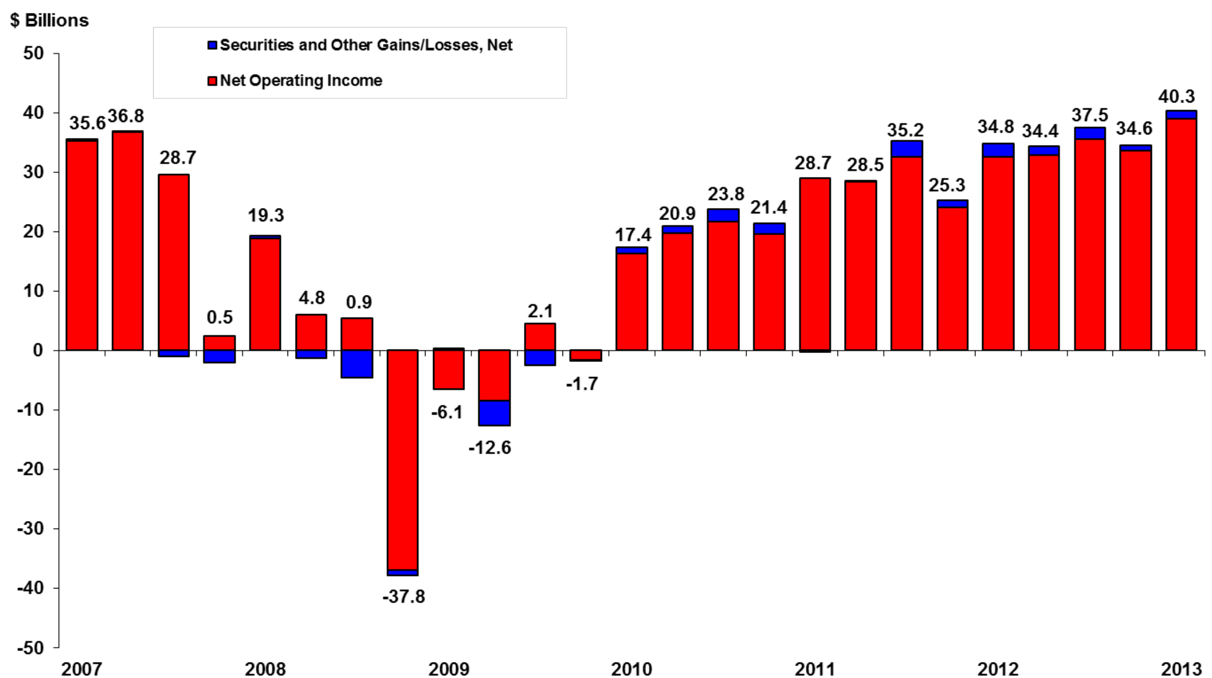
Remarks by
Martin J. Gruenberg, FDIC Chairman,
on the
First Quarter 2013 Quarterly Banking Profile
May 29, 2013

Good morning, and welcome to our release of first quarter results for FDIC-insured institutions. Today's report shows further progress in the recovery that has been underway in the banking industry for more than three years. We saw improvement in asset quality indicators over the quarter, a continued increase in the number of profitable institutions, and further declines in the number of problem banks and bank failures.

