

An Update on Emerging Issues in Banking

New Reporting Offers Insight Into Bank Activities

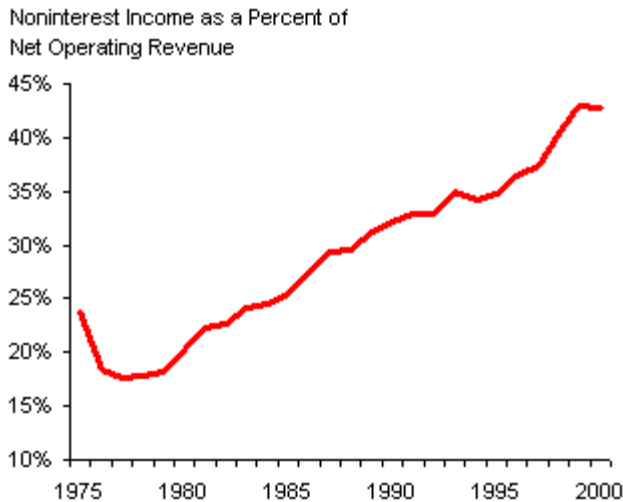
April 18, 2002

Noninterest income has grown in importance at commercial banks for almost 25 years. Until last year, however, the quarterly Reports of Income that banks filed with federal regulators provided only limited detail on noninterest revenues. Last year, these reports began to include more detail on the relative importance of different activities and products to bank earnings. The new data show that some significant revenue sources are overwhelmingly concentrated in a few institutions, while other activities—notably insurance—are conducted by thousands of small banks across the U.S.

Noninterest income has become more important for banks (Chart 1) as nonbank competition for loan customers, especially in sectors such as home mortgage lending and lending to large commercial borrowers, has limited growth in net interest income. At the same time, banks' enhanced ability to market and deliver fee-earning transactional services, made possible by advances in telecommunications and data processing, and the development of new financial products, aided by deregulation and innovation, have produced a growing number of sources of noninterest income. This trend has been evident at both large and small banks, although larger banks have consistently obtained a significantly greater share of their revenues from noninterest sources. Greater diversification in revenues should promote greater stability and consistency in bank earnings. While some noninterest revenue sources are sensitive to conditions in financial markets, and may be more volatile over time than net interest income, other noninterest revenues, notably those obtained from transaction-based services, should be less susceptible to cyclical influences.

Chart 1

Noninterest Income Provides a Growing Share of Bank Revenues



Net Operating Revenue is the sum of Net Interest Income and Noninterest Income.
Source: FDIC *Historical Statistics on Banking*

Before 2001, banks reported the amounts of their noninterest income that consisted of service charges on deposit accounts, fiduciary (trust) income, and revenues from trading operations. Any other sources of noninterest income were reported in the residual categories of "Other Fee Income" and "All Other Noninterest Income." The new report format introduced in the first quarter of 2001 still includes fiduciary income, deposit service charges, and trading revenues, but it now also breaks out income from investment banking services, revenues from venture capital investments, servicing fees, income from asset securitization activities, insurance commissions and fees, and proceeds from sales of loans, other real estate, and other assets. With this information, it is possible to examine the relative importance of each of these income sources to bank revenues, and see how widespread these business lines are among insured commercial banks.

During 2000, the residual categories of "other fee income" and "all other noninterest income" together comprised almost two-thirds (62.5 percent) of all noninterest income reported by insured commercial banks. The new categories reported in 2001 provide a more detailed look at roughly half of these "other" revenues. The data show that securitization income (net gains on sales of securitized assets plus non-servicing fees), at \$16.4 billion for the year, represented the largest amount of any of the new categories. The next-highest category was servicing fees, at \$11.6 billion. Fees and commissions from investment banking, advisory, brokerage, and underwriting services totaled \$9.1 billion in 2001. Sales of loans, other real estate, and other assets yielded net gains of \$7.0 billion. Insurance commissions and fees totaled \$2.9 billion, while venture capital activities produced a net loss of \$740 million for the year. The remaining category of "all other" noninterest income, which includes income from unconsolidated subsidiaries, data processing services, ATM usage fees charged to depositors from other institutions, as well as service charges and fees for a

variety of other services, was still the largest component of total noninterest income. At \$51.3 billion, it represented 32.7 percent of commercial banks' noninterest income in 2001.

