BANKING BRIEF

FOR PENNSYLVANIA, NEW JERSEY, AND DELAWARE

Third Quarter 2008

Profitability continued to decline sharply in the third quarter, with large financial organizations particularly hard hit. Asset quality problems – especially real estate loans – continue to be a drag on earnings at banks in all categories (see below). At both large organizations and community banks, the ratio of nonperforming loans to total loans continued to increase. Capital ratios fell slightly in the quarter. Net interest margins and expense ratios have remained relatively stable. Deposits grew at all categories of institutions, possibly due to customers switching their assets from stocks and other investments.

Profitability at large organizations as measured by return on average assets (ROAA) dropped to 0.23 percent nationally and 0.12 percent locally (see table on the last page).[1] Moreover, the number of institutions reporting negative net income in the quarter increased from 16 in the second quarter to 22 in the third quarter nationally (out of 99 organizations). At tri-state area banks, this number remained at three (out of 18 organizations). The main problem continues to be residential real estate (RRE) loans, with commercial real estate (CRE) also a concern.[2] In addition to losses from bad loans, large organizations had substantial losses on securities and asset sales in the quarter.

ROAA at community banks was more than double that of the large organizations in the third quarter, but the smaller banks have substantial problems as well. Nationally, the number of community banks reporting negative quarterly net income rose from 627 to 826 (out of 5,595), and locally this number rose from 25 to 33 (out of 174). Their nonperforming loan ratios continue to rise, led by CRE loans, especially construction loans. Moreover, as will be shown below, some of these institutions are substantially under-reserved.

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[1] Unless otherwise noted, all financial data are from Federal Financial Institutions Examination Council call reports. Growth numbers in the table on the back page are annualized, but numbers presented in the text and figures are not. One large organization in the national sample, JPMorgan Chase & Company (Chase), acquired Washington Mutual Bank (WAMU) in the third quarter. WAMU was a thrift institution and as such its balance sheet is not included before the third quarter. At the time it was acquired, WAMU had total assets of $307 billion, total loans of $233 billion, real estate loans of $229 billion, and total deposits of $188 billion. Therefore, the numbers presented in the table, in the text below, and in the charts do not include Chase. This exclusion is temporary to avoid distortions in the data. For the third quarter, bank subsidiaries of Chase that would otherwise have been included in the sample had total assets of $1.77 trillion, total loans of $703.4 billion (commercial $142.8 billion, real estate $370.3 billion, consumer $96.5 billion), total deposits of $1.01 trillion, and net income of $6.29 billion.

[2] RRE loans are defined as the sum of mortgages secured by first liens, mortgages secured by junior liens, and home equity lines of credit. CRE loans are defined as the sum of construction and land development loans, mortgages secured by multifamily properties, and loans secured by nonfarm, nonresidential properties.

Large Organizations

While profits continued to fall at large organizations, the ratio of nonperforming loans to total loans kept climbing both locally and nationally.[3] This ratio increased by 37 basis points nationally and 22 basis points locally in the third quarter. As during the last several quarters, the primary driver of the increase in nonperforming loans is RRE loans. RRE loans represent 30.9 percent of large organizations' loans nationally and 43.5 percent of their nonperforming loans. For tri-state area banks, these numbers are 34.0 percent of all loans and 49.2 percent of nonperforming loans. Nonperforming RRE loans increased 26.3 percent nationally in the third quarter and 31.6 locally. The ratio of nonperforming RRE loans to total RRE loans is now well over 3 percent both locally and nationally and continues to climb (Figure 1).

Net charge-offs at large organizations also continued to increase.[4] Total net charge-offs increased 17.5 percent nationally in the third quarter and 19.6 percent locally. The ratio of net charge-offs to average loans continued to increase in the quarter both locally and nationally (Figure 2). Both nationally and locally, over one-third of all net charge-offs were RRE loans. Net charge-offs of RRE loans increased 21.8 percent nationally and 12.1 percent locally in the third quarter.

The primary problems in RRE lending at large organizations have come from mortgages, particularly those secured by first liens. These make up a little over 60 percent of all RRE loans both locally and nationally, and they account for over 80 percent of nonperforming RRE loans and roughly half of net charge-offs in both areas. Home equity lines of credit (HELOCs) account for about 10 percent of total loans both locally and nationally, 4.8 percent of nonperforming loans nationally and 6.4 percent locally, and slightly over 12 percent of net charge-offs both locally and nationally. Mortgages secured by junior liens account for about 3 percent of total loans both locally and nationally and roughly the same percentage of nonperforming loans. They account for 7.8 percent of net charge-offs nationally and 5.6 percent locally. Growth of nonperformers and charge-offs for HELOCs and junior lien mortgages was similar to that of first lien mortgages. It is important to note that nonperforming HELOCs and junior lien loans often become total losses, while at least some percentage of senior lien loans are usually recovered through asset sales.[5]

For managed loans the numbers were not much better.[6] Nonperforming loans there make up 2.2 percent of these loans nationally and 2.1 percent locally. The ratio of net charge-offs to average managed loans is 0.33 percent nationally and 0.45 percent locally. Likewise for managed RRE loans, where nonperforming RRE loans are 2.7 percent of all RRE loans nationally and 3.2 percent locally. However, for both total loans and RRE loans, the growth rates for nonperforming managed loans and net charge-offs are roughly the same as for total loans.

In addition to the problems with RRE loans, large organizations are facing increasing problems

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[3] Nonperforming loans are defined as loans past due 90 days or more plus nonaccruing loans. For historical perspective, the nonperforming loan ratio for all commercial banks between 1997 and 2007 was 1.07 percent. However, at the bottom of the last real estate cycle in 1991, this ratio was 3.70 percent. Source: FDIC Historical Statistics on Banking: www2.fdic.gov/hsob/index.asp.

[4] Unless otherwise noted, all income statement items are on a quarterly basis. That is, only the amounts actually booked in the quarter are shown, as opposed to the year-to-date numbers on the actual call reports.

[5] The ratio of recoveries to charge-offs at large organizations nationally was 9.9 percent. This ratio was 2.8 percent for RRE loans, 2.7 percent for mortgages, 3.0 percent for junior lien mortgages, and 0.03 percent for HELOCs. The corresponding numbers for tri-state area banks are 9.7 percent for all loans, 3.4 percent for RRE loans, 4.0 percent for mortgages, 4.2 percent for junior lien mortgages, and 0.02 percent for HELOCs. For historical perspective, the ratio for all loans between 1997 and 2007 was 19.9 percent. At the bottom of the last real estate cycle in 1991 this ratio was 12.0 percent. Source: FDIC Historical Statistics on Banking: www2.fdic.gov/hsob/index.asp.

[6] Managed loans are loans outstanding plus loans securitized and sold where the latter is done with recourse.

Figure 1

Nonperforming RRE Loans/Total RRE Loans

Large Organizations

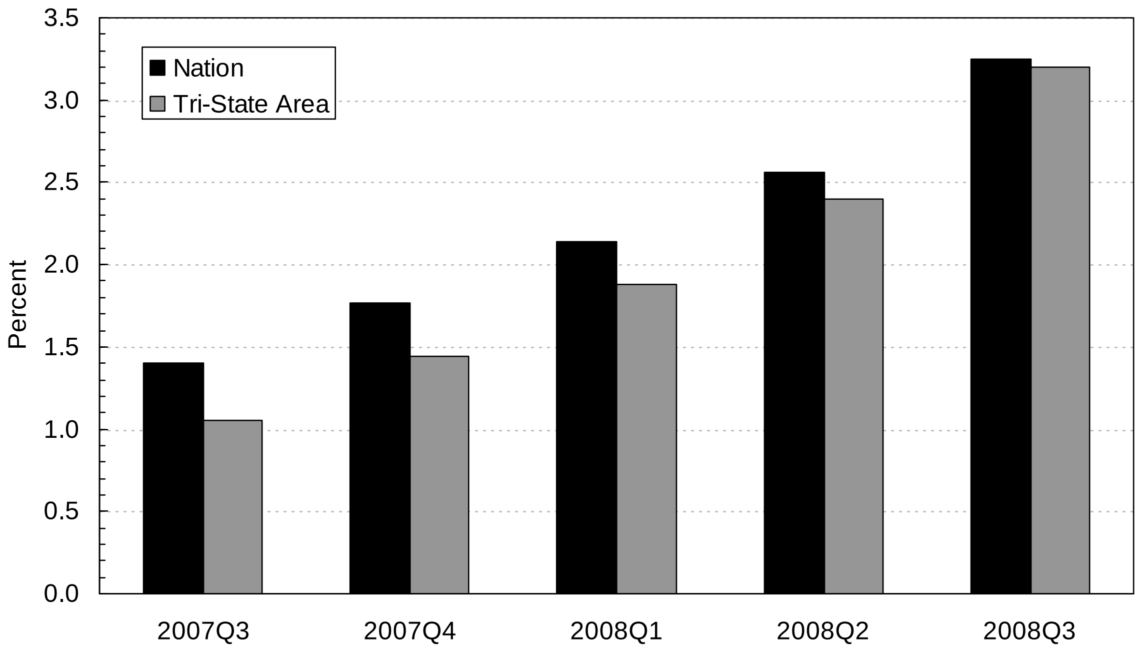
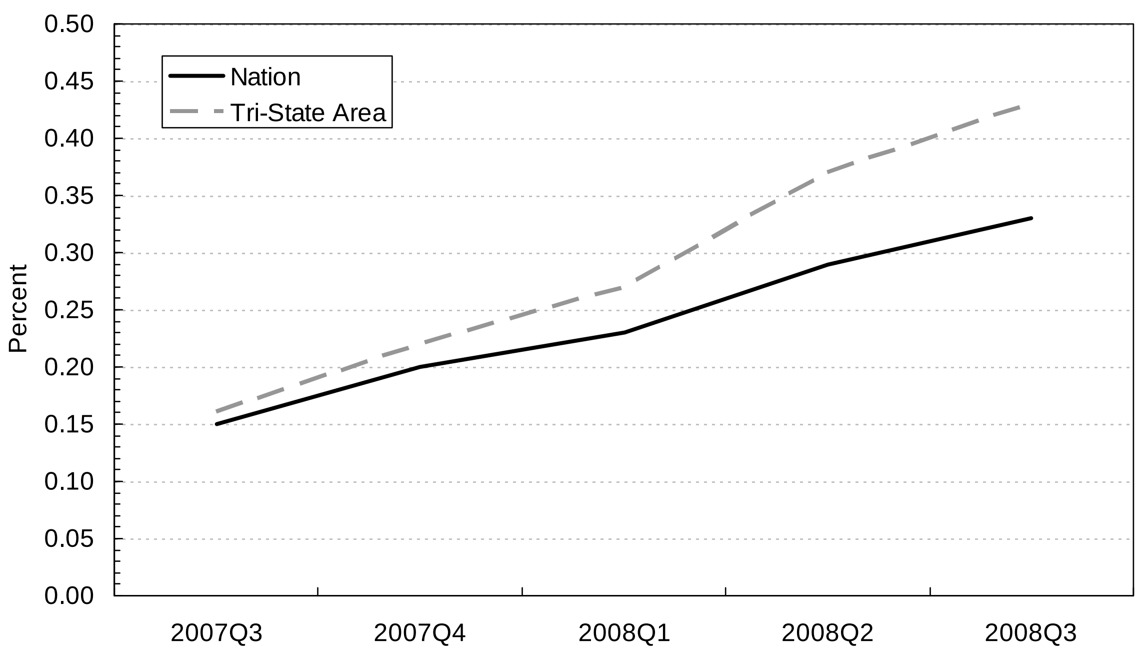


