The FDIC Quarterly Banking Profile

L. William Seidman, Chairman

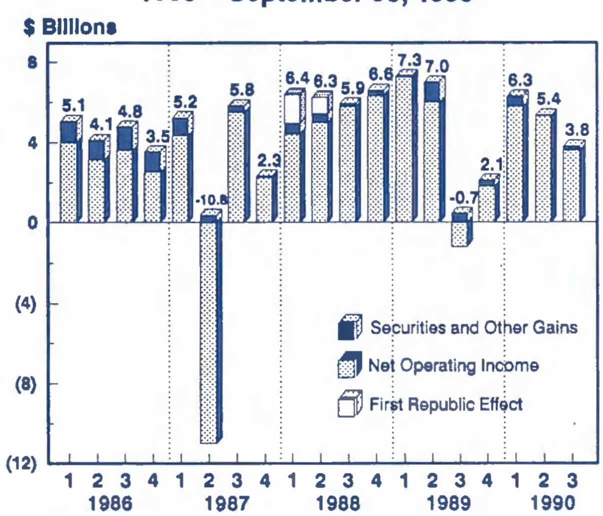
Third Quarter, 1990

COMMERCIAL BANKING PERFORMANCE – THIRD QUARTER, 1990

- ***Banks Earn $3.75 Billion In Third Quarter***
- ***Eastern Banks Face Continued Real Estate Worries***
- ***Northeastern Banks Report Aggregate Loss for Quarter***
- ***Western Banks Continue to Outperform Rest of U.S.***
- ***Asset Growth Remains Dependent on Real Estate***

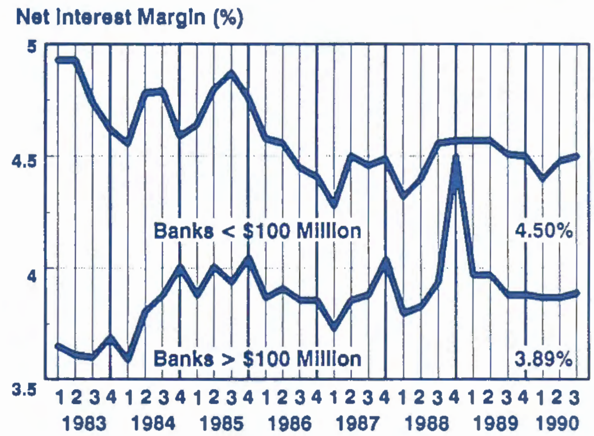
Under continuing pressure from troubled domestic assets, commercial banks earned $3.75 billion in the third quarter of 1990, a decline of 29 percent from their $5.3 billion profit in the second quarter. This result is a substantial improvement from the $770 million net loss experienced in the third quarter of 1989. The average annualized return on assets for the quarter is 0.45 percent. For the first nine months of 1990, bank earnings totalled $15.4 billion, 13 percent higher than earnings in the first three quarters of last year. The improvement over 1989 is attributable to the large additions to reserves for losses on loans to developing countries (LDCs) made by money-center banks in the second half of last year. Absent last year's LDC loan-loss provisioning, industry earnings would show a year-to-year decline.

Chart A - Quarterly Net Income of FDIC-Insured Banks 1986 - September 30, 1990



Banks set aside $8.3 billion in provisions for future loan losses in the third quarter, $1.9 billion more than in the second quarter. This amount was $4.4 billion below the provision in last year's third quarter, when banks added $7.7 billion to their reserves for LDC loans. Net loan charge-offs of $6.1 billion were $2.5 billion lower than in the previous quarter, but $1.2 billion higher than twelve months ago. Net loan losses continue to run ahead of last year's pace. The $30.5 billion in net loan charge-offs that banks have taken in the four quarters ended September 30 is the largest amount of any four-quarter period.

