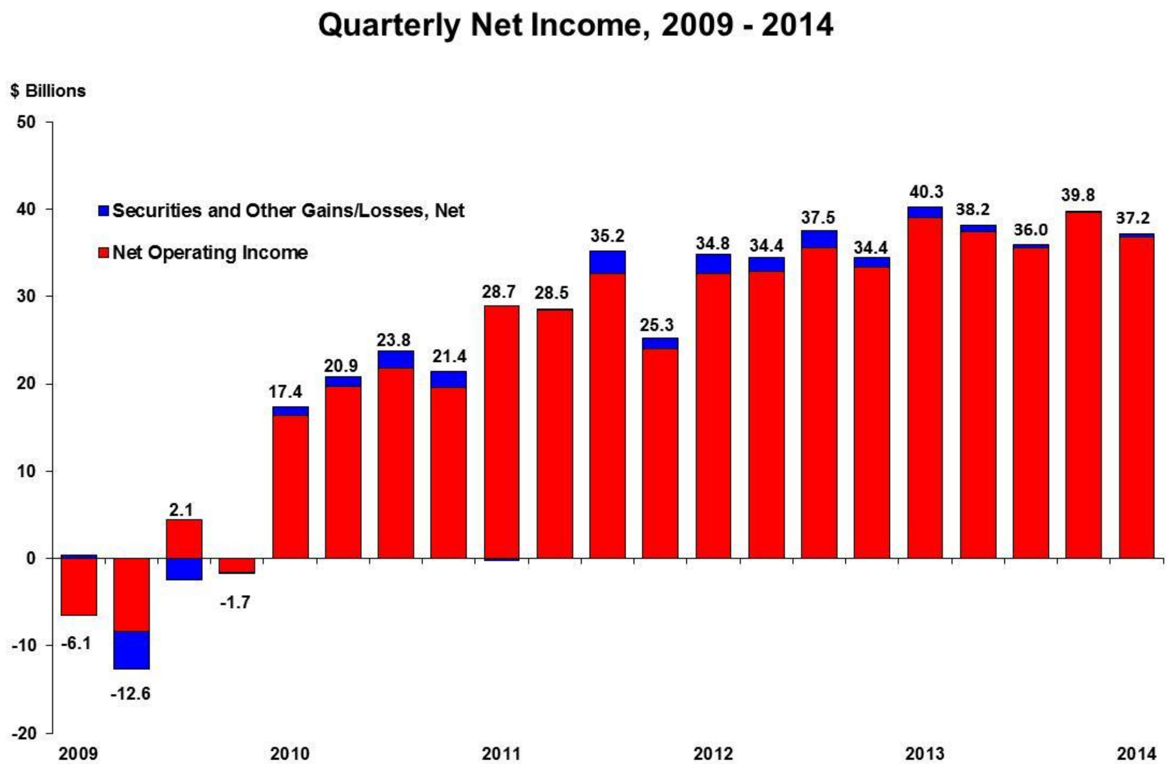
Opening Statement by FDIC Chairman Martin J. Gruenberg on the First Quarter 2014 Quarterly Banking Profile

May 28, 2014

Good morning, and welcome to our release of first quarter 2014 results for FDIC-insured institutions.

Before presenting results for the industry, I would like to note that this quarter we are expanding our reporting in the FDIC *Quarterly Banking Profile* to include a new section on the performance of community banks. In December 2012, the FDIC released the *Community Banking Study* which examined institutions that provide traditional, relationship-based banking services in their communities. Based on criteria we developed for identifying community banks, they currently represent 93 percent of all FDIC-insured institutions and 14 percent of industry assets. By publishing a quarterly report of community bank performance, it is our goal to provide a deeper understanding of this important part of the banking industry.