Figure 2

Quarterly Net Charge-Offs/Average Loans

Large Organizations



with CRE loans. These represent 20.1 percent of all loans nationally and 16.7 percent locally. Nonperforming CRE loans continued to grow in the third quarter: 22.5 percent nationally and 22.1 percent locally. The ratio of nonperforming CRE loans to total CRE loans is now roughly the same as that for RRE loans (Figure 3). Net charge-offs of CRE loans increased only 11.2 percent nationally but were up 35.8 percent locally in the quarter. As a percentage of average loans they were 0.27 percent for banks in the tri-state area, up from 0.21 percent in the second quarter, and 0.33 percent nationally, barely changed from 0.30 percent in the previous quarter.

The vast majority of the large organizations' problems with CRE loans can be traced to construction lending. While these loans represent only about one-third of CRE lending both locally and nationally, they account for approximately three-quarters of the nonperforming CRE loans and slightly under 90 percent of charge-offs on CRE loans. Nonperforming construction loans now represent nearly 7.6 percent of all construction loans nationwide and 8 percent of construction loans at tri-state area banks (Figure 4), and net charge-offs on construction loans as a percentage of average construction loans are nearly double the charge-off rate for all loans (Figure 5). While there are little data to support this, anecdotal evidence suggests that much of the nonperforming and charged-off construction loans were for residential real estate construction.[7]

Other types of loans are performing much better than real estate, but they are still affected. The ratio of nonperforming commercial and industrial (C&I) loans to C&I loans is only 0.9 percent nationally and 1.0 percent locally, and the ratio of net charge-offs on C&I loans to average C&I loans was 0.2 percent nationally and 0.3 percent locally.[8] Both of these showed small increases in the third quarter. Total nonperforming C&I loans increased 15.2 percent in the third quarter nationally and 8.5 percent locally, while net charge-offs on C&I loans increased 27.9 percent nationally and 15.4 percent locally.

The ratio of nonperforming consumer loans to total consumer loans was 1.6 percent nationally and 1.7 percent locally. The majority of nonperforming consumer loans were credit cards, 51 percent in the nation and 63 percent in the tri-state area.[9] The ratio of nonperforming credit card loans to total credit card loans was 2.8 percent nationally and 2.6 percent locally, and these numbers haven't changed substantially in the last year. The situation with charge-offs is only slightly worse. The ratio of net charge-offs on credit card loans to average credit card loans was 1.4 percent nationally and 1.5 percent locally. These ratios have increased about 15 to 20 basis points in the last year but have not risen substantially in the last quarter or two.

The increase in nonperforming loans and charge-offs is taking a toll on the large organizations' provisioning as well. This directly affects their profitability because loan-loss provisions (the income statement item for addition to loan-loss reserves) comes directly out of revenues. Loan-loss provisions are now approximately one-third of operating income, whereas a year ago they were about 10 percent (Figure 6).[10] This situation is likely to continue for some time as increases in loan-loss reserves are not keeping up with the rise in nonperforming loans and charge-offs. The ratio of net charge-offs to loan-loss provision has not decreased in the last several quarters both locally and nationally (Figure 7). The loan-loss coverage ratios of large organizations are now at or below 100 percent

[7] Call report data do not differentiate between the purposes of construction loans; therefore, it is impossible to state whether a particular institution lends primarily to finance residential construction or commercial construction.

[8] C&I loans represent 22-23 percent of all loans both locally and nationally.

[9] Consumer loans represent approximately 15 percent of all loans both locally and nationally, and roughly a third of consumer loans are credit card loans in both categories. There has been speculation in the press and elsewhere that the quality of credit card loans is going to fall substantially in the near future. This may or may not be the case, but the numbers are not showing a substantial decline in this area.

[10] Operating income is defined as the sum of net interest income and noninterest income.

Figure 3

Nonperforming CRE Lns/CRE Lns

Large Organizations

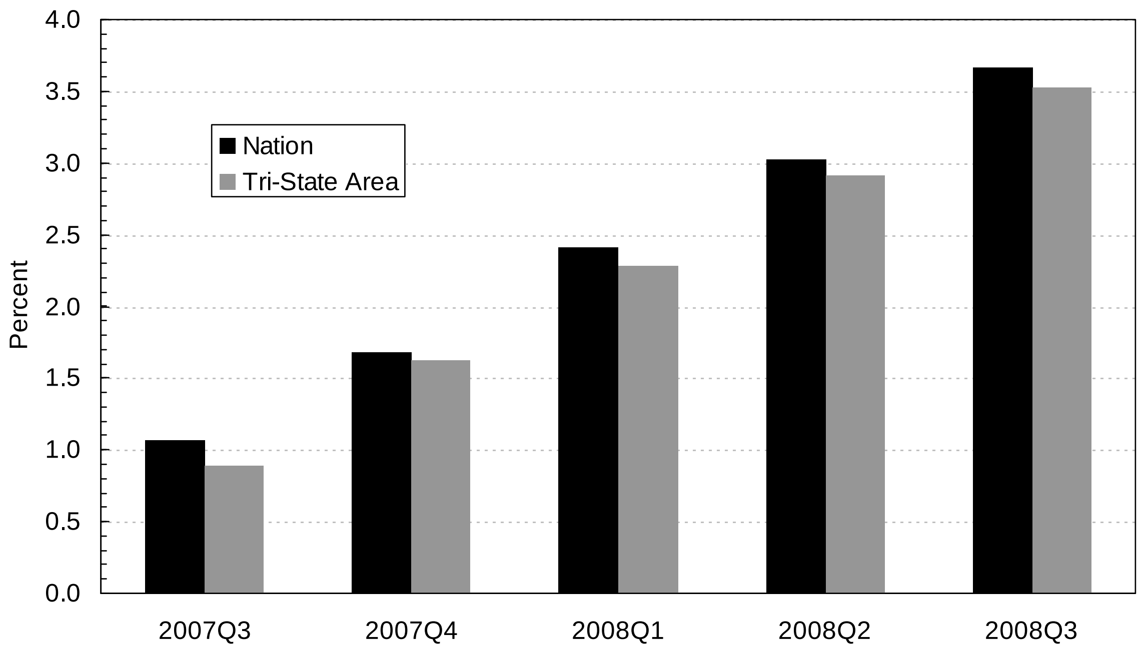
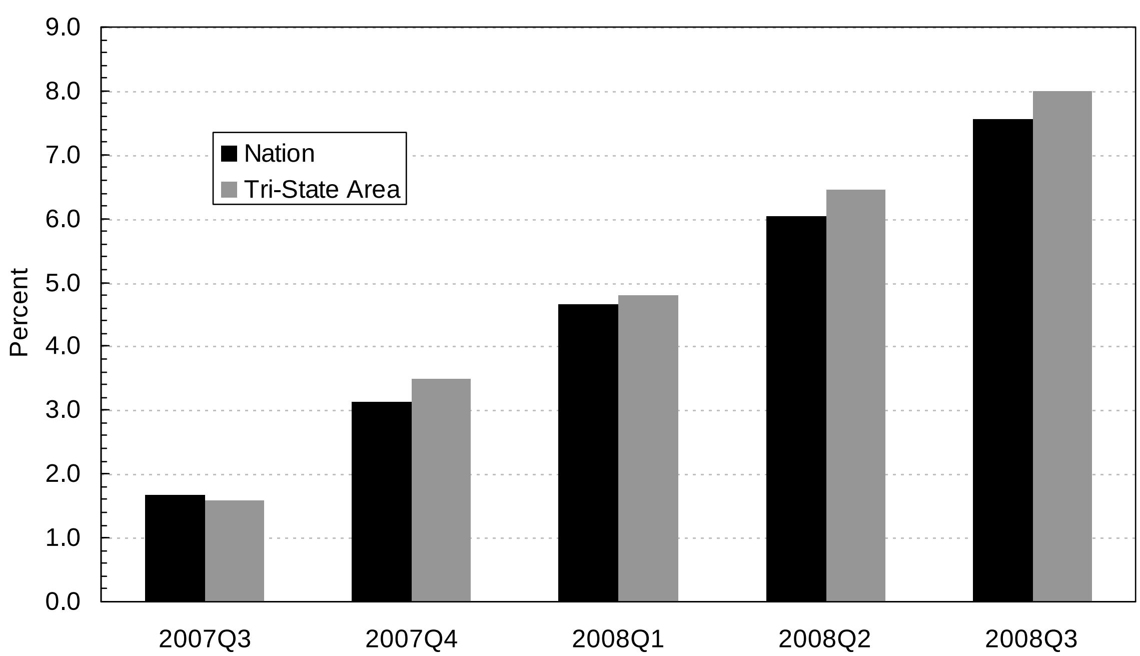