Chart B - Quarterly Net Interest Margins, 1983 - September 30, 1990



Retained earnings contributed $740 million to banks' net worth in the third quarter. Cash dividends paid by banks in the third quarter amounted to 80 percent of industry net income, so the industry's equity capital ratio increased by only two basis points. Banks' lending margins were largely unchanged, either from the previous quarter, or from a year earlier. Both interest income and interest expense were slightly below the levels of a year ago.

Total assets of commercial banks increased by $20 billion during the third quarter. Bank's real estate loans grew by $15.4 billion, their holdings of mortgage-backed securities increased by $12 billion, and their inventory of foreclosed properties grew by $2.3 billion. Together, these three categories of real

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estate assets increased by $29.7 billion in the third quarter, $9.7 billion more than the growth in total assets. Banks' total real estate assets now constitute 30.6 percent of total commercial bank assets; as recently as the end of 1984, they were only 18.8 percent of total assets.

Asset quality indicators continue to decline for the banking industry, reflecting the problems of real estate and commercial loans at banks in many eastern states. The proportion of troubled loans in banks' loan portfolios continues to rise, despite the high level of loan charge-offs. At the end of September, noncurrent loans and leases plus other real estate owned totalled $89.6 billion, $14.2 billion higher than twelve months earlier. Their share of total assets - 2.65 percent - is the highest level reached since banks began reporting the data in 1982. In contrast, loss reserves at commercial banks ended the third quarter slightly below the level of a year ago. Reserve coverage of noncurrent loans has decreased in each of the past three quarters. Currently, banks have 73 cents in reserves for each dollar of noncurrent loans, down from 83 cents a year ago.

Banks in the Northeast Region are experiencing the greatest asset-quality difficulties. Noncurrent loans and leases increased by 10 percent during the third quarter, while foreclosed real estate has grown to more than three times the amount of a year ago. The erosion in loan quality has been greatest in real estate loans, but losses on commercial and consumer loans have also risen from the levels of a year ago. The Region's banks registered a net loss for the third time in the last five quarters.

Banks in the Southeast Region have not had the same degree of asset-quality deterioration, but are following a similar trend. They have the second-highest growth rate for problem assets, after Northeast Region banks. Central Region banks have also shown signs of weakness in their real estate loans. Southwest Region banks continue to recover from past asset quality difficulties, reporting an aggregate net profit for the third consecutive quarter. Banks in the West Region are still turning in strong performance indicators.

The number of commercial banks on the FDIC's "Problem List" fell only slightly in the third quarter, to 1,006 from 1,014 at the end of June. Thirty-five banks failed in the third quarter, compared to 63 in the second quarter. At the present pace, the number of commercial bank failures for the full year will be below 200 for the first time since 1986.

Bank earnings are unlikely to show improvement in the fourth quarter, as the growth in problem assets points to more credit losses, concentrated among larger banking companies in the eastern U.S. Losses from commercial real estate loans, LDC loans and loans to highly-leveraged commercial borrowers (HLTs) are likely to increase. The relatively low level of reserves in relation to problem assets means that another round of loan-loss provisioning probably will prove necessary. There is little prospect of a near-term improvement in the Northeast as the national economy slows, and there are signs that banks in other areas east of the Mississippi River are feeling the pinch from worsening asset quality.

