



BANKING BRIEF

FOR PENNSYLVANIA, NEW JERSEY, AND DELAWARE

Third Quarter 2006

Many of the trends established in the past year continued in the third quarter. Profitability, as measured by return on average assets (ROA), was essentially flat, and on an annual basis it decreased. Still, ROA is quite high by historical standards.¹ Net interest margins were flat at smaller banks both locally and nationally, while they declined at the large institutions.

Loan quality continued to deteriorate, with the ratio of nonperforming loans to total loans increasing slightly at both large banking organizations and community banks locally and nationally. At community banks, nonperforming commercial real-estate (CRE) and home equity loans (HE) accounted for the increase in the ratio of nonperforming loans to total loans. At the large organizations, real-estate loan quality in general declined, with increases in nonperforming CRE, mortgage, and HE loans.

Mortgages in 2005

In September 2006 the Federal Financial Institutions Examination Council (FFIEC) released data on mortgage lending transactions in 2005 at commercial banks, savings associations, credit unions, and mortgage companies covered by the Home Mortgage Disclosure Act (HMDA). The transactions include mortgages, home improvement loans, and refinancings. The information also includes the disposition of the application (whether it was approved, denied, or withdrawn) and, since last year, interest rate data on higher-priced loans.²

The number of applications in the nation for all types of loans increased 8.3 percent in 2005. Home mortgage applications rose 19.9 percent. Total originations increased by only 4.0 percent nationally; home mortgage originations rose 15.8 percent. In the tri-state area, total applications were up 7.4 percent and mortgage applications rose 15.3 percent. Total originations increased 3.4 percent, and home mortgage originations increased 10.0 percent. Mortgage refinancings declined both locally and nationally.

The national denial rate on home purchase loans dropped slightly from last year, from 15 to 14 percent, but in the tri-state area the rate rose from 9.2 percent to 13.3 percent. As in the past, denial rates vary among ethnic groups (see chart).³ As would be expected, income is a major factor in the denial rates for home mortgages. Nationally, applications from low- or moderate-income persons were denied 18.7 percent of the time. Middle-income persons were denied 13.0 percent of the time; upper-income persons had a denial rate of 11.5 percent.⁴ The comparable denial rates in the tri-state area were 17.0, 11.4, and 9.4 percent, respectively.

The incidence of higher-cost mortgages also appears to vary by ethnicity, as shown in the chart. Blacks and Hispanics were the most likely to receive a high-priced loan; whites and Asians were the least likely. The overall incidence of higher-priced loans in 2005 was influenced by several factors, including interest rates, the lender, and characteristics related to credit risk (such as income and loan amount). After adjusting for these effects, the incidence of higher-priced mortgages in the national data was 23 percent for blacks, 18 percent for Hispanics, 15 percent for whites, and 14 percent for Asians.⁵ Also, the HMDA data do not include other information relevant to the credit decision (such as the loan-to-value ratio and a credit score). The inclusion of such information in the analysis could alter the disparity across ethnic groups.

¹ The historical weighted average ROA from 1989 to 2004 is approximately 1.13 percent. See FDIC Historical Statistics on Banking at www2.fdic.gov/hsob/SelectRpt.asp?EntryTyp=10.

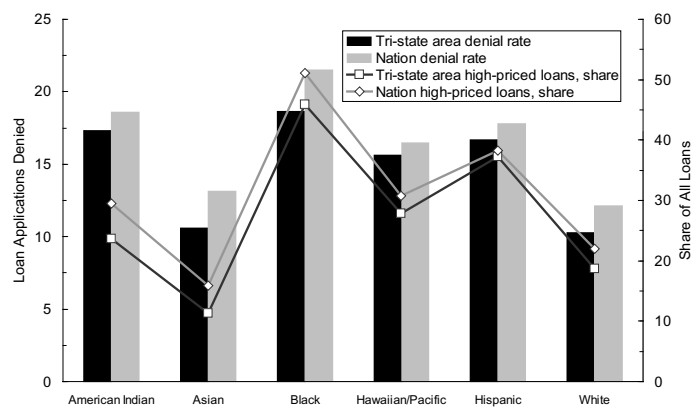
² Specifically, lenders are required to report interest rate spreads if the annual percentage rate (APR) on the loan exceeds the APR on U.S. Treasury securities of comparable maturity by three percentage points on first liens and five percentage points on junior liens.