Chart 1



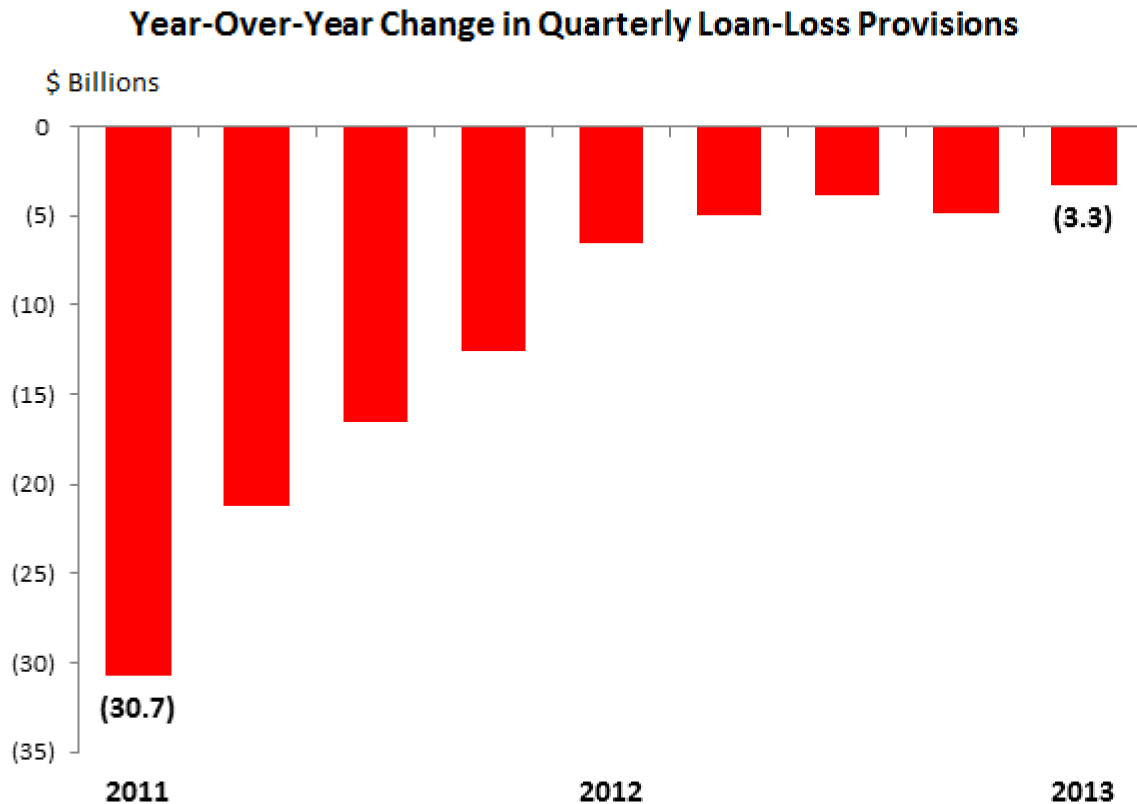
First quarter net income rose to 40.3 billion dollars. While this is an all-time quarterly high, we note that the previous high occurred more than six years ago when the industry was 20 percent smaller, in terms of total assets, than it is today.

We also note that large, nonrecurring income and expense items at some of the industry's largest institutions exerted a significant influence on the quarterly change in

net income and helped push industry net income above 40 billion dollars for the first time.

In recent years, lower loan loss provisions have been the primary driver of higher industry earnings. But as problem loans decline at institutions in all size groups, the year-over-year reduction in the industry's provision expense is becoming progressively smaller. The next chart shows that the year-over-year decline in industry loan loss provisions in the first quarter of 3.3 billion dollars was about one-tenth the size that it was only two years ago.