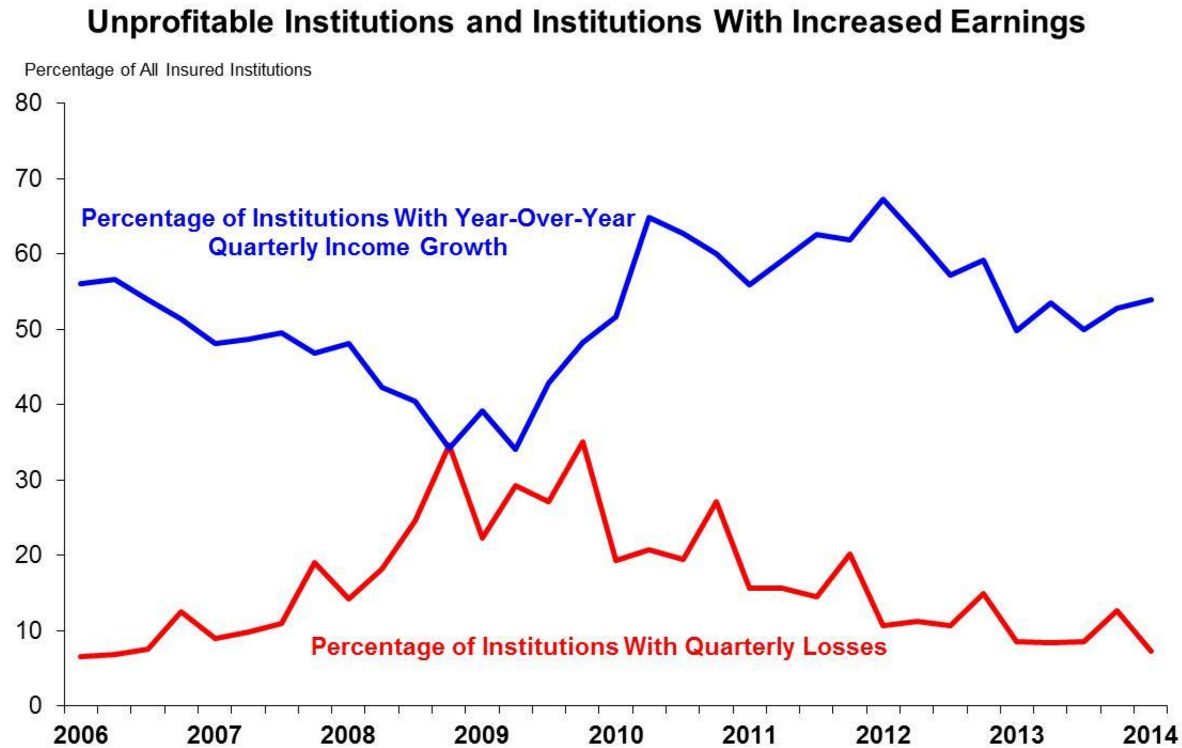
Chart 1:



Turning to first quarter results, the industry reported net income of 37.2 billion dollars. This was 3.1 billion dollars less than the industry earned a year ago. The decline was due primarily to lower noninterest income from reduced mortgage-related activity, much of which can be traced to last year's rise in longer-term interest rates, and from lower trading income. Additionally, noninterest income was higher one year ago due to a one-time gain at one institution.

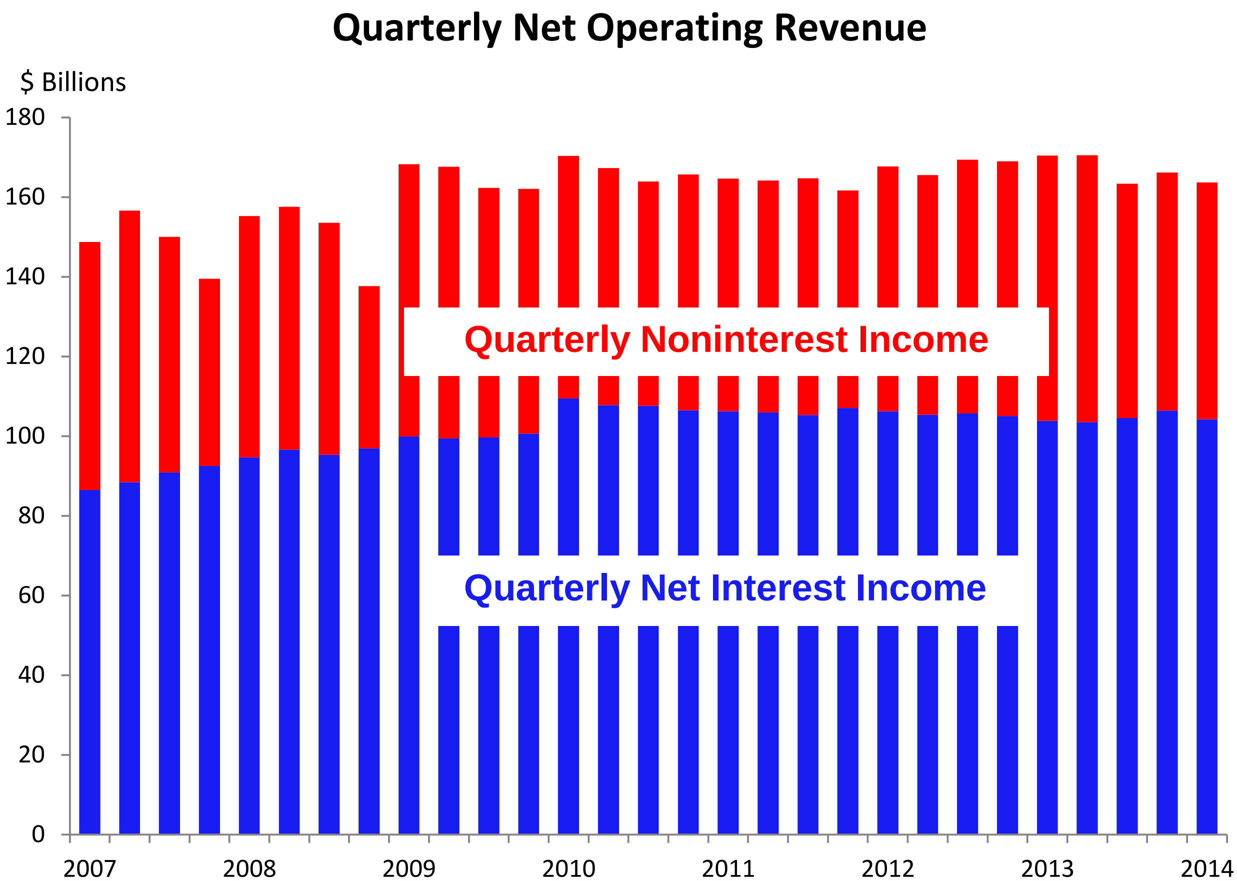
Community banks as a group earned 4.4 billion dollars in the first quarter. Although this was 1 ½ percent less than they earned a year ago, the decline in net income at community banks was significantly smaller than the industry's decline of nearly 8 percent.

