Chairman's Opening Statement

First Quarter 2016 Quarterly Banking Profile

June 1, 2016

Good morning, and welcome to our release of first quarter 2016 results for FDIC-insured institutions.

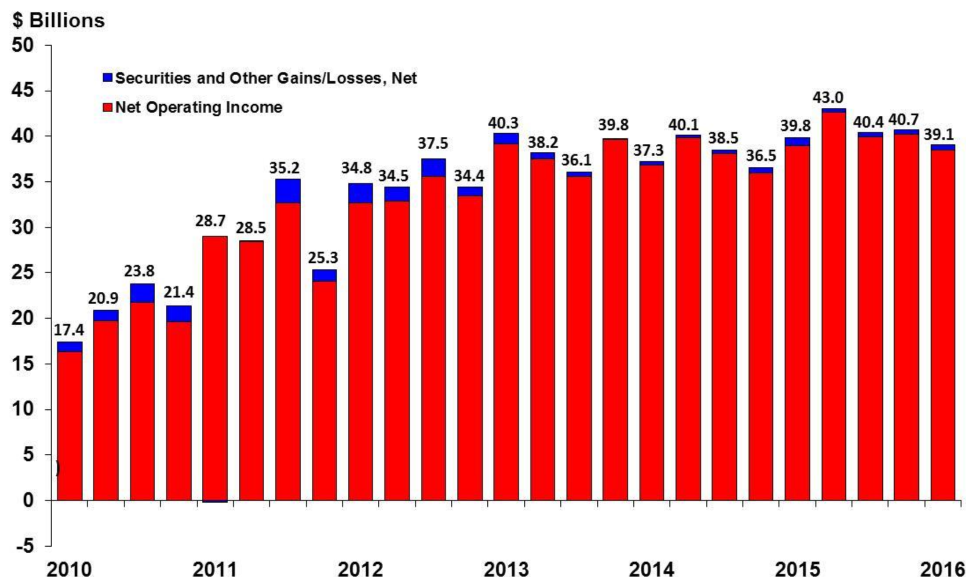
Overall, the banking industry reported mixed results for the first quarter.

By many measures, the industry had a positive quarter. Revenue increased from a year earlier, loan balances grew at the fastest 12-month rate since 2008, the share of unprofitable banks fell to an 18-year low, and the number of "problem banks" continued to decline.

However, banks are operating in a challenging environment. Net income declined in the first quarter, noncurrent loans to the oil and gas industry rose sharply, trading income was down, and net interest margins remained low by historical standards.

Community banks reported another solid quarter, as most of the industry's trading operations and direct loans to oil and gas producers are in larger institutions. Net income at community banks grew considerably from a year earlier. And revenue growth, loan growth and net interest margins at community banks were appreciably higher than the overall industry.

Chart 1:



Our first chart shows that net income was 39.1 billion dollars in the first quarter, down 2 percent from a year earlier. This was the first year-over-year decline in net income since the fourth quarter of 2014.

The decline in net income reported this quarter was largely due to a sharp increase in reserves at larger institutions to recognize potential losses from noncurrent commercial and industrial loans related to the energy sector.

In contrast to the overall industry, community banks reported net income growth of 7.4 percent from a year earlier. Quarterly net income improved at a majority of banks, and the share of unprofitable banks continued to decline.

Chart 2:

