Statement
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On the Release
Of
The FDIC's Preliminary Bank Earnings Report

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Welcome to this press conference announcing the FDIC's first Preliminary Bank Earnings Report. Most of you routinely cover our Quarterly Banking Profile, our comprehensive publication of data on the condition of the banking and thrift industries. It takes us several days to analyze the data that goes into that publication, and several more to prepare the publication and its accompanying graph book. However, we don't want to keep you - and the public - waiting until that publication is printed for information on quarterly commercial bank earnings - and our read on it. So we have decided to release that information as quickly as we can in a preliminary report, with the comprehensive Quarterly Banking Profile to follow when it is completed. Today is the first release of the preliminary earnings data.

And what do the data show?

Earnings of the commercial banking industry rebounded sharply to $19.3 billion from $14.7 billion in the second quarter - a 32 percent rise. This rebound resulted in banking's third-highest quarterly earnings ever. You'll recall that a few large banks in the second quarter reported earnings that were depressed by restructurings and credit-related charges. Their depressed earnings in turn depressed earnings for the industry as a whole. Unlike earlier in the year, no comparable problems plagued the commercial banking industry in the third quarter. But concerns for the future remain - particularly in credit quality.

These concerns darken an otherwise sunny picture.

Loan-loss provisions were 26 percent above the level of a year ago, absorbing significantly more of the industry's net operating revenues. These provisions reflect rising loan losses and growing inventories of noncurrent loans, particularly in banks' loans to commercial and industrial borrowers. In the third quarter, commercial loan charge-offs and noncurrent commercial loans together totaled $17.7 billion. In the fourth quarter of 1997, they amounted to $7.5 billion. In less than three years, they have more than doubled. This is our most significant concern for the future - that this deteriorating trend will continue.

Moreover, net charge-offs on all loans were up more than 16 percent from the third quarter of 1999. Almost one third of all loan charge-offs occurred in loans to commercial and industrial borrowers; these charge-offs were almost 44 percent higher than a year ago. The decline in credit quality is concentrated among large institutions.

In the third quarter, commercial banks increased their reserves for loan losses by $602 million - or 1 percent. However, this increase did not keep pace with the growth in banks' loans, and the industry's ratio of reserves to loans declined, continuing a 13-year trend. Over the past 10 years, reserves as a percentage of total loans and leases have declined from 2.54 percent to 1.66 percent. A year ago, the ratio was 1.74 percent. Because reserve growth also continues to lag behind growth in noncurrent loans, the industry's "coverage ratio" declined in the third quarter from $1.69 for every $1.00 of noncurrent loans to $1.61. A year ago, banks held $1.77 in reserves for every $1.00 of noncurrent loans.

In short, while earnings strength remained widespread, we are seeing signs that banks may be having difficulty sustaining their profitability. As the report in front of you shows, among those signs, fewer than half of all commercial banks reported a higher quarterly return on assets than they reported a year ago. Net interest margins continued to decline. Growth in several types of noninterest income - which has been the strongest source of rising bank revenues - is slowing. By historical standards, profitability remains strong, but bankers - and bank regulators - cannot be complacent.

With me today are Don Inscoe and Ross Waldrop, the FDIC analysts who prepared the FDIC Preliminary Bank Earnings Report. We will be happy to address your questions.