Figure 4

Nonperforming Construction Lns/Construction Lns

Large Organizations



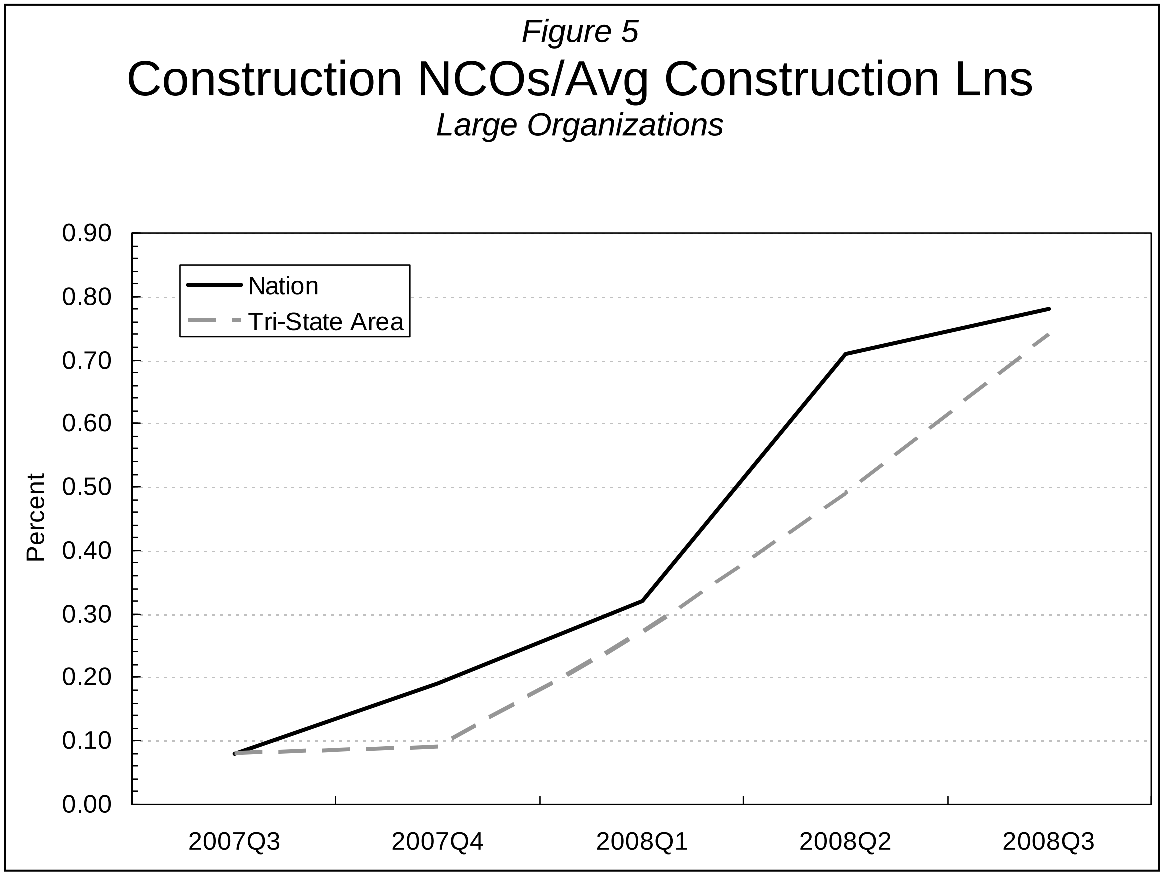


Figure 5
Construction NCOs/Avg Construction Lns
Large Organizations
0.90
0.80
0.70
0.60
0.50
0.40
0.30
0.20
0.10
0.00
Percent
Nation
Tri-State Area
2007Q3
2007Q4
2008Q1
2008Q2
2008Q3

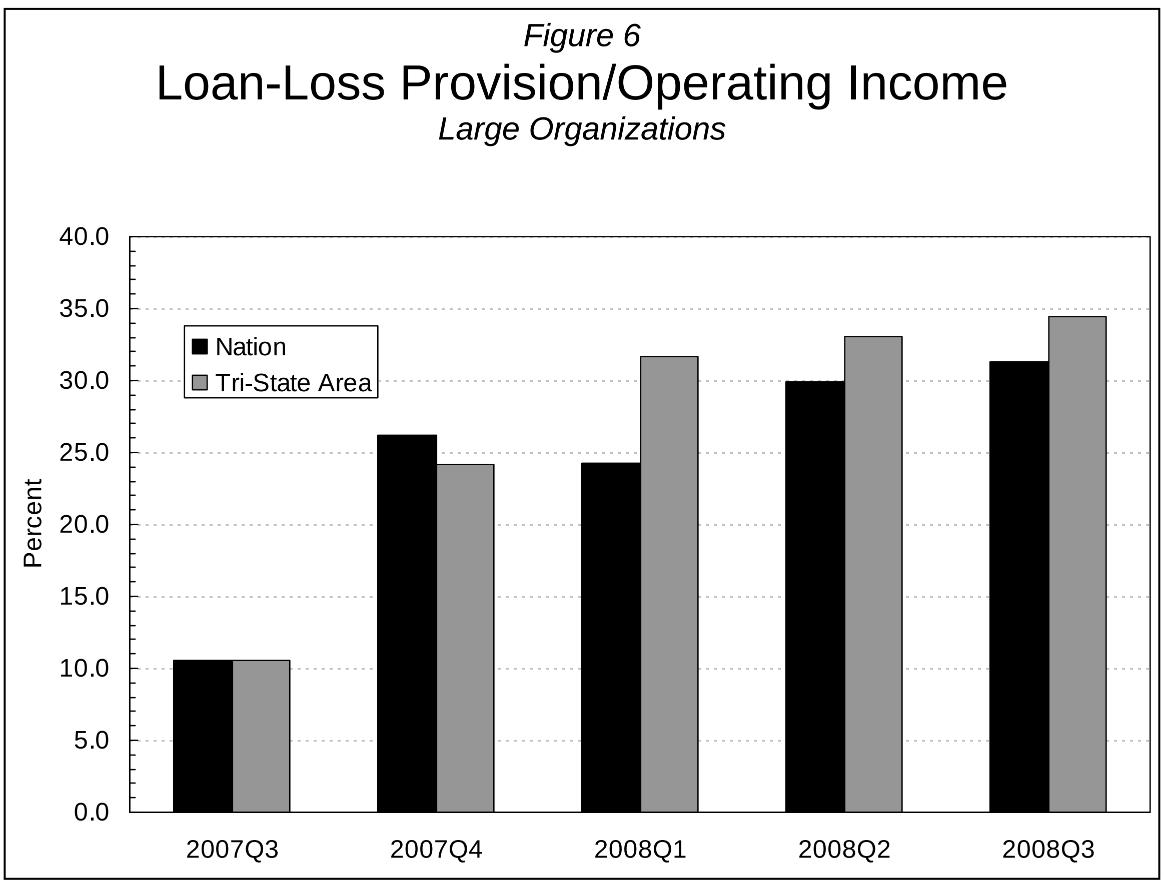
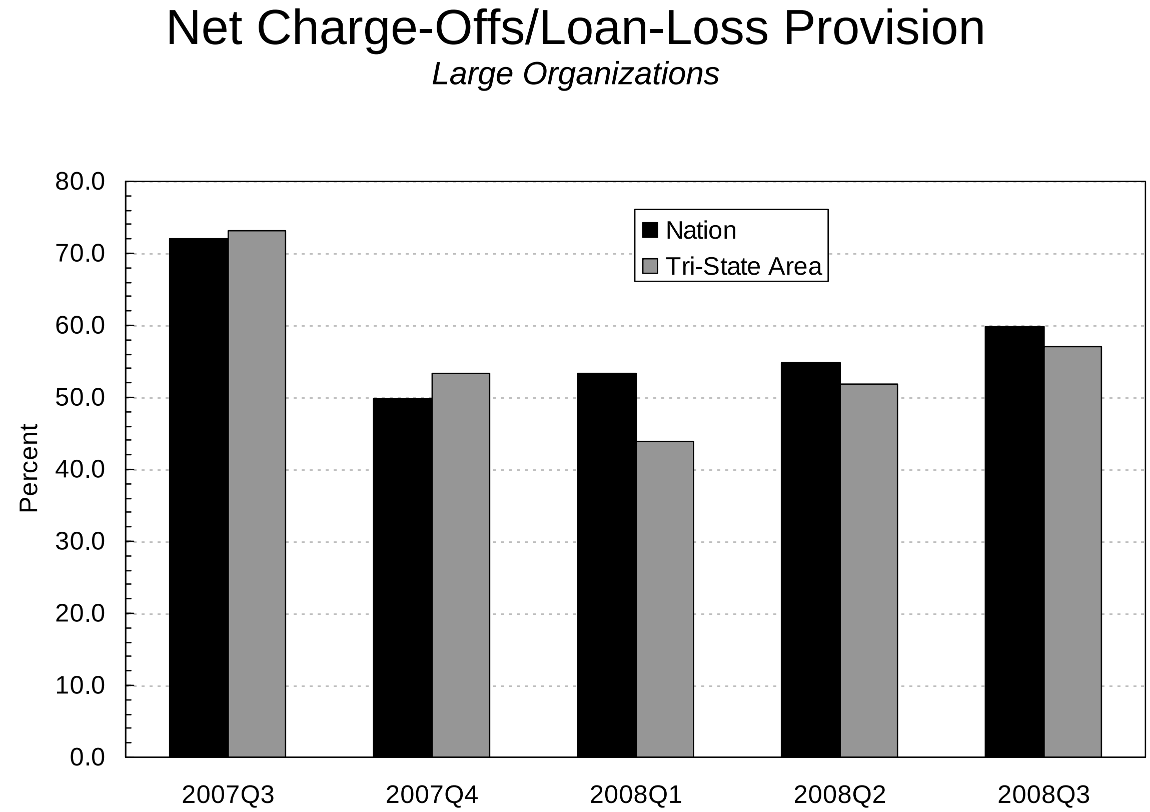


Figure 6
Loan-Loss Provision/Operating Income
Large Organizations
40.0
35.0
30.0
25.0
20.0
15.0
10.0
5.0
0.0
Percent
Nation
Tri-State Area
2007Q3
2007Q4
2008Q1
2008Q2
2008Q3

Figure 7



(Figure 8).[11] This means that if all nonperforming loans currently on the banks' books were charged off immediately, their reserves would not be sufficient to cover the losses and the remainder would be charged directly to capital. Loan-loss reserves grew 14.7 percent nationally and 17.0 percent locally, but both are insufficient to match the growth of nonperforming loans and net charge-offs (see above).

