BANKING BRIEF
FOR PENNSYLVANIA, NEW JERSEY, AND DELAWARE

First Quarter Highlights

- *Year over year, profitability (ROA) continued to improve at all categories of banks.*

- *Year over year, loans grew modestly at all categories of banks, with commercial and industrial lending showing more rapid growth. However, loans were flat or decreasing from the fourth to the first quarter.*

- *Loan quality improved year over year at all categories of banks, as both nonperforming loans and net charge-offs decreased.*

- *Residential real estate (RRE) loan quality improved at large organizations but was nearly unchanged at community banks. RRE loans grew slightly at local community banks but were nearly flat at community banks nationally and at large organizations.*

- *Commercial real estate (CRE) lending showed some growth at community banks nationally and locally but shrank at large organizations. Nonperforming loans and net charge-offs dropped substantially at all categories of banks.*

- *Construction lending remains a problem, with shrinking outstandings and large amounts of nonperforming loans at all categories of banks. Nonperforming loans and net charge-offs have dropped substantially.*

- *Loan-loss coverage increased at community banks but decreased at large organizations. In all cases, it is still below historical norms. Reserves are down at all categories of banks except local community banks, where they were nearly unchanged. Loan-loss provisions decreased for all types of banks as well.*

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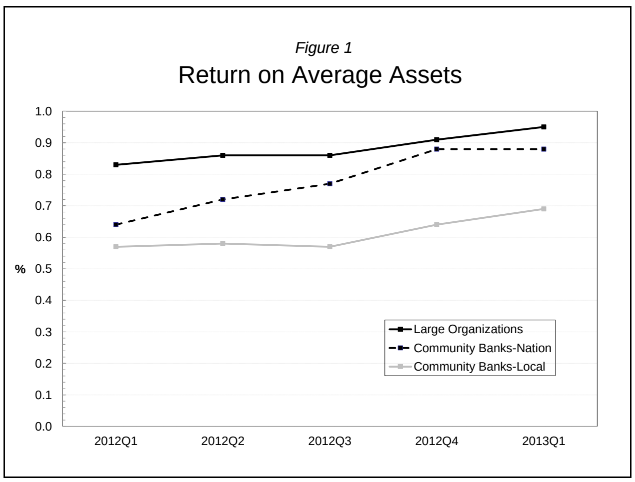
Summary Table of Bank Structure and Conditions – First Quarter 2013

	Community Banking Organizations						*Large Organizations*			
	Nation			*Tri-State*				*Nation*		
	$ Bill	% Change From		$ Bill	% Change From			$ Bill	% Change From	
	13Q1	12Q4	12Q1	13Q1	12Q4	12Q1		13Q1	12Q4	12Q1
Total Assets	1,899.5	-2.63	2.53	102.3	-3.65	4.04	Total Assets	10,558.7	-0.62	4.65
Total Loans	1,164.2	-1.92	3.50	68.2	1.49	6.15	Total Loans	5,206.3	0.31	4.67
C&I	188.4	0.90	6.95	9.6	8.00	7.66	C&I	1,211.5	8.55	12.85
Real Estate	860.6	-0.50	2.70	52.5	1.08	4.76	Real Estate	2,605.3	-3.39	0.03
Consumer	49.8	-5.45	1.24	2.5	-3.57	2.96	Consumer	707.1	-6.76	1.14
Total Deposits	1,593.9	-1.68	2.85	85.5	-4.35	3.94	Total Deposits	7,867.6	0.25	7.09
Ratios (in %)	**13Q1**	**12Q4**	**12Q1**	**13Q1**	**12Q4**	**12Q1**	**Ratios (in %)**	**13Q1**	**12Q4**	**12Q1**
Net Income/Avg Assets (ROA)	0.88	0.88	0.64	0.69	0.64	0.57	Net Income/Avg Assets (ROA)	0.95	0.91	0.83
Net Interest Inc/Avg Assets (NIM)	3.39	3.43	3.47	3.25	3.27	3.34	Net Interest Inc/Avg Assets (NIM)	2.57	2.61	2.69
Noninterest Inc/Avg Assets	1.00	0.99	0.91	1.30	1.27	1.19	Noninterest Inc/Avg Assets	1.84	1.82	1.82
Noninterest Exp/Avg Assets	3.05	3.06	3.06	3.26	3.24	3.23	Noninterest Exp/Avg Assets	2.82	2.90	2.98
Loans/Deposits	73.04	73.08	72.58	79.77	78.60	78.12	Loans/Deposits	66.17	66.16	67.71
Equity/Assets	10.86	10.74	10.64	10.23	9.96	10.15	Equity/Assets	11.06	10.96	11.08
Nonperforming Loans/Total Loans	2.35	2.44	3.18	2.12	2.30	2.83	Nonperforming Loans/Total Loans	3.82	4.05	4.57

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 special purpose banks such as credit card banks 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, 2012. The community banking organization sample is based on the remaining banking organizations. 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 5,270 for the nation; (2) large banking organizations — 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.

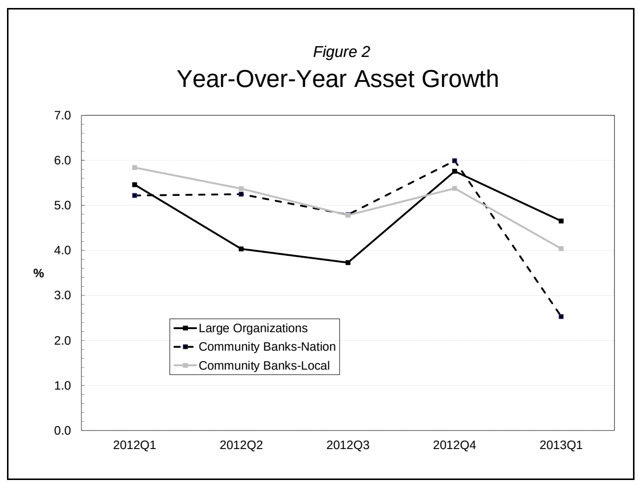
First Quarter 2013

Year-over-year profitability increased strongly at all categories of banks in the first quarter.[1] Profits also increased from the fourth quarter of 2012, but not as substantially. In addition, except at large organizations, the number of firms showing positive net income increased as well. Year-over-year profitability as measured by return on average assets (ROA) increased 24 basis points at community banks nationally, to 0.88 percent; increased 15 basis points at community banks locally, to 0.69 percent; and increased 12 basis points at large organizations, to 0.95 percent (Figure 1).[2]



As has been the case for the previous several quarters, the increased profitability can be attributed primarily to the continued improvement in loan quality, which resulted in lower loan-loss provisions; increased asset sales also contributed to increasing income. Net charge-offs (NCOs) and nonperforming loans (NPLs) continued to decrease.[3] Improved loan quality more than made up for decreasing net interest margins. As a result, large organizations have seen a 23 percent increase in quarterly net income from the first quarter of 2012 and an 18 percent decrease in their loan-loss reserves (see "Provisioning and Reserves" below). Community banks experienced similar results with net income increasing 7.8 percent nationally and 31.7 percent locally, while reserves dropped 6 percent nationally and increased slightly locally. Local community banks also had higher noninterest income.

Year over year, assets of community banks nationally grew at a 2.5 percent rate, while asset growth at local community banks was 4.0 percent (Figure 2). At large organizations, asset growth was 4.7 percent. However, assets at all three categories of banks shrunk from the fourth quarter of 2012 to the first quarter of 2013.



The growth in assets was fueled mainly by increases in loans as growth in banks' securities portfolios slowed. Loans increased 4.7 percent at large organizations, 3.5 percent at national community banks, and 6.2 percent at local community banks (Figure 3). The market value of securities increased only 1.8 percent at national community banks, shrank slightly (-0.8

[1] Out of 5,270 community banks in the national sample, 4,856 reported positive quarterly profits. This was an increase of 361 from the fourth quarter of 2012. Locally, 162 out of 174 banks reported positive profits, an increase of 14 from the fourth quarter of 2012. For large organizations, 96 out of 102 were profitable, unchanged from the previous quarter.

[2] See Summary Table of Bank Structure and Conditions on page 2.

[3] NPLs are defined as loans past due 90 or more days plus nonaccruing loans.

percent) at local community banks, and increased 3.4 percent at large organizations.