Chart C - Troubled Real Estate Asset* Rates by State
September 30, 1990

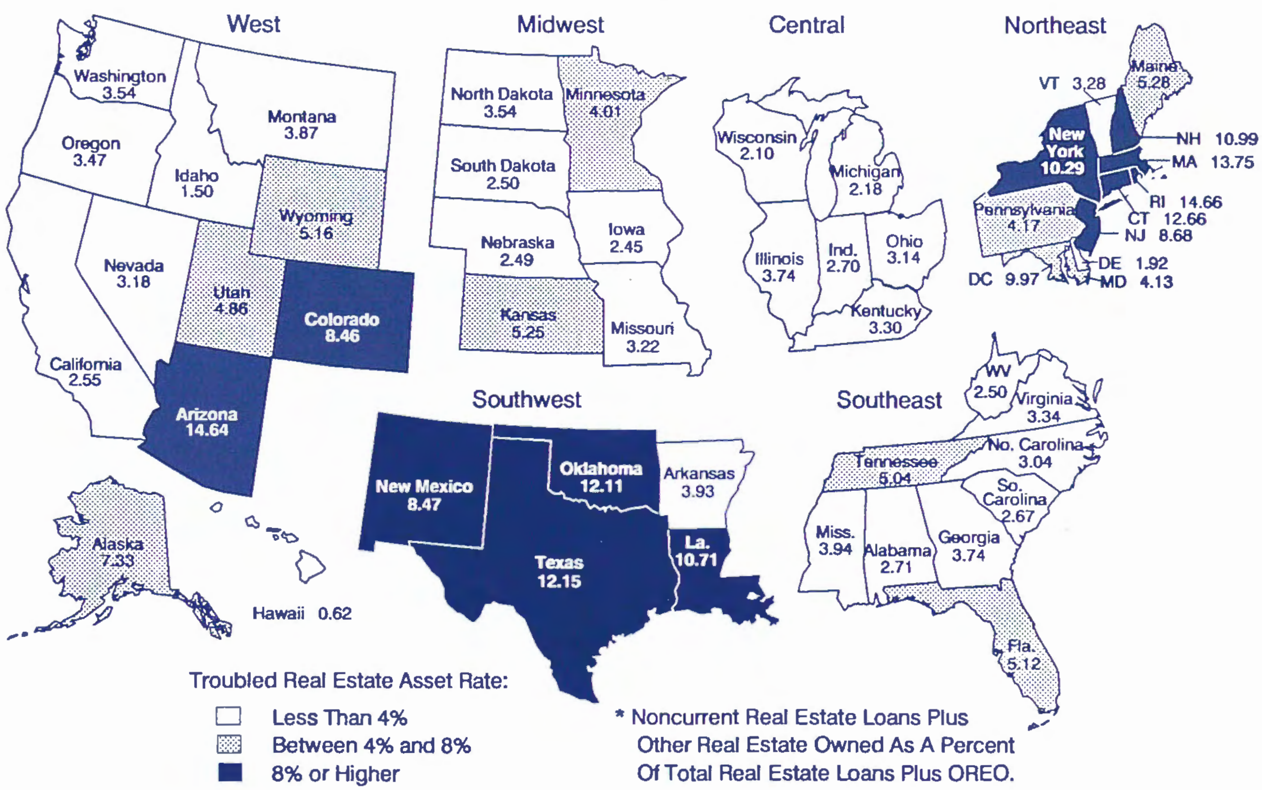

Table I. Selected Indicators, FDIC-Insured Commercial Banks

	1990*	1989*	1989	1988	1987	1986	1985
Return on assets	0.62%	0.57%	0.49%	0.82%	0.12%	0.63%	0.70%
Return on equity	9.70	9.02	7.79	13.30	2.00	9.94	11.31
Equity capital to assets	6.45	6.34	6.21	6.28	6.04	6.20	6.20
Primary capital ratio	7.93	8.03	7.92	7.84	7.70	7.22	6.91
Noncurrent loans and leases plus other real estate to assets	2.65	2.34	2.28	2.14	2.46	1.94	1.87
Net charge-offs to loans	1.36	0.90	1.16	1.00	0.92	0.98	0.84
Asset growth rate	4.90	4.15	5.37	4.36	2.01	7.71	8.86
Net operating income growth	15.04	-26.74	-38.80	1905.16	-91.04	-20.65	6.30
Percentage of unprofitable banks	11.15	10.81	12.37	14.65	17.66	19.79	17.09
Number of problem banks	1,006	1,151	1,092	1,394	1,559	1,457	1,098
Number of failed/assisted banks	134	162	206	221	201	144	118

**Through September 30; ratios annualized where appropriate*

Table II. Aggregate Condition and Income Data, FDIC-Insured Commercial Banks

(dollar figures in millions)

