for losses	26,244	24,833	20,936	25.4
Net loans and leases	1,644,720	1,616,537	1,532,346	7.3
Temporary investments	448,879	457,776	422,966	6.2
Securities over 1 year	318,714	300,914	271,523	17.4
All other assets	362,279	354,723	344,101	5.3
Total liabilities and capital	$2,774,592	$2,729,950	$2,570,936	7.9
Noninterest-bearing deposits	469,663	438,322	411,097	14.2
Interest-bearing deposits	1,678,103	1,675,582	1,588,307	5.7
Other borrowed funds	327,528	319,483	275,012	19.1
Subordinated debt	16,194	15,386	12,323	31.4
All other liabilities	107,328	107,896	122,762	-12.6
Equity capital	175,776	173,281	161,435	8.9
Nonperforming assets	56,615	54,777	53,343	6.1
Loan commitments and letters of credit	733,101	734,924	682,231	7.5
Domestic office assets	2,357,871	2,311,758	2,160,717	9.1
Foreign office assets	416,721	418,192	410,219	1.6
Domestic office deposits	1,826,075	1,780,719	1,670,330	9.3
Foreign office deposits	321,691	333,185	329,074	-2.2

INCOME DATA	Prelim. 1st Half 1986	1st Half 1985	% Change	Prelim. 2nd Qtr 1986	2nd Qtr 1985	% Change
Total interest income	$121,626	$123,987	-1.9	$59,279	$62,239	-4.8
Total interest expense	74,673	79,713	-6.3	35,832	39,599	-9.5
Net interest income	46,953	44,274	6.1	23,447	22,640	3.6
Provisions for loan losses	9,963	7,304	36.4	5,295	4,311	22.8
Total noninterest income	16,955	14,227	19.2	8,540	7,384	15.7
Total noninterest expense	43,581	39,665	9.9	21,929	20,321	7.9
Applicable income taxes	3,133	3,046	2.9	1,551	1,458	6.4
Net operating income	7,231	8,485	-14.8	3,212	3,934	-18.4
Securities gains, net	1,881	789	284.7	920	600	53.3
Extraordinary gains, net	140	210	-33.3	42	155	-72.9
Net Income	9,252	9,484	-2.4	4,174	4,689	-11.0
Net charge-offs	6,900	5,055	36.5	3,877	2,873	34.9
Net additions to capital stock	390	461	-15.4	240	373	-35.7
Cash dividends on capital stock	7,346	7,199	2.0	2,010	1,946	3.3

Selected Performance and Condition Indicators, FDIC-Insured Commercial Banks

	1982	1983	1984	1985	1986*
Return on assets	0.71%	0.66%	0.65%	0.70%	0.67%
Return on equity	12.11	10.70	10.73	11.31	10.72
Equity capital to assets	5.87	6.00	6.15	6.20	6.33
Nonperforming assets to assets	1.85	1.97	1.97	1.87	2.04
Net charge-offs to loans	0.56	0.67	0.76	0.84	0.86
Asset growth rate	8.12	6.75	7.11	8.86	7.92
Net operating income growth	-0.62	-3.69	-3.40	6.30	-14.78

*For 1986, performance ratios are annualized where appropriate, and growth rates refer to the 12 months through June 30.

Preliminary Bank Data and Performance and Condition Ratios, Distributed by Asset Size and by Region, Second Quarter 1986 *(Dollar figures in billions, ratios in %)*

