Statement by FDIC Chairman Sheila Bair at the Quarterly Banking Profile Press Conference, August 27, 2009

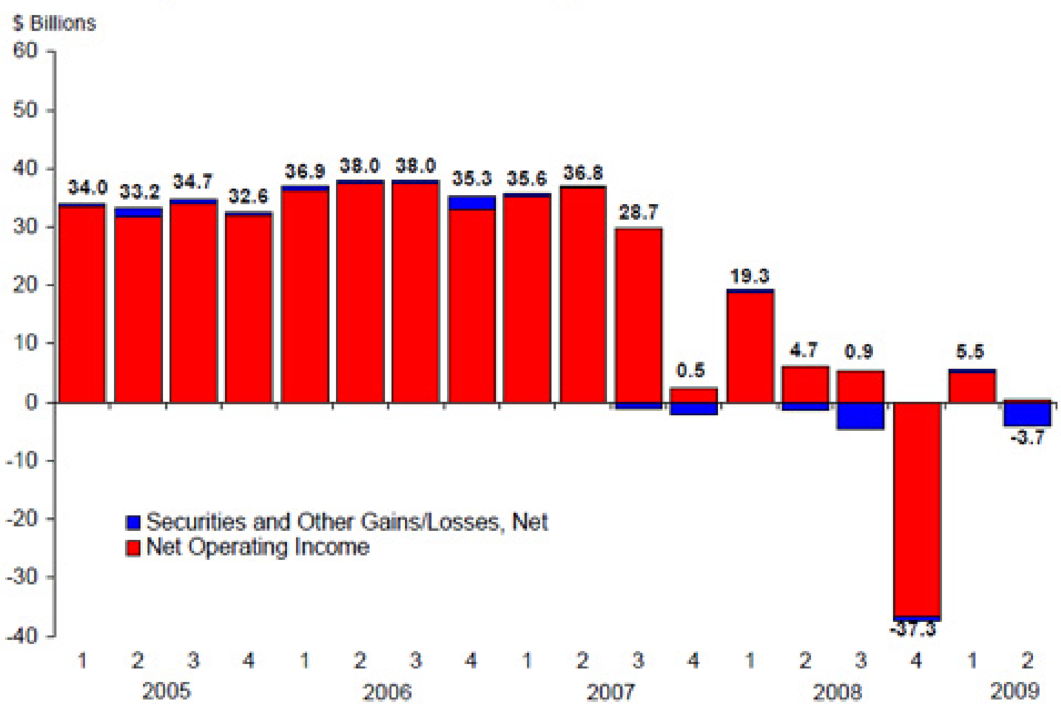
Good morning everybody, and welcome to our briefing on industry results for the second quarter.

We've all seen the good news that has come out on the economy in the past few weeks. While challenges remain, evidence is building that the American economy is starting to grow again. But no matter how challenging the environment ... the FDIC has ample resources to continue protecting insured depositors as we have for the last 75 years. No insured depositor has ever lost a penny of insured deposits ... and no one ever will.

One of the themes of today's quarterly profile is that banking industry performance is -- as always -- a lagging indicator. The banking industry, too, can look forward to better times ahead. But, for now, the difficult and necessary process of recognizing loan losses and cleaning up balance sheets continues to be reflected in the industry's bottom line.

Insured institutions posted a $3.7 billion net loss in the second quarter. As this first chart shows, they earned $424 million in net operating income. But one-time losses and other items totaling $4.1 billion pulled the overall results into negative territory.