Chart 2:



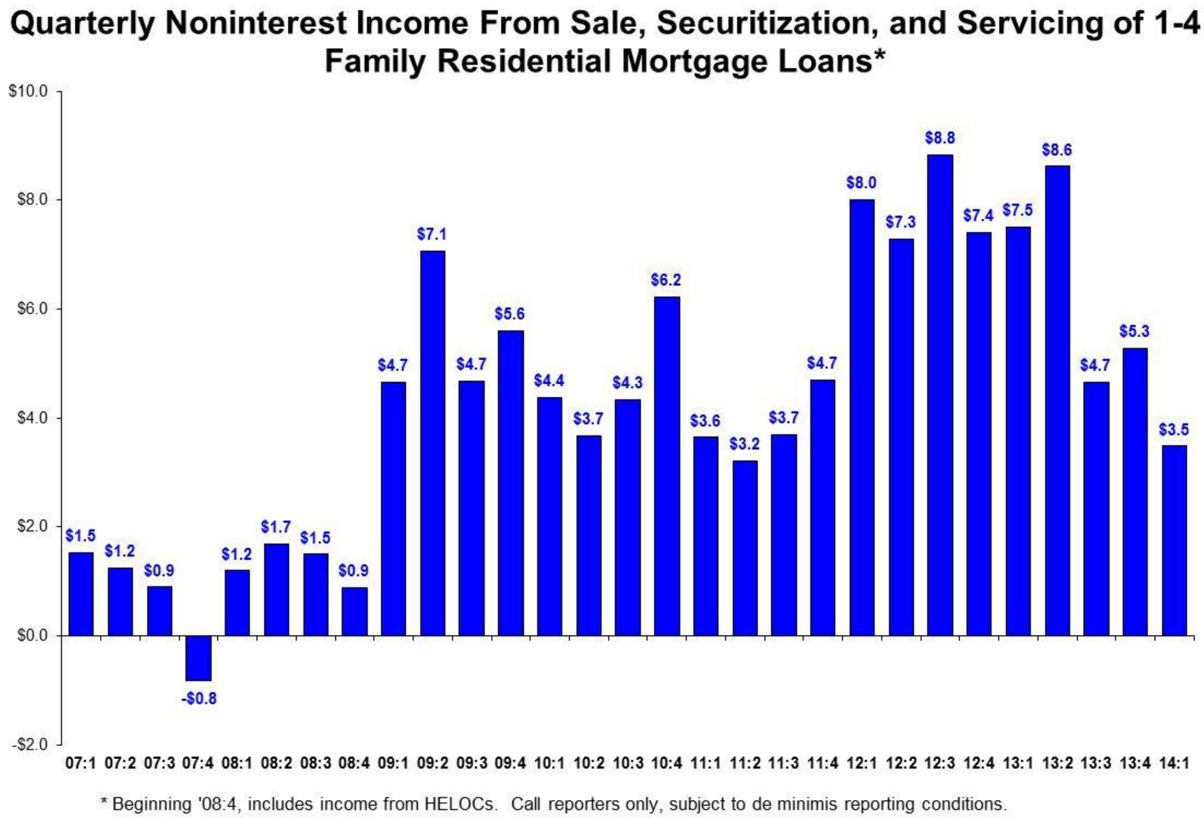
While overall industry earnings declined, a majority of banks reported an increase in quarterly net income from a year ago. The number of unprofitable institutions also declined. During the quarter, the percentage of banks that reported a net loss was the lowest since the second quarter of 2006.