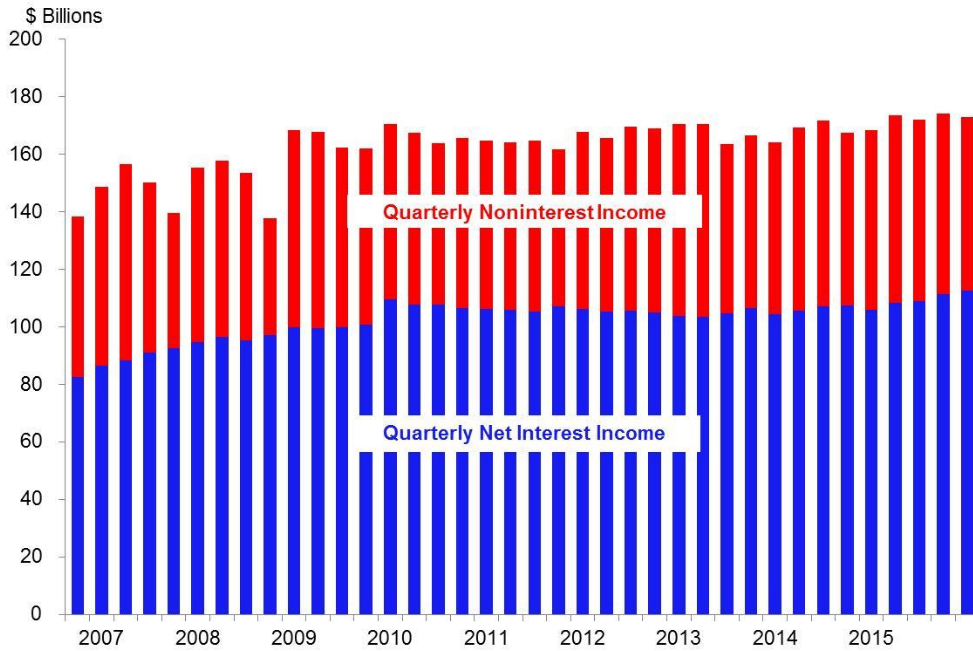
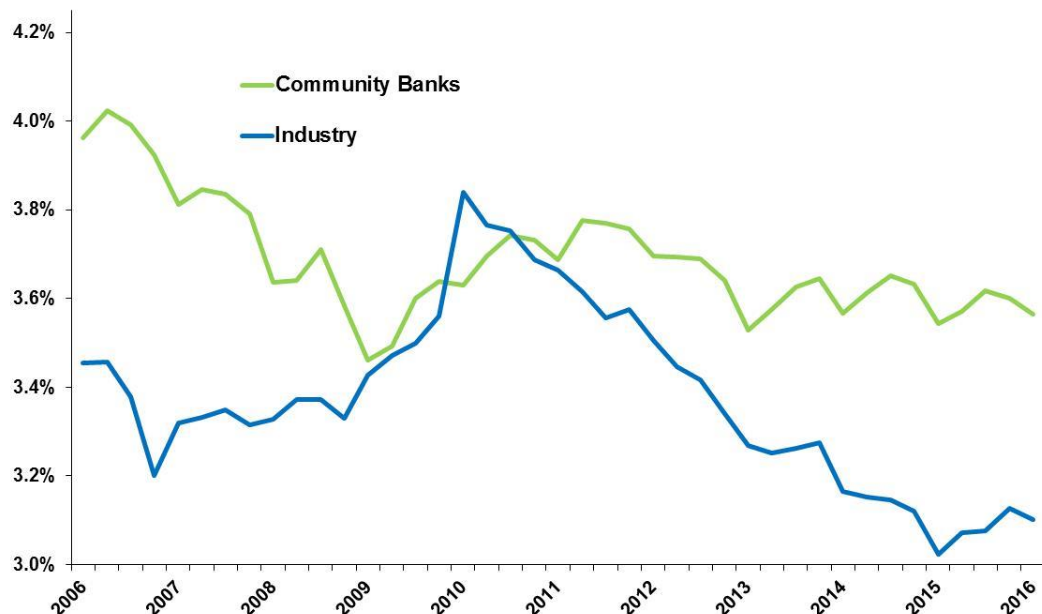


Chart 2 shows that net operating revenue of nearly 173 billion dollars in the first quarter was 2.7 percent higher than a year earlier. While net interest income continued to trend up, noninterest income fell primarily due to a large decline in trading income at the largest banks.