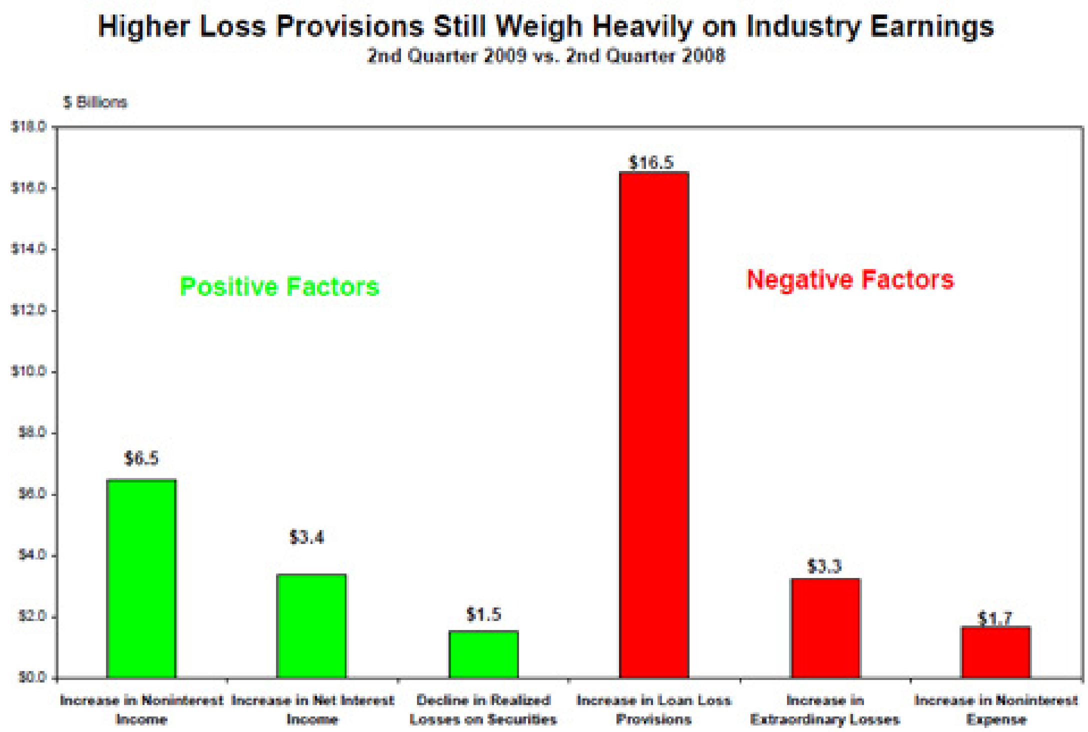
The Industry Posted Its Second Quarterly Loss in the Past 18 Years



Positive net operating income was achieved even after a special assessment of about five and a half billion dollars to bolster the Deposit Insurance Fund.

Higher provisions push earnings lower

As this next chart shows, deteriorating loan quality is having the greatest impact on industry earnings, as insured institutions continue to set aside reserves to cover loan losses.