	Preliminary 3rd Qtr 1990	2nd Qtr 1990	3rd Qtr 1989	%Change 89:3-90:3
Number of banks reporting	12,399	12,502	12,825	-3.3
Total employees (full-time equivalent)	1,516,379	1,532,706	1,527,928	-0.8
CONDITION DATA				
Total assets	$3,381,202	$3,361,005	$3,223,245	4.9
Real estate loans	819,742	804,328	743,605	10.2
Commercial & industrial loans	620,654	621,257	616,723	0.6
Loans to individuals	399,858	391,914	388,125	3.0
Farm loans	33,639	32,314	31,799	5.8
Other loans and leases	231,029	231,544	244,435	-5.5
Total loans and leases	2,104,921	2,081,357	2,024,688	4.0
LESS: Reserve for losses	52,342	50,160	52,911	-1.1
Net loans and leases	2,052,579	2,031,197	1,971,777	4.1
Temporary investments	466,897	486,333	464,712	0.5
Securities over 1 year	449,270	434,318	400,221	12.3
All other assets	412,457	409,158	386,535	6.7
Total liabilities and capital	3,381,202	3,361,005	3,223,245	4.9
Noninterest-bearing deposits	440,880	450,331	441,792	-0.2
Interest-bearing deposits	2,160,849	2,138,187	2,025,402	6.7
Other borrowed funds	421,069	420,719	424,344	-0.8
Subordinated debt	19,139	19,733	18,936	1.1
All other liabilities	121,073	115,804	108,572	11.5
Equity capital	218,192	216,230	204,198	6.8
Primary capital	270,201	266,297	260,564	3.7
Noncurrent loans and leases	71,595	66,303	63,428	12.9
Other real estate owned	17,955	15,615	11,907	50.8
Loan commitments and letters of credit[1]	1,296,301	1,291,092	[1]	[1]
Domestic office assets	2,964,416	2,941,150	2,812,158	5.4
Foreign office assets	416,786	419,856	411,087	1.4
Domestic office deposits	2,272,285	2,258,457	2,143,757	6.0
Foreign office deposits	329,444	330,061	323,438	1.9
Earning assets	2,968,746	2,951,847	2,836,709	4.6
Volatile liabilities	1,135,906	1,140,683	1,145,644	-0.8

INCOME DATA	Preliminary First Three Qtrs. 1990	First Three Qtrs. 1989	%Change	Preliminary 3rd Qtr 1990	3rd Qtr 1989	% Change
Total interest income	$240,085	$235,640	1.9	$80,533	$80,899	-0.4
Total interest expense	154,152	151,753	1.6	51,293	52,897	-3.0
Net interest income	85,932	83,887	2.4	29,240	28,002	4.4
Provision for loan losses	20,319	20,655	-1.6	8,250	12,740	-35.3
Total noninterest income	40,572	37,267	8.9	13,634	12,805	6.5
Total noninterest expense	84,645	79,612	6.3	28,816	27,122	6.2
Applicable income taxes	6,806	8,078	-15.8	2,180	2,154	1.2
Net operating income	14,735	12,809	15.0	3,628	-1,211	N/M
Securities gains, net	235	523	-55.0	73	310	-76.5
Extraordinary gains, net	443	290	52.8	53	131	-59.4
Net income	15,413	13,621	13.2	3,754	-770	N/M
Net charge-offs	21,083	13,286	58.7	6,138	4,862	26.3
Net additions to capital stock	819	270	202.9	-12	-49	N/M
Cash dividends on capital stock	9,633	10,026	-3.9	3,014	3,391	-11.1

[1]See Notes to Users, p.6

N/M - not meaningful

Table III. First Three Quarters 1990 Bank Data *(Dollar figures in billions, ratios in %)*