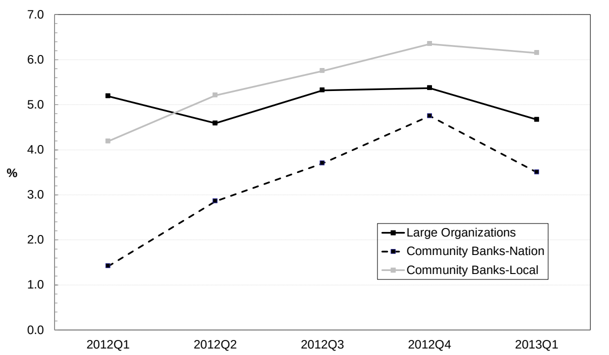


Figure 3
Year-Over-Year Loan Growth

Loan growth remained strong for commercial and industrial (C&I) lending, while both real estate lending and consumer lending growth were flat at large organizations and slightly better at community banks.

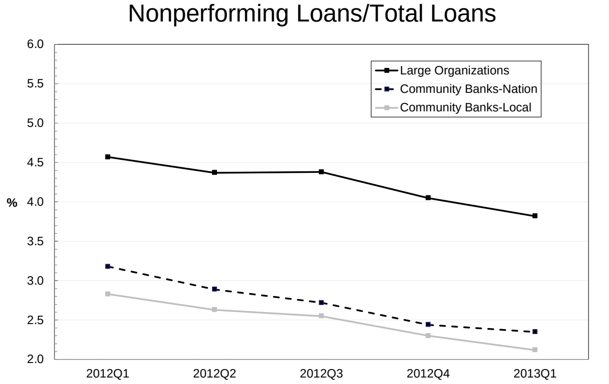


Figure 4
Nonperforming Loans/Total Loans

Loan quality continued to improve at all categories of banks. At large organizations, the ratio of NPLs to total loans (the NPL ratio) decreased by 75 basis points from last year, to 3.82 percent (Figure 4).[4]

At community banks nationally, the NPL ratio has decreased 83 basis points since last year, to 2.35 percent. Locally, the NPL ratio fell by 71 basis points, to 2.12 percent.

Overall, asset quality has also improved at all categories of banks.[5] Foreclosed real estate, known as other real estate owned (OREO), fell substantially from last year at all categories of banks. At large organizations, OREO decreased by 11.8 percent. At community banks, the decrease was 14.9 percent nationally and 8.4 percent locally, but OREO did increase in the first quarter at tri-state area banks. Combining the decrease in OREO with improved loan quality, the ratio of nonperforming assets (NPAs) to total assets has fallen at all three categories of banks in the past year (Figure 5).[6]

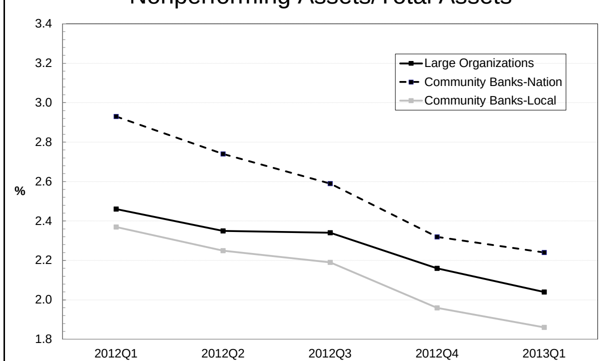


Figure 5
Nonperforming Assets/Total Assets

[4] For historical perspective, the average NPL ratio for all commercial banks between 2001 and 2011 was 2.31 percent. At the bottom of the last real estate cycle in 1991, this ratio stood at 3.70 percent. Source: FDIC Historical Statistics on Banking, http://www2.fdic.gov/hsob/index.asp.

[5] Asset quality refers to nonperforming assets. These are defined as NPLs plus other real estate owned.

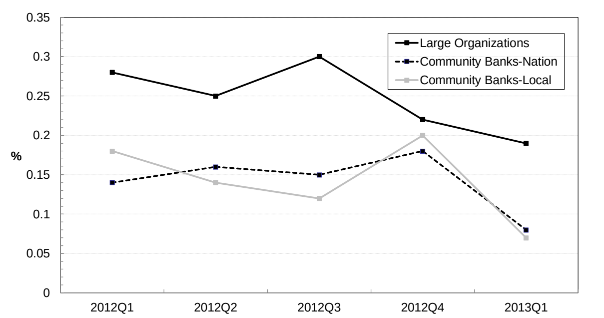
[6] Loan quality refers to NPLs only, while asset quality refers to NPAs. These are the sum of NPLs and OREO. For historical perspective, the average ratio of NPAs to total assets for all commercial banks between 2001 and 2011 was 1.44 percent. At the bottom of the last real estate cycle in 1991, this ratio stood at 3.02 percent. Source: FDIC Historical Statistics on Banking, http://www2.fdic.gov/hsob/index.asp.

At large organizations, the NPA ratio has fallen 42 basis points in the past year, to 2.04 percent. At community banks nationally, the decrease was 69 basis points, to 2.24 percent, and locally the NPA ratio fell 51 basis points, to 1.86 percent.

NCOs tell a similar story, with all categories of banks experiencing large decreases. The ratio of NCOs to average loans (the NCO ratio) fell 9 basis points over the year at large organizations, to 0.19 percent (Figure 6).

Figure 6

Quarterly Net Charge-Offs/Average Loans

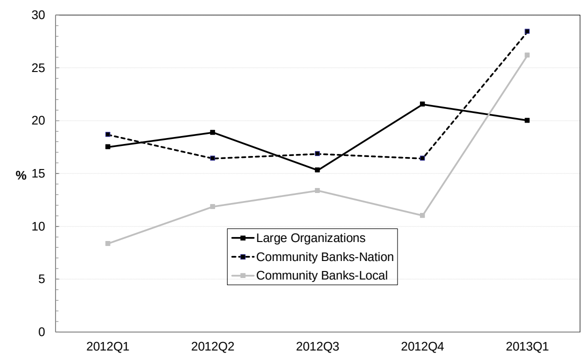


Community banks both locally and nationally continued to have a lower NCO ratio than the large organizations. For community banks in the nation, the NCO ratio has fallen 6 basis points over the year, to 0.08 percent. At tri-state area community banks, the NCO ratio has fallen 11 basis points over the past year, to 0.07 percent. At both large organizations and community banks, NCOs fell in nearly all categories of loans.

At large organizations, gross charge-offs have fallen 26 percent in the past year, and recoveries have fallen 15 percent. At community banks nationally, charge-offs have fallen over 34 percent in the past year, while recoveries were basically unchanged. At local community banks, charge-offs fell 45 percent and recoveries increased 73 percent since last year. As a result, the ratio of recoveries to charge-offs has increased substantially at community banks, and it increased somewhat at large organizations (Figure 7).

Figure 7

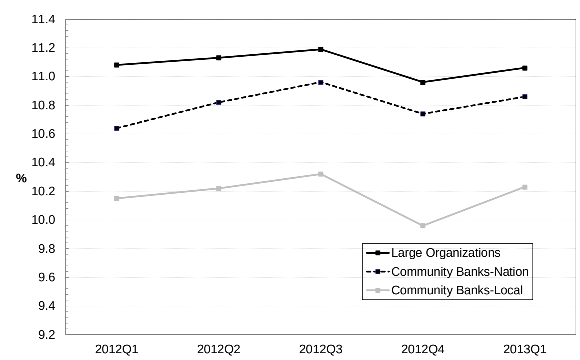
Recoveries/Charge-Offs



Capital ratios, defined as the ratio of total equity to assets, are up somewhat from a year ago at community banks but fell slightly at large organizations (Figure 8). In all cases, total equity increased somewhat, while assets grew at a slower rate.

Figure 8

Equity-to-Assets Ratios



The number of bank failures fell sharply in the first quarter. The Federal Deposit Insurance Corporation reported only four bank failures for the entire quarter, the lowest total in several years. In the first quarter of 2012, 16 failures were reported. This news was somewhat tempered by the fact that, as of May 14, 2013, there have already been eight failures in the second quarter. None of these failures occurred in the tri-state area.