Table 1

Noninterest Income Of Insured Commercial Banks, 2001 (Amounts in \$ Thousands)				
Noninterest Income Category	Full Year Amount	% of Total	# of Banks Reporting	Combined Share of 5 Largest Reported Amounts
Income from fiduciary activities	20,751,226	13.2%	1,668	39.4%
Service charges on deposit accounts	26,472,609	16.8%	7,909	33.9%
Trading revenues	12,524,834	8.0%	175	82.6%
On interest-rate contracts	6,075,878	3.9%	106	85.1%
On foreign exchange contracts	4,338,966	2.8%	47	82.5%
On equity contracts	1,878,327	1.2%	20	95.4%
On commodity & other contracts	231,663	0.1%	10	N/M
Investment banking & other fees	9,096,981	5.8%	2,178	55.8%
Venture capital revenue	-740,222	-0.5%	61	N/M
Servicing fees	11,568,730	7.4%	1,626	41.5%
Securitization income	16,349,975	10.4%	100	64.0%
Insurance commissions & fees	2,874,938	1.8%	4,063	38.4%
Net gains/losses on loan sales	4,642,565	3.0%	1,739	47.5%
Net gains/losses on sales of OREO	65,348	0.0%	2,129	N/M
Net gains/losses on sales of other assets	2,249,208	1.4%	2,321	84.6%
Other noninterest income	51,335,770	32.7%	7,983	21.2%
Total noninterest income	157,171,912		8,050	

Source: Bank Call Reports (Research Information System)

Table 1 shows the amounts of noninterest income in its component categories, as well as the number of banks reporting non-zero amounts in each category. It also shows the share of income in each category represented by the combined totals of the five largest amounts reported, to provide an indication of how highly concentrated each underlying activity was within the banking industry during 2001. Based on the frequency of nonzero amounts reported, service charges on deposit accounts were the most widespread and were the largest identifiable dollar category. Although far less important in terms of dollars, insurance-related activities were the next most widespread; more than half of the 8,080 commercial banks at year-end reported some income from these activities. At the other end of the scale, only 61 banks reported any results from venture capital investments,

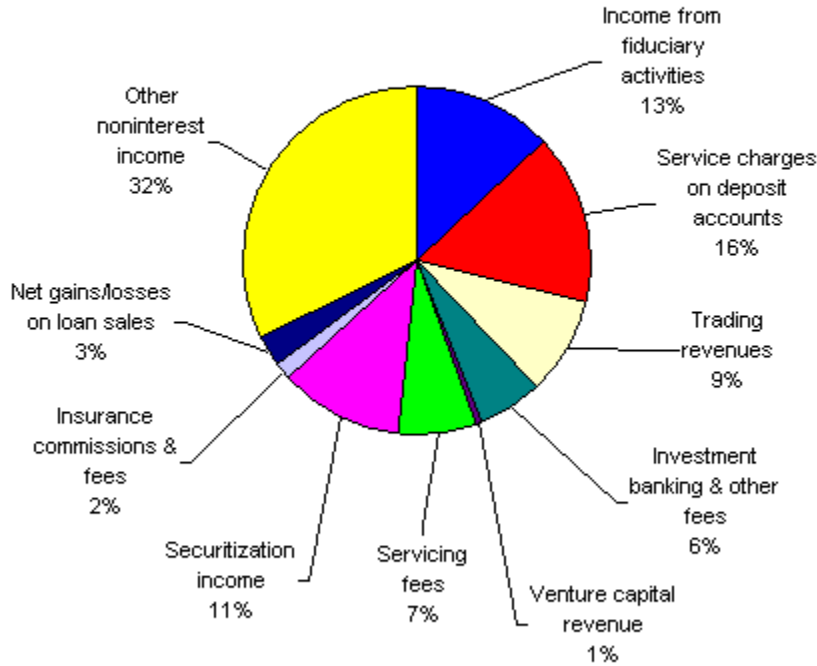
and only 100 banks reported any income from securitization activities.

As an indicator of concentration within different activities, the combined shares of the five largest reporters in each category varied widely. The five largest reporters accounted for 84.6 percent of the \$2.2 billion in gains from sales of other assets, and almost two-thirds of the \$16.4 billion in securitization income reported by commercial banks in 2001, while the five largest amounts reported for insurance commissions and fees represented only 38.4 percent of the industry's total income in this category. Most of the industry's income from securitization activities was earned by 24 specialized credit-card banks; they accounted for 86.4 percent of all securitization income reported in 2001.