Chart 3:



This next chart shows that net operating revenue—which is the sum of net interest income in blue and noninterest income in red—has been flat since the financial crisis.

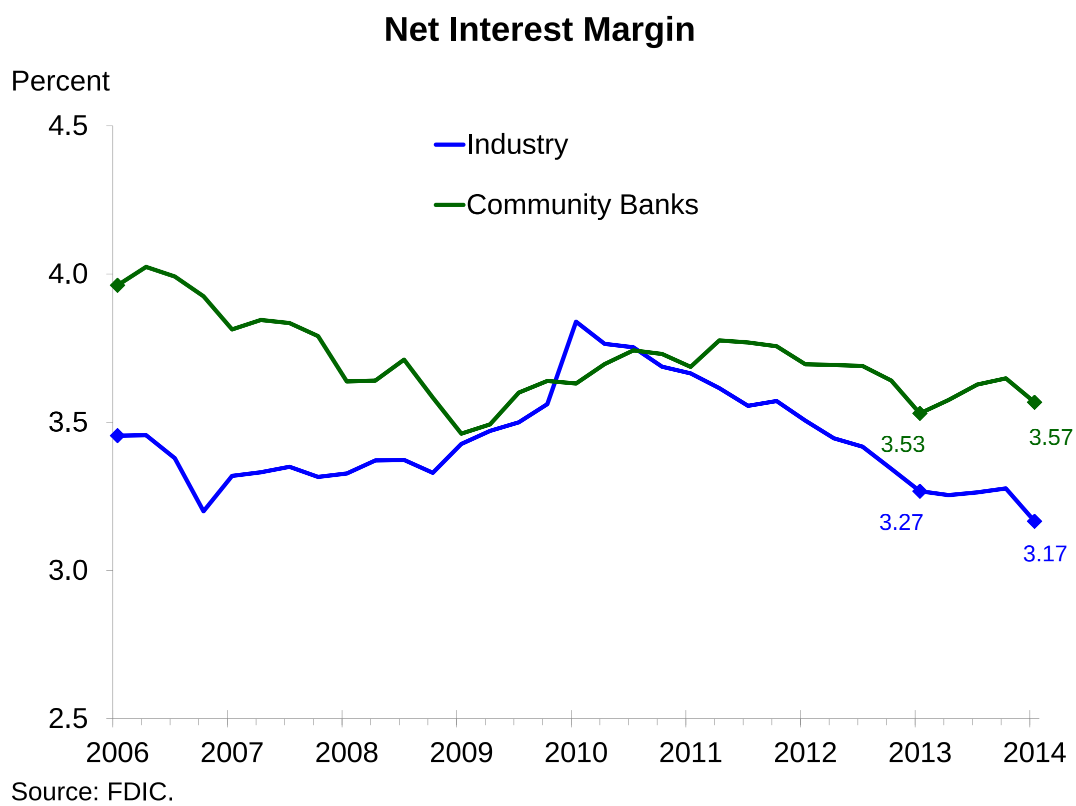
Chart 4:



A large share of the recent year-over-year decline in noninterest income was from reduced mortgage-related activities, including the origination, sale, and servicing of mortgage loans. Since the increase in longer-term interest rates in the second quarter of 2013, mortgage income over the past three quarters has been about half of what it was over the previous six quarters.

The 4 billion dollar decline in mortgage-related income from a year ago was over half the 7.1 billion dollar decline in total noninterest income. The remainder came primarily from lower trading revenue and a one-time gain in noninterest income a year ago at one institution.