Residential Real Estate Lending[7]

The nationwide and local residential real estate (RRE) markets continued their modest recovery in the first quarter. The Federal Reserve Board's *Beige Book*, as of March 6 (survey dated February 13), reported that existing home sales were growing strongly in five Federal Reserve Districts and at a slight or moderate pace in most others. It also reported that construction was, for the most part, unchanged across the country.[8]

By most measures, local real estate markets continued to improve in the first quarter. In the Philadelphia region, construction was up strongly, and sales showed a moderate increase. This increase in sales was enough to inspire the confidence of real estate brokers in stronger growth in the near future. In the New York region (which includes northern New Jersey), both builders and agents were increasingly optimistic, but growth was relatively small. Also, there is still a substantial inventory of foreclosed and distressed properties. The Cleveland District (which includes western Pennsylvania) reported increased construction activity and higher prices along with "significantly" higher sales.

Sales of both new and existing homes have increased since both the first quarter of last year and the end of the fourth quarter (Figure 9). Sales of new homes have grown modestly over the past year. The percentage of delinquent mortgages decreased 49 basis points from a year ago, and the percentage of mortgages in foreclosure has decreased 64 basis points (Figure 10).

Figure 9

Sales of New and Existing Homes

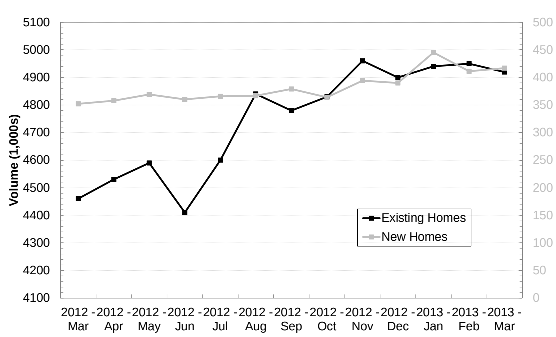
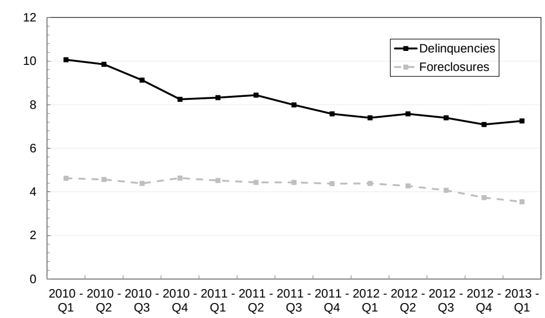


Figure 10

Delinquency and Foreclosure Rates

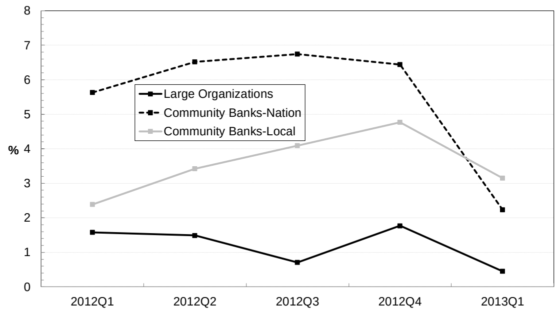


RRE loans outstanding increased modestly year over year at community banks but have shown little growth at large organizations (Figure 11). From the first quarter of 2012 to the first quarter of 2013, RRE loans outstanding grew 2.2 percent at community banks nationally and 3.2 percent locally. At large organizations, loans outstanding were basically flat, increasing only 0.5 percent since last year. Also, except at local community banks, loans outstanding decreased at all banks from the fourth to the first quarter.

[7] See Table 1 in the Appendix for a full summary of the data used in this section.

[8] For further information, see http://www.federalreserve.gov/monetarypolicy/beigebook/files/Beigebook_20130306.pdf.

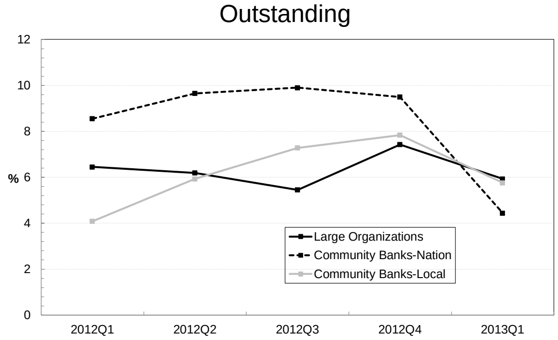
Figure 11
Annual Change in RRE* Loans Outstanding



*Residential real estate

Behind the overall RRE loan numbers, some interesting things are going on. Mortgages secured by first liens, which make up most RRE loans in all categories of banks, have been rising strongly in the previous several quarters, but that growth slowed somewhat this quarter, particularly at community banks (Figure 12).[9] Much of this slowdown is likely caused by temporary factors. The FRB's H.8 report on bank assets and liabilities showed an 8.4 percent annualized increase in mortgages outstanding in January 2013, followed by small decreases in February and March (0.8 and 0.4 percent,

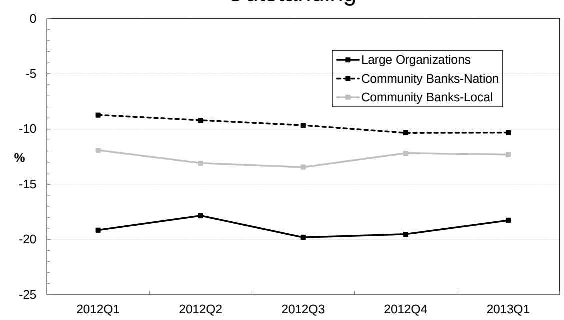
Figure 12
Annual Change in First Lien Mortgages Outstanding



respectively). In the first month of the second quarter, the annualized growth rate was 7.0 percent.[10]

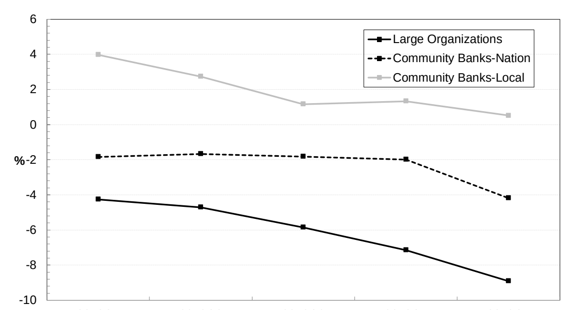
While senior liens are showing growth, other components of RRE lending have, for the most part, been shrinking for some time. Mortgages secured by junior liens have been decreasing at an annual rate near 20 percent for at least the last year at large organizations and at double or near double-digit rates at community banks both locally and nationally (Figure 13).

Figure 13
Annual Change in Junior Lien Mortgages Outstanding



The third component of RRE loans, Home Equity Lines of Credit (HELOCs), also fell this

Figure 14
Annual Change in HELOCs* Outstanding



*Home Equity Lines of Credit

[9] Mortgages secured by first liens make up 69.8 percent of all RRE loans at large organizations, 80 percent of RRE loans at community banks nationally, and 74.3 percent at local community banks.

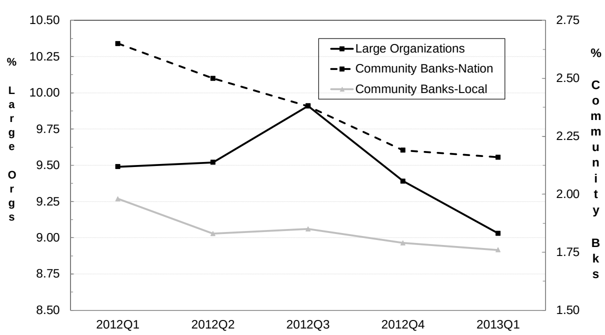
[10] For further information, see http://www.federalreserve.gov/releases/h8/current/default.htm.

quarter. HELOCs had been declining slightly at all banks except local community banks for some time. In the first quarter, these declines accelerated, and growth at local community banks came to a standstill (Figure 14).

The quality of RRE loans continued to improve, but large organizations are still carrying a substantial portfolio of NPLs. The RRE NPL ratio at large banks fell for the second consecutive quarter, to 9.03 percent. This represents a 46-basis-point drop from the first quarter of last year (Figure 15 – Note the different scales for community banks (left y-axis) and large organizations (right y-axis)).

