BANKING BRIEF

FOR PENNSYLVANIA, NEW JERSEY, AND DELAWARE

First Quarter 2002

Amid rising unemployment rates, the charge-off rate for consumer loans rose from 3.3 percent to 4.1 percent over the quarter, fueled by an increase in credit card chargeoffs at large banks and already high rates at smaller banks (see figure).[1] Although average charge-off rates for business and real estate loans edged down slightly from fourth quarter 2001, both rates were higher than a year ago. Nonperforming loans rose from 1 percent to 1.2 percent over the year at community banks, and from 1.5 percent to 1.8 percent at large banking institutions in the nation.

So far, however, banks continue to exhibit strong levels of profitability, earning an average return on assets of 1.1 percent at the national level and 1.3 percent in tri-state area banks. Year-to-year figures for community banks displayed healthy growth in all loan categories except consumer loans. On the other hand, large banking organizations in the nation registered a 31.6 percent increase in consumer loans over the quarter, reflecting the recent acquisition of Banamex by Citigroup. Community banks continued to extend a growing number of business loans, while the outstanding volume of these loans at larger banks was down 9 percent from last quarter and 10 percent from a year ago. The Senior Loan Officer Opinion Survey for April 2002 indicated that about one-third of reporting domestic banks experienced weaker demand for C&I loans from both large and small firms over the last quarter. This is down from about one-half in the last survey. Also, although standards and terms for business loans underwent further tightening, a significantly smaller fraction of banks tightened standards over the last quarter compared with the fourth quarter of 2001.

NONBANKING ACTIVITIES OF THIRD DISTRICT HOLDING COMPANIES

Prior to the passage of the Gramm-Leach-Bliley Act (GLBA), the Federal Reserve Board approved a number of activities permissible for bank holding companies and their nonbanking subsidiaries that were financial in nature or incidental to financial activity. These included making, acquiring, and servicing loans and other extensions of credit; providing trust activities; acting as an investment or financial advisor; performing certain insurance agency and underwriting activities directly related to banking; performing appraisals of real estate and tangible and intangible personal property; acting as an intermediary for the financing of commercial and industrial income-producing real estate; providing certain securities brokerage services; underwriting and dealing in government obligations and money market instruments; and providing tax planning and preparation services.

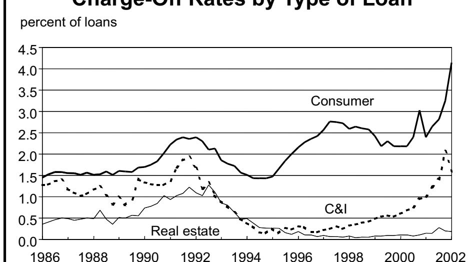
Under GLBA, a bank holding company that meets certain qualifications (its depository institutions must be well-managed and well-capitalized, and have at least a satisfactory rating under the Community Reinvestment Act) can elect to become a financial holding company (FHC). An FHC can engage in additional activities not otherwise permitted for a bank holding company, generally without obtaining the FRB's prior approval. These include securities underwriting and distribution, merchant banking, certain insurance activities, and other activities the FRB determines (1) to be financial in nature or incidental to that financial activity, or (2) are complementary to a financial activity and do not pose a substantial risk to the company's or the financial system's safety and soundness.

To date, there are 30 FHCs in the Third District. Five do not engage in nonbanking activities. Most of the activities these banks participate in were allowed before the passage of GLBA. Roughly one-third of the FHCs in the District are larger banking institutions (those with assets greater than $1 billion). These institutions provide a wide array of financial services, including financial planning, investment management, insurance, and brokerage services. All larger institutions either underwrite or serve as an insurance agent or broker.

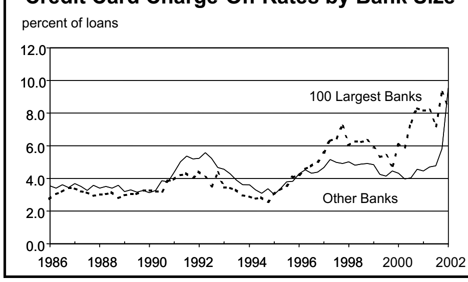
In our previous survey, conducted in early 2000, none of the smaller bank holding companies in the Third District had engaged in the new activities available to them under GLBA.[2] By the end of 2001, however, nine of the smaller companies were offering insurance products. Eight of these companies were in a joint venture that formed an offshore reinsurance company. Each bank individually owned a segregated cell through which its respective premiums and losses from credit life and accident and health insurance were funded and for which each bank had sole responsibility.