Just as large and small banks show different relative levels of noninterest income, they also show significant differences in the composition of their noninterest revenues. Larger banks as a group exhibit greater diversification in their noninterest revenues. For commercial banks with assets greater than \$1 billion, three of the new categories—securitization income (11 percent), servicing fees (7 percent), and investment banking income (6 percent)—provide more than 5 percent of the group's aggregate noninterest income. The largest identifiable category for large banks, service charges, comprised only 16 percent of their noninterest income (Chart 2). Banks with less than \$1 billion in assets, in contrast, have more of their noninterest revenues (29%) concentrated in service charges. Of the newly reported activities, only servicing fees (7 percent) provided more than 5 percent of aggregate noninterest income for small banks in 2001 (Chart 3).

Large Bank Revenues Indicate a Variety of Products and Services

Composition of Noninterest Income, Commercial Banks with Assets Greater Than \$1 Billion, Full Year 2001.

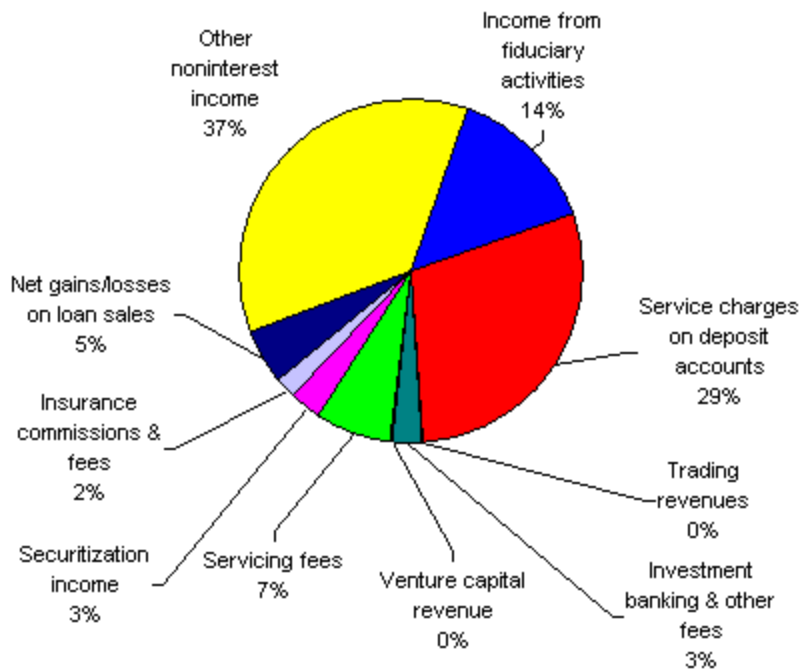


Source: Bank Call Reports (Research Information System)

Chart 3

Smaller Banks' Revenues Show Less Diversity Than Large Banks'

Composition of Noninterest Income, Commercial Banks with Assets Less Than \$1 Billion, Full Year 2001.



Source: Bank Call Reports (Research Information System)

