PRESS RELEASE

Federal Deposit Insurance Corporation

November 21, 1996

Media Contact:
Jay Rosenstein (202) 898-7303
Robert M. Garsson (202) 898-6993

FDIC REVIEW OF LENDING PRACTICES SHOWS NO MAJOR CHANGES IN RISK

FOR IMMEDIATE RELEASE

Loan underwriting standards at most FDIC-supervised institutions examined in recent months remain solid and unchanged from previous reviews, according to a new report from the agency. However, as with the first FDIC underwriting report, which was issued in April, about one in 10 institutions was characterized as having higher-than-normal risk in its underwriting practices. "Very few of the banks the FDIC examined showed risky underwriting practices," Chairman Ricki Helfer said today. "Our supervisory staff will monitor loans closely in those few areas where weaknesses have been noted."

Underwriting encompasses the terms and conditions of loan agreements that determine the riskiness of a particular credit. FDIC examiners give their general assessment of an institution's underwriting standards and comment on potential problem areas, such as lending to relatively weak borrowers, relying on substandard collateral, and funding speculative projects.

The review of loan underwriting practices, obtained through an examiner reporting system implemented in early 1995, is one of a number of initiatives launched by the FDIC to provide early warnings of potential loan problems in the banking system. The information gathered during examinations also helps allocate examiner resources and identify potential weaknesses in underwriting practices that can be addressed during on-site examinations.

For the latest period, examiners reported on lending practices at 1,383 state-chartered institutions for which the FDIC is the primary federal regulator. The results cover reports filed during the six months that ended September 1996. Most of the banks were small, community-based institutions. Overall, those institutions represented 12 percent of all FDIC-insured institutions and six percent of the assets.

The FDIC report found that the vast majority (90 percent) had not changed their practices since their last examination, although five percent were judged to have looser underwriting standards. When asked to report on specific practices, FDIC examiners cited only a few areas of potential concern:

- Twelve percent of the institutions were characterized by higher-than-normal risk in their lending practices;

- Twenty-eight percent frequently failed to adjust loan pricing based on loan quality;

- Eleven percent of "active" construction lenders were cited for funding speculative projects; and

- The phase-out of farm subsidies was identified by examiners as a problem area at 40 percent of the banks active in agricultural lending.

In contrast, almost all institutions active in credit card lending showed average or below-average underwriting risk for these loans. Of the six banks that specialized in credit card lending examined during the period, none showed notable weaknesses in current underwriting practices.

"Despite these positive findings about credit card lending," Chairman Helfer said, "the recent increases in personal bankruptcies and credit card charge-offs remain a concern." She noted that the report primarily covered banks whose credit card loans are only a small percentage of their assets.