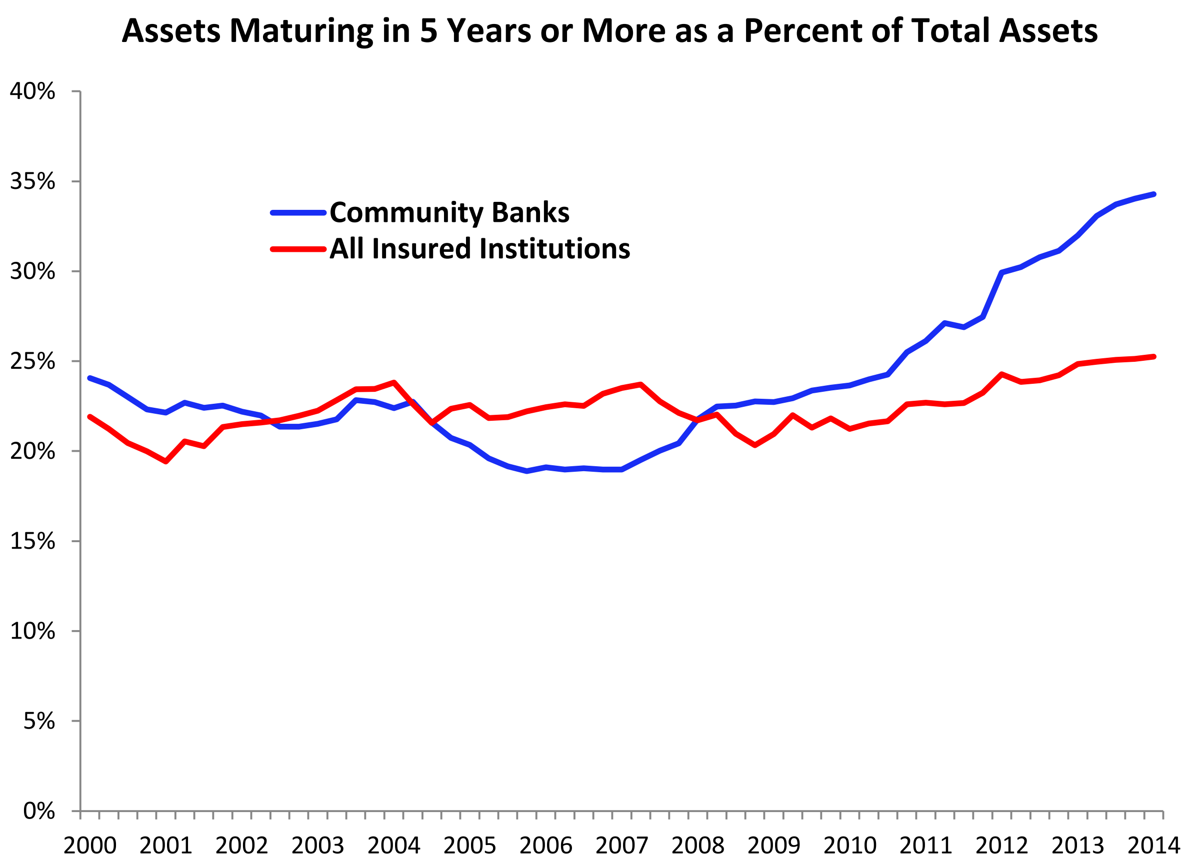
Chart 5:



Net interest income increased slightly from a year ago and more than two-thirds of all banks reported higher net interest income from a year ago. This is a positive effect of the rise in longer-term rates we saw in mid-2013. The steeper yield curve has been favorable for margins at institutions that fund at the short-end of the yield curve and invest over the medium- to long-term.

Community banks have benefited most over the past year from the steeper yield curve, as their average net interest margin was up 4 basis points from a year ago. In contrast, larger banks have increased their portfolio of lower-yielding, short-term assets and they saw their margins decline. Overall, the average net interest margin for the industry declined by 10 basis points.