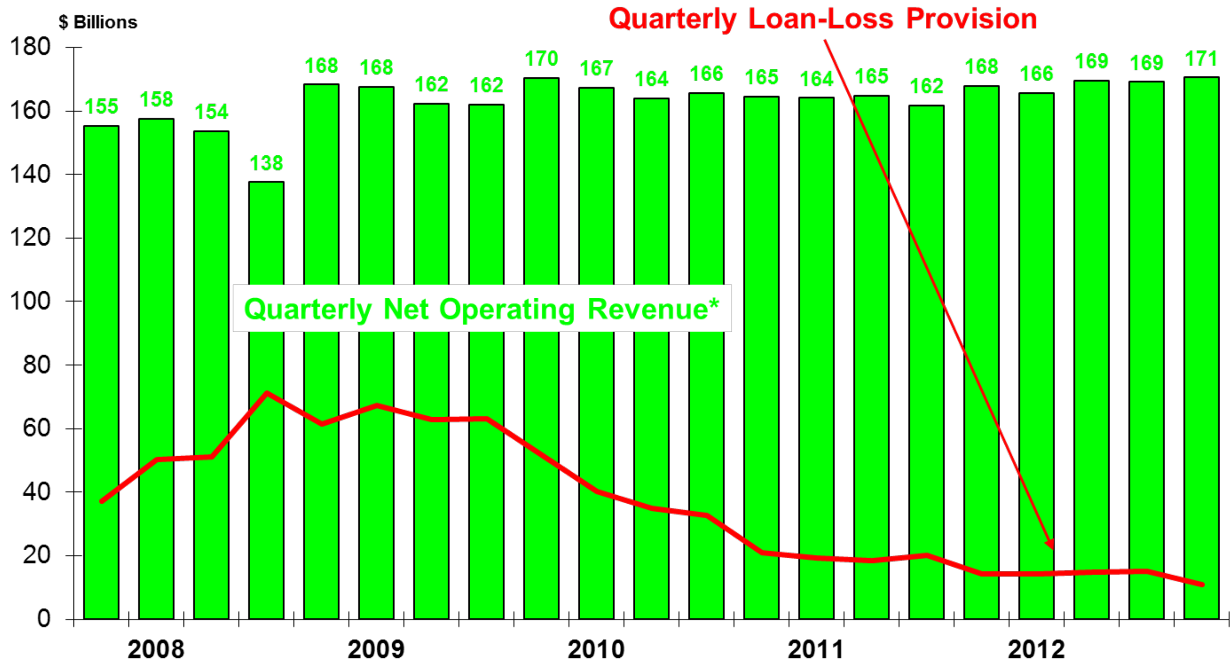
Chart 2



As the impact of declining provision expenses diminishes, future earnings for the industry increasingly will be determined by revenues. Total net operating revenue for the industry was 171 billion dollars during the quarter, up slightly from recent quarters, but essentially flat.

Chart 3

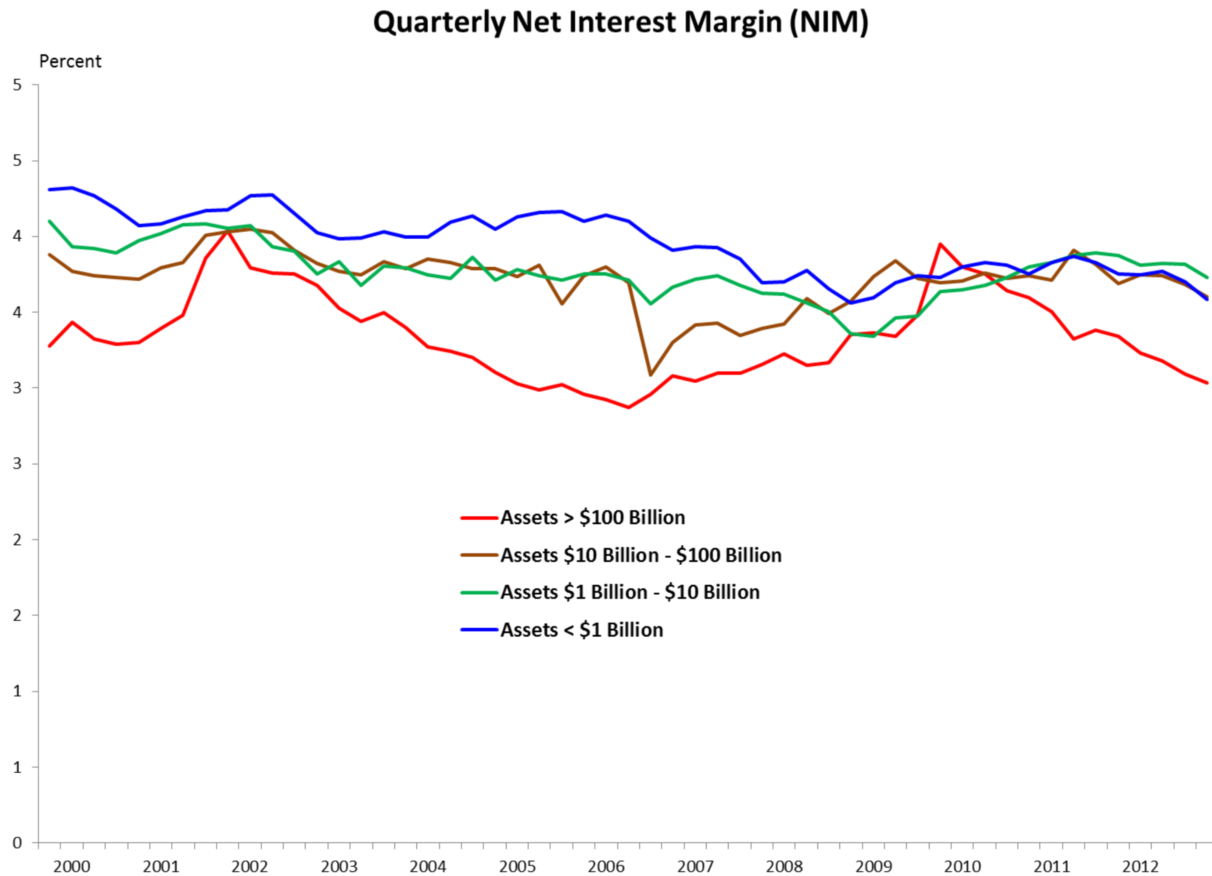
Quarterly Revenue and Loan-Loss Provision, 2008 - 2013



* Net operating revenue = net interest income + noninterest income

The principal reason why revenue has been nearly flat—growing just 1.6 percent from a year ago—is the downward pressure on net interest margins that banks have experienced in this low interest rate, flat yield curve environment.