Figure 15

Nonperforming RRE* Loans/Total RRE Loans

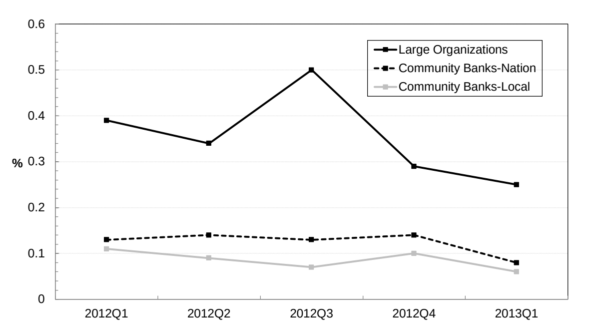


*Residential real estate

Local community banks have better RRE loan quality than either the large organizations or national community banks. The RRE NPL ratio at local community banks decreased 22 basis points in the past year, to 1.76 percent.

Figure 16

Net Charge-Offs on RRE* Loans/Avg. RRE Loans



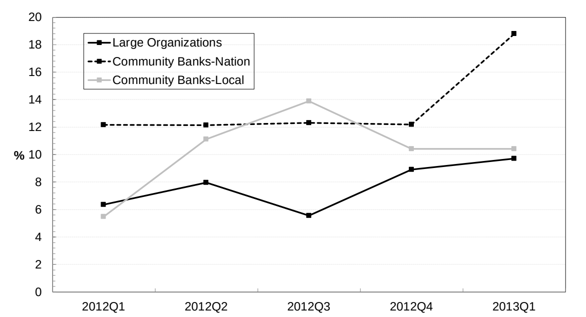
*Residential real estate

The improvement in loan quality at large organizations is also reflected in the RRE NCO ratio. At large organizations, this ratio has been somewhat erratic in the past year, but it has decreased 14 basis points, to 0.25 percent, in the last year (Figure 16).

NCOs at community banks have fallen in the past year as well. The RRE NCO ratio has decreased 5 basis points nationally, to 0.08 percent, and 5 points locally, to 0.07 percent. In the cases of both large organizations and community banks, charge-offs decreased and recoveries increased. Recovery ratios also showed improvement from last year (Figure 17).

Figure 17

Recovery Ratio on RRE Loans



*Residential real estate

Commercial Real Estate Lending[11]

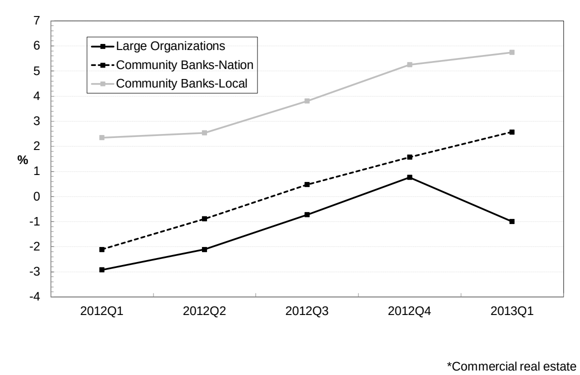
Commercial real estate (CRE) market conditions remained mixed both locally and nationally. The *Beige Book* reported that most CRE markets nationwide showed some improvement in construction and demand for commercial space. For the most part, in the Philadelphia District there was modest growth in commercial leasing activity and slight growth in construction. The New York District reported decreasing office and industrial vacancy rates but also decreasing rents. The

[11] See Table 2 in the Appendix for a full summary of the data used in this section.

Cleveland District reported a slight slowing of activity in both leasing and construction.

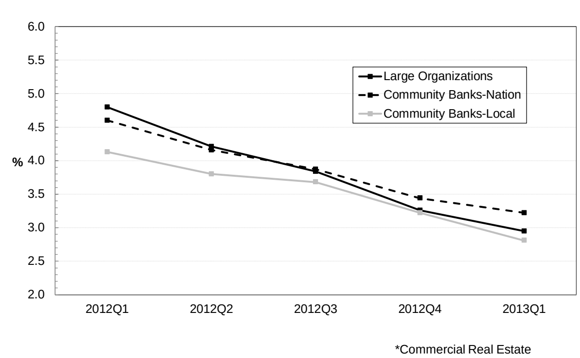
CRE lending results were mixed in the first quarter, with loan quality improving, while loan growth remained anemic except at local community banks. Year over year, CRE loans outstanding shrank 1 percent at large organizations, grew about 2.6 percent at community banks nationally, but showed a 5.7 percent growth rate at tri-state area community banks (Figure 18).

Figure 18
Annual Change in CRE* Loans Outstanding



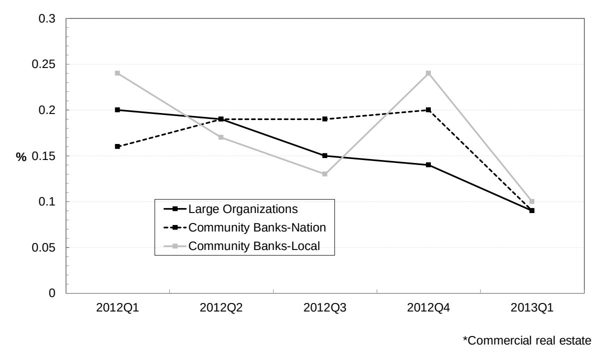
The quality of CRE loans improved substantially at all categories of banks, as CRE NPL ratios continued to decline. However, bad construction loans are still weighing down the banks' CRE loan portfolios (see Figures 22 and 23 below). At large organizations, the CRE NPL ratio has decreased nearly 1.9 percentage points from the first quarter of 2012, to 2.95 percent (Figure 19). The CRE NPL ratio decreased nearly 1.4 percentage points at community banks nationally from last year, to 3.22 percent, and 1.3 percentage points at community banks locally, to 2.81 percent.

Figure 19
Nonperforming CRE* Loans/Total CRE Loans



NCO ratios have decreased at all categories of banks as well. Since last year, the CRE NCO ratio at large organizations has decreased by 11 basis points, to 0.09 percent. At community banks, there was a decrease of 7 basis points nationally, to 0.09 percent, and a decrease of 14 basis points locally, to 0.10 percent (Figure 20).

Figure 20
Net Charge-Offs on CRE* Loans/Avg CRE Loans



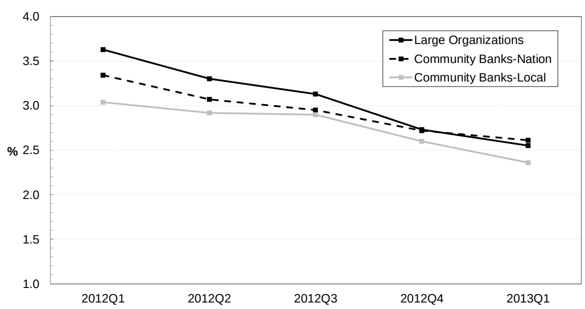
Total CRE NCOs are also down substantially at all categories of banks since last year, and, after rising in the fourth quarter, shrank substantially in the first quarter as well. Both the *Beige Book* and the *Senior Loan Officer Opinion Survey* report that credit quality is improving despite some loosening in lending standards.[12]

As noted above, construction loans continue to be a drag on CRE loan quality. CRE loans can be broken down into three categories: construction loans, loans secured by multifamily properties, and commercial mortgages. At both

[12] The Senior Loan Officer Opinion Survey is from April 2013. For further information on this survey, see http://www.federalreserve.gov/boarddocs/SnLoanSurvey/201305/default.htm.

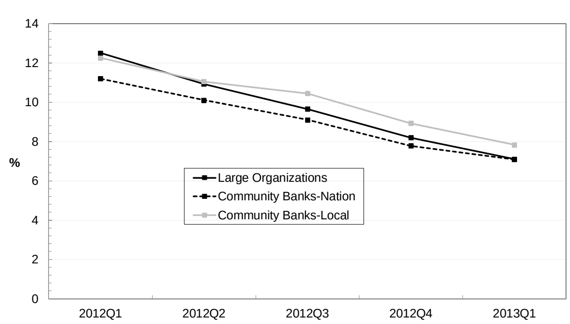
large organizations and community banks, commercial mortgages make up the vast majority of their CRE loan portfolios, but these types of loans are in relatively good shape. The NPL ratio continued to fall at all categories of banks (Figure 21). It now stands at 2.55 percent for large organizations, 2.61 percent for community banks nationwide, and 2.36 percent for local community banks.