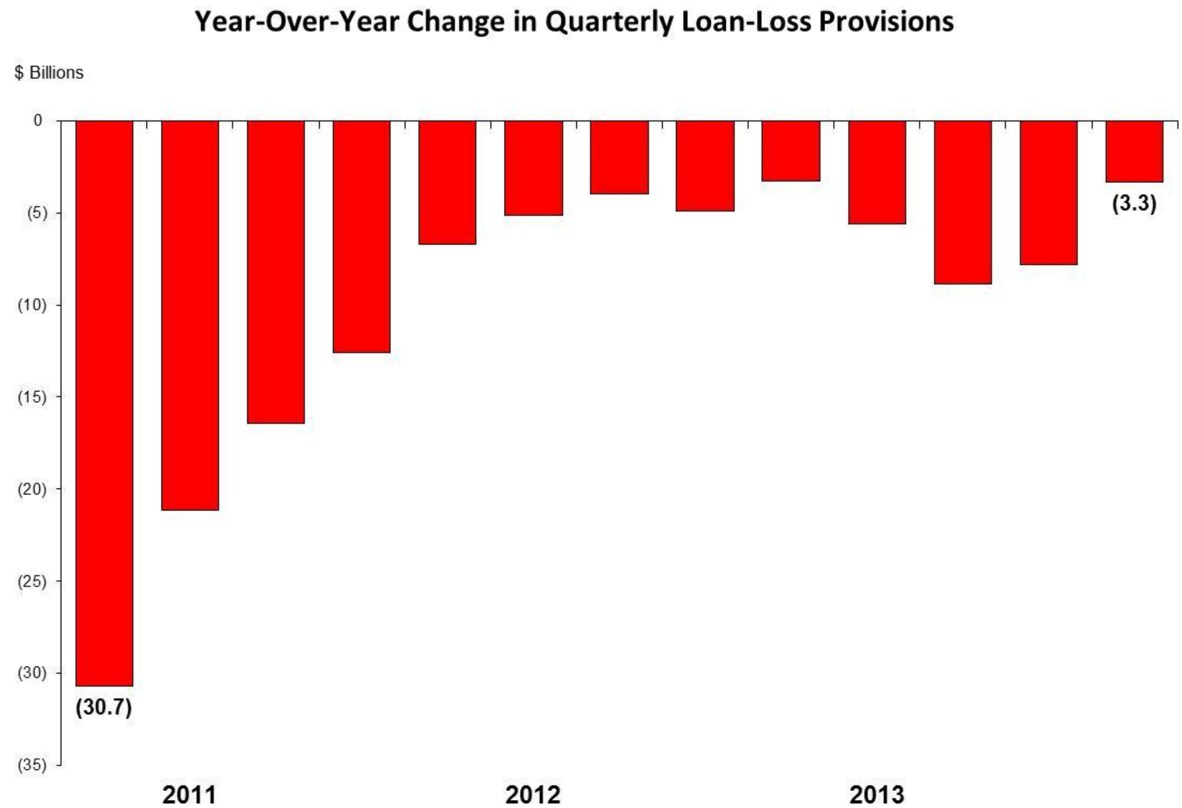
Chart 6:



The next chart shows that banks have been going out further on the yield curve. The proportion of industry assets that mature in 5 years or more has been trending up since 2009. Among community banks, the upward trend is more pronounced, having risen 15 percentage points since 2007. The difference between community banks and the overall industry is due to the largest banks, which have increased their short-term investments including reserves held at the Fed.

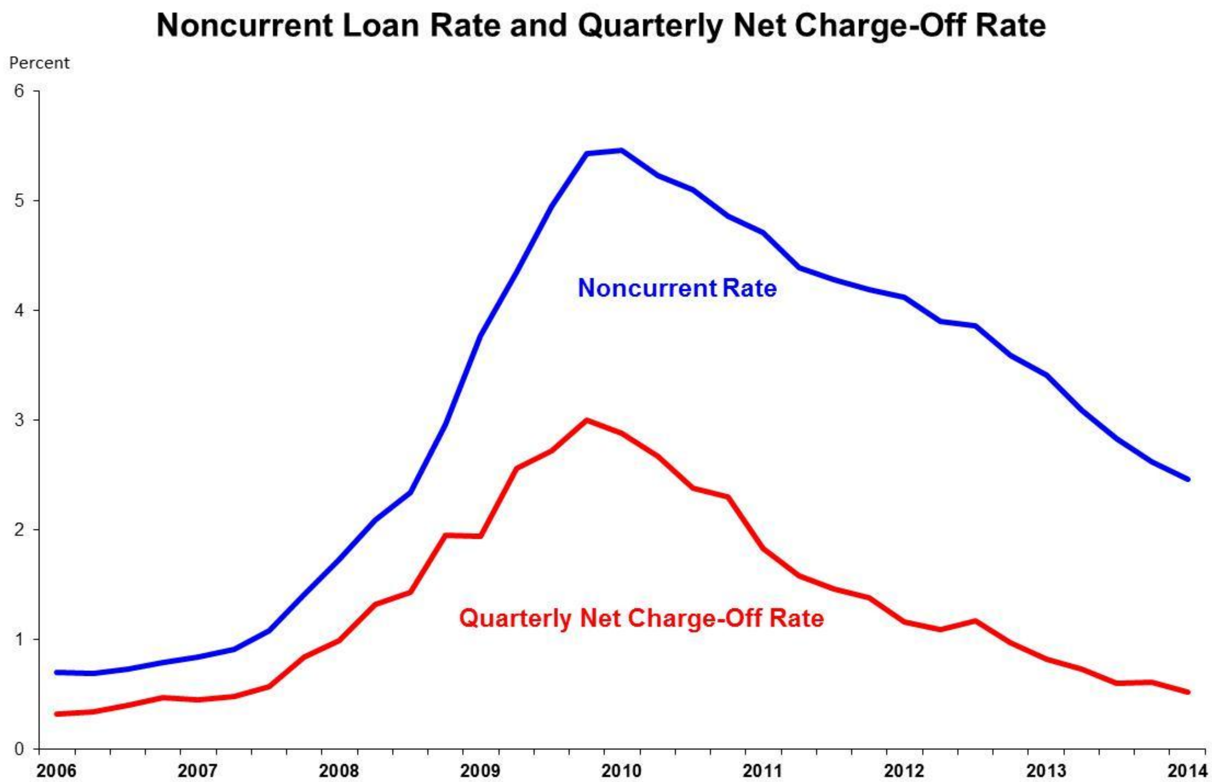
This “reach for yield” has benefited interest income at many institutions—and community banks in particular—but it has left banks more vulnerable to interest rate risk as rates rise.