Chart 4

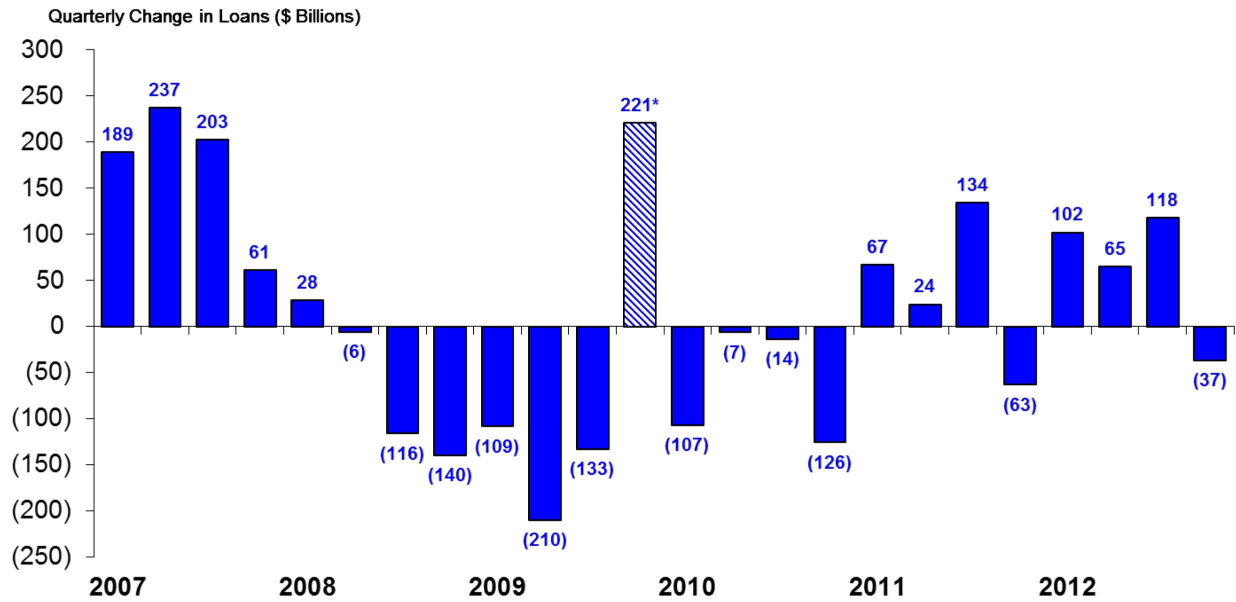


The industry's net interest margin in the first quarter fell to 3.27 percent, the lowest level since the third quarter of 2006. As you can see in this next chart, the biggest decline has been at large institutions. But the downward trend is important for smaller banks because they are more dependent on net interest income as a source of revenue.

Insured institutions added more than half a trillion dollars in interest-earning assets to their balance sheets over the past year. Yet, the interest income produced by these assets fell by 6 billion dollars. This is because older, higher-yielding assets are maturing off bank balance sheets and are being replaced by lower-yielding assets.