		Asset Size Distribution						Geographic Distribution					
	All Banks	Less than $25 Million	$25-100 Million	$100-300 Million	$300-1,000 Million	$1-3 Billion	Greater than $3 Billion	Northeast Region	Southeast Region	Central Region	Midwest Region	Southwest Region	West Region
Number of banks reporting	14,311	5,065	6,597	1,813	518	198	120	1,081	1,970	3,162	3,366	3,140	1,592
Total assets	$2,774.6	$74.1	$332.5	$289.6	$261.7	$338.0	$1,478.7	$1,055.7	$350.3	$436.6	$193.5	$294.5	$444.0
Total deposits	2,147.8	65.4	296.5	254.4	218.1	267.5	1,045.9	756.8	281.3	351.1	153.1	241.7	363.8
% of total banks	100.0%	35.4%	46.1%	12.7%	3.6%	1.4%	0.8%	7.6%	13.8%	22.1%	23.5%	21.9%	11.1%
Asset share (%)	100.0	2.7	12.0	10.4	9.4	12.2	53.3	38.1	12.6	15.7	7.0	10.6	16.0
Deposit share (%)	100.0	3.0	13.8	11.8	10.2	12.5	48.7	35.2	13.1	16.4	7.1	11.3	16.9
Number of unprofitable banks	2,384	1,251	903	166	51	11	2	53	169	251	678	834	399
Number of failed banks	38	18	16	4	0	0	0	0	4	4	10	13	7
Performance ratios *(annualized)*													
Yield on earning assets	9.80%	10.81%	10.49%	10.29%	10.30%	9.99%	9.79%	9.79%	10.17%	9.78%	10.32%	9.50%	10.65%
Cost of funding earning assets	5.92	6.05	6.01	5.87	5.86	5.72	6.23	6.18	5.77	5.95	6.16	5.95	5.91
Net interest margin	3.88	4.76	4.49	4.42	4.44	4.27	3.56	3.60	4.40	3.83	4.16	3.55	4.74
Net noninterest expense to earning assets	2.21	3.24	2.78	2.71	2.78	1.63	1.87	1.96	2.60	2.18	1.87	2.33	2.89
Net operating income to assets	0.47	0.11	0.57	0.69	0.60	0.67	0.35	0.61	0.95	0.81	0.58	-0.20	-0.13
Return on assets	0.61	0.29	0.76	0.86	0.75	0.79	0.48	0.77	1.08	0.90	0.78	-0.03	-0.02
Return on equity	9.57	2.96	9.02	11.42	10.66	11.86	9.06	13.04	15.91	12.80	10.32	-0.47	-0.51
Net charge-offs to loans and leases	0.94	1.85	1.29	0.93	0.95	0.74	0.93	0.63	0.54	0.65	2.03	1.82	1.23
Condition Ratios													
Loss reserve to loans and leases	1.57%	1.62%	1.44%	1.37%	1.49%	1.41%	1.67%	1.43%	1.29%	1.44%	1.84%	2.01%	1.81%
Nonperforming assets to assets	2.04	2.72	2.31	1.95	1.87	1.57	2.10	1.60	1.09	1.52	2.44	3.57	3.17
Equity capital ratio	6.34	9.98	8.37	7.47	6.97	6.69	5.28	5.83	6.80	7.03	7.54	6.93	5.58
Primary capital ratio	7.16	10.77	9.10	8.14	7.73	7.37	6.20	6.60	7.27	7.78	8.50	8.06	6.62
Net loans and leases to assets	59.28	49.67	51.88	55.96	60.01	60.95	61.56	59.19	57.81	56.35	53.97	58.23	66.52
Net assets repriceable in one year or less to assets	-4.76	-4.74	-6.87	-6.45	-7.56	-4.10	-3.61	-3.22	-7.94	-3.00	-9.16	-5.62	-5.15
Growth Rates *(from year-ago quarter)*													
Assets	7.9%	7.3%	7.7%	9.2%	12.4%	15.0%	10.8%	11.4%	13.6%	5.8%	6.5%	0.5%	3.9%
Earning assets	8.5	7.3	7.7	9.2	13.1	15.0	11.9	12.2	13.8	6.5	6.1	1.5	4.4
Loans and leases	7.3	4.3	5.2	9.3	14.3	16.3	10.5	11.2	14.7	5.4	2.2	-0.3	4.6
Loss reserve	25.4	24.5	23.6	22.8	32.6	30.3	30.8	23.0	21.1	19.9	28.1	37.6	27.0
Net charge-offs	34.9	23.6	23.1	26.7	63.5	60.2	25.0	66.4	16.4	7.3	41.8	60.0	10.7
Nonperforming assets	6.1	23.9	22.6	23.2	30.7	16.5	0.9	-4.2	15.2	-2.6	11.8	37.2	2.4
Deposits	7.4	8.3	8.2	9.6	12.6	14.9	10.1	10.4	12.8	6.3	5.4	0.8	4.3
Equity capital	8.9	1.7	5.9	8.7	10.2	20.3	12.9	15.0	13.0	8.0	5.4	-1.8	3.8
Interest income	-4.8	-2.0	-2.0	-0.4	2.5	3.9	-2.5	-3.2	2.6	-4.1	-4.3	-11.4	-9.8
Interest expense	-9.5	-4.5	-5.2	-4.3	-1.5	-0.9	-8.5	-8.7	-1.9	-8.9	-6.4	-13.1	-17.3
Net interest income	3.6	1.4	2.8	5.3	8.2	11.2	10.0	8.2	6.6	4.3	-1.0	-8.5	1.7
Loan loss expense	22.8	16.0	12.0	22.3	46.9	85.3	24.4	28.2	-5.0	5.8	16.8	75.1	12.5
Noninterest income	15.7	13.1	7.0	8.8	13.1	16.8	25.2	23.0	13.1	10.8	32.2	-0.5	7.8
Noninterest expense	7.9	7.7	8.8	9.1	16.3	10.7	13.9	15.2	10.1	4.6	9.1	3.0	-0.9
Net operating income	-18.4	-66.4	-23.4	-14.0	-25.5	-15.8	-11.7	3.8	7.5	9.9	-16.3	-135.6	-303.1
Net income	-11.0	-44.4	-13.3	-5.8	-17.4	-6.1	-6.7	2.6	14.3	10.3	-3.4	-104.7	-133.3