Chart 7:



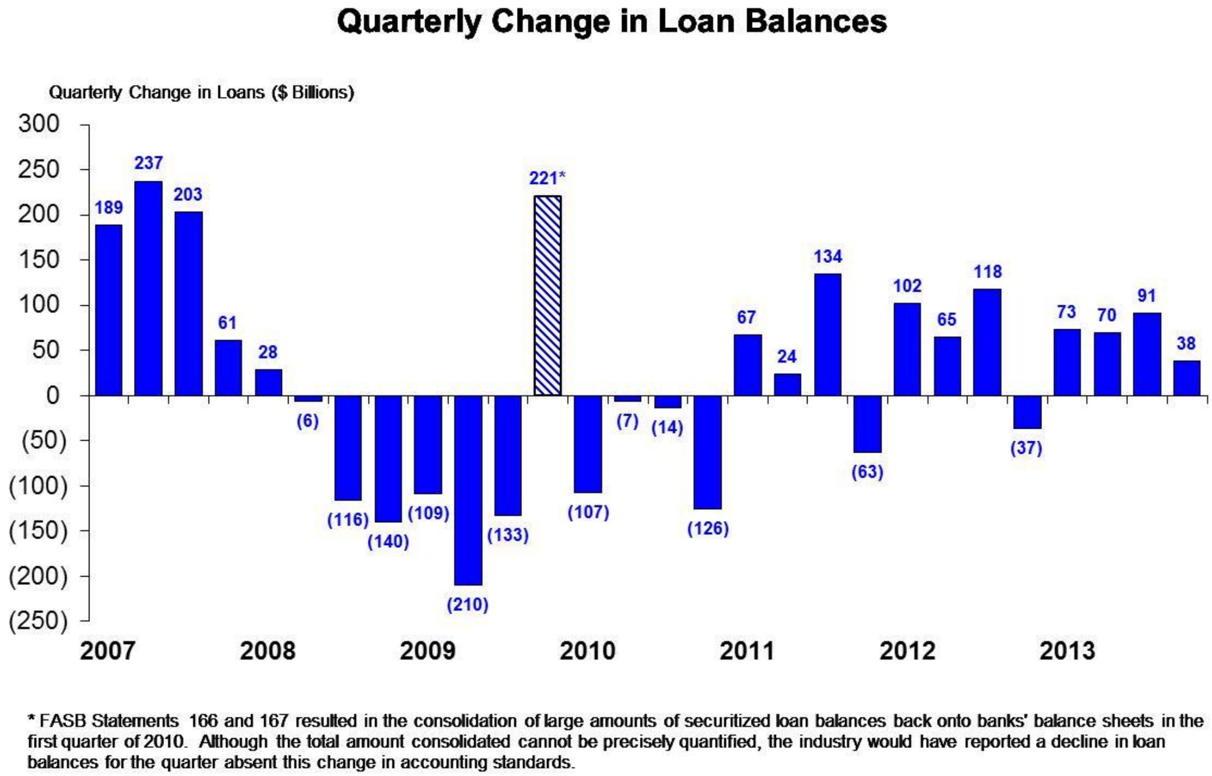
The most consistent and significant contributor to earnings continues to be lower provisions for loan losses. However, as this chart shows, the benefits to earnings from lower provisions are diminishing. Throughout much of the post-crisis recovery period, the reduction in loan-loss provisions has tracked the improvement in credit quality.

Chart 8:



As you can see in this chart, loan losses have declined as credit quality has improved. While the net charge-off rate is approaching its pre-crisis level, the rate of improvement has slowed. Going forward, earnings will be increasingly dependent on sources other than a decline in loss provisions.