Figure 21
Nonperforming Commercial Mortgages/ Commercial Mortgages



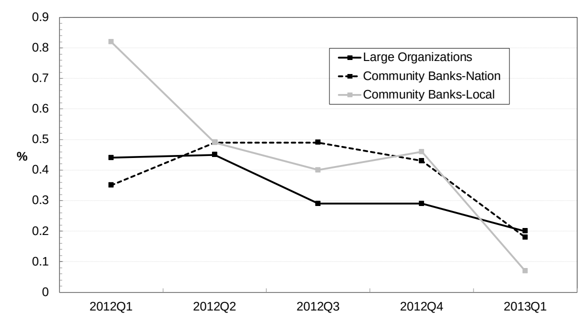
Construction loan quality has vastly improved in the past year, but both NPLs and charge-offs remain high. NPL ratios have shrunk by 4 to 5 percentage points at all categories of banks but remain over 7 percent (Figure 22). Total construction NPLs have also dropped over 40 percent at all categories of banks.

Figure 22
Construction Loan NPL Ratios



Construction loans have also contributed heavily in banks' CRE NCOs. According to this measure of loan quality, the construction loan portfolio is performing significantly better, with construction loan NCOs decreasing in the high double digits in the past year (see Table 2 in the Appendix). The NCO ratio for construction loans has dropped and is now nearly in line with that of all other loans (Figure 23, compare with Figure 6).

Figure 23
Construction Loan NCO Ratios

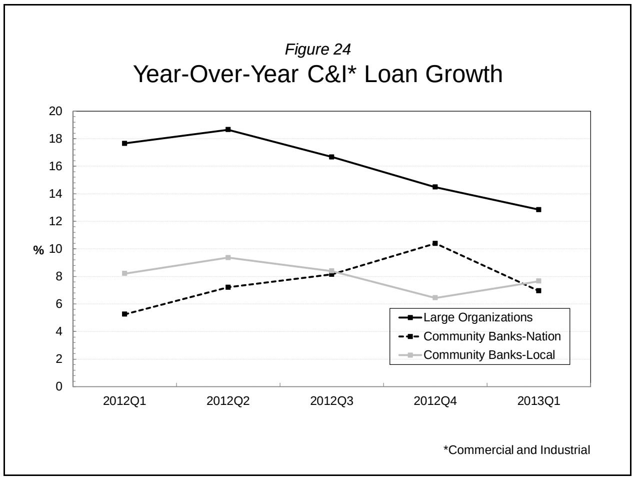


Commercial & Industrial Lending[13]

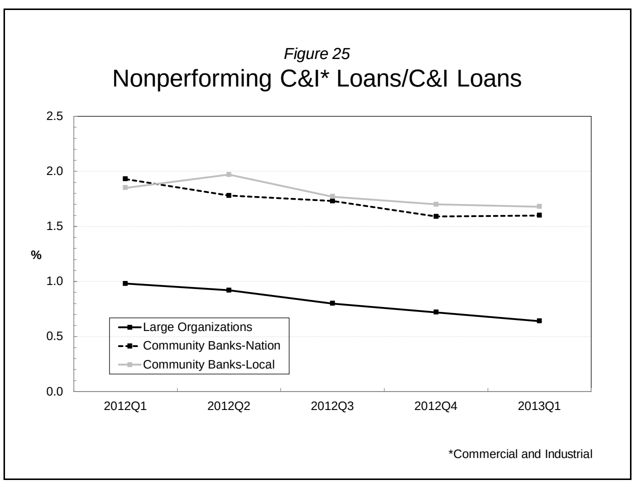
C&I lending continued to be the brightest spot for bank lending in the first quarter, both in terms of growth and quality. Lending growth has slowed somewhat, but it still remains robust. At large organizations, C&I loans grew 12.9 percent in the past year (Table 3 and Figure 24). At community banks, C&I lending grew 7.0 percent nationally and 7.7 percent locally. However, at community banks nationwide, loan growth was essentially flat from the fourth to the first quarter.

The Federal Reserve Board's *Senior Loan Officer Opinion Survey* for April 2013 reported that loan demand was mixed, with some firms reporting increased demand and others reporting

[13] See Table 3 in the Appendix for a full summary of the data used in this section.

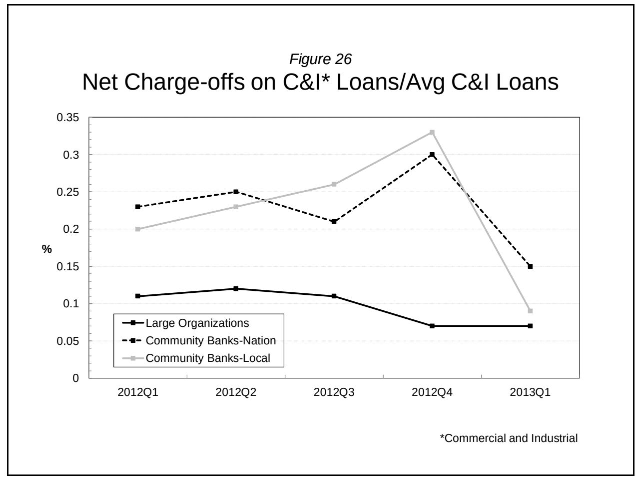


no change in demand. On the supply side, most firms reported they had loosened their lending standards on all types of borrowers. Nearly all lenders noted that one reason for easing terms was more aggressive competition from other firms. A smaller fraction also cited an improved economic outlook.



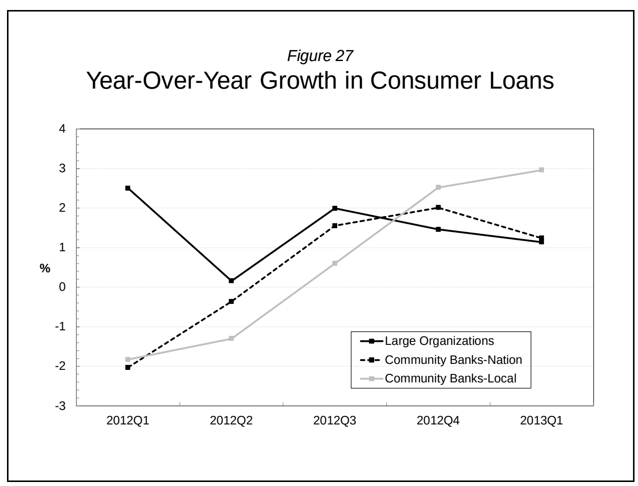
The C&I NPL ratio has fallen moderately at all categories of banks since last year (Figure 25). Total NPLs fell sharply over the year, but increased somewhat from the fourth quarter of 2012 at community banks. This could indicate either that they have eased their standards too much or that they are being outcompeted for the best borrowers from large organizations and other firms.

The NCO ratio has also fallen at all categories of banks (Figure 26). At large organizations, the C&I NCO ratio has fallen 4 basis points since one year ago. At community banks, it has fallen 8 basis points nationally and 11 basis point locally.



<u>Consumer Lending</u>[14]

Overall, consumer lending remained weak in the first quarter, but there are few quality problems. Large organizations conduct the vast majority of consumer lending. Their consumer lending was basically flat, growing only 1.1 percent year over year (Figure 27). At

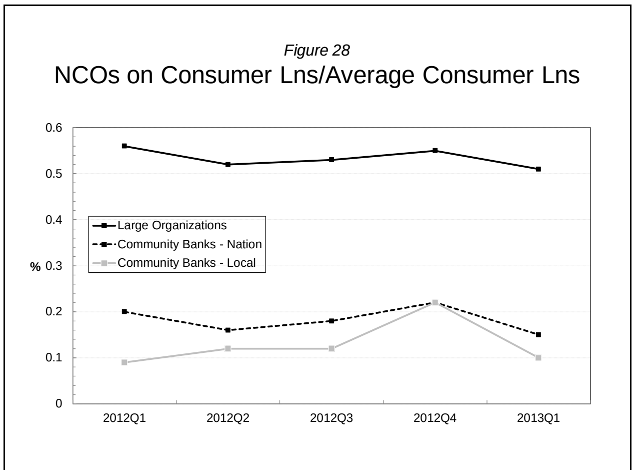


[14] See Table 4 in the Appendix for a full summary of the data used in this section.

community banks nationally, consumer lending grew only 1.2 percent, while at community banks locally, consumer lending grew 3 percent.

