FDIC State Profile

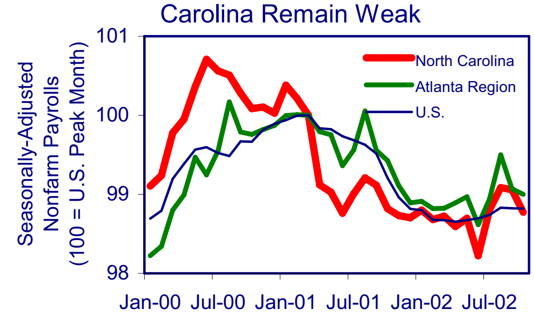
SPRING 2003

North Carolina

North Carolina is struggling to emerge from the recent recession, but significant layoffs in the finance, high-tech, and manufacturing sectors continue to threaten the recovery.

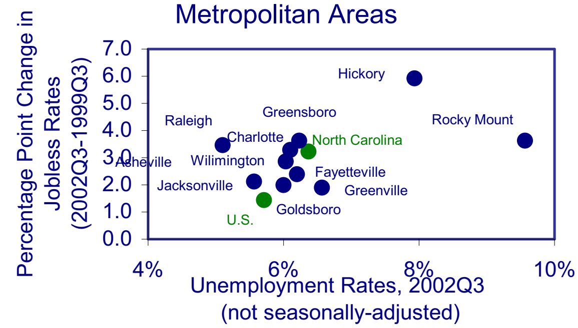
- Employment growth in North Carolina peaked in mid-2000; however, the state did not fall into recession until early 2001 (see **Chart 1**). Between the cyclical peak in June 2000 and October 2002, 76,000 jobs were lost, a decline of 1.9 percent. The economy appeared to improve by the beginning of third quarter 2002; however, a recent surge in layoff announcements in several industries could weaken the state's chances for economic recovery.
- The North Carolina labor market has worsened during the past three years, reflecting the effects of the recession. The nation's unemployment rose 1.4 percentage