		Asset Size Distribution				Geographic Distribution					
						EAST			WEST		
	All Banks	Less than $100 Million	$100 Million to $1 Billion	$1-10 Billion	Greater than $10 Billion	Northeast Region	Southeast Region	Central Region	Midwest Region	Southwest Region	West Region
FIRST THREE QUARTERS *Preliminary (The way it is . . .)*											
Number of banks reporting	12,399	9,367	2,653	331	48	1,075	1,960	2,746	2,961	2,193	1,464
Total assets	$3,381.20	$359.37	$638.06	$1,037.44	$1,346.34	$1,326.12	$498.96	$544.20	$216.17	$263.28	$532.47
Total deposits	2,601.73	318.10	548.15	783.45	952.03	953.97	390.10	433.53	176.50	222.25	425.37
Net income *(in millions)*	15,413	2,222	4,035	4,163	4,993	2,342	2,611	3,455	1,706	1,122	4,177
Percentage of banks losing money	11.1%	12.1%	7.2%	15.1%	20.8%	21.6%	12.6%	4.5%	5.0%	17.0%	17.5%
Percentage of banks with earnings gains	53.0%	52.7%	55.1%	44.7%	56.3%	39.7%	55.6%	55.8%	51.8%	55.0%	53.5%
Performance Ratios *(annualized)*											
Yield on earning assets	11.02%	10.41%	10.61%	10.67%	11.67%	11.68%	10.55%	10.41%	10.56%	10.09%	11.11%
Cost of funding earning assets	7.08	5.95	6.10	6.44	8.39	8.22	6.38	6.50	6.27	6.38	6.16
Net interest margin	3.94	4.46	4.51	4.23	3.29	3.46	4.17	3.91	4.29	3.71	4.95
Net noninterest expense to earning assets	2.02	2.75	2.56	1.99	1.58	1.75	2.29	2.06	1.91	2.32	2.32
Net operating cash flow to assets	1.69	1.56	1.76	1.98	1.46	1.50	1.67	1.64	2.13	1.18	2.28
Net operating income to assets	0.59	0.81	0.86	0.54	0.45	0.21	0.69	0.87	1.06	0.54	1.03
Return on assets	0.62	0.84	0.87	0.55	0.50	0.24	0.71	0.87	1.07	0.58	1.07
Return on equity	9.70	9.20	11.27	8.41	10.12	4.30	10.02	12.37	13.59	8.87	16.63
Net charge-offs to loans and leases	1.36	0.55	0.77	1.33	1.83	1.94	0.78	0.86	0.95	1.49	1.07
Loan loss provision to net charge-offs	96.37	132.76	116.83	138.75	65.38	91.37	150.26	95.14	111.61	71.39	91.75
Condition Ratios											
Loss allowance to:											
Loans and leases	2.49%	1.68%	1.64%	2.22%	3.27%	3.37%	1.63%	1.62%	1.86%	2.65%	2.18%