Revenue growth was particularly strong at community banks at nearly 7 percent.

Chart 3:



Our next chart shows that the average quarterly net interest margin for the industry was higher than a year earlier, as margins rose at the majority of banks. It also shows that community banks continued to experience higher margins than the rest of the industry.

However, margins remain low by historical standards as they have been under pressure in this challenging, low interest rate environment.

Chart 4:

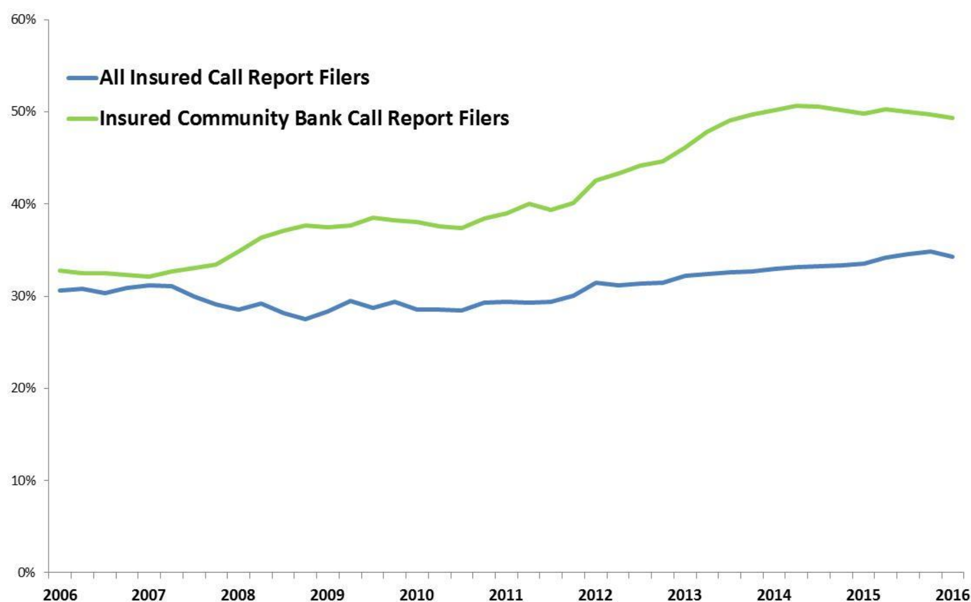
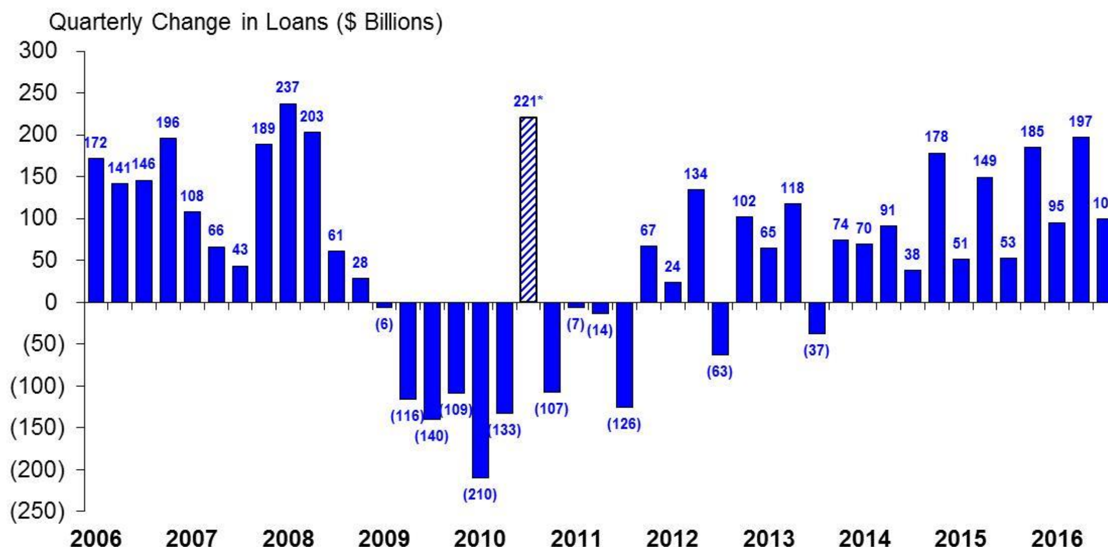