Loan growth has slowed to a crawl at these banks, and this situation is likely to continue for some time (see last page). It appears that most loans currently being made by large organizations are from preexisting lines of credit, and these lines are being drawn down. Total unused commitments (not including credit cards) decreased 9.7 percent nationally and 11.5 percent locally in the third quarter.[12] As a percentage of assets they had been decreasing gradually for at least a year, but they fell at a sharper rate in the third quarter (Figure 9).

In addition, banks are losing money on assets other than loans as well. Realized losses on securities exploded in the third quarter, with banks nationally losing $4.4 billion and tri-state area banks $2.4 billion (Figure 10).[13] At banks nationwide, mortgage-backed securities (MBS) issued by the government (GNMA) and

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[11] The loan-loss coverage ratio is the ratio of loan-loss provision to nonperforming loans. For historical perspective, the loan-loss coverage ratio for all commercial banks between 1997 and 2007 was 146.4 percent. At the bottom of the last real estate cycle in 1991, this ratio was 72.6 percent. Source: FDIC Historical Statistics on Banking: www2.fdic.gov/hsob/index.asp.

[12] Unused commitments include home equity lines of credit, credit card lines, secured commitments to fund one- to four-family housing construction, secured commitments to fund other real estate construction, commitments to fund construction that are not secured, commitments to underwrite securities, financial standby letters of credit, performance standby letters of credit, commercial letters of credit, and securities lent.

[13] Realized gains and losses on securities as reported are a net position. Thus, although tri-state area banks are a subset of the national sample, their total can exceed that of banks nationally. The securities discussed here do not include trading account securities.

Figure 8

Loan-Loss Coverage Ratios

Large Organizations

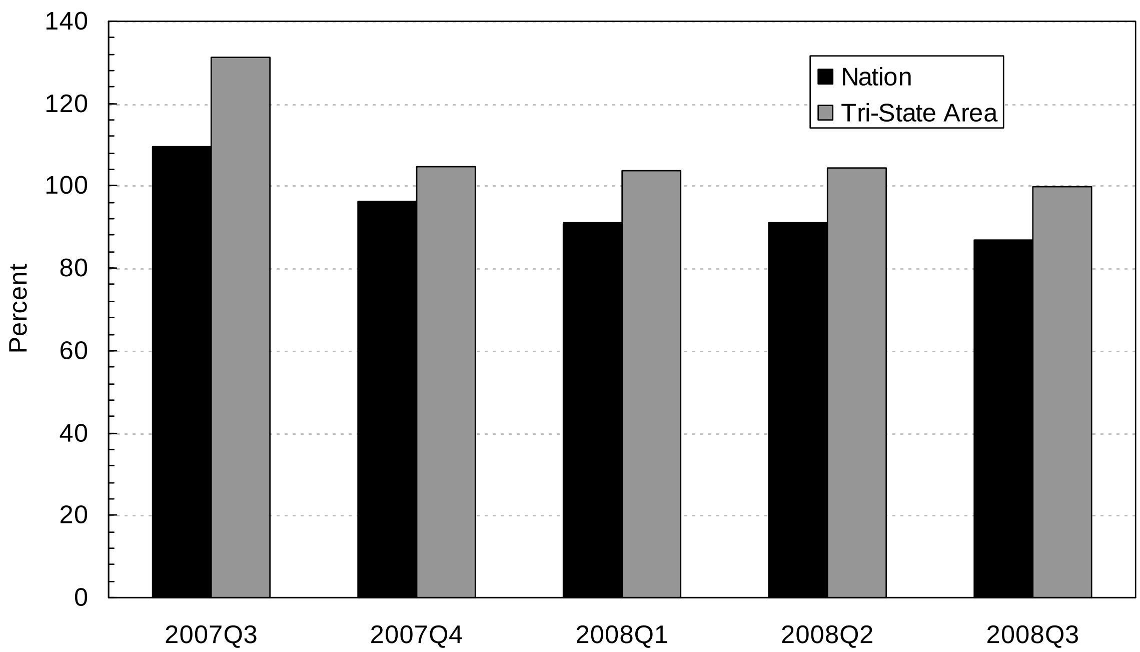


Figure 9

Unused Commitments/Assets
Excluding Unused Lines on Credit Cards

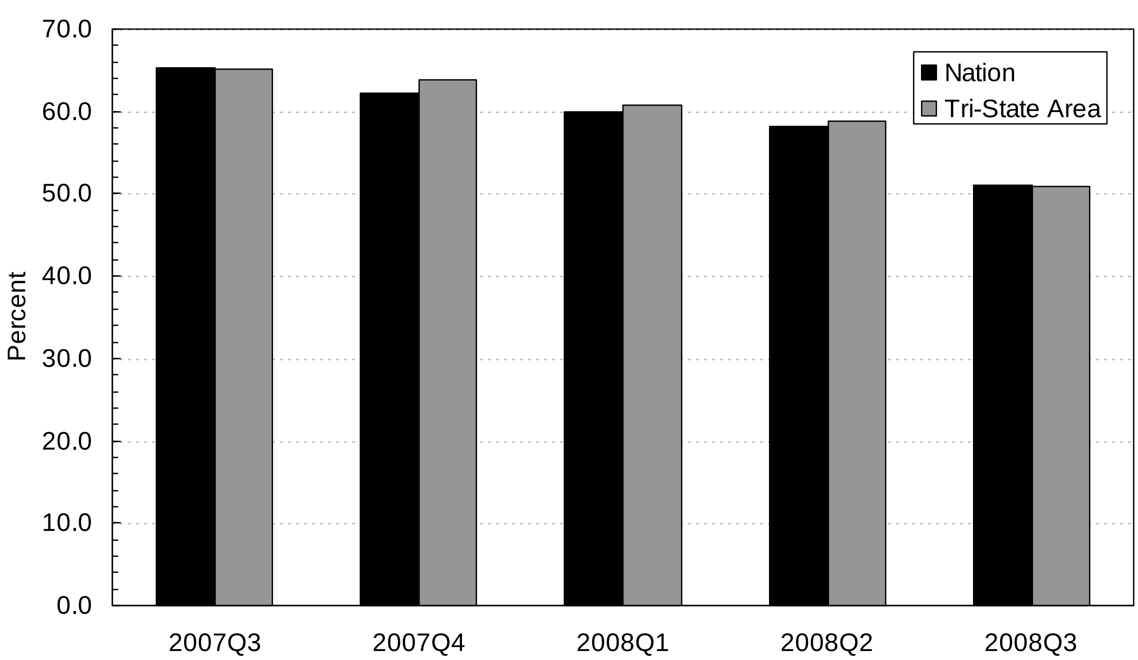


Figure 10

Realized Gains/Losses on Securities

Large Organizations

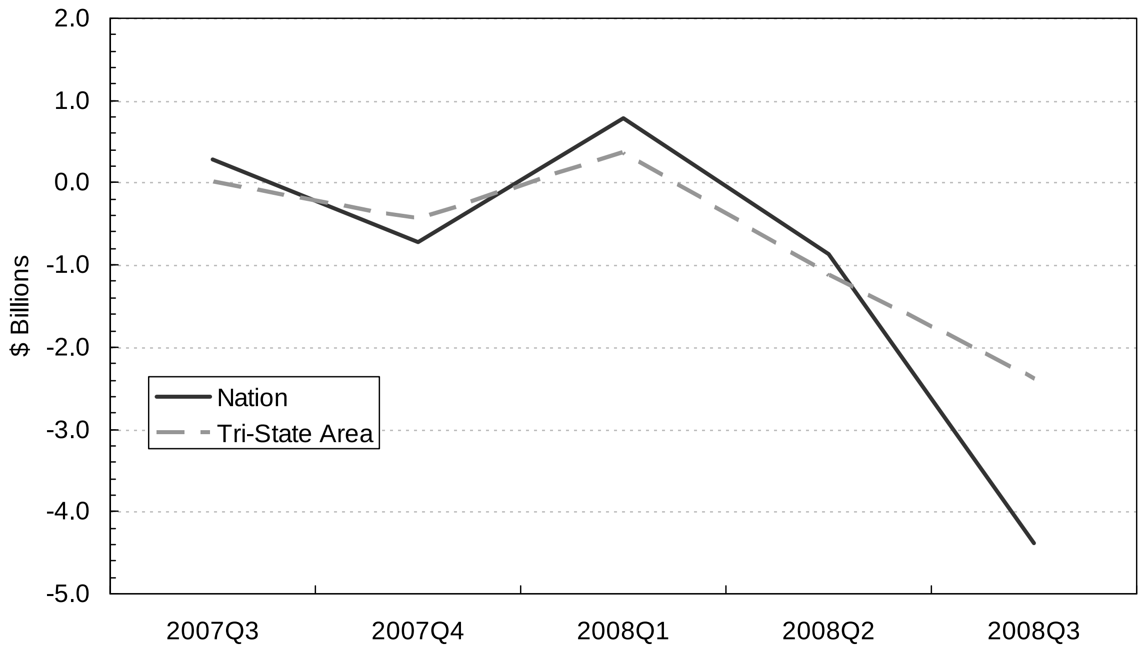
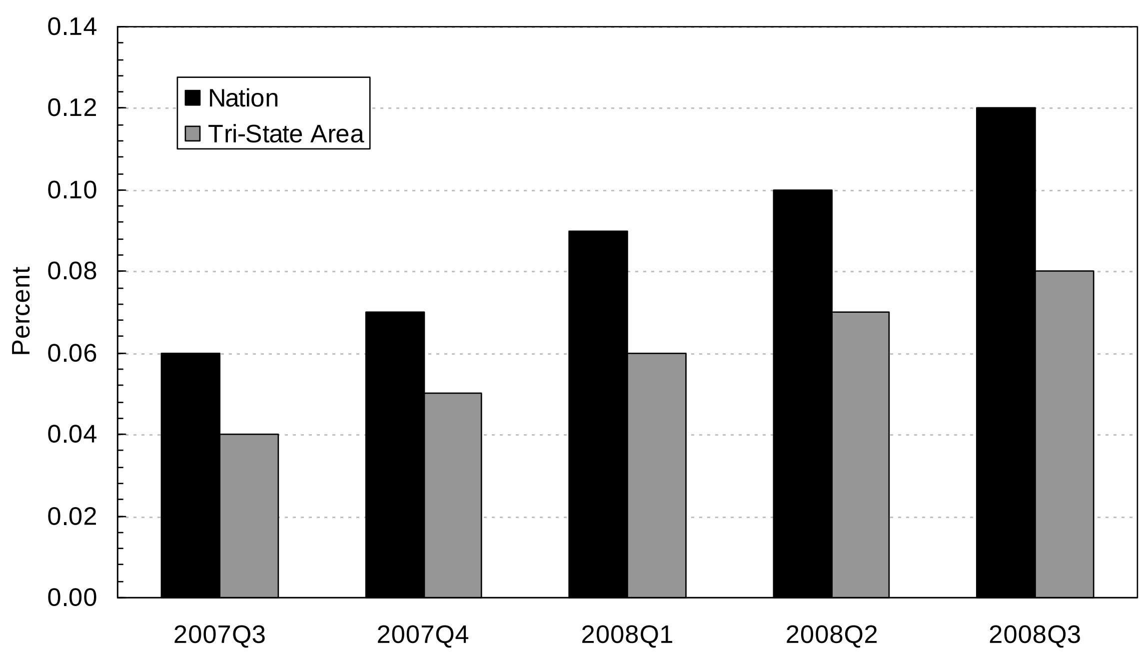