Noncurrent loans and leases	73.11	80.76	74.19	74.39	71.41	66.14	78.89	81.88	97.82	75.51	86.63
Noncurrent loans and leases plus other real estate to assets	2.65	1.73	1.87	2.49	3.38	3.73	1.75	1.49	1.49	2.89	2.34
Equity capital ratio	6.45	9.19	7.80	6.55	5.01	5.57	7.18	7.10	8.04	6.70	6.55
Primary capital ratio	7.93	10.04	8.70	7.78	7.14	7.67	8.05	8.03	9.01	7.84	7.97
Net loans and leases to deposits	78.89	59.41	70.54	84.11	85.92	83.79	79.31	75.49	69.57	54.63	87.55
Growth Rates *(year-to-year)*											
Assets	4.9%	7.6%	9.9%	8.1%	8.4%	4.1%	7.0%	3.8%	3.4%	2.9%	7.8%
Equity capital	6.8	5.1	10.7	7.9	11.7	1.6	8.6	6.2	7.1	17.1	12.8
Net interest income	2.4	5.6	8.0	6.8	3.8	-0.5	6.8	2.5	0.3	6.2	3.8
Net income	13.2	-0.1	-2.4	-31.4	330.8	141.3	-19.0	-13.1	-0.1	795.8	15.5
Noncurrent loans and leases plus other real estate owned	18.9	2.9	23.5	53.8	18.5	40.8	50.2	16.6	5.3	-37.5	1.8
Net charge-offs	58.7	1.1	44.4	48.8	93.0	116.0	67.9	36.5	-12.4	-7.5	12.4
Loan loss provision	-1.6	3.8	28.8	60.3	-32.2	-6.9	86.8	15.4	-0.4	-48.2	-4.5
PRIOR FIRST THREE QUARTERS *(The way it was . . .)*											
Return on assets 1989	0.57%	0.89%	0.93%	0.84%	0.08%	0.10%	0.95%	1.04%	1.12%	0.07%	1.00%
1987	0.02	0.67	0.73	0.59	-1.04	-0.39	0.99	0.44	0.66	-0.47	-0.16
1985	0.76	0.89	0.92	0.89	0.52	0.80	1.12	0.85	0.85	0.63	0.40
Equity capital ratio 1989	6.34	9.15	7.60	6.38	4.80	5.70	7.07	6.94	7.77	5.88	6.25
1987	6.13	8.77	7.48	6.26	4.34	5.42	7.05	6.79	7.62	6.45	5.63
1985	6.32	8.76	7.30	6.04	4.90	5.66	6.91	6.96	7.68	7.17	5.61
Noncurrent loans and leases plus other real estate to assets 1989	2.34	1.91	1.76	1.78	3.24	2.75	1.24	1.33	1.46	4.76	2.48
1987	2.07	2.27	2.00	1.87	3.53	2.52	1.14	1.39	2.04	5.49	3.55
1985	2.17	2.19	1.77	1.66	2.55	1.83	1.10	1.62	2.45	2.83	3.07
Net charge-offs to loans and leases 1989	0.90	0.64	0.63	0.91	1.08	0.93	0.50	0.66	1.11	1.52	1.06
1987	0.80	1.02	0.82	0.76	0.79	0.58	0.53	0.54	1.43	1.93	1.00
1985	0.71	1.02	0.68	0.61	0.71	0.43	0.48	0.58	1.38	1.15	1.07