Chart 5

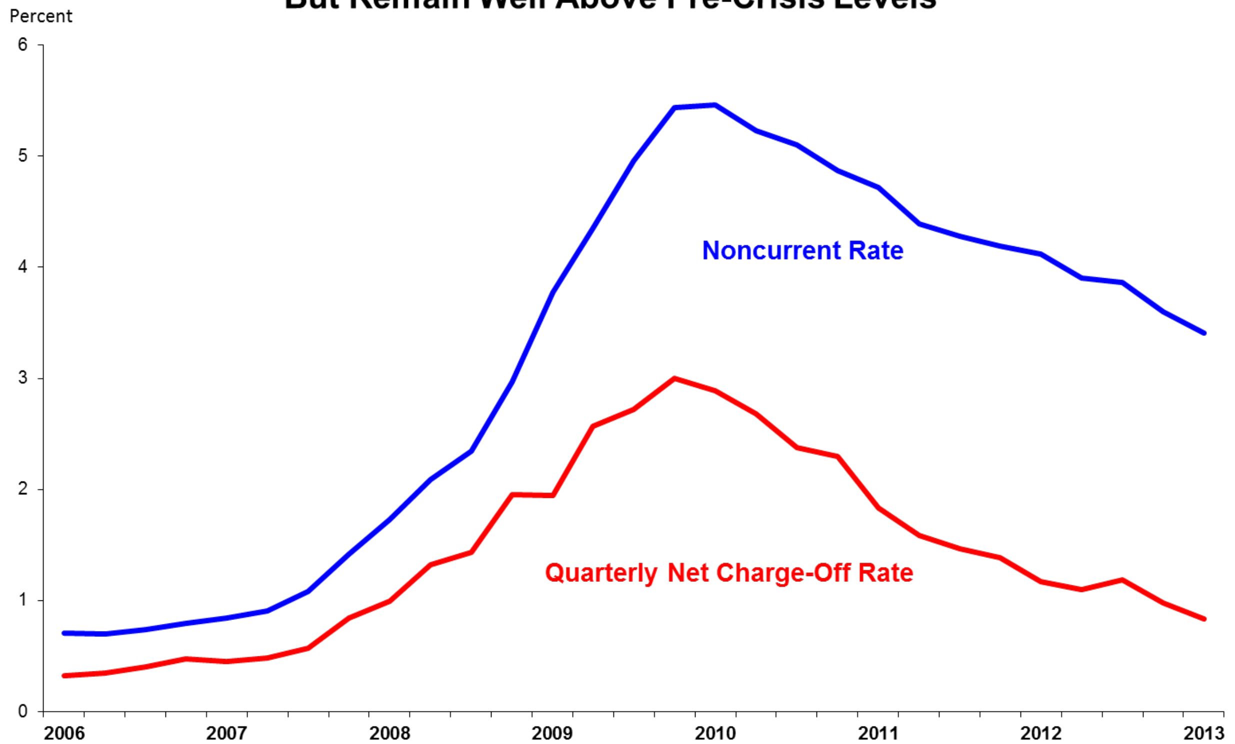
Quarterly Change in Loan Balances



* FASB Statements 166 and 167 resulted in the consolidation of large amounts of securitized loan balances back onto banks' balance sheets in the first quarter of 2010. Although the total amount consolidated cannot be precisely quantified, the industry would have reported a decline in loan balances for the quarter absent this change in accounting standards.

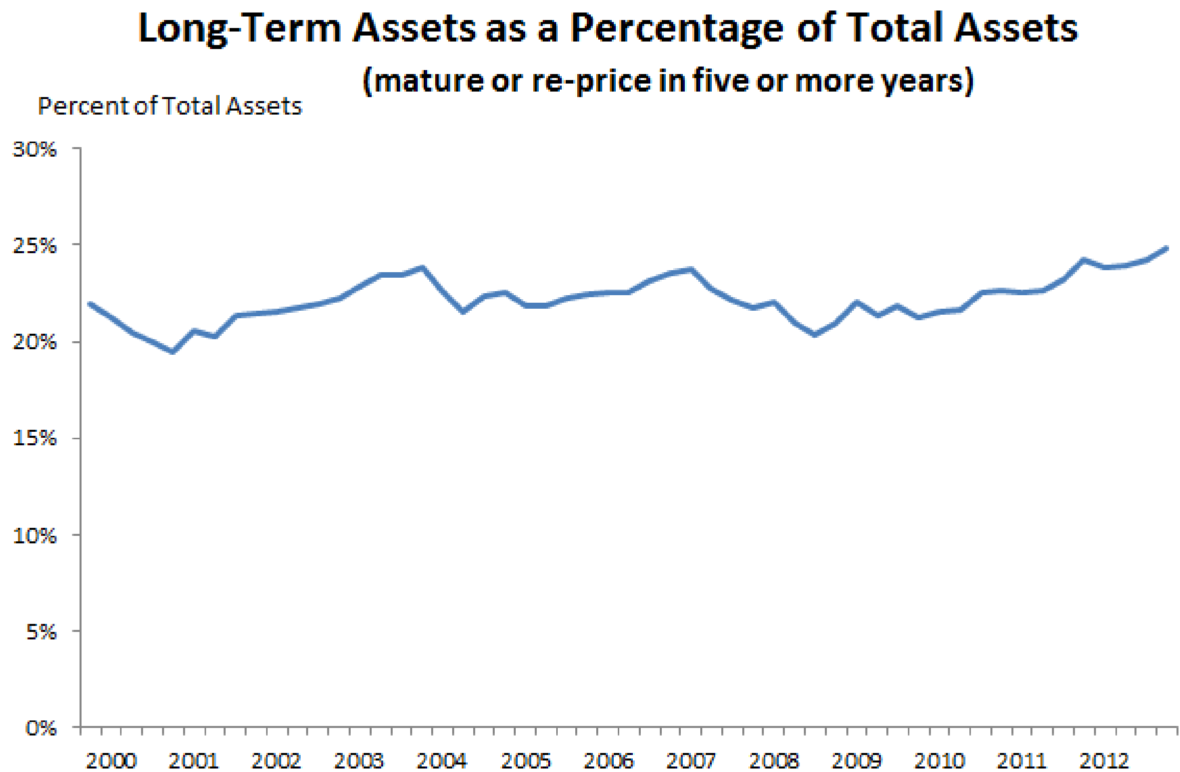
Loan balances posted a seasonal decline in the first quarter, similar to what we have seen over the past two years, but to a lesser extent. The underlying trend in loan growth has been generally positive as the industry has recovered over the past several years.