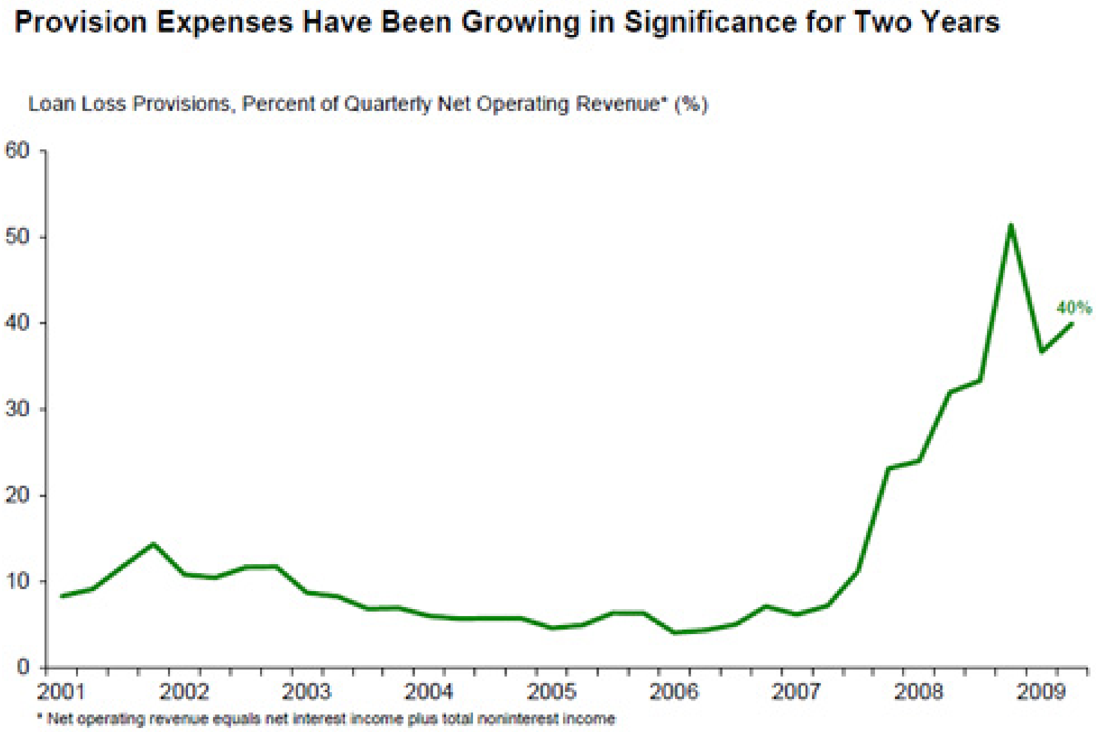


Of all the major earnings components, the amount that insured institutions added to their reserves for loan losses was, by far, the largest drag on industry earnings compared to a year ago. As you can see, loss provisions were $16.5 billion higher than a year ago. In all, banks and thrifts set aside $67 billion to cover bad loans in the second quarter.

Other factors that weighed on earnings included expenses stemming from write-downs of asset-backed commercial paper, which increased extraordinary losses ... and higher deposit insurance premiums. (Absent these premiums, non-interest expense would have declined, reflecting banks' efforts to cut costs.)

The upward trend in loan-loss provisions dates back to the second half of 2006. But while the early losses were related to residential loans and complex mortgage-related assets ... where the crisis really began ... we're now seeing problems with more conventional types of retail and commercial loans that have been hit hard by the recession.

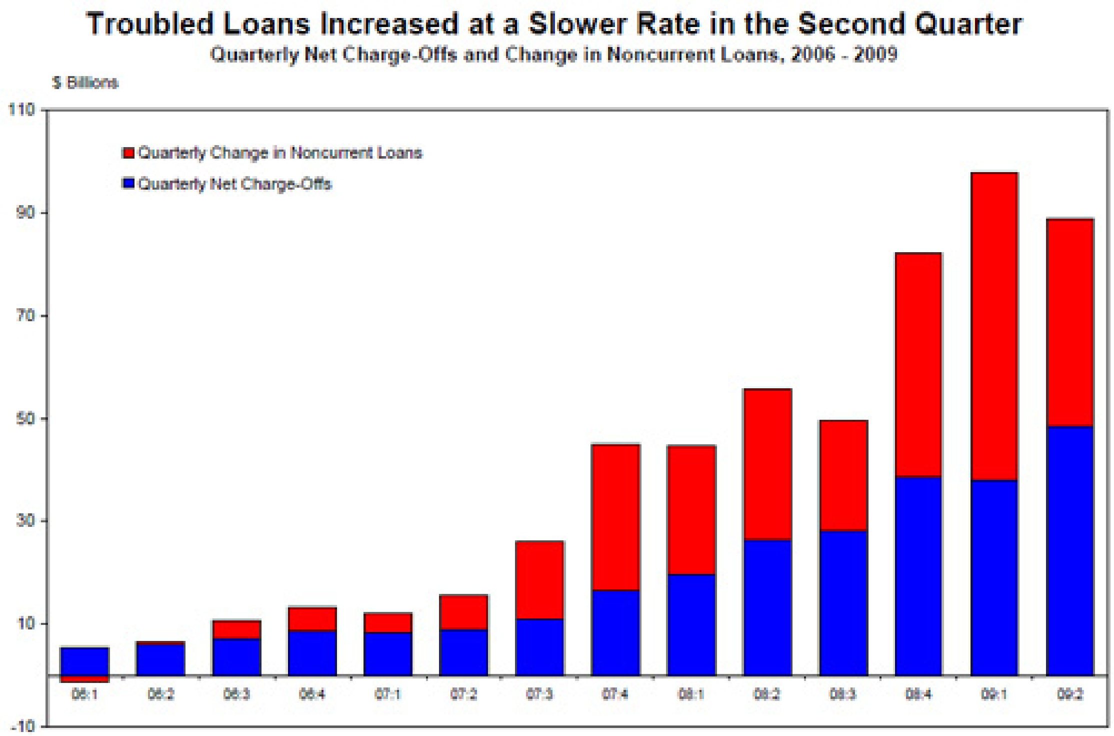
This chart shows how loss provisions have grown as a share of the industry's net revenues.



