

Statement by  
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On the Release of the  
Quarterly Banking Profile  
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The numbers you have before you this morning show that commercial banks continue to enjoy great profitability. They also show an increase in credit-quality problems in loans to individuals - particularly credit card loans. Finally, these numbers shed light on the continuing problems of the Savings Association Insurance Fund.

The earnings of commercial banks have never been better. If the commercial banking industry maintains the earnings strength it displayed during the first half of 1996 for the next six months, it will -- for the first time ever -- earn more than \$50 billion in one year. Bank earnings in the first half of 1996 were more than 10 percent higher than earnings in the first half of 1995.

In the second quarter of 1996, commercial banks earned \$13.78 billion -- the second time the industry's profits have exceeded \$13 billion and a 15-percent improvement over the \$12 billion that commercial banks earned in the second quarter of 1995.

The average return on assets (ROA) at commercial banks has exceeded one percent for fourteen consecutive quarters. ROA -- a basic yardstick of profitability -- stood at an annualized 1.27 percent in the second quarter, up from 1.16 percent a year ago. This was the third-highest quarterly ROA that commercial banks have ever registered.

Moreover, stronger earnings were widespread. Almost three-quarters of all banks (72 percent) reported higher earnings than a year earlier, and more than two-thirds (70 percent) reported ROAs above one percent.

Earnings are not the only way to measure the financial strength of the banking industry. Another important measure is the coverage ratio. This ratio is the amount of money banks have in loan loss reserves compared to their noncurrent loans -- loans past due 90 or more days or in nonaccrual status. As this chart shows, banks have a record \$1.77 in reserves for every dollar of noncurrent loans. That compares to \$1.67 a year ago and \$1.46 two years ago. As recently as 1993, commercial banks had less than a dollar in reserves for every dollar in noncurrent loans.

The recent trends for commercial banks have not all been positive, however. Banks charged off \$3.8 billion in loans in the second quarter -- a billion dollars more than they charged off in the second quarter of last year, or an increase of 36 percent. It was the second-highest quarterly amount charged off in the last ten quarters. The highest was the \$4 billion charged off in the fourth quarter of last year.

Much of the rise in losses in the second quarter occurred at banks with assets of more than \$1 billion.

As this chart shows, the increase in loan losses was due -- in large part -- to charge-offs on loans to individuals. Charge-off rates on these loans have risen sharply from 1.40 percent in the second quarter of 1994 to 2.24 percent in the second quarter of 1996.

In fact, net charge-offs on bank credit-card loans accounted for almost two-thirds of all loan losses in the second quarter. The annualized charge-off rate on those loans in the second quarter was 4.48 percent -- the highest level since the fourth quarter of 1992.

Bank credit card loans also continued to increase rapidly -- growing more than \$7.3 billion in the second quarter. As this chart shows, in terms of both loans outstanding and unused commitments, the 12-month growth rate for credit card credit has slowed the last year -- from a peak of 33.8 percent in the second quarter of 1995 to 20.6 percent in the second quarter of 1996. The growth, however, is still dramatic. Credit card loans that banks have made grew \$55.4 billion during the last twelve months, while commitments rose \$213.2 billion. Credit made available through credit cards has more than doubled since the end of 1992.

Despite these concerns, the outlook for commercial banks remains bright. Thirty new banks were chartered during the quarter, bringing the total number of new charters in the first half of 1996 to 59. If this pace continues, we will outdistance the 102 new bank charters issued last year. Mergers absorbed 175 banks in the second quarter and two banks failed, bringing the number of commercial banks down from 9,838 at the end of last March to 9,689.

The thrift industry also shrank in the second quarter of 1996. Although total assets grew, the number of thrifts -- Bank Insurance Fund (BIF) and Savings Association Insurance Fund (SAIF) insured institutions -- dropped below 2,000 for the first time since 1937. The number of SAIF insured thrifts declined from 1,622 in the first quarter to 1,599 in the second. Such shrinkage will concentrate risks that the SAIF covers, leading to an actuarially and structurally unsound deposit insurance fund.

This kind of shrinkage is not the only problem the SAIF faces.

As this chart shows, the SAIF increased from 51 cents for every dollar of insured deposits at the end of the first quarter of 1996 to 55 cents at mid-year. However, the increase in the SAIF's reserve ratio came -- not only from a \$264 million rise in the fund balance -- but also from a decline of nearly \$3 billion in SAIF-insured deposits. This decline reflects continuing shifting of deposits from the SAIF to the BIF -- a process called "migration." One organization has reduced its SAIF deposits by more than \$9 billion in this way, including the shifting of \$3 billion in the most recent quarter. As you know, Federal regulatory agencies have recently approved several applications from thrift organizations to acquire BIF-member affiliates.

At current assessment rates, the SAIF needs an assessment base of \$333 billion to generate the money necessary for it to meet obligations issued by the Financing Corporation (FICO) that pay for thrift failures in the 1980s. This chart shows that the "cushion" -- the surplus in the FICO assessment base above \$333 billion -- has been shrinking steadily since the SAIF was created in 1989. At the end of the second quarter, it was about \$110 billion above the required base, down from a \$118 billion cushion in only one quarter. Most of the erosion in the FICO base over the years can be attributed to charter conversions and branch sales to BIF members, but migration of deposits from SAIF to BIF also clearly threatens both the viability of the SAIF and its ability to meet its FICO obligation. As this chart also shows, SAIF deposits that have the potential to migrate to the BIF in the near future exceed the FICO cushion.

The SAIF is structurally unsound. It cannot resolve its own problems. Those problems have to be addressed. In the brief time remaining this year, I urge Congress to adopt a comprehensive legislative package that would capitalize the SAIF, establish a framework for addressing charter issues and the merger of the BIF and the SAIF, and provide regulatory burden relief for banks.

I only hope that recent legislation removing the tax penalties for converting from a thrift charter to a bank charter will not give thrifts incentives to walk away from this compromise legislation to avoid paying the special assessment of \$5 billion and to migrate deposits from the SAIF to the BIF. It is in everyone's interest -- banks, thrifts, their customers and the financial system -- to get this issue behind us. With me today are Don Inscoe, the manager of the FDIC Statistics Branch, and Ross Waldrop, Tim Critchfield and Jim McFadyen, the FDIC analysts who put together the Quarterly Banking Profile. We will now entertain questions.