Chart 6



The next chart shows that asset quality continues to improve. The net charge-off rate during the quarter was the lowest for the industry since the fourth quarter of 2007. While noncurrent loans remain elevated by historical norms, the trend remains positive.

Chart 7

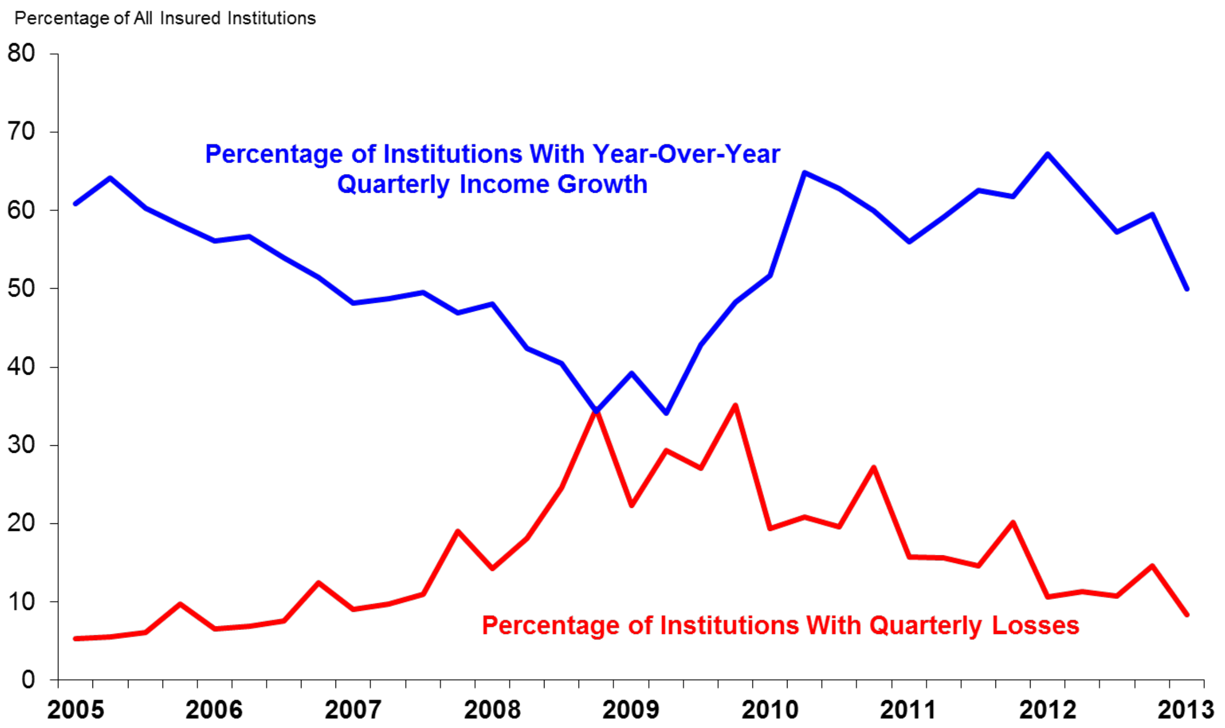


The low interest rate environment has created an incentive for lenders to seek longer-term, higher-yielding loans and for borrowers to lock in historically low interest rates for longer terms.

This next chart illustrates the extent to which the industry has been increasing the share of longer-term assets that mature or re-price in five or more years. While this shift has helped to limit the decline in net interest margins, it also potentially exposes institutions to additional risk when interest rates rise.

This has been a matter of supervisory focus for the banking agencies. In the current environment, institutions should have robust processes for measuring and, where necessary, mitigating their exposure to potential increases in interest rates.