In the second quarter, loss provisions were 10 times what they were three years ago. The obvious reason for this is the ongoing need to bolster reserves in the face of rising levels of troubled loans. These credit problems will outlast the recession by at least a couple of quarters.

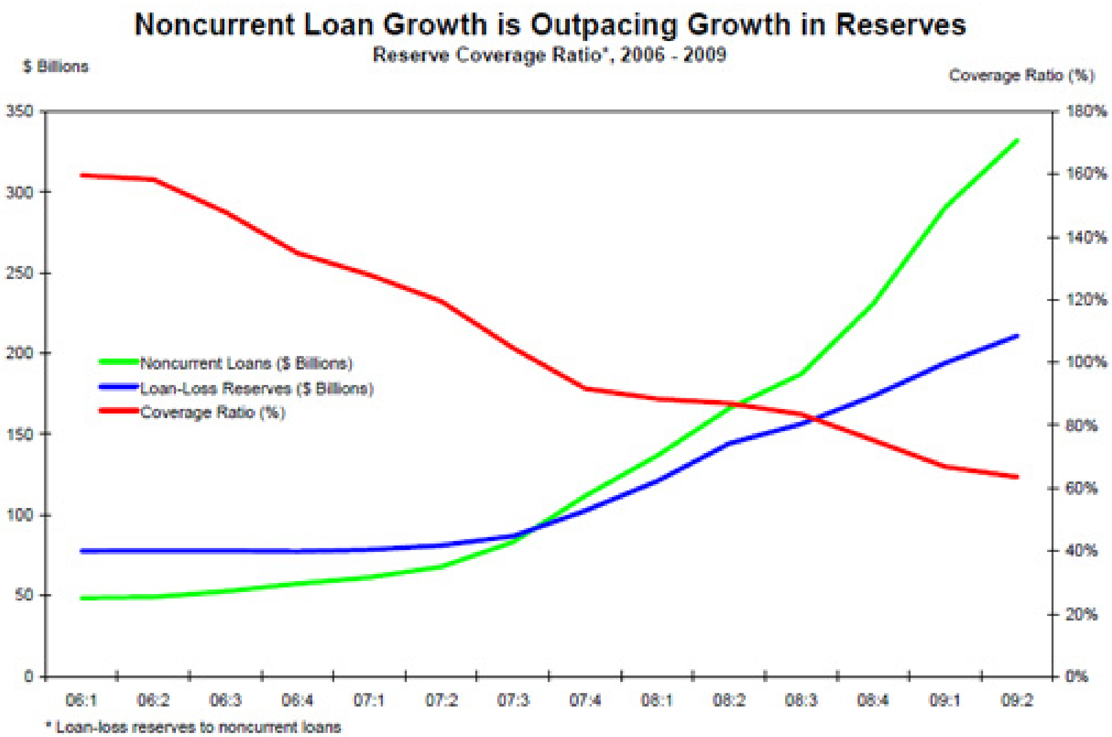
Problem loans still increasing

This chart shows the amount of loans that have been written off each quarter (that's the blue segment) ... as well as the quarterly change in the amount of non-current loans remaining on banks' balance sheets (that's the red segment).



The chart shows that both charge-offs and non-current loan levels are still rising. The continued growth in these categories lifted the net charge-off rate and the non-current loan rate to historic highs in the second quarter. And as you can see from this next chart, the gap has also been growing between the level of non-current loans (that's the green line) ... and the industry's reserves (that's the blue line).

This widening gap is driving the high loss provisions. And it's the reason that we expect provisions to remain at elevated levels for some time.