Figure 11

Other Real Estate Owned/Total Assets

Large Organizations



government-sponsored enterprises (FNMA and FHLMC, hereafter referred to as GSEs) represent 48.0 percent of banks' portfolios (by reported value), and the number for the tri-state area is 56.9 percent.[14] Other securities that make up a significant part of the portfolios are MBS from private issuers (15.5 percent nationally and 19.1 percent locally), other asset-backed securities (14.3 and 11.1 percent, respectively), foreign debt securities (7.1 and 4.8 percent), and securities of state and local governments (5.8 and 3.7 percent). It should be noted that asset-backed securities (ABS) increased from 7.5 percent of total securities to 14.3 percent nationally and from 8.8 to 11.1 percent locally. One possible reason for the increases in ABS is that banks are purchasing them from unconsolidated affiliates such as structured investment vehicles (SIV).

Large organizations saw a substantial drop in income from asset sales in the third quarter and, in some categories, saw substantial losses. Total income from asset sales fell 53.3 percent nationwide and 86.1 percent at tri-state area banks in the quarter. The recent turmoil in the financial markets has nearly shut down the market for securitizing loans, and income from loan sales fell 58.5 percent nationally and 75.8 percent locally. However, income from loan sales is still positive. Banks have been experiencing absolute losses in sales of other real estate owned (OREO), and this can be directly tied to their real estate loan problems.[15]

OREO increased 18.6 percent nationwide and 18.3 percent locally in the third quarter. As a percentage of assets, it has doubled both nationally and locally in the past year (Figure 11). While it represents a relatively small share of the large organizations' balance sheets, it is regarded as a nonperforming asset because banks earn nothing on OREO. Losses on OREO in the third quarter were $310.4 million nationally and $72.8 million locally, and the losses increased 22.4 and 11.4 percent, respectively. As long as the residential real estate markets continue to slump, these losses will increase.

In summary, large organizations continue to experience substantial problems in their real estate loan portfolios. Nonperforming loans and net charge-offs continued to increase in the third quarter, but at a decreasing rate. However, it is too early to state with any certainty that the inflection point in this loan cycle has been reached. There are also substantial weaknesses in the banks' securities portfolios; they are heavily weighted in MBS, and other nonperforming assets such as OREO continue to be added to the balance sheets. The real estate loan problems will continue to be a significant drag on earnings for some time because the banks are under-reserved. Other assets such as C&I loans and the trading accounts are performing much better, but these are vulnerable to the general economic situation as well.

Community Banks

Tri-state area community banks are outperforming both large organizations and community banks nationwide. They have higher ROAA, asset growth, loan growth, and deposit growth.[16] However, there are many problems affecting community banks both nationwide and locally. First, capital ratios have fallen nearly 50 basis points both locally and nationally in the past year, and they continued to fall in the third quarter (see table on last page). The number of community banks with equity-to-asset ratios of less than 6 percent continued to climb as well.[17] In the nation, 68 out of 5,595 banks had an equity-to-assets ratio under 6 percent, an increase of 19 banks from the second quarter. For the tri-state area, the increase from the second to third quarter was only one, to six (out of 174). A second

[14] Securities are reported at book value if they are held to maturity and at market value if they are available for sale.

[15] OREO is basically foreclosed real estate.

[16] It is possible that much of the growth in real estate lending at these institutions is due to a slowdown in loan purchases at the GSEs.

[17] Regulation Y defines an institution as well-capitalized if it has a tier one leverage ratio of over 6 percent. Total equity contains some items not included in tier one capital, so this is not the same as saying they are well-capitalized for regulatory purposes. However, for most institutions, it is a close proxy.

problem for community banks nationwide is that they face some of the same asset quality problems the larger banks are facing, especially in CRE lending. Third, community banks both in the tri-state area and nationwide are now substantially under-reserved, yet some institutions continue to expand their loan commitments. Finally, the securities portfolios of community banks have substantial investments in state and municipal debt, which could become a problem soon.

The ratio of nonperforming loans to total loans increased 19 basis points nationally, to 2.47 percent, and nine basis points locally, to 1.60 percent. Total nonperforming loans increased 13.5 percent nationally and 11.3 percent locally. These increases are less than in the previous several quarters. Net charge-offs increased 21.8 percent nationally but decreased 28.7 percent locally. Also, net charge-offs as a percentage of average loans are substantially lower at community banks than the larger organizations (Figure 12).

Most of the asset quality problems community banks are experiencing are in CRE loans. These represent 47.7 percent of all loans at banks in the nation and 45.9 percent at banks locally. However, they comprise 71.7 percent and 68.2 percent of nonperforming loans, respectively. Nonperforming CRE loans increased 14.3 percent nationally and 12.3 percent locally in the third quarter. That these increases are slowing is good news. However, the ratio of nonperforming CRE loans to total CRE loans is now over 3 percent nationally, and it continues to increase locally (Figure 13).

Net charge-offs on CRE loans increased 32.8 percent nationally but dropped 54.1 percent locally. This decrease at tri-state area banks follows a large increase in the second quarter. Only about 40 institutions in the tri-state sample reported charge-offs on CRE loans in either quarter, so this most likely represents short-term fluctuations in the data. However, net charge-offs on CRE loans are still at a level almost double that of a year ago.

The major problems with CRE lending have been in construction loans. These comprise about one-third of all CRE loans nationally and less than one-quarter locally but represent over 70 percent of nonperforming CRE loans and 85 percent of net charge-offs for banks nationwide. The corresponding figures for banks in the tri-state area are 54 percent of nonperforming loans and 52 percent of net charge-offs. The ratio of nonperforming construction loans to total construction loans for community banks mirrors that for large organizations (Figure 14). Net charge-offs on construction loans increased 31.8 percent nationally but decreased 67.2 percent locally. The large local decrease follows a large increase in the second quarter followed by a decrease in the third quarter, the same swings seen in charge-offs of CRE loans. Net charge-offs on construction loans are only about 20 percent higher now than they were a year ago at local community banks.

The majority of CRE loans at community banks are loans secured by nonfarm, nonresidential properties. These account for about 60 percent of CRE loans nationally and over 70 percent locally. At banks nationwide, nonperforming loans in this category increased 21.2 percent and net charge-offs increased 14.6 percent. The corresponding figures for tri-state area banks were a 1.2 percent increase in nonperforming loans and a 23.7 percent decrease in net charge-offs. In spite of the increase at banks nationally, the ratio of nonperforming business property loans to total business property loans is still relatively low (but increasing), while this ratio fell in the third quarter at tri-state area banks (Figure 15).

The main reason community banks are performing better than large banks is that they've avoided many of the problems large organizations have had with RRE loans. RRE loans make up 22.0 percent of the loans of community banks nationally and about one-third of those at banks locally. However, the ratio of nonperforming RRE loans to total RRE loans is much lower at community banks (Figure 16). Moreover, nonperforming RRE loans increased only 13.6 percent nationally and 12.9 percent locally, and net charge-offs on RRE loans decreased by 15 percent nationally and were basically flat locally.

While community banks are undoubtedly in better shape than large organizations in terms of asset quality, there are some problems that could arise in the future. First, loan-loss reserves are