Chart 4 shows that community banks continued to hold a larger share of longer-term assets on their balance sheets than the overall industry. This has helped community banks sustain their net interest margins in a low rate environment, but it has left them more exposed to interest rate risk. This is a matter of continuing supervisory attention.

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.

Our next chart shows that loan balances rose 100 billion dollars during the first quarter. The increase was led by a 71 billion dollar increase in commercial and industrial (C&I) loans and a 38 billion dollar increase in commercial real estate loans. Credit card balances declined 33 billion dollars, a seasonal trend that is common during the first quarter when consumers pay down credit card balances after the holidays.

During the past 12 months, loan balances grew 6.9 percent. This is the highest 12-month growth rate since mid-2008.

Loan growth was even stronger at community banks during the past 12 months at 8.9 percent. Loan growth at community banks was led by an 11.9 percent increase in commercial real estate loans, an 8.6 percent increase in C&I loans, and a 5 percent increase in 1-4 family residential mortgages.

Chart 6:

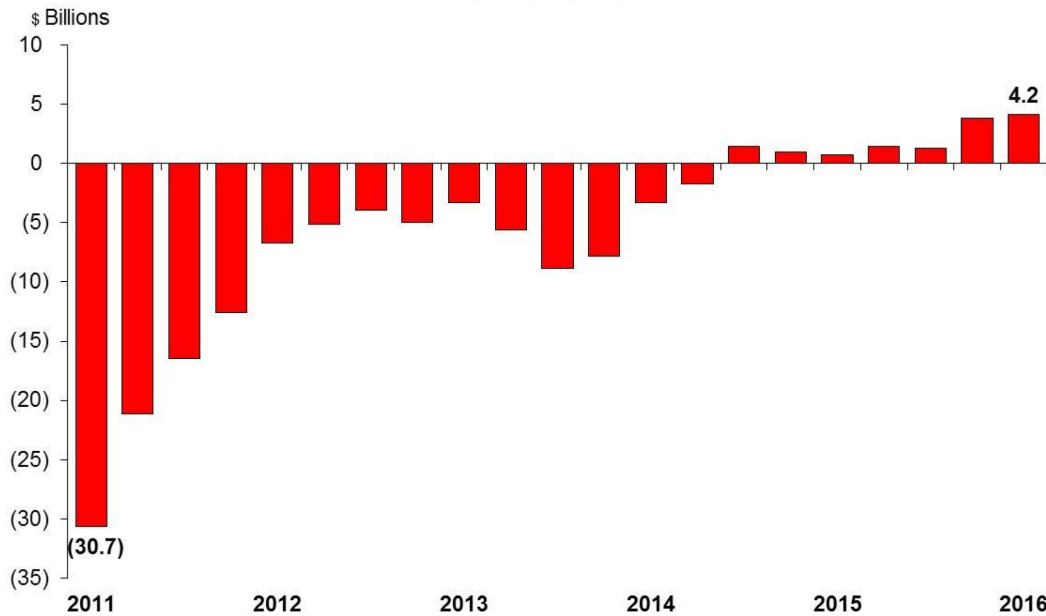
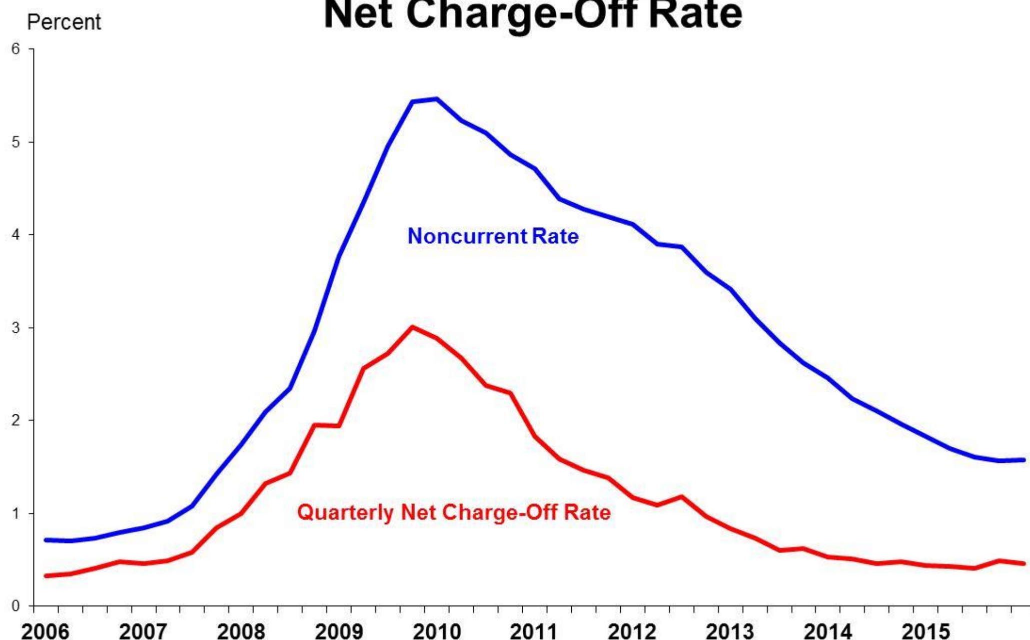