REGIONS: Northeast — Connecticut, Delaware, District of Columbia, Maine, Maryland, Massachusetts, New Hampshire, New Jersey, New York, Pennsylvania, Puerto Rico, Rhode Island, Vermont

Southeast — Alabama, Florida, Georgia, Mississippi, North Carolina, South Carolina, Tennessee, Virginia, West Virginia

Central — Illinois, Indiana, Kentucky, Michigan, Ohio, Wisconsin

Midwest — Iowa, Kansas, Minnesota, Missouri, Nebraska, North Dakota, South Dakota

Southwest — Arkansas, Louisiana, New Mexico, Oklahoma, Texas

West — Alaska, Arizona, California, Colorado, Hawaii, Idaho, Montana, Nevada, Oregon, Pacific Islands, Utah, Washington, Wyoming

NOTES TO USERS

Computation Methodology for Performance and Condition Ratios

All income figures used in calculating performance ratios represent amounts for that quarter, annualized.

All asset and liability figures used in calculating performance ratios represent *average* amounts (beginning-of-period amount plus end-of-period amount, divided by two).

All asset and liability figures used in calculating the condition ratios represent amounts as of the end of the period.

Definitions

"Problem" Banks — Federal regulators assign to each financial institution a uniform composite rating, based upon an evaluation of financial and operational criteria. The rating is based on a scale of 1 to 5 in ascending order of supervisory concern. "Problem" banks are those institutions with financial, operational or managerial weaknesses that threaten their continued financial viability. Depending upon the degree of risk and supervisory concern, they are rated either "4" or "5".

Earning Assets — all loans and other investments that earn interest, dividend or fee income.

Yield on Earning Assets — total interest, dividend and fee income earned on loans and investments as a percentage of average earning assets.

Cost of Funding Earning Assets — total interest expense paid on deposits and other borrowed money as a percentage of average earning assets.

Net Interest Margin — the difference between the yield on earning assets and the cost of funding them, i.e., the profit margin a bank earns on its loans and investments.

Net Noninterest Expense — total noninterest expense, excluding the expense of providing for loan losses, less total noninterest income. A measure of banks' overhead costs.

Net Operating Income — income after taxes but before gains (or losses) from securities transactions and nonrecurring items. The profit earned on banks' regular banking business.

Return on Assets — net income (including securities transactions and nonrecurring items) as a percentage of average total assets. A basic yardstick of bank profitability.

Return on Equity — net income as a percentage of average total equity capital.

Net Charge-offs — total loans and leases charged off due to uncollectibility, less amounts recovered on previous charge-offs.

Nonperforming Assets — the sum of loans past-due 90 days or more, loans in nonaccrual status and real estate owned other than bank premises.

Primary Capital — total equity capital plus the allowance for loan and lease losses plus minority interests in consolidated subsidiaries plus qualifying mandatory convertible debt, less intangible assets except purchased mortgage servicing rights.

Net Loans and Leases — total loans and leases less unearned income and the allowance for loan and lease losses.

Net Assets Repriceable in One Year or Less — short-term and variable rate interest-earning assets, minus interest-bearing liabilities maturing or repriceable within the same one-year interval. A measure of banks' sensitivity to interest rate changes, where a positive value indicates that banks' income from assets is more sensitive to movements in interest rates than is the expense of their liabilities, and vice-versa for a negative value.

Temporary Investments — the sum of interest-bearing balances due from depository institutions, federal funds sold and resold, trading-account assets and investment securities with remaining maturities of one year or less. These are banks' more liquid investments.

Loan Loss Expense — the addition to the allowance for loan and lease losses, the reserve maintained to absorb expected loan losses.

Additional information regarding bank performance, bank failures and economic issues affecting the banking industry is available in the *Banking and Economic Review,* published by the Division of Research and Strategic Planning, FDIC. Information on legislative issues and changes in state and federal laws and regulations governing banks is contained in the *Regulatory Review,* also published by the Division of Research and Strategic Planning. Single-copy subscriptions are available to the public free of charge. Requests should be mailed to:

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