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Federal Deposit Insurance Corporation

FOR IMMEDIATE RELEASE
March 20, 2000

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## FDIC REPORT IDENTIFIES WEAKNESSES IN COMMERCIAL AND INDUSTRIAL LOAN PORTFOLIOS

Rapidly growing commercial loan portfolios and weakening indicators of commercial credit quality raise concerns about the future performance of commercial and industrial (C&I) loan portfolios at financial institutions insured by the Federal Deposit Insurance Corporation (FDIC), according to a report released today by the FDIC.

In the first quarter 2000 edition of the Regional Outlook, FDIC analysts point to several indicators of weakening business credit quality, including increasing corporate indebtedness, stress in some prominent industry sectors, adverse trends in corporate bond defaults and the results of a recent interagency review of large commercial credits.

"C&I lending is a large and fast growing segment of commercial bank loan portfolios. The signs of commercial credit quality deterioration that we are seeing today mean that insured institutions need to be more vigilant in their loan underwriting and administration," said FDIC Chairman Donna Tanoue.

In the Kansas City edition of the Regional Outlook, analysts examine some of the challenges confronting FDIC-insured institutions serving rural communities. Emerging trends suggest that if rural areas continue to lose population, many banks and thrifts may eventually be located in counties with population bases that will make it difficult to maintain infrastructure and public services. This situation could lead to consolidation among rural banks or more aggressive strategies to attract loans and deposits.

The FDIC analysts note that population continues to decline in a significant number of rural counties. Moreover, in over 20 percent of these rural counties the exodus rate is accelerating. Insured institutions in these counties have reported slower loan and deposit growth, higher concentrations of agricultural loans, and a greater reliance on nontraditional funding sources, such as Federal Home Loan Bank borrowings, than institutions in counties with growing populations.

Another report in the Regional Outlook shows that exposure to international economic conditions varies widely by industry. For example, the machinery and transportation equipment industries are highly exposed to international markets while the printing and publishing industry faces little competition from imports and is not dependent on exports. As a result, economic conditions abroad are particularly important in any assessment of these firms' future revenue growth and profitability.

Other regional highlights include:

- In the Atlanta Region, strong economic growth in urban areas may be driving an increase in de novo bank activity. Analysts conclude that it is likely that the critical period in the life cycle of a de novo bank extends beyond the first three years of operation.

- In the San Francisco Region, strong economic growth in urban areas has helped drive merger and acquisition and de novo activity to the highest level in the last decade.

- In the Boston Region, commercial lending activity has been brisk for several years. Rapid commercial loan growth has been partially offset, however, by slow growth or even declines in other higher risk sectors of the loan portfolio.

- In the Dallas Region, record levels of government payments are helping to maintain net farm income above the decade average. The effect of the North American Free Trade Agreement on job growth has been marginally positive.

- In the Memphis Region, many insured financial institutions are changing asset compositions to improve yields; some may be accepting greater credit risk and market sensitivity in the process.

- In the Chicago Region, commercial and industrial loan levels are growing rapidly and rising interest rates may dampen the profitability of residential real estate lenders.

- In the New York Region, during the past five years non-interest income increased to 50 percent of operating income and has offset the effect of lower net interest margins on bank earnings.

The Regional Outlook for each FDIC region and the National Edition are available on the Internet via the World Wide Web at http://www.fdic.gov/bank/analytical/regional/index.html. Printed copies of the Regional Outlook are available from the FDIC's Public Information Center (800-276-6003 or (703) 562-2200). To subscribe to the Regional Outlook, contact the Center.