Chart 1

Noninterest Income Provides a Growing Share of Bank Revenues

Year	No. of Inst.	Total Interest Income	Total Interest Expense	Net Interest Income	Total Non-Interest Income	Total Non-Interest Expense	Provision for Loan and Lease Losses	Pre-tax Net Operating Income	Securities Gains/Losses (-)	Applicable Income Taxes	Net Extra-ordinary Items	Net Income		
2000	8,315	427,985,443	224,195,004	203,790,442	152,750,779	215,752,512	29,254,257	111,534,449	-2,285,246	38,043,448	-30,226	71,175,520	1975	24%
1999	8,580	367,321,536	175,128,619	192,192,909	144,399,890	204,195,999	21,813,747	110,583,061	181,015	39,377,440	168,882	71,555,517		18%
1998	8,774	362,019,427	179,266,364	182,753,063	123,698,673	194,142,572	22,215,610	90,093,554	3,130,738	31,946,386	506,756	61,784,652		18%
1997	9,142	339,540,553	165,038,458	174,502,093	104,498,556	169,982,976	19,851,445	89,166,230	1,841,825	31,871,301	19,084	59,155,806		18%
1996	9,527	312,742,340	149,988,642	162,753,698	93,568,711	160,698,237	16,285,397	79,338,775	1,113,584	28,190,602	88,396	52,350,138		18%
1995	9,940	302,382,735	148,172,638	154,210,062	82,425,540	149,728,728	12,602,826	74,304,083	540,982	26,125,448	25,671	48,745,268	1980	20%
1994	10,451	257,828,305	111,277,545	146,550,766	76,276,366	144,234,492	10,965,161	67,627,473	-570,667	22,419,323	-15,227	44,622,203		22%
1993	10,958	245,055,191	105,742,497	139,312,686	74,954,193	139,695,401	16,813,860	57,757,626	3,059,652	19,852,095	2,069,971	43,035,111		23%
1992	11,462	255,223,143	121,804,746	133,418,416	65,648,171	130,965,454	26,048,204	42,052,910	4,005,452	14,480,572	408,755	31,986,575		24%
1991	11,921	289,214,022	167,302,352	121,911,675	59,739,039	124,794,714	34,314,237	22,541,758	2,971,851	8,264,847	686,675	17,935,435		25%
1990	12,343	320,475,804	204,952,380	115,523,415	54,899,362	115,768,467	32,087,055	22,567,264	481,249	7,704,184	646,766	15,991,078	1985	25%
1989	12,709	317,371,442	205,141,604	112,229,834	50,915,568	108,121,205	31,020,096	24,004,105	801,197	9,540,222	309,802	15,574,853		27%
1988	13,123	272,276,911	165,027,852	107,249,055	44,953,378	101,329,856	17,164,470	33,708,111	279,458	9,987,808	812,450	24,812,194		29%
1987	13,703	244,839,538	144,952,607	99,886,934	41,481,014	97,244,511	37,543,826	6,579,608	1,427,364	5,404,283	200,526	2,803,219		30%
1986	14,199	237,765,872	142,829,241	94,935,622	35,876,520	90,249,964	22,105,877	18,457,310	3,950,856	5,265,640	276,192	17,417,674		31%
1985	14,407	248,220,304	157,322,506	90,897,788	31,054,038	82,364,741	17,774,041	21,813,054	1,565,198	5,628,710	227,500	17,977,015	1990	32%
1984	14,482	250,339,385	169,078,046	81,261,268	26,510,416	73,811,526	13,816,166	20,144,063	-140,398	4,721,246	218,111	15,499,844		33%
1983	14,469	217,226,000	143,887,000	73,339,000	23,269,000	66,909,000	10,802,000	18,896,000	-21,000	4,017,000	73,000	14,931,000		33%
1982	14,451	238,316,000	169,343,000	68,972,000	20,176,000	61,561,000	8,342,000	19,245,000	-1,280,000	3,037,000	68,000	14,996,000		35%
1981	14,414	231,274,000	169,840,000	61,431,000	17,527,000	53,658,000	5,066,000	20,234,000	-1,583,000	3,904,000	56,000	14,803,000		34%
1980	14,434	176,419,000	120,122,000	56,297,000	14,348,000	46,662,000	4,478,000	19,505,000	-854,000	4,658,000	17,000	14,010,000	1995	35%
1979	14,364	138,900,000	87,912,000	50,988,000	11,381,000	40,692,000	3,785,000	17,891,000	-650,000	4,442,000	39,000	12,838,000		37%
1977	14,3	103,957	59,383,	44,574,	9,625,0	35,573,	3,526,00	15,101,0	-447,000	3,940,000	45,000	10,759,		37%