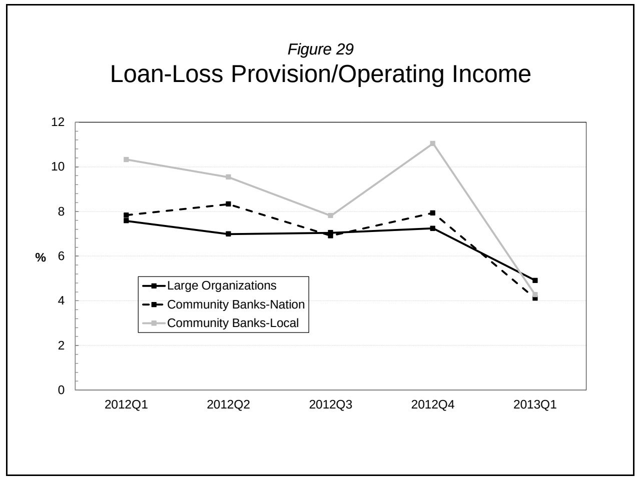
NPL ratios on consumer loans have been low: 1.10 percent for large organizations, 0.72 percent for community banks nationally, and 0.48 percent for tri-state area community banks.

The most reliable measure of quality for consumer loans is NCOs. Many consumer loans are lines of credit with flexible repayment schedules, so NPLs are difficult to calculate, and when consumer loans go bad, they are often a total loss. NCO ratios fell at all categories of banks (Figure 28). For large organizations, the ratio fell 5 basis points, to 0.51 percent. For community banks, the ratio fell 5 basis points, to 0.15 percent nationally, and locally the ratio rose 1 basis point, to 0.1 percent.



Provisioning and Reserves[15]

Banks continued to ease up on their provisioning and reserves in response to falling NPLs and charge-offs. At large organizations, loan-loss reserves have fallen nearly 18 percent in the past year.[16] At community banks, loan-loss reserves have fallen by nearly 6 percent nationally, and locally they were nearly flat, rising 1.6 percent. Loan-loss provisions have also decreased, both overall and as a percentage of operating income.[17] Over the year, quarterly loan-loss provisions were down 34 percent at large organizations, 47 percent at community banks nationally, and 57 percent at local community banks. The ratio of loan-loss



provisions to operating income fell 2.7 percentage points, to 4.91 percent, at large organizations; decreased 3.7 percentage points, to 4.11 percent, at community banks nationally; and fell 6 percentage points, to 4.27 percent, at local community banks (Figure 29). It should be noted that in each category this ratio is somewhat bumpy, rising some quarters and falling in others.

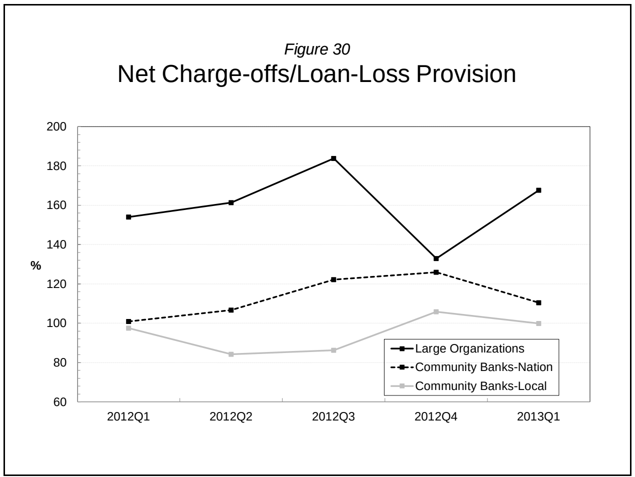
As noted above, the falling loan-loss provisions and consequent decreases in reserves can be justified as a reaction to improving loan quality, but at the same time all the measures of

[15] See Table 5 in the Appendix for a full summary of the data used in this section.

[16] As reported here, loan-loss reserves are the balance-sheet item, and loan-loss provisions are from the income statement.

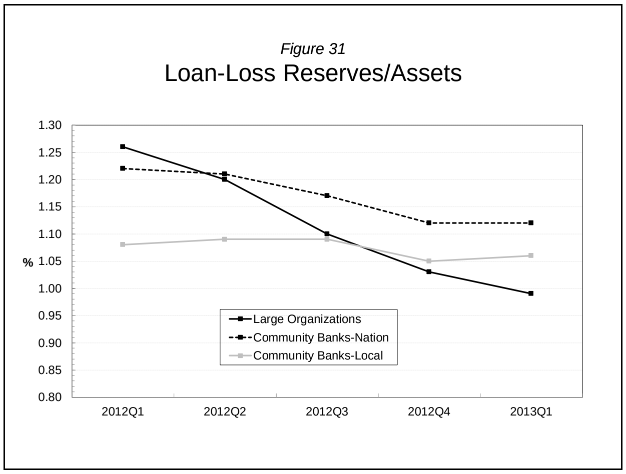
[17] Operating income is defined as the sum of net interest income and noninterest income. For historical perspective, the average ratio of loan-loss provision to operating income for all commercial banks between 2001 and 2011 was 14.84 percent. At the bottom of the last real estate cycle in 1991, this ratio was 18.9 percent. Source: FDIC Historical Statistics on Banking, http://www2.fdic.gov/hsob/index.asp.

coverage against losses remain outside of historical norms. At all categories of banks except local community banks, the ratio of NCOs to loan-loss provisions is over 100 percent (Figure 30).[18] At local community banks, it is 99.9 percent. In other words, each quarter banks are charging off (net of recoveries) more loans than they are provisioning for. Large organizations have the highest ratio at 167.6 percent, and their ratio has increased in the past year. At community banks,



the ratios are somewhat lower, but they have also increased in the past year. The NCOs to loan-loss provision ratio has increased a little under 10 percentage points, to 110.5 percent, at community banks nationally. At local community banks, the ratio increased about 2.5 percentage points. In both cases though, the ratio decreased from the fourth to the first quarter.

The decrease in provisioning has resulted in a drop in overall reserves. Loan-loss reserves as a percent of total assets have decreased from the first quarter of last year in all categories of banks, though the drop was small at local community banks (Figure 31). At large



organizations, the ratio has fallen 27 basis points since last year, to 0.99 percent. At community banks, the drop was 10 basis points nationally and 2 basis points locally.

Loan-loss coverage remains well outside historical norms at all categories of banks. At large organizations, loan-loss coverage fell over 3 percentage points from last year, to 52.3 percent (Figure 32). It did increase in the past quarter and has been increasing for several quarters.

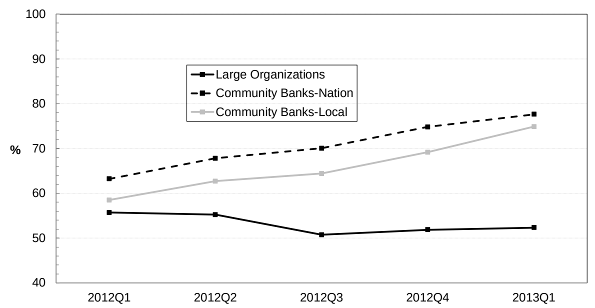
The situation is somewhat better at community banks, as improving loan quality has enabled community banks to increase their loan-loss coverage in each quarter since last year. The loan-loss coverage ratio at community banks nationally has increased over 14 percentage points in the past year, to 77.7 percent. Locally, loan-loss coverage increased over 16 percentage points, to 74.9 percent.[19]

[18] For historical perspective, the average ratio of NCOs to loan-loss provision for all commercial banks between 2001 and 2011 was 97.03 percent. At the bottom of the last real estate cycle in 1991, this ratio was 95.8 percent. Source: FDIC Historical Statistics on Banking, http://www2.fdic.gov/hsob/index.asp.

[19] The loan-loss coverage ratio is defined as the ratio of loan-loss reserves to NPLs. For historical perspective, the average loan-loss coverage ratio for all commercial banks between 2001 and 2011 was 114.8 percent. At the bottom of the last real estate cycle in 1991, this ratio stood at 72.6 percent. Source: FDIC Historical Statistics on Banking, http://www2.fdic.gov/hsob/index.asp.