Figure 12

Quarterly Net Charge-Offs/Average Loans

Community Banks

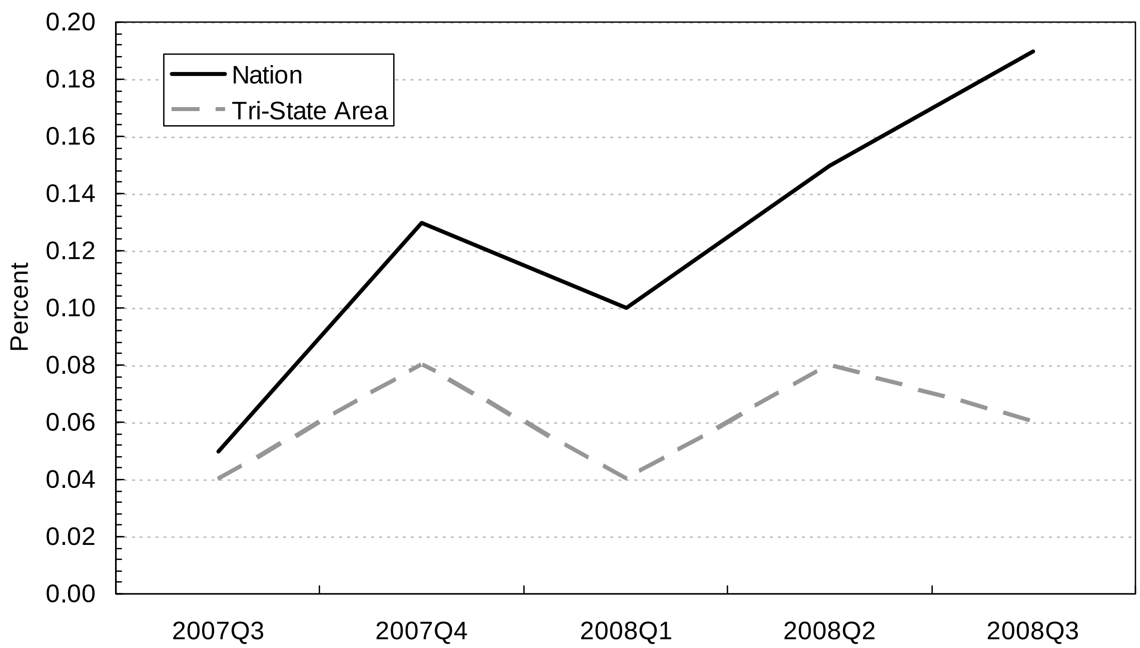


Figure 13

Nonperforming CRE Loans/Total CRE Loans

Community Banks

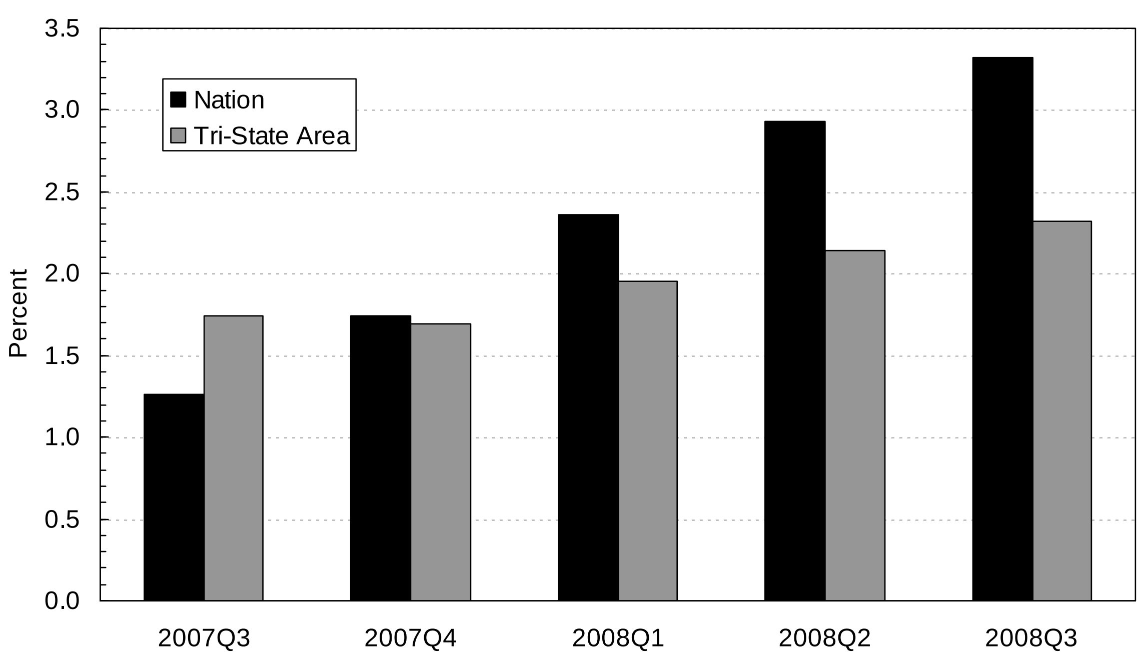


Figure 14

Nonperforming Construction Lns/Construction Lns

Community Banks

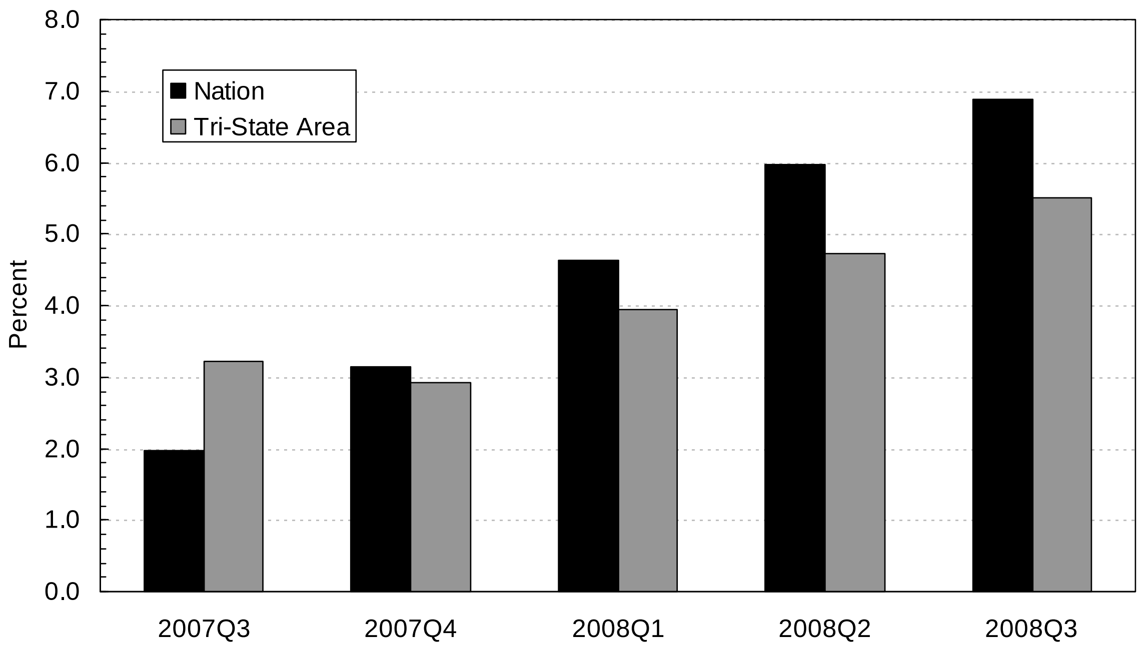
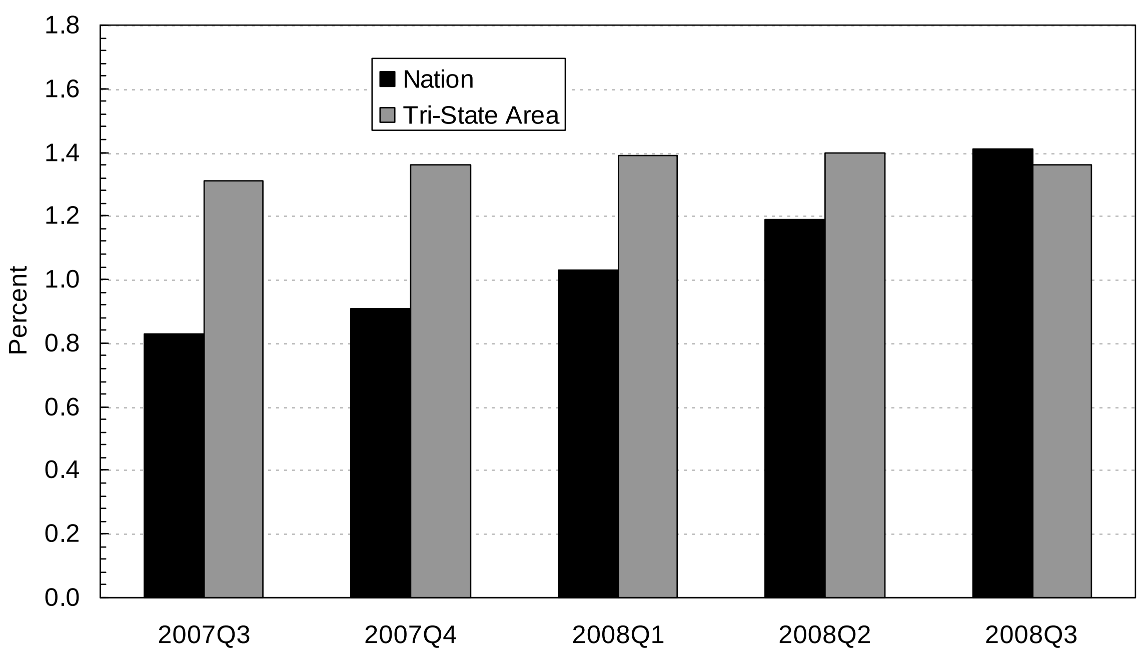
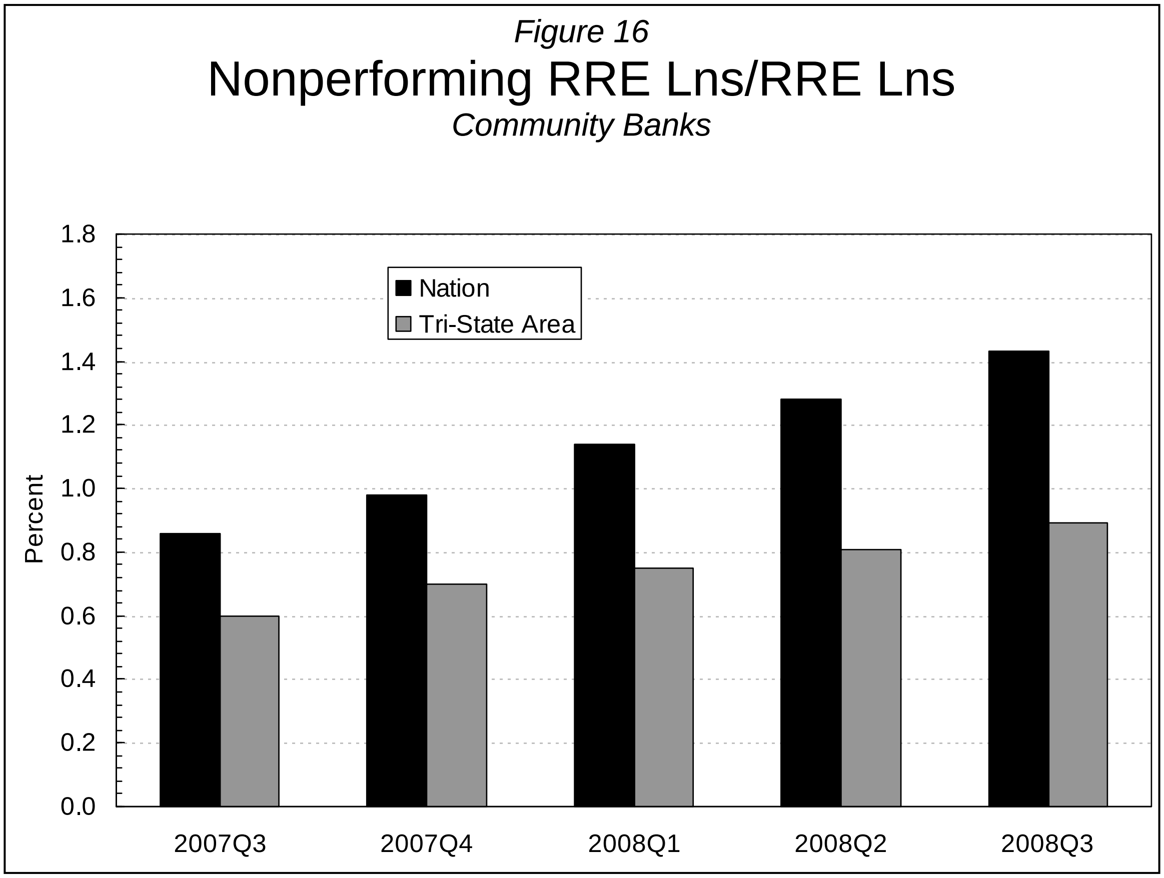