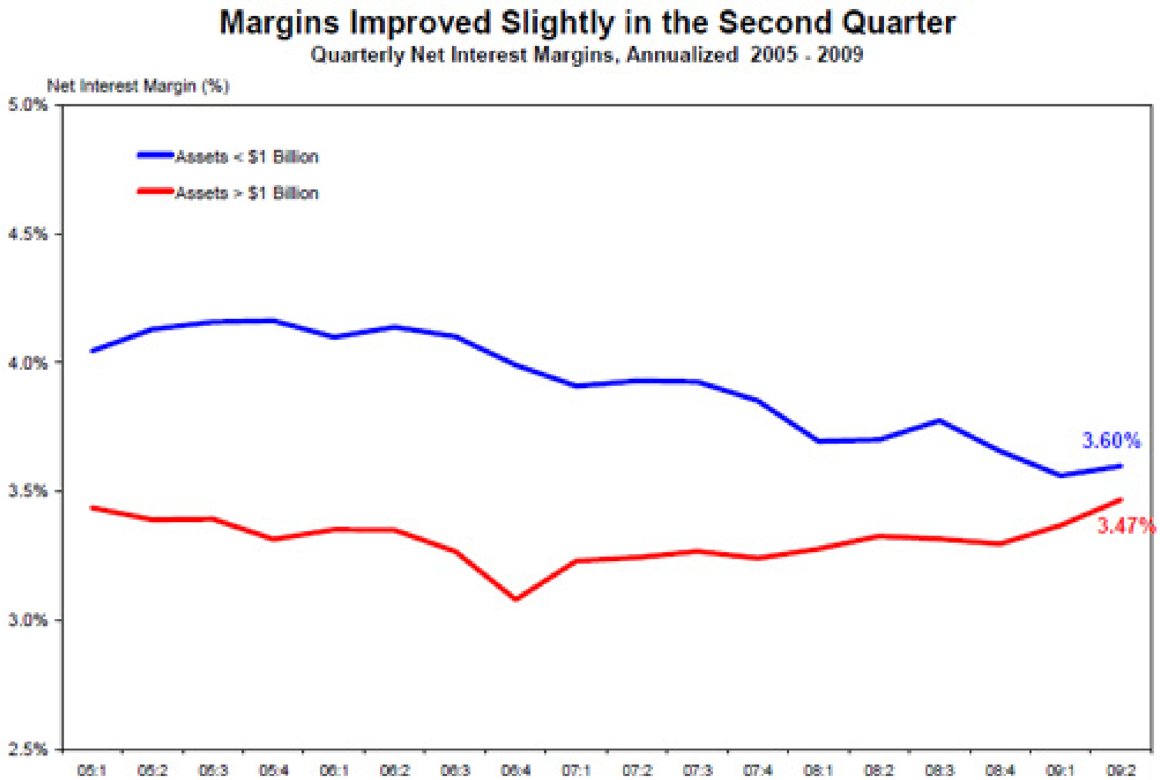


Areas of improvement

Not all of the news in the second quarter was bad. While total non-current loans and net charge-offs continued to rise, the increase was smaller than in the first quarter. Also, non-current home equity and junior lien mortgages declined for the first time in six quarters. And the volume of loans that were 30 to 89 days past due, fell across all major loan categories.

Are these signs of a turning point in asset quality? This may turn out to be the case. But we're going to need another quarter or two to confirm a trend.