Figure 32

Loan-Loss Coverage Ratio



Securities[20]

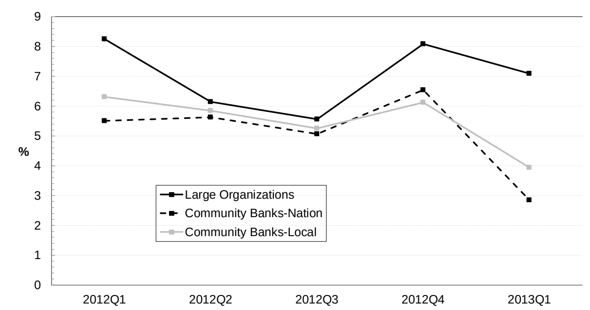
The market value of securities has increased year over year except at local community banks. Also, large organizations' securities portfolios lost value from the fourth quarter of 2012 to the first quarter of 2013.[21] Large organizations also posted a realized gain of over $1.6 billion.[22] Community banks nationally reported a realized gain of $230.5 million on securities in the first quarter. Local community banks reported a realized gain of $15.6 million on their securities in the quarter after realizing a loss last quarter.

Funding Sources[23]

Year over year, deposit growth slowed at all categories of banks (Figure 33). This was especially true at community banks. Additionally, deposit growth from the fourth quarter of 2012 was negative at community banks and flat at large organizations. The shrinkage was fairly consistent across all types of accounts, with only savings accounts showing some growth.

Figure 33

Year-Over-Year Growth in Deposits



Not only did overall deposit growth slow year over year but core deposit growth was also very slow at community banks (Figure 34).[24] At large organizations it was somewhat better, but it didn't match overall deposit growth. Core deposits are the least expensive and most stable form of funding for banks, so this slowdown in growth could adversely affect interest margins going forward.

[20] See Table 6 in the Appendix for a full summary of the data used in this section. The figure for percent of assets uses the value of securities as reported on the banks' balance sheets. Securities there are reported at book value if they are held to maturity and market value if they are available for sale.

[21] Changes in market value can either be indicative of increases in the value of securities that were already owned or due to purchases or sales of securities.

[22] Realized and unrealized gains and losses are net positions. Thus, the tri-state area sample can have larger gains or losses than the national sample, even though the tri-state sample is a subset of the national sample.

[23] See Table 7 in the Appendix for a full summary of the data used in this section.

[24] Core deposits are defined as total domestic deposits less the sum of brokered deposits in denominations of less than $100,000 and all deposits in denominations greater than $100,000.

Figure 34
Year-Over-Year Growth in Core Deposits

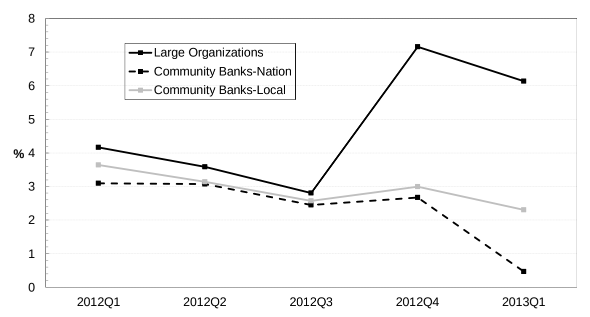
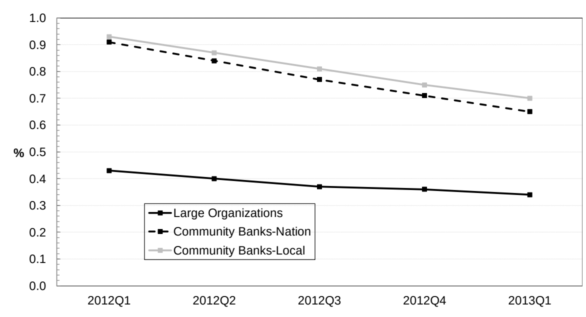
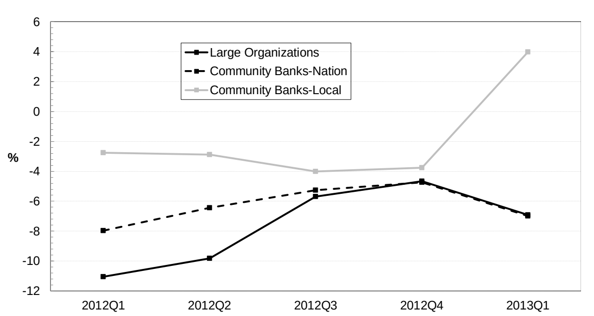


Figure 36
Implicit Interest Rate on Deposits



Nondeposit funding continued to fall year over year at all categories of banks except local community banks. All categories excluding local community banks had a decrease in the first quarter (Figure 35).[25]

Figure 35
Year-Over-Year Growth in Nondeposit Debt



Large organizations continue to have a funding advantage over community banks in terms of both deposits and nondeposit funding. The implicit interest rate on deposits continued to fall at all categories of banks, but large organizations pay only a fraction of what community banks pay both nationally and locally (Figure 36).[26] This holds true for nondeposit funding as well.

Regulatory Capital[27]

Both large organizations and community banks appear to be in fairly good shape as far as their capitalization goes. All of the 102 large organizations in the sample had equity-to-assets ratios of at least 6 percent, and all but two had equity-to-assets ratios of over 7 percent.[28] At community banks nationally, 97.3 percent of the institutions had equity-to-assets ratios of at least 6 percent, and all but two of these banks had

[25] Nondeposit funding consists of fed funds purchased, securities sold under agreements to repurchase (repos), subordinated debt, FHLB advances, and other borrowings.

[26] The implicit interest is computed by dividing the annualized interest paid by the average total balance.

[27] See Table 8 in the Appendix for a full summary of the data used in this section.

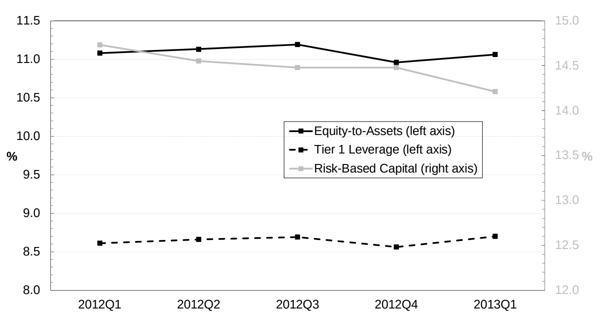
[28] Regulation Y defines capital in terms of zones. Institutions in Zone 1 have tier 1 capital-to-assets ratios above 7 percent, those in Zone 2 are between 6 and 7 percent, and those in Zone 3 have ratios below 6 percent. An institution is considered well capitalized if it is in Zones 1 or 2 and undercapitalized if it is in Zone 3. While total equity capital and tier 1 capital are not identical, in most cases they are close proxies. For further information on capital guidelines, see http://www.federalreserve.gov/bankinforeg/reglisting.htm#Y.

ratios of at least 7 percent. Locally, 98.3 percent (171 out of 174) of the institutions had a capital ratio of at least 6 percent, and 94.3 percent (164) had an equity-to-assets ratio of at least 7 percent. As shown below, capital ratios have improved since last year.

Year over year, capitalization at large organizations was a mixed bag, with equity-to-assets ratios basically unchanged, tier 1 leverage ratios increasing, and risk-based capital ratios falling. Regardless, capitalization remained somewhat higher than historical norms.[29] Year over year, the equity-to-assets ratio at large organizations has fallen 2 basis points, the tier 1 leverage ratio has increased 9 basis points, and the risk-based capital ratio has decreased 52 basis points (Figure 37 – note the different scales on the y-axes).[30] The equity-to-assets and

Figure 37

Regulatory Capital – Large Organizations

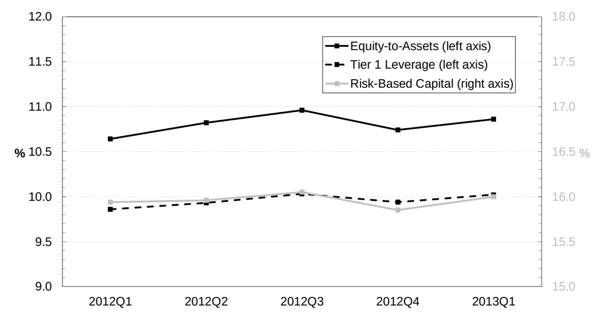


tier 1 leverage ratios have been fairly stable for the past year, but the risk-based ratio has been falling nearly every quarter.

Community banks nationally have increased their capitalization from last year. Since last year, the equity-to-assets ratio at these banks has increased 22 basis points; the tier 1 leverage ratio has increased 16 basis points; and the risk-based capital ratio has increased 6 basis points (Figure 38 – note the different scales on the y-axes).