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1977	14,411	82,252,000	44,565,000	37,687,000	8,106,000	30,925,000	3,303,000	11,565,000	142,000	2,875,000	47,000	8,879,000		40%
1976	14,410	73,033,000	39,328,000	33,705,000	7,630,000	27,731,000	3,691,000	9,914,000	312,000	2,409,000	26,000	7,843,000		43%
1975	14,384	57,917,000	30,240,000	27,675,000	8,643,000	23,729,000	3,612,000	8,977,000	37,000	1,793,000	34,000	7,255,000	2000	43%
1974	14,230	61,218,304	35,070,707	26,148,000	6,925,858	21,545,066	2,290,000	9,238,000	-87,000	2,084,000	11,920	7,078,920		20.9%
1973	13,976	47,034,126	24,489,474	22,545,000	5,999,992	18,571,197	1,263,695	8,709,305	-27,000	2,122,000	21,561	6,581,866		21.0%
1972	13,733	35,029,550	15,602,943	19,427,000	5,220,22	16,423,000	972,238	7,251,762	92,000	1,708,000	20,000	5,655,762		21.2%
1971	13,612	31,628,167	13,603,029	18,025,000	4,747,470	15,191,318	868,000	6,713,000	213,000	1,689,000	-639	5,236,361		20.8%
1970	13,511	30,513,367	12,455,568	18,057,000	4,202,192	14,428,000	703,150	7,126,850	-104,000	2,173,000	-12,810	4,837,040		18.9%
1969	13,473	27,284,580	11,532,649	15,753,000	3,521,000	12,024,000	521,064	6,727,936	-237,000	2,164,000	6,914	4,333,850		18.3%
1968	13,487	22,501,000	9,314,986	13,186,000	2,974,000	10,140,000	512,000	5,509,000	-457,000	1,266,000	N/A	3,786,000		18.4%
1967	13,514	19,152,000	7,733,664	11,418,000	2,626,000	8,903,000	434,000	4,707,000	-21,000	1,177,154	N/A	3,508,846		18.7%
1966	13,538	17,135,311	6,627,811	10,508,000	2,373,049	8,001,000	417,000	4,462,000	-392,447	1,029,906	N/A	3,039,647		18.4%
1965	13,544	14,714,998	5,316,463	9,399,000	2,113,598	7,298,404	324,000	3,891,000	-426	1,029,162	N/A	2,861,412		18.4%
1964	13,493	13,110,723	4,241,087	8,870,000	1,924,674	6,780,301	251,000	3,764,000	-14,000	1,148,000	N/A	2,602,000		17.8%
1963	13,291	11,769,514	3,574,160	8,196,000	1,750,146	6,205,747	238,000	3,502,000	118,000	1,227,000	N/A	2,393,000		17.6%
1962	13,124	10,570,237	2,911,371	7,659,000	1,659,832	5,746,184	167,000	3,406,000	198,000	1,256,000	N/A	2,348,000		17.8%
1961	13,115	9,539,866	2,146,465	7,394,000	1,549,882	5,383,121	190,000	3,371,000	409,000	1,406,000	N/A	2,374,000		17.3%
1960	13,126	9,176,124	1,874,495	7,302,000	1,578,332	5,141,947	206,000	3,532,000	110,000	1,384,000	N/A	2,257,000		17.8%
1959	13,114	8,247,427	1,661,819	6,585,000	1,456,000	4,853,000	53,000	3,135,000	-698,000	884,000	N/A	1,553,000		18.1%
1958	13,124	7,187,001	1,407,102	5,780,000	1,333,549	4,286,200	61,000	2,766,000	588,000	1,271,000	N/A	2,082,000		18.7%
1957	13,165	6,817,876	1,193,487	5,625,000	1,243,996	4,046,849	72,000	2,750,000	-173,000	998,000	N/A	1,578,000		18.1%
1956	13,218	6,125,887	853,638	5,272,000	1,122,401	3,725,264	92,000	2,577,000	-286,000	815,000	N/A	1,476,000		17.6%
1955	13,237	5,381,731	703,911	4,677,000	1,020,131	3,370,149	49,000	2,278,000	-164,000	794,000	N/A	1,320,000		17.9%
1954	13,323	4,860,554	629,809	4,231,000	930,856	3,086,997	44,000	2,031,000	350,000	908,000	N/A	1,473,000		18.0%
1953	13,432	4,660,704	561,643	4,098,000	837,205	2,901,868	59,000	1,974,000	-117,000	786,000	N/A	1,070,000		17.0%
1952	13,439	4,160,052	482,655	3,677,000	786,790	2,603,125	35,000	1,826,000	-64,000	695,000	N/A	1,067,000		17.6%
1951	13,455	3,658,157	398,887	3,259,000	755,208	2,344,819	35,000	1,634,000	-27,000	559,000	N/A	1,047,000		18.8%
1950	13,446	3,248,881	351,669	2,897,000	700,276	2,119,959	29,000	1,448,000	52,000	428,000	N/A	1,072,000		19.5%