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

Table IV. Third Quarter 1990 Bank Data *(Dollar figures in billions, ratios in %)*

		Asset Size Distribution				Geographic Distribution					
						EAST			WEST		
	All Banks	Less than $100 Million	$100 Million to $1 Billion	$1-10 Billion	Greater than $10 Billion	Northeast Region	Southeast Region	Central Region	Midwest Region	Southwest Region	West Region
PRELIMINARY THIRD QUARTER *(The way it is . . .)*											
Number of banks reporting	12,399	9,367	2,653	331	48	1,075	1,960	2,746	2,961	2,193	1,464
Net income *(in millions)*	3,754	721	1,283	1,034	715	-363	753	1,194	563	339	1,267
Percentage of banks losing money	11.6%	12.2%	8.3%	18.4%	25.0%	23.4%	13.7%	5.3%	5.8%	15.6%	17.2%
Percentage of banks with earnings gains	55.5%	54.5%	59.9%	47.1%	58.3%	43.0%	56.9%	56.8%	54.3%	58.0%	58.9%
Performance Ratios *(annualized)*											
Yield on earning assets	10.91%	10.48%	10.74%	10.68%	11.29%	11.29%	10.53%	10.50%	10.57%	10.19%	11.21%
Cost of funding earning assets	6.95	5.97	6.17	6.46	8.00	7.86	6.38	6.51	6.28	6.35	6.24
Net interest margin	3.96	4.50	4.57	4.23	3.28	3.44	4.16	3.99	4.29	3.85	4.96
Net noninterest expense to earning assets	2.06	2.81	2.59	1.99	1.62	1.76	2.32	2.05	1.91	2.49	2.40
Net operating cash flow to assets	1.67	1.54	1.79	1.97	1.42	1.45	1.64	1.73	2.14	1.16	2.23
Net operating income to assets	0.43	0.76	0.80	0.39	0.20	-0.13	0.59	0.88	1.03	0.50	0.94
Return on assets	0.45	0.81	0.81	0.40	0.21	-0.11	0.61	0.88	1.05	0.52	0.95
Return on equity	6.92	8.81	10.45	6.12	4.25	-1.96	8.45	12.51	13.12	7.74	14.75
Net charge-offs to loans and leases	1.18	0.61	1.03	1.41	1.19	1.46	0.93	0.66	0.93	2.03	1.01
Loan loss provision to net charge-offs	134.39	129.61	106.09	148.26	133.12	156.65	143.58	143.11	117.11	59.28	107.71
Growth Rates *(year-to-year)*											
Net interest income	4.4%	7.7%	11.2%	6.5%	7.3%	-0.3%	9.1%	6.2%	1.0%	11.9%	6.5%
Net income	N/M	2.0	2.3	-46.7	N/M	N/M	-26.5	-3.3	0.7	N/M	19.9
Net charge-offs	26.3	4.1	66.4	35.4	24.8	50.5	72.9	8.5	-35.4	11.6	1.9
Loan loss provision	-35.3	5.1	33.7	44.7	-62.1	-48.5	99.3	1.2	1.8	-54.6	-14.1
PRIOR THIRD QUARTERS *(The way it was . . .)*											
Return on assets . . . 1989	-0.10%	0.83%	0.81%	0.81%	-1.60%	-1.41%	0.89%	0.95%	1.08%	-0.24%	0.86%
. . . 1987	0.79	0.63	0.75	0.82	0.85	0.94	1.05	0.92	0.99	-0.47	0.76
. . . 1985	0.77	0.86	0.90	0.90	0.58	0.80	1.13	0.86	0.83	0.55	0.54
Net charge-offs to loans and leases . 1989	0.97	0.71	0.74	1.05	1.08	0.99	0.58	0.64	1.47	1.73	1.10
. . . 1987	0.83	1.06	0.88	0.76	0.76	0.58	0.57	0.61	1.44	2.18	0.96
. . . 1985	0.82	1.19	0.83	0.80	0.80	0.49	0.53	0.63	1.59	1.37	1.29

N/M - not meaningful

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NOTES TO USERS

COMPUTATION METHODOLOGY FOR PERFORMANCE AND CONDITION RATIOS

All income figures used in calculating performance ratios represent amounts for that period, annualized (multiplied by the number of periods in a year).

All asset and liability figures used in calculating performance ratios represent **average** amounts for the period (beginning-of-period amount plus end-of-period amount plus any periods in between, divided by the total number of periods).

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

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 and before gains (or losses) from securities transactions and from nonrecurring items. The profit earned on banks' regular banking business.

Net Operating Cash Flow—pre-tax net operating income before the provision for loan and lease losses; a measurement of banks' cash flow, net of interest and overhead expenses, from regular operations. Previously referred to as "adjusted net operating income".

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

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

Loan Commitments and Letters of Credit—includes unused credit card commitments and overdraft plans, reflecting Call report revisions effective March 31, 1990.

Net Charge-offs—total loans and leases charged off (removed from balance sheet because of uncollectibility) during the quarter, less amounts recovered on loans and leases previously charged off.

Noncurrent Loans & Leases—the sum of loans past-due 90 days or more and loans in nonaccrual status.

Other Real Estate Owned—primarily foreclosed property. Direct and indirect investments in real estate ventures are excluded where appropriate.

Primary Capital—total equity capital plus the allowance for loan and lease losses plus minority interests in consolidated subsidiaries plus qualifying mandatory convertible debt (cannot exceed 20 percent of total primary capital), 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.

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.

Volatile Liabilities—the sum of large denomination time deposits, foreign office deposits, federal funds purchased, and other borrowed money.

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