BANKING BRIEF

Federal Reserve Bank of Philadelphia

For Pennsylvania, New Jersey, and Delaware

Third Quarter 2000

Community banking organizations in the region and the nation outperformed their larger brethren in terms of return on assets (ROA) and growth in assets, all loan categories, and deposits. A little more than 50 percent of the decline in assets in large banks in the District can be attributed to FleetBoston's divestiture of 134 branches to Sovereign (which is not included in the totals because it is a thrift organization). However, the decline in loans at large banks appears to be widespread, affecting half of the large banking organizations in the tri-state area. According to the most recent Federal Reserve Survey of Senior Loan Officers, banks in the nation continue to tighten terms on loans by increasing interest rates, premiums on riskier loans, and fees for credit lines, especially to borrowers with no prior relationship with the institution and those trying to finance mergers and acquisitions. Consistent with the relatively weak loan growth at larger institutions, reports from respondents indicate tighter terms for large borrowers, who bank disproportionately with larger banks.

THE NEW DATA ON HOME LENDING

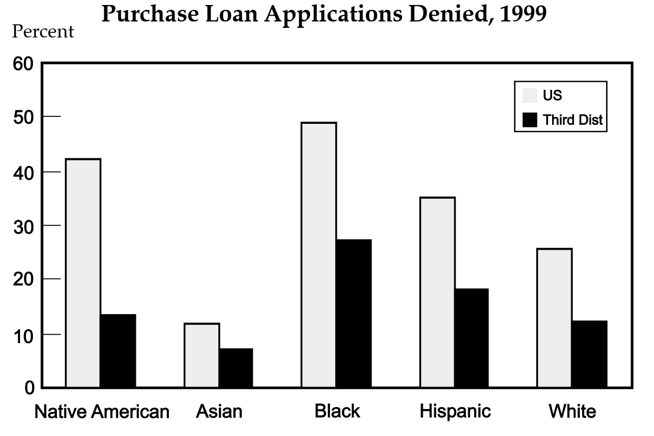
The Federal Financial Institutions Examination Council recently released data on 1999 home lending activity in metropolitan statistical areas (MSAs) and rural areas throughout the nation. The data reflect lending activity for more than 7800 institutions covered by the Home Mortgage Disclosure Act (HMDA), which include depository institutions with more than $30 million in assets as well as mortgage companies that make a substantial number of home loans. Nationally, loans and applications decreased 7.1 percent from the previous year, reflecting decreased refinancing activity. In the Third District, as in the nation, the number of home purchase loans extended in 1999 (conventional plus government-insured loan originations) rose for all racial/ethnic groups compared with 1998. In the District, the number of originations increased 32.2 percent for Native Americans, 18.6 percent for Asians, 12.5 percent for blacks, and 21.5 percent for Hispanics. Lending to white borrowers rose 3.2 percent. However, to a significant extent, higher growth rates for minorities merely reflect lower initial levels of home ownership. Nationally, 73 percent of white families owned their own homes in 1999, compared with 47 percent of African Americans and 45 percent of Hispanics.

For the first time in several years, the overall denial rate for conventional home purchase loans in the nation declined from the prior year — from 29 to 28 percent. Denial rates for these loans continued to vary among racial and ethnic groups (see Figure). Forty-nine percent of black applicants, 42.1 percent of Native American applicants, 35 percent of Hispanics, 25.5 percent of whites, and 11.8 percent of Asian applicants were denied conventional home purchase loans in 1999 in the nation. These rates were lower than in 1998 for each group except Asians, for whom denial rates were unchanged. In the District, the overall denial rates for conventional home purchase loans were lower than for the nation: 13.3 percent for Native American applicants, 7.17 percent for Asians, 27.1 percent for blacks, 18.2 percent for Hispanics, and 12.3 percent for whites.

It is important to interpret the HMDA data with care. Although the data provide useful information about trends in denial rates by racial/ethnic groups over time, the HMDA data lack key underwriting information, such as an applicant's loan-to-value ratio, household composition, liquid assets, and credit history, as well as information about the property itself, such as sales price and appraisal value.[1] Therefore, from the raw HMDA data one cannot determine whether the observed disparities are the result of illegal discrimination or differences in creditworthiness among applicants. Even a formal lending model that takes into account those factors affecting an applicant's creditworthiness may still produce unreliable results unless we know how lenders weigh the relative importance of the various financial factors when making lending decisions.

To address these issues, the Federal Reserve applies a statistical model to a sample of loan applications by minority and nonminority applicants with *similar* qualifications to determine if a pattern of discrimination can be detected at a particular bank. The model provides an estimate of the probability of loan denial for each type of applicant. This probability depends on the financial circumstances of the applicant, the characteristics of the loan being requested, and property characteristics.[2] If the result of the statistical analysis indicates that the race of the applicant is a significant predictor of loan disposition, then this is viewed as an initial indication that a pattern of discrimination may exist and a further review of the bank's practices may be warranted.