1949	13,436	2,975,206	336,685	2,638,000	650,905	1,970,570	59,000	1,259,000	35,000	325,000	N/A	968,000	19.8%
1948	13,419	2,797,697	325,232	2,473,000	642,386	1,852,356	28,000	1,235,000	-19,000	275,000	N/A	941,000	20.6%
1947	13,403	2,540,943	306,911	2,234,000	601,913	1,687,469	53,000	1,096,000	-18,000	302,000	N/A	775,000	21.2%
1946	13,359	2,346,137	279,333	2,067,000	576,135	1,505,420	-3,000	1,141,000	76,000	323,000	N/A	894,000	21.8%
1945	13,302	2,027,175	247,538	1,779,000	577,859	1,309,173	-11,000	1,059,000	134,000	299,000	N/A	894,000	24.5%
1944	13,268	1,788,253	201,530	1,586,000	519,402	1,199,437	-14,000	920,000	19,000	203,000	N/A	736,000	24.7%
1943	13,274	1,567,412	178,726	1,388,000	484,142	1,118,345	-10,000	764,000	-13,000	128,000	N/A	623,000	25.9%
1942	13,347	1,427,298	189,533	1,237,000	419,540	1,085,179	12,000	560,000	-54,000	80,000	N/A	426,000	25.3%
1941	13,427	1,357,175	208,193	1,149,000	446,483	1,101,531	33,000	460,000	-16,000	8,000	N/A	436,000	28.0%
1940	13,438	1,268,650	218,577	1,049,000	435,928	1,033,191	48,000	404,000	-15,000	6,000	N/A	383,000	29.4%
1939	13,534	1,248,681	234,307	1,015,000	423,392	992,045	71,000	375,000	0	5,000	N/A	370,000	29.4%
1938	13,657	1,236,854	249,990	987,000	409,068	968,050	94,000	334,000	-49,000	4,000	N/A	281,000	29.3%
1937	13,795	1,282,019	260,878	1,021,000	409,512	958,453	52,000	421,000	-59,000	5,000	N/A	357,000	28.6%
1936	13,969	1,236,991	273,383	964,000	504,638	949,833	140,000	379,000	113,000	2,000	N/A	490,000	34.4%
1935	14,123	1,190,727	298,196	893,000	582,979	853,888	237,000	385,000	-211,000	N/A	N/A	174,000	39.5%
1934	14,137	1,241,092	327,723	913,000	469,533	863,300	500,000	20,000	-377,000	N/A	N/A	-357,000	34.0%

Chart 2

Large Bank Revenues Indicate a Variety of Products and Services

	<u>Assets > \$1 Billion</u> <u>2001</u>	<u>% of</u> <u>Total</u>
Income from fiduciary activities	18,709,045	13.1%
Service charges on deposit accounts	22,310,156	15.6%
Trading revenues	12,514,131	8.8%
On interest-rate contracts	6,067,261	4.2%
On foreign exchange contracts	4,336,854	3.0%
On equity contracts	1,878,353	1.3%
On commodity & other contracts	231,663	0.2%
Investment banking & other fees	8,685,482	6.1%
Venture capital revenue	-745,193	-0.5%
Servicing fees	10,545,446	7.4%
Securitization income	15,917,146	11.1%
Insurance commissions & fees	2,603,886	1.8%
Net gains/losses on loan sales	3,877,895	2.7%
Net gains/losses on sales of OREO	48,527	0.0%
Other noninterest income	46,130,607	32.3%
Total noninterest income	142,826,143	

Chart 3

Smaller Banks' Revenues Show Less Diversity

	<u>Assets < \$1 Billion</u> <u>2001</u>	<u>% of</u> <u>Total</u>
Income from fiduciary activities	2,042,181	14.2%
Service charges on deposit accounts	4,162,453	29.0%
Trading revenues	10,703	0.1%
On interest-rate contracts	8,617	0.1%
On foreign exchange contracts	2,112	0.0%
On equity contracts	-26	0.0%
On commodity & other contracts	0	0.0%
Investment banking & other fees	411,499	2.9%
Venture capital revenue	4,971	0.0%
Servicing fees	1,023,284	7.1%
Securitization income	432,829	3.0%
Insurance commissions & fees	271,052	1.9%
Net gains/losses on loan sales	764,670	5.3%
Net gains/losses on sales of OREO	16,821	0.1%
Other noninterest income	5,205,163	36.3%
Total noninterest income	14,345,769	