Figure 15

Nonperforming Business RE Lns/Business RE Lns

Community Banks





inadequate. The loan-loss coverage ratio stands at 65 percent nationally and slightly under 80 percent locally, and it continues to fall (Figure 17). Loan-loss provisions increased only 3.3 percent nationally and 4.9 percent locally. The ratio of net charge-offs to loan-loss provision is over 70 percent nationally and rising, while the ratio of loan-loss provision to operating income is falling (Figures 18 and 19). In spite of the need to increase reserves, community banks nationally paid out over 120 percent of their quarterly net income in dividends. Tri-state area banks paid out fewer dividends, less than 80 percent of income.

In addition to the problems with reserves, community banks both nationally and locally are carrying a substantial amount of OREO on their books. The ratio of OREO to total assets at community banks nationally is triple that of large organizations and substantially higher than that of community banks locally. The local banks are still carrying more than double the OREO of large organizations nationally (Figure 20). OREO also continues to grow: 25.3 percent nationally and 10.9 percent locally in the quarter.

A third potential problem is that community banks nationally are increasing their loan commitments. Total unused commitments (not including credit cards) increased 15.8 percent for banks nationwide while decreasing slightly at tri-state area banks. In part, this is because their commitments to fund real estate are falling at a slower rate than those at larger banks, but they've also expanded some commercial loan commitments. In addition, for the past year or so, community banks nationwide have been expanding their credit card commitments. Unused credit card lines have increased 37.8 percent at these banks in the last year, while actual credit card lending is up over 48 percent in that period. Much of the expansion in both actual lending and lines of credit has occurred in the last quarter or two. This is somewhat different from tri-state area banks, where credit card lending has increased 37.0 percent but unused lines of credit are down 8.2 percent. It is possible that these are commercial credit cards and the expansion of credit card lending and (outside the tri-state area) available credit is consistent with

Figure 17

Loan-Loss Coverage Ratios

Community Banks

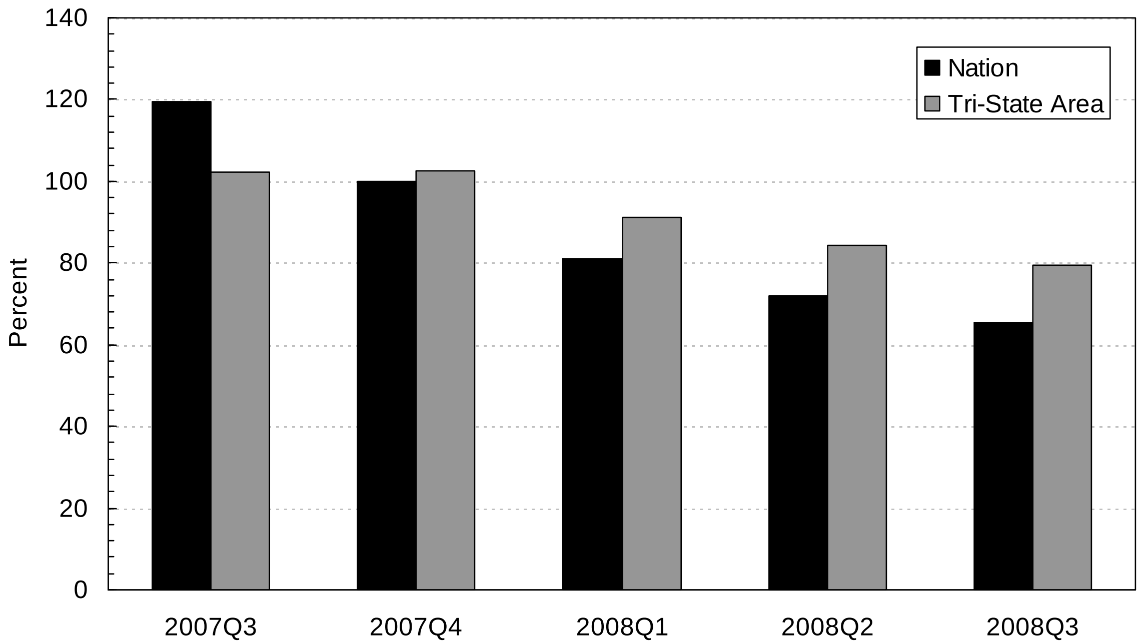
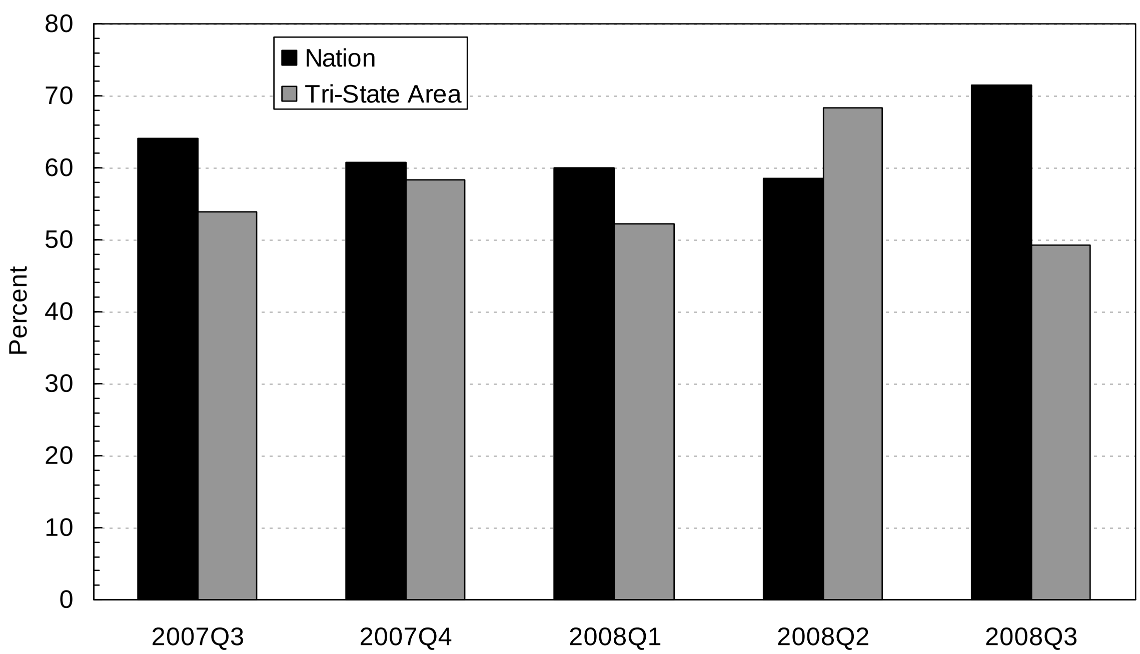