Percent of Conventional Home Purchase Loan Applications Denied, 1999



[1] A. Munnell, L. Browne, J. McEnearney, and G. Tootell, "Mortgage Lending in Boston: Interpreting HMDA Data," Working Paper Series 92-7, Federal Reserve Bank of Boston (1992).

[2] P. Calem and G. Canner, "Integrating Statistical Analysis into Fair Lending Exams: The Fed's Approach," in A. Yezer, ed., *Fair Lending Analysis: A Compendium of Essays on the Use of Statistics* (1995).

Third Quarter 2000

Community Banking Organizations

	Tri-State			*Nation*		
	$Bill	% change from		$Bill	% change from	
	00Q3	**00Q2**	**99Q3**	**00Q3**	**00Q2**	**99Q3**
Total Assets	76.5	6.7	7.6	1144.8	10.4	10.1
Total Loans	47.9	7.3	10.8	740.5	12.1	14.2
Business	6.2	3.7	7.6	135.3	8.3	14.4
Real Estate	34.6	7.3	11.8	472.4	14.4	16.6
Consumer	5.5	12.2	8.8	86.1	6.2	7.1
Total Deposits	59.9	8.5	8.0	928.9	11.3	9.2
Ratios (in %)	**00Q3**	**00Q2**	**99Q3**	**00Q3**	**00Q2**	**99Q3**
Net Income/ Avg Assets (ROA)	1.2	1.2	1.2	1.2	1.2	1.2
Net Interest Inc/ Avg Assets (NIM)	3.7	3.7	3.8	4.1	4.1	4.1
Noninterest Inc/ Avg Assets	1.1	1.1	1.0	1.0	1.0	1.0
Noninterest Exp/ Avg Assets	3.0	3.0	3.0	3.1	3.2	3.2
Loans/Deposits	80.0	80.2	78.0	79.7	79.6	76.2
Equity/Assets	8.5	8.5	8.5	9.1	9.1	9.2
Nonperforming Loans/ Total Loans	0.7	0.7	0.7	0.8	0.8	0.9

Large Banking Organizations

	Tri-State			*Nation*		
	$Bill	% change from		$Bill	% change from	
	00Q3	**00Q2**	**99Q3**	**00Q3**	**00Q2**	**99Q3**
Total Assets	849.6	-12.5	0.2	4553.8	0.8	7.7
Total Loans	538.8	-5.7	0.2	2792.1	4.7	9.6
Business	192.9	-6.5	1.6	886.7	2.5	8.7
Real Estate	215.5	-5.0	0.9	1138.4	4.6	14.1
Consumer	45.9	-16.6	-10.1	340.6	6.6	2.3
Total Deposits	551.0	-8.9	-0.5	2908.6	-0.9	5.7
Ratios (in %)	**00Q3**	**00Q2**	**99Q3**	**00Q3**	**00Q2**	**99Q3**
Net Income/ Avg Assets (ROA)	1.0	1.1	1.2	1.1	1.2	1.2
Net Interest Inc/ Avg Assets (NIM)	3.3	3.3	3.3	3.1	3.2	3.2
Noninterest Inc/ Avg Assets	2.8	2.9	2.8	2.4	2.5	2.4
Noninterest Exp/ Avg Assets	3.9	3.9	3.8	3.4	3.4	3.5
Loans/Deposits	97.8	97.0	97.1	96.0	94.7	92.6
Equity/Assets	8.5	8.5	8.5	8.1	8.1	8.0
Nonperforming Loans/ Total Loans	1.1	1.2	0.9	1.0	1.0	1.0

A banking organization is an independent bank or all the banks within a highest-level bank holding company; however, banks less than five years old and those whose credit card loans make up greater than 50 percent of their total loans are excluded. The large banking organization sample is based on banking organizations whose total assets were at least as large as those of the 100th largest banking organization in the United States as of December 31, 1999. The community banking organization sample is based on the remaining banking organizations. Tri-state large banking organizations are those large banking organizations that have either at least 5 percent of the deposits of the region or any state therein or at least 5 percent of their deposits in the region. Tri-state community banking organizations are those community banking organizations that are headquartered in the region. The numbers of banking organizations in the categories are as follows: (1) community banking organizations —190 for the tri-state area and 6076 for the nation; (2) large banking organizations —18 for the tri-state area and 97 for the nation. Ratios are aggregates, that is, the numerators and denominators are summed across all banks in the group, then divided. Data are adjusted for mergers.

Any questions or comments should be directed to Victoria Geyfman at (215) 574-6431 or victoria.geyfman@phil.frb.org. Detailed documentation on the methodology used in constructing this document, back issues, and the current issue of *Banking Brief* are available on our web site at www.phil.frb.org/econ/bb/index.html. To subscribe to this publication, please contact the Publications Desk at (215) 574-6428 or lois.newell@phil.frb.org.

FEDERAL RESERVE BANK OF PHILADELPHIA