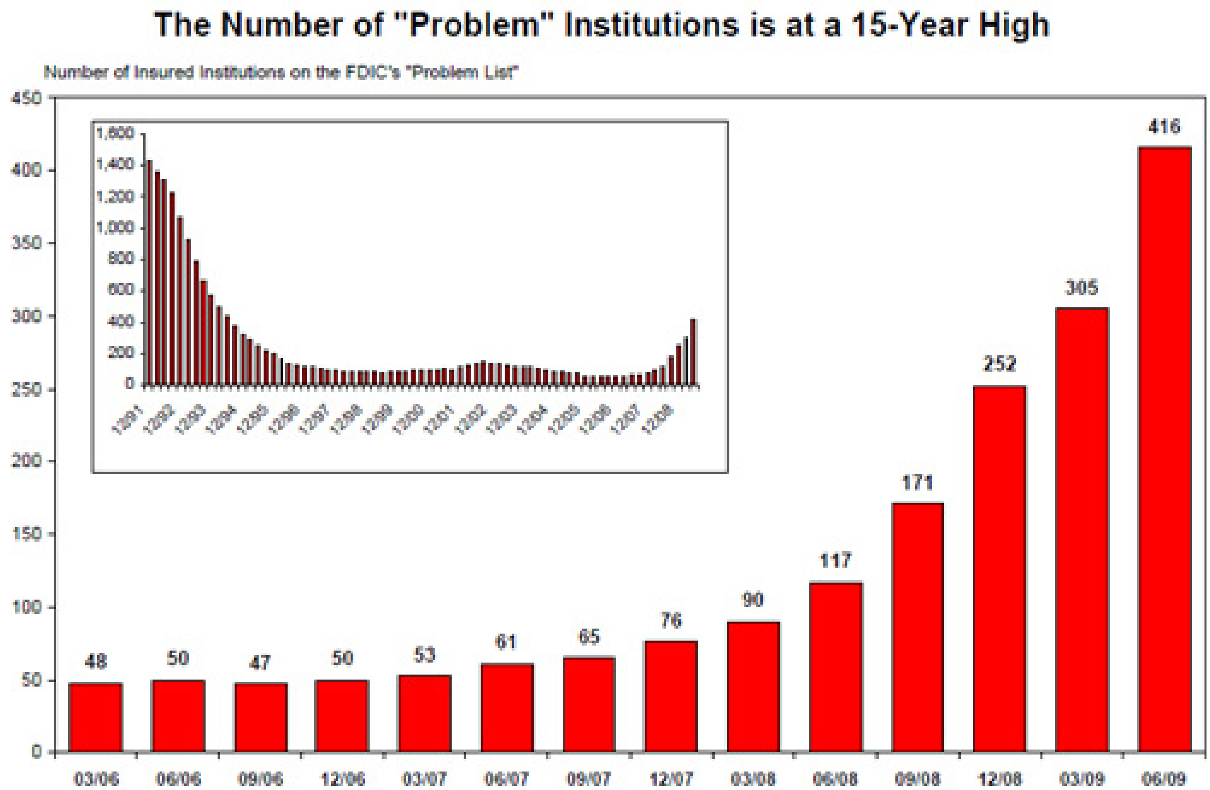
Another positive during the quarter was an improvement in net interest margins for community banks as well as for larger institutions. This is good news for community banks, since three-fourths of their revenues come from net interest income.



In many important respects, financial markets are returning to normal. Combined with the positive economic news in recent weeks, we're hopeful that this will lead to a moderation in credit problems in coming quarters. But, as our report shows, cleaning up balance sheets is a painful process that takes time. This process is absolutely necessary in order to restore the industry's profitability, and to strengthen its capacity to lend to businesses and consumers.

Problem list grows

As banks and thrifts continue cleaning up their balance sheets, more are coming onto our problem list. The number rose during the quarter to 416. This chart shows the trend since the Problem List hit an historic low in 2006, when bank profits were at record highs. Although the number continues to increase, it's still well below the levels seen during the last crisis.



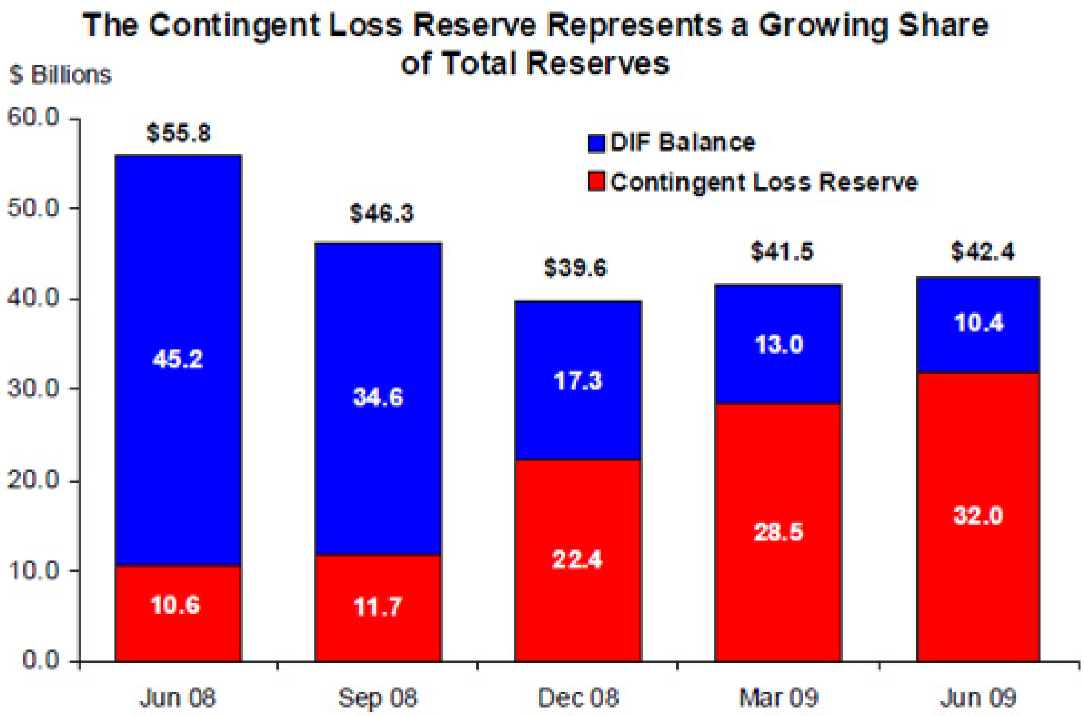
As you know, the number of failures is also up. There have been 81 so far this year. We expect the numbers of problem banks and failures will remain elevated, even as the economy begins to recover. (Problem banks and bank failures also tend to be lagging economic indicators.)