Figure 38

Regulatory Capital – All Community Banks



At local banks, the equity-to-assets and tier 1 leverage ratios rose, but the risk-based ratio fell year over year. Since last year, the equity-to-assets ratio at local banks has risen 8 basis points, the tier 1 leverage ratio increased by 11 basis point, and the risk-based capital ratio has fallen 6 basis points (Figure 39 – note the different scales on the y-axes). The risk-based capital ratio rose 21 basis points from the fourth to the first quarter.

The primary drivers of these capital increases at community banks, both locally and nationally, were surplus and retained earnings, while common and preferred stock decreased.

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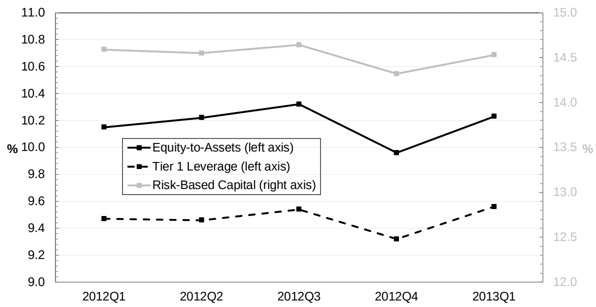
[29] The average ratio of total equity to total assets at all commercial banks from 2001 to 2011 was 10.03 percent. Source: FDIC Historical Statistics on Banking, http://www2.fdic.gov/hsob/index.asp.

[30] Tier 1 leverage and risk-based capital are the two main ratios regulators use to determine if a bank is adequately capitalized. For further information, see the Call Report instructions at http://www.ffiec.gov/forms031.htm.

Figure 39

Regulatory Capital – Local Community Banks



Appendix – Data Tables for Each Section

Table 1 - Summary of Residential Real Estate Lending

	Large Organizations	Community Banks	
	Nation	Tri-State Area	Nation
1. Year–over–year growth			
Total RRE loans	0.5%	3.2%	2.2%
RRE NPLs	-4.5%	-8.6%	-16.6%
RRE NCOs	-34.7%	-42.0%	-38.2%
2. Shares			
RRE Lns/Total Lns	33.1%	30.8%	25.4%
RRE NPLs/Total NPLs	78.3%	25.6%	23.3%
RRE NCOs/Total NCOs	45.0%	26.0%	24.7%
3. Performance Ratios			
RRE NPLs/Total RRE Lns	9.03%	1.76%	2.16%
RRE NCOs/Avg. RRE Lns	0.25%	0.06%	0.08%
4. Outstandings ($millions)			
Total RRE Lns	1,722,130.2	20,985.0	295,259.2
RRE NPLs	155,489.3	369.0	6,385.3
RRE NCOs	4,345.4	12.8	229.1

Table 2 - Summary of Commercial Real Estate Lending

	Large Organizations	Community Banks	
	Nation	Tri-State Area	Nation
1. Year–over–year growth			
Total CRE loans	-1.0%	5.7%	2.6%
CRE NPLs	-39.3%	-28.1%	-28.2%
CRE NCOs	-56.2%	-58.8%	-46.8%
2. Shares			
CRE Lns/Total Lns	15.5%	45.2%	44.0%
CRE NPLs/Total NPLs	12.0%	60.1%	60.3%
CRE NCOs/Total NCOs	7.3%	58.3%	46.4%
3. Performance Ratios			
CRE NPLs/Total CRE Lns	2.95%	2.81%	3.22%
CRE NCOs/Avg. CRE Lns	0.09%	0.10%	0.09%
4. Outstandings ($millions)			
Total CRE Lns	806,821.4	30,821.6	511,839.0
CRE NPLs	23,773.2	867.0	16,493.5
CRE NCOs	704.1	28.8	430.8

Table 3 - Summary of Commercial & Industrial Lending

	Large Organizations	Community Banks	
	Nation	Tri-State Area	Nation
1. Year–over–year growth			
Total C&I loans	12.9%	7.7%	7.0%
C&I NPLs	-26.7%	-2.2%	-11.3%
C&I NCOs	-27.6%	-52.5%	-28.1%
2. Shares			
C&I Lns/Total Lns	23.3%	14.1%	16.2%
C&I NPLs/Total NPLs	3.9%	11.2%	11.0%
C&I NCOs/Total NCOs	8.5%	16.7%	29.8%
3. Performance Ratios			
C&I NPLs/Total C&I Lns	0.64%	1.68%	1.60%
C&I NCOs/Avg. C&I Lns	0.07%	0.09%	0.15%
4. Outstandings ($millions)			
Total C&I Lns	1,211,529.5	9,631.7	188,436.5
C&I NPLs	7,746.8	162.0	3,008.8
C&I NCOs	822.8	8.3	277.0

Table 4 - Summary of Consumer Lending

	Large Organizations	Community Banks	
	Nation	Tri-State Area	Nation
1. Year–over–year growth			
Total Consumer loans	1.1%	3.0%	1.2%
Consumer NPLs	-22.0%	-8.9%	-4.2%
Consumer NCOs	-7.4%	23.2%	-25.4%
2. Shares			
Consumer Lns/Total Lns	13.6%	3.7%	4.3%
Consumer NPLs/Total NPLs	3.9%	0.9%	1.3%
Consumer NCOs/Total NCOs	37.2%	5.3%	7.9%
3. Performance Ratios			
Cons NPLs/Total Cons Lns	1.10%	0.48%	0.72%
Cons NCOs/Avg. Cons Lns	0.51%	0.10%	0.15%
4. Outstandings ($millions)			
Total Consumer Lns	707,144.8	2,546.5	49,752.7
Consumer NPLs	7,808.0	12.3	356.0
Consumer NCOs	3,586.2	2.6	73.0

Table 5 - Provision for Loan Losses and Loan-Loss Reserves

	Large Organizations	Community Banks	
	Nation	Tri-State Area	Nation
Loan-loss Reserve ($millions)	104,012.3	1,081.2	21,256.1
Change from Last Quarter	-17.7%	-0.4%	-1.7%
Change from Last Year	-17.9%	1.6%	-6.0%
Net Charge-Offs/LL Provision	167.6%	99.9%	110.5%
LL Provision/Operating Inc.	4.9%	4.3%	4.1%
Loan-loss Coverage Ratio	52.3%	74.9%	77.7%

Table 6 - Summary of Securities Portfolios

	Large Organizations	Community Banks	
	Nation	Tri-State Area	Nation
Securities/Assets	21.0%	21.7%	23.5%
Market Value ($millions)	2,216,609.7	22,283.6	447,572.4
Change from Last Quarter	-5.5%	1.8%	3.0%
Change from Last Year	3.4%	-0.8%	1.8%
Realized Gain/Loss	1,599.9	15.6	230.5
Pct of Average Securities	0.07%	0.07%	0.05%
Market Value/Book Value	102.2%	102.2	102.0

Table 7 - Structure of Liabilities

	Large Organizations	Community Banks	
	Nation	Tri-State Area	Nation
Deposits ($millions)	7,867,614.6	85,487.7	1,593,934.6
Pct. of Assets	74.5%	83.5%	83.9%
Change from Last Quarter	0.3%	-4.4%	-1.7%
Change from Last Year	7.1%	3.9%	2.9%
Core Deposits/Deposits	37.0%	67.2%	65.3%
Implicit Rate on Deposits	0.34%	0.70%	0.65%
Nondeposit Debt ($millions)	950,107.9	5,264.9	84,406.5
Pct. of Assets	9.0%	5.1%	4.4%
Change from Last Quarter	-7.4%	-11.9%	-24.6%
Change from Last Year	-6.9%	4.0%	-7.0%
Implicit Rate on Debt	1.48%	2.12%	2.04%

Table 8 - Capitalization Measures

	Large Organizations	Community Banks	
Ratios	Nation	Tri-State Area	Nation
Total Equity/Total Assets	11.06%	10.23%	10.86%
Change fr. Last Qtr. (basis pts)	10	27	12
Change fr. Last Yr. (basis pts)	-2	8	22
Tier 1 Leverage Ratio	8.70%	9.56%	10.02%
Change fr. Last Qtr. (basis pts)	14	24	8
Change fr. Last Yr. (basis pts)	9	9	16
Risk-Based Capital Ratio	14.21%	14.53%	16.00%
Change fr. Last Qtr. (basis pts)	-27	21	15
Change fr. Last Yr. (basis pts)	-52	-6	6