Chart 6 shows provision expenses set aside to recognize potential future loan losses. Provision expenses have increased on a year-over-year basis for seven quarters. While some of this increase reflects the general growth in loan portfolios and associated credit risk, a rising share is attributable to stress in loans to oil and gas producers as energy prices remain low.

Chart 7:



Our next chart shows asset quality indicators.

Reflective of the stress in the energy sector loans, noncurrent loan balances increased during the first quarter for the first time in six years.

Net charge-offs grew from a year earlier for the second consecutive quarter, although fewer than half of all banks reported an increase and the net charge-off rate remained at its pre-crisis level.

Chart 8:

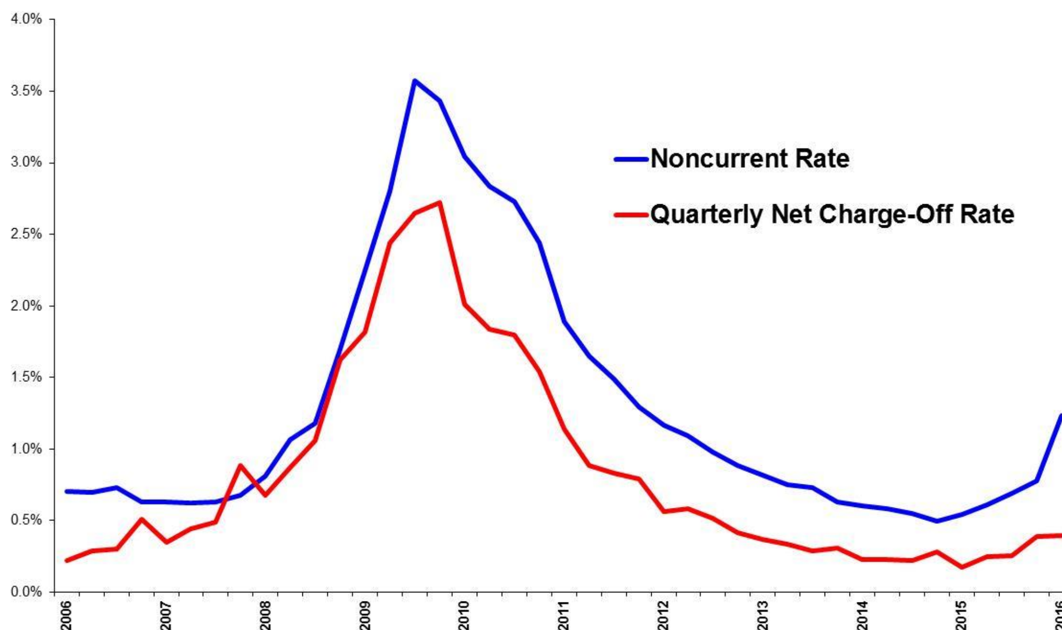
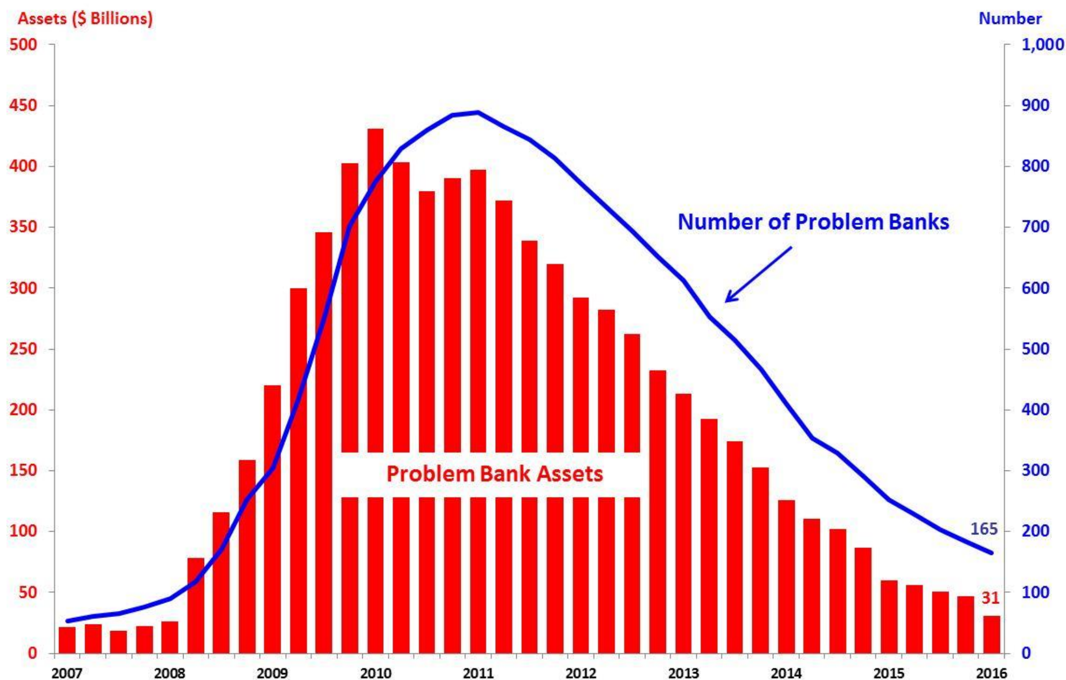


Chart 8 shows the noncurrent rate and net charge-off rate for commercial and industrial loans.

Noncurrent C&I loans have risen for five quarters. During the first quarter, noncurrent C&I loans rose 65 percent as low energy prices continued to challenge oil and gas producers.

The net charge-off rate for C&I loans has risen for four quarters, but still remains close to its pre-crisis level.