DIF update

Now let me turn to how failures are affecting the Deposit Insurance Fund, or the DIF. First: failures cost money. And the costs are charged to the DIF. But one thing that you should know is that the DIF balance has already been adjusted downward for the cost of failures that are expected to occur over the next year. Just as banks set aside reserves for loan losses, we set aside reserves for anticipated bank failures.

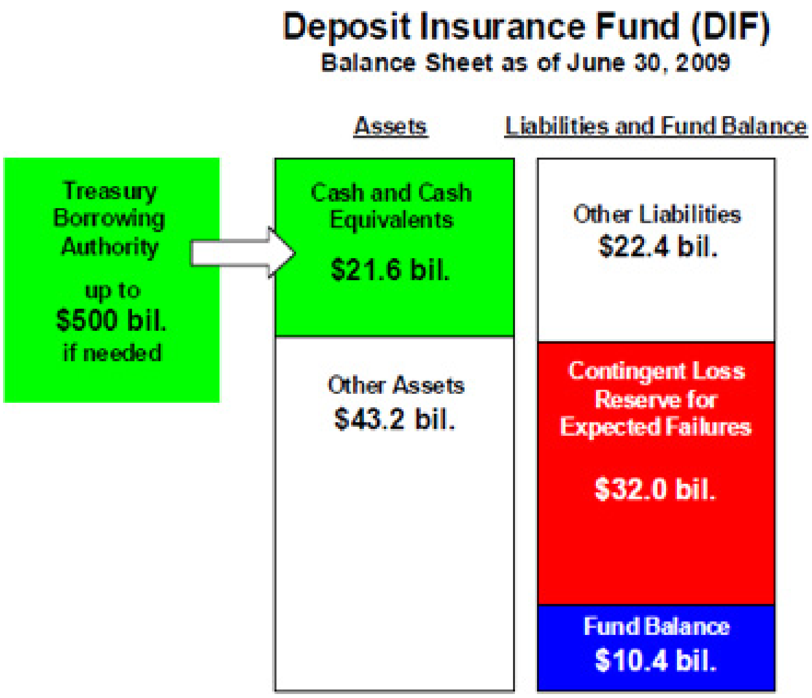
Our total reserves -- consisting of both the DIF balance and a contingent loss reserve -- are available to absorb losses. The DIF balance reflects the net worth of the insurance fund. It's also a guide for setting deposit insurance premiums for our industry-funded system. So when a bank fails, to the extent that we have already reserved for a failure, the loss comes out of the contingent loss reserve. For example, when Colonial Bank failed two weeks ago ... there was no reduction in the fund because the estimated loss had already been reserved for.

We review the adequacy of the contingent loss reserve every quarter, and make adjustments as warranted. As illustrated in this chart, we have been shifting large sums to the contingent loss reserve as our failure projections have grown. The total reserves are now over $42 billion.



FDIC resources run deep

Our total reserves should be distinguished from the cash resources at our disposal to protect depositors. As this last chart shows ... our sources of liquidity to protect depositors in future failures include not only the $22 billion of cash and Treasury securities held by the DIF as of June 30, but also the ability to borrow up to $500 billion from the Treasury. To sum up, a decline in the fund balance does NOT diminish our ability to protect insured depositors.



Conclusion

The FDIC was created specifically for times such as these. Our resources are strong. Your insured deposits are safe. And again, no insured depositor has ever lost a penny of insured deposits ... and no one ever will. Thank you very much.