Figure 18

Net Charge-offs/Loan-Loss Provision

Community Banks



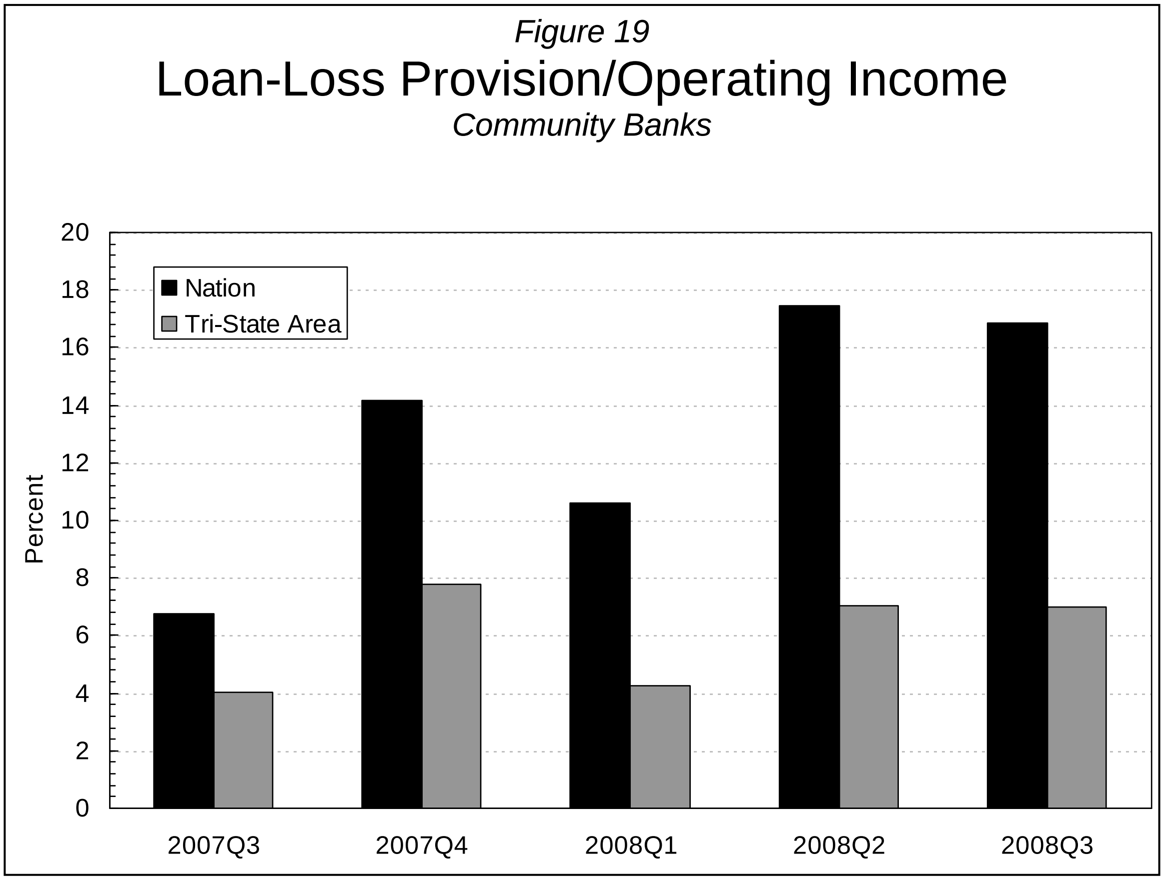


Figure 19
Loan-Loss Provision/Operating Income
Community Banks
Percent
20
18
16
14
12
10
8
6
4
2
0
Nation
Tri-State Area
2007Q3
2007Q4
2008Q1
2008Q2
2008Q3

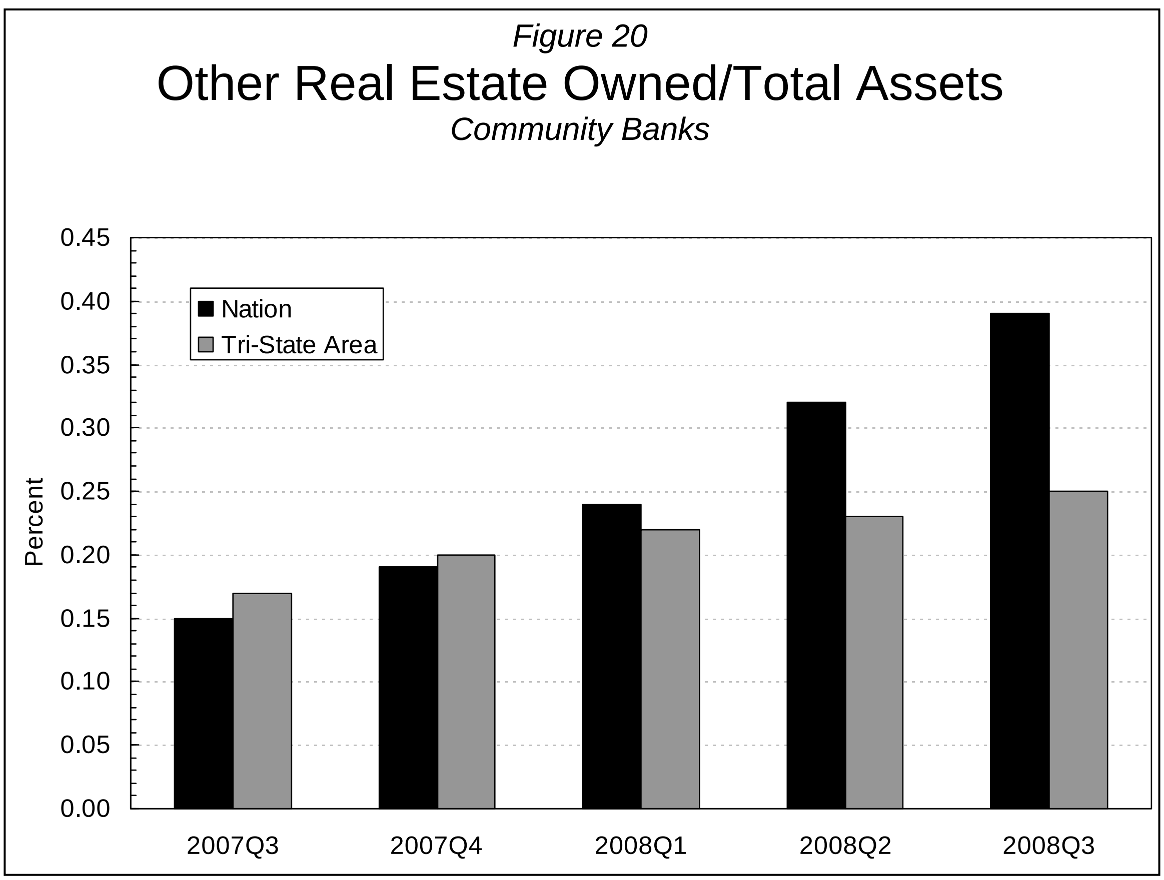


Figure 20
Other Real Estate Owned/Total Assets
Community Banks
Percent
0.45
0.40
0.35
0.30
0.25
0.20
0.15
0.10
0.05
0.00
Nation
Tri-State Area
2007Q3
2007Q4
2008Q1
2008Q2
2008Q3

community banks' attempts to gain more customers at the expense of larger organizations.[18]

The securities portfolios of community banks are substantially different from those of large organizations. As in the large organizations, government-backed MBS make up the largest portion of the portfolios, 41.3 percent nationally and 41.5 percent locally. However, private MBS make up a much smaller portion, 3.4 and 3.8 percent respectively, and ABS are practically nonexistent on their balance sheets. In addition to government-backed MBS, nearly all of the securities portfolios of community banks are made up of securities of GSEs (28.1 percent nationally and 23.1 percent locally) and securities of states and municipalities (20.5 and 20.1 percent). The latter holdings make the banks particularly vulnerable; many municipalities are reporting revenue shortfalls due to increasing numbers of foreclosed properties. Indeed, the market value of these securities fell only slightly both locally and nationally in the third quarter, but it is possible that the holdings of state and local debt will have a substantial impact on the value of the community banks' portfolios in the future.

In summary, community banks nationally are experiencing some of the same problems as the larger banks but to a lesser extent. Community banks locally are outperforming both their counterparts nationally and the larger organizations. In both cases, they are less reliant on RRE loans and appear to have been more prudent in the RRE loans they did make. Their experience with CRE lending, particularly construction loans, mirrors that of large organizations. It also appears that one major reason for the performance of local community banks is their decreased reliance on construction lending. Banks both nationally and locally need to build up their reserves quickly, even at the expense of income and dividends. They are also carrying too much OREO on their books, but it is unlikely they will be able to change that without a substantial improvement in the real estate markets.

[18] This was mentioned in the previous issue of *Banking Brief*. There are no hard data to back this statement, but there has been substantial anecdotal evidence that community banks are attempting to take customers away from the large organizations.

Third Quarter 2008

	Community Banking Organizations						Large Banking Organizations						
	Tri-State			*Nation*				*Tri-State*			*Nation**		
	$ Bill	**% Change From**		**$ Bill**	**% Change From**			**$ Bill**	**% Change From**		**$ Bill**	**% Change From**	
	08Q3	**08Q2**	**07Q3**	**08Q3**	**08Q2**	**07Q3**		**08Q3**	**08Q2**	**07Q3**	**08Q3**	**08Q2**	**07Q3**
Total Assets	81.0	9.14	6.82	1778.6	4.36	7.05	Total Assets	3258.1	10.30	9.41	7469.0	11.46	8.19
Total Loans	57.0	11.08	9.98	1278.1	6.43	8.92	Total Loans	1742.6	0.75	6.07	4374.2	-0.58	4.25
Business	7.2	3.78	10.48	199.9	-0.85	8.51	Business	411.3	15.83	11.32	1002.1	5.65	7.13
Real Estate	45.8	12.60	10.23	950.3	8.26	9.92	Real Estate	954.2	-3.23	1.61	2375.4	-2.27	2.10
Consumer	2.1	16.05	3.44	63.9	2.91	-0.43	Consumer	178.3	-2.14	13.38	542.7	-2.65	6.68
Total Deposits	63.0	10.36	4.74	1402.6	4.65	5.50	Total Deposits	2127.5	14.43	11.69	4970.1	9.83	7.15
Ratios (in %)	**08Q3**	**08Q2**	**07Q3**	**08Q3**	**08Q2**	**07Q3**	**Ratios (in %)**	**08Q3**	**08Q2**	**07Q3**	**08Q3**	**08Q2**	**07Q3**
Net Income/Avg Assets (ROA)	0.79	0.91	1.05	0.50	0.76	1.13	Net Income/Avg Assets (ROA)	0.12	0.29	1.04	0.23	0.39	1.09
Net Interest Inc/Avg Assets (NIM)	3.21	3.21	3.22	3.50	3.55	3.71	Net Interest Inc/Avg Assets (NIM)	2.31	2.32	2.41	2.69	2.70	2.72
Noninterest Inc/Avg Assets	1.29	1.35	1.37	0.91	0.93	0.93	Noninterest Inc/Avg Assets	1.45	1.33	1.77	1.50	1.46	1.86
Noninterest Exp/Avg Assets	3.11	3.11	3.11	3.06	3.01	2.93	Noninterest Exp/Avg Assets	2.45	2.39	2.48	2.72	2.71	2.71
Loans/Deposits	90.52	90.37	86.20	91.12	90.74	88.26	Loans/Deposits	81.91	84.56	86.25	88.01	90.23	90.46
Equity/Assets	9.57	9.80	10.03	9.90	9.99	10.36	Equity/Assets	9.85	10.09	9.61	9.48	9.82	9.70
Nonperforming Loans/Total Loans	1.60	1.51	1.18	2.47	2.28	1.07	Nonperforming Loans/Total Loans	2.45	2.23	0.78	2.26	1.89	0.98

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, 2007. 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 — 174 for the tri-state area and 5,595 for the nation; (2) large banking organizations — 18 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.

* These numbers exclude JP Morgan Chase & Co. due to its acquisition of a large thrift in the third quarter.

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/research-and-data/publications/banking-brief. To subscribe to this publication, please go to www.philadelphiafed.org/philscriber/user/dsp_content.cfm.