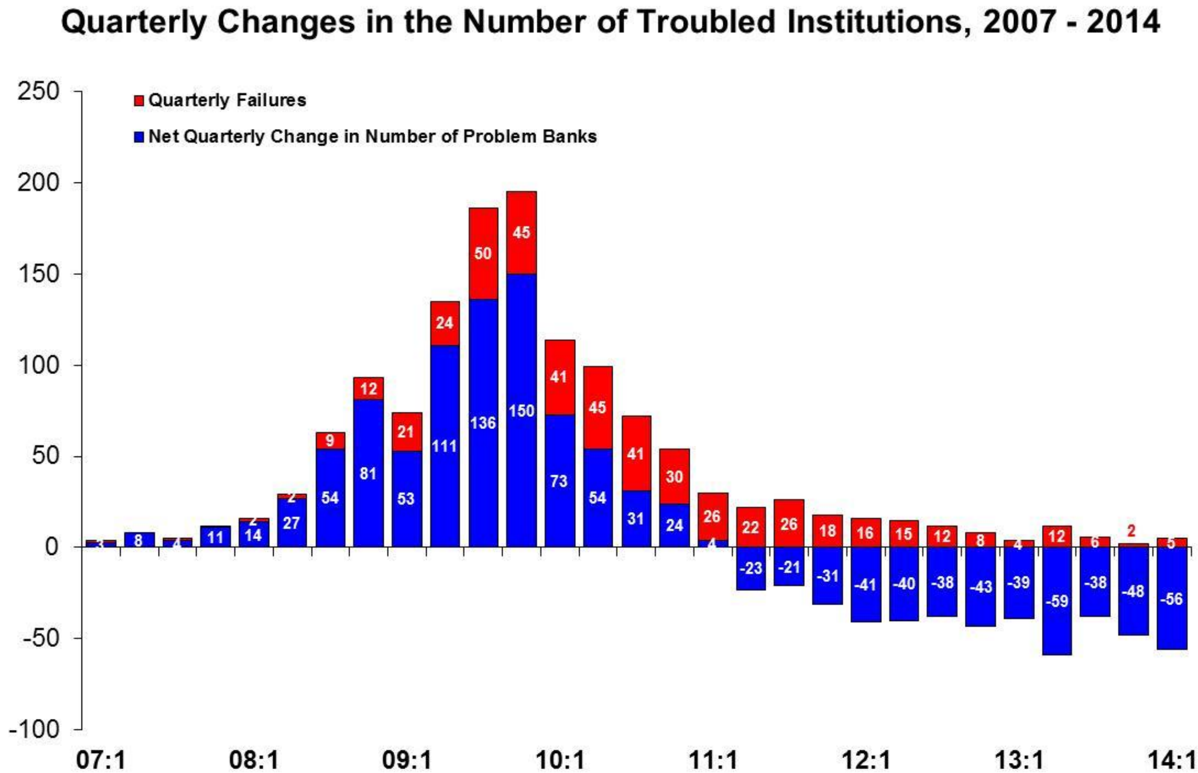
Chart 9:



Loan portfolios registered modest growth in the first quarter, unlike the past three years where we saw a decline in loan balances during the first quarter. The seasonal decline in credit card balances along with fewer mortgages held for sale were more than offset by growth in almost all other major loan categories. The 12-month growth rate this quarter in industry loan balances reached a post-crisis high of 3.6 percent.

Loan growth was stronger at community banks, where loan balances increased by 6.7 percent over the past 12 months and all major loan categories saw an improvement. Community banks also increased their small loans to businesses from a year ago, and they hold 45 percent of small business loans.

Chart 10:



We continue to see an improvement in the number of "problem" banks. The number of banks on the "Problem List" declined from 467 to 411 during the quarter. It is now less than half of the peak of 888 we saw three years ago. Five insured institutions failed in the first quarter.

The Deposit Insurance Fund balance rose to 48.9 billion dollars as of March 31, up from 47.2 billion dollars at year-end 2013. Assessment income drove the first quarter increase in the Fund balance.

Estimated insured deposits were 6.1 trillion dollars, up 1.9 percent. The reserve ratio—which is the Fund balance as a percentage of estimated insured deposits—increased to 0.80 percent at March 31 from 0.79 percent at the end of 2013. A year ago, the reserve ratio was 0.60 percent. As required by law, the Deposit Insurance Fund must achieve a minimum reserve ratio of 1.35 percent by 2020.

In summary, we saw further improvement in the condition of the banking industry in the first quarter. Asset quality continues to improve, loan balances are trending up, fewer institutions are unprofitable, and the number of problem banks continues to decline. However, industry revenue has been affected by narrow margins, modest loan growth, and a decline in noninterest income as higher interest rates have reduced mortgage-related activity and trading income fell. The current interest rate environment has created an incentive for institutions to reach for yield, and this is a matter of ongoing supervisory attention. Nonetheless, the first quarter results show a continuation of the recovery in the banking industry.

Thank you.

I am happy to take a few questions.