Currently, one in five small banks engages in discount brokerage, but usually through third-party arrangements. However, 80 percent of large banks offer investment advisory, asset management, and brokerage services. Of the 30 FHCs in our District, only two engage in activities that could be considered merchant banking and were not previously allowed for bank holding companies.

Charge-Off Rates by Type of Loan



Credit Card Charge-Off Rates by Bank Size



[1] The charge-off rate is the value of loans removed from the books and charged against reserves, less any recoveries, divided by average loans outstanding. The Federal Reserve Board measures bank size by consolidated assets adjusted for mergers; "other" banks are those smaller than the 100 largest.

[2] See this publication for the first quarter of 2000.

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First Quarter 2002

	Community Banking Organizations						*Large Banking Organizations*						
	Tri-State			*Nation*				*Tri-State*			*Nation*		
	$Bill	**% change from**		**$Bill**	**% change from**			**$Bill**	**% change from**		**$Bill**	**% change from**	
	02Q1	**01Q4**	**01Q1**	**02Q1**	**01Q4**	**01Q1**		**02Q1**	**01Q4**	**01Q1**	**02Q1**	**01Q4**	**01Q1**
Total Assets	$74.9	8.6%	10.1%	$1256.3	6.4%	8.9%	Total Assets	$887.2	-15.2%	-2.5%	$4790.2	-5.3%	0.6%
Total Loans	46.4	7.3	9.9	800.8	4.6	8.7	Total Loans	550.8	-5.8	-5.2	2800.3	-1.3	-1.2
Business	6.6	0.6	11.9	141.8	2.0	5.4	Business	172.9	-6.7	-12.7	796.9	-9.4	-10.5
Real Estate	34.2	10.5	11.1	535.3	8.8	12.0	Real Estate	241.1	-6.9	-0.5	1216.0	0.9	3.1
Consumer	3.9	-9.6	-4.5	78.4	-8.0	-2.7	Consumer	52.9	-9.2	-6.9	379.8	31.6	10.9
Total Deposits	59.1	8.5	10.8	1019.7	6.7	8.5	Total Deposits	591.1	-15.8	-2.5	3098.8	-6.2	1.8

Ratios (in %)	**02Q1**	**01Q4**	**01Q1**	**02Q1**	**01Q4**	**01Q1**	**Ratios (in %)**	**02Q1**	**01Q4**	**01Q1**	**02Q1**	**01Q4**	**01Q1**
Net Income/ Avg Assets (ROA)	1.2%	1.2%	1.2%	1.1%	1.1%	1.1%	Net Income/ Avg Assets (ROA)	1.1%	1.0%	1.1%	1.1%	1.1%	1.1%
Net Interest Inc/ Avg Assets (NIM)	3.6	3.6	3.7	3.9	3.9	4.0	Net Interest Inc/ Avg Assets (NIM)	3.2	3.1	3.3	3.1	3.1	3.1
Noninterest Inc/ Avg Assets	1.2	1.2	1.2	1.1	1.1	1.0	Noninterest Inc/ Avg Assets	2.4	2.4	2.7	2.2	2.2	2.3
Noninterest Exp/ Avg Assets	3.1	3.1	3.1	3.1	3.1	3.2	Noninterest Exp/ Avg Assets	3.2	3.2	3.6	3.2	3.2	3.3
Loans/Deposits	78.5	78.7	79.1	78.5	78.9	78.4	Loans/Deposits	93.2	90.6	95.8	90.4	89.2	93.1
Equity/Assets	9.0	9.0	9.3	9.4	9.4	9.5	Equity/Assets	9.5	9.5	8.5	8.8	8.8	8.2
Nonperforming Loans/ Total Loans	1.0	0.9	0.7	1.2	1.0	1.0	Nonperforming Loans/ Total Loans	1.5	1.3	1.3	1.8	1.5	1.5

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, 2001. 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 —200 for the tri-state area and 6099 for the nation; (2) large banking organizations —19 for the tri-state area and 99 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. Quarterly percentage changes are compound annualized rates.

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.