Chart 8

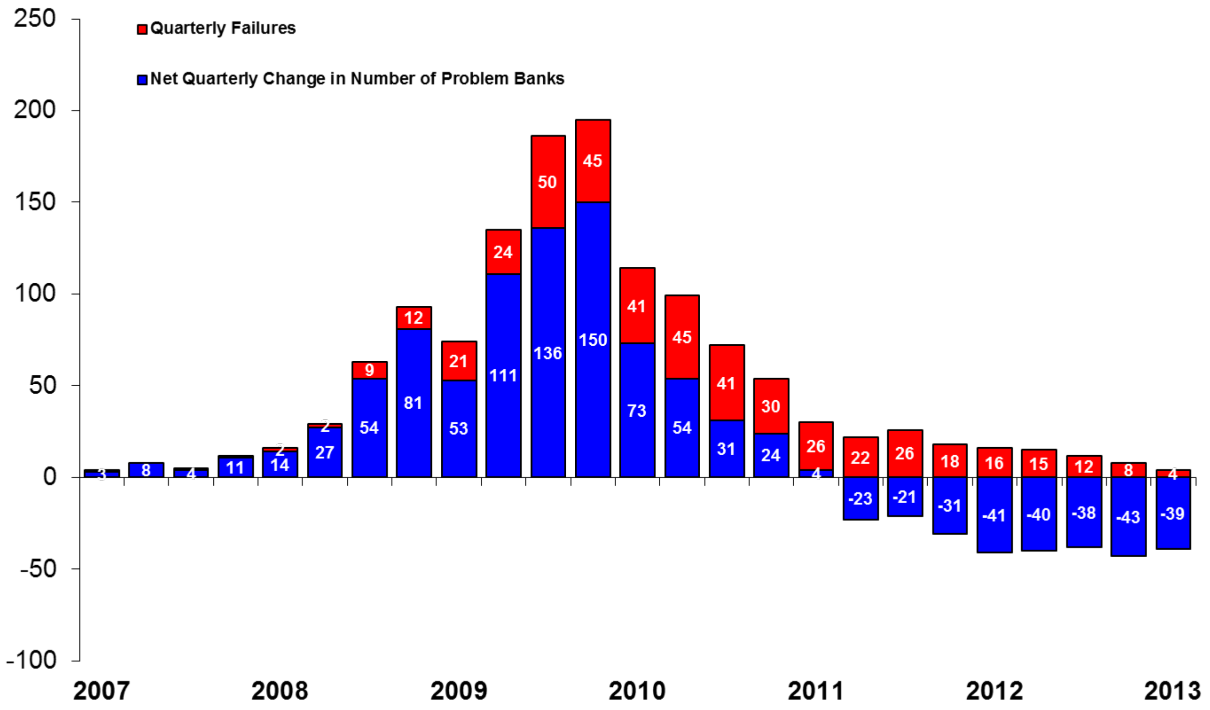


The red line in the next chart shows that the share of institutions reporting quarterly losses is trending down. At just 8.4 percent, it is now the lowest it has been since before the crisis.

The blue line shows that half of all banks reported a year-over-year increase in their earnings. With revenues rising slowly and with loan loss provisions leveling off, we see an industry where more institutions are profitable, but fewer are able to continue increasing their net income.