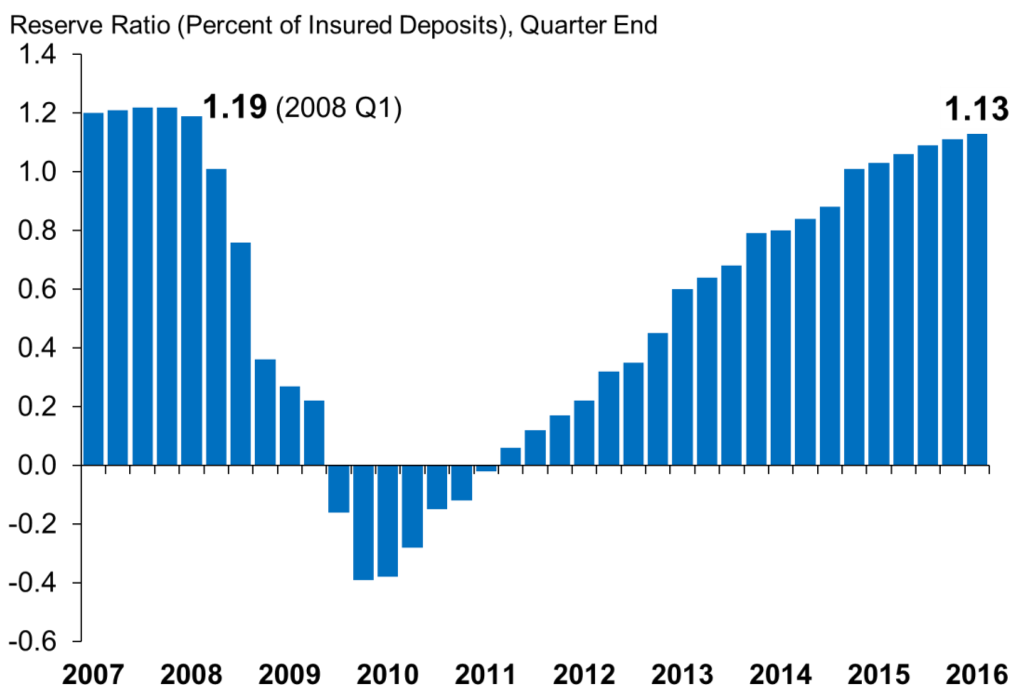
Chart 9:



The number of banks on the "Problem List" fell to 165 at the end of the first quarter. This is the fewest problem banks since mid-2008. Total assets of problem banks fell to 31 billion dollars, the lowest level since the first quarter of 2008.

There was one bank failure during the first quarter.

Chart 10:



The Deposit Insurance Fund balance was 75.1 billion dollars on March 31, up 2.5 billion dollars from last quarter. Revenues from assessments were primarily responsible for the increase.

Estimated insured deposits rose to 6.7 trillion dollars at the end of March, an increase of 2.0 percent during the quarter.

Chart 10 shows that the reserve ratio, which is the Fund balance as a percentage of estimated insured deposits, increased to 1.13 percent on March 31 from 1.11 percent at the end of 2015.

As required by law, the Deposit Insurance Fund must achieve a minimum reserve ratio of 1.35 percent by September 30, 2020.

We are on track to meet this mandate.

In summary, the banking industry reported mixed first quarter results.

Revenue increased from a year earlier, loan balances expanded at the highest 12-month rate since 2008, unprofitable banks were at an 18-year low, and there were fewer banks on the problem list.

However, the banking industry faces challenges. Net income declined as noncurrent loans to the oil and gas industry rose sharply and trading income fell. And net interest margins remained low by historical standards.

In contrast to the overall industry, community banks reported robust growth in net income and stronger revenue and loan growth as most factors that adversely affected the industry were concentrated at larger institutions.

The mixed first quarter results reflect an evolving economic environment. A prolonged period of low interest rates has narrowed margins and caused some institutions to reach for yield. More recently, low energy prices have led to a sharp increase in noncurrent loans to oil and gas producers. The

full impact of low energy prices on the banking industry remains to be seen, particularly for consumer and business loans in energy-producing regions of the country.

We will continue to monitor closely the evolving environment in which the U.S. banking industry is operating. And we will remain vigilant in our supervisory activities.

Thank you.

I am happy to take your questions.