³ The denial rates reported are on all home purchase loans. A substantial number of applications (over 21 percent both locally and nationally) did not report race. The denial rate of these applications was approximately 19 percent nationally and 21 percent in the tri-state area.

⁴ Low and moderate income is defined as less than 80 percent of the median for the metropolitan area in which the person lives. Middle income is defined as between 80 and 120 percent of the MSA median, and upper income is defined as greater than 120 percent of the MSA median.

⁵ See Avery and Canner, "Higher-Priced Home Lending and the 2005 HMDA Data," *Federal Reserve Bulletin*, 2006, www.federalreserve.gov/pubs/bulletin/2006/hmda/bull06hmda.pdf.

Application Outcome and Loan Pricing



Third Quarter 2006

Community Banking Organizations

	Tri-State			Nation		
	\$Bill	% change from		\$Bill	% change from	
	06Q3	06Q2	05Q3	06Q3	06Q2	05Q3
Total Assets	92.1	5.38	5.74	1692.7	7.14	8.13
Total Loans	62.0	7.32	10.14	1166.2	10.31	11.42
Business	8.5	2.61	7.34	179.9	7.88	9.78
Real Estate	49.0	8.16	11.48	853.9	10.77	12.77
Consumer	2.6	-1.76	-5.23	69.3	1.20	-0.98
Total Deposits	72.3	7.45	6.86	1343.5	6.28	8.22
Ratios (in %)	06Q3	06Q2	05Q3	06Q3	06Q2	05Q3
Net Income/ Avg Assets (ROA)	1.13	1.14	1.16	1.21	1.20	1.23
Net Interest Inc/ Avg Assets (NIM)	3.40	3.40	3.41	3.79	3.79	3.77
Noninterest Inc/ Avg Assets	1.17	1.16	1.15	0.94	0.95	0.99
Noninterest Exp/ Avg Assets	2.91	2.90	2.90	2.92	2.93	2.93
Loans/Deposits	85.70	85.73	83.16	86.8	86.00	84.3
Equity/Assets	10.36	10.36	10.14	9.99	9.99	9.77
Nonperforming Loans/ Total Loans	0.78	0.75	0.57	0.70	0.66	0.64

Large Banking Organizations

	Tri-State			Nation		
	\$Bill	% change from		\$Bill	% change from	
	06Q3	06Q2	05Q3	06Q3	06Q2	05Q3
Total Assets	2363.3	4.39	8.00	7477.8	6.52	9.75
Total Loans	1306.8	2.07	10.89	4176.7	3.62	8.25
Business	261.7	-2.65	11.81	879.5	5.30	12.55
Real Estate	780.9	2.82	11.88	2254.2	4.63	8.67
Consumer	107.9	13.02	7.58	554	8.41	2.13
Total Deposits	1527.8	7.08	5.37	4822.6	2.87	9.08
Ratios (in %)	06Q3	06Q2	05Q3	06Q3	06Q2	05Q3
Net Income/ Avg Assets (ROA)	1.28	1.29	1.39	1.24	1.25	1.24
Net Interest Inc/ Avg Assets (NIM)	2.57	2.61	2.75	2.70	2.73	2.80
Noninterest Inc/ Avg Assets	2.00	1.96	1.98	2.30	2.33	2.29
Noninterest Exp/ Avg Assets	2.57	2.58	2.64	2.95	2.98	3.05
Loans/Deposits	85.53	86.56	81.27	86.61	86.45	87.27
Equity/Assets	9.88	9.88	9.87	9.56	9.56	9.59
Nonperforming Loans/ Total Loans	0.43	0.40	0.45	0.71	0.67	0.67

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, 2005. 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 their deposits in 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 — 181 for the tri-state area and 5751 for the nation; (2) large banking organizations — 18 for the tri-state area and 102 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 Jim DiSalvo at (215) 574-3820 or jim.disalvo@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 website at www.philadelphiafed.org/econ/bb/index.html. To subscribe to this publication, please go to http://www.philadelphiafed.org/phil_mailing_list/dsp_user_login.cfm.