Chart 9

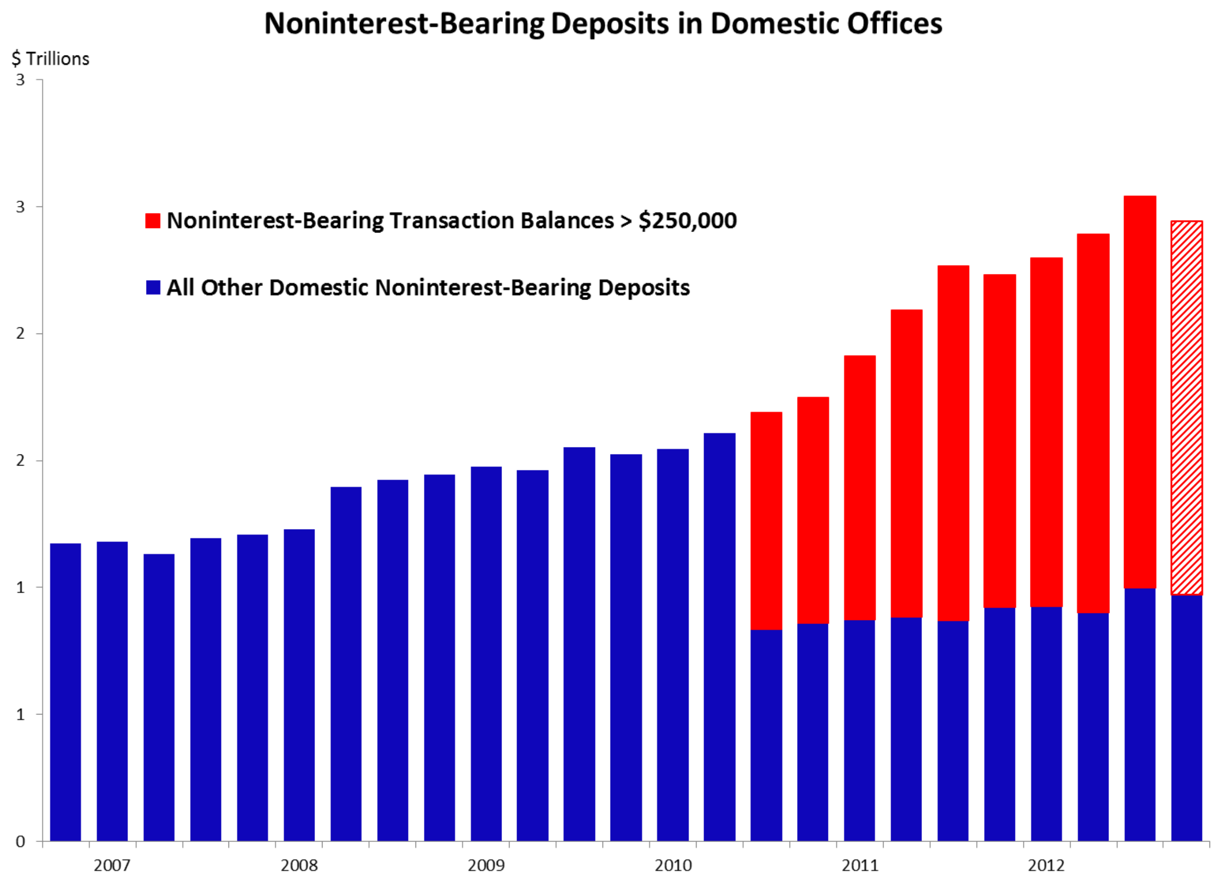
Quarterly Changes in the Number of Troubled Institutions, 2007 - 2013



We continue to see fewer "problem" banks and bank failures. The number of banks on the "Problem List" declined to 612 in the first quarter from 651 at year-end 2012. This is the eighth straight quarterly decline. And the number of banks on the list is now 276 below the peak of 888 in the first quarter of 2011.

Only four insured institutions failed in the first quarter, the lowest since the second quarter of 2008. So far this year, 13 banks have failed, compared to 24 banks over the same period last year.

Chart 10



The temporary unlimited deposit insurance coverage provided to noninterest-bearing transaction deposits as part of the Dodd-Frank Act ended last year. During the previous two years, account balances above the basic 250,000 dollar FDIC coverage level experienced considerable growth, as illustrated by the red bars in this chart.

The impact of the expiration of the additional deposit insurance coverage on deposit levels in the first quarter was limited. The amount of noninterest-bearing transaction deposits above the 250,000 dollar level declined by about 70 billion dollars, or less than 5 percent.

The Deposit Insurance Fund balance rose to 35.7 billion dollars as of March 31, up from 33.0 billion dollars at the end of last year. Assessment income was primarily responsible for the growth in the DIF balance.

Estimated insured deposits declined by 18.7 percent to 6.0 trillion dollars in the first quarter, primarily because of the expiration of the noninterest-bearing transaction account coverage. However, deposits covered by the 250,000 dollar limit rose by 2.6 percent in the first quarter.

The reserve ratio—the DIF balance as a percentage of estimated insured deposits—rose to 0.59 percent at March 31 from a revised 0.44 percent at year-end 2012. Expiration of the temporary insurance accounted for almost 12 of the 15 basis point increase in the reserve ratio. The DIF must achieve a minimum reserve ratio of 1.35 percent by 2020.

In summary, asset quality continues to improve, more institutions are profitable, and the number of failures and problem institutions continues to decline. However, industry revenue remains flat, primarily due to lower net interest margins and slow growth in loan portfolios. This environment of tighter margins and slow loan growth creates an incentive for institutions to reach for yield, which is a matter of ongoing supervisory attention. Nonetheless, these results show overall that the process of recovery continues for the banking industry.

Thank you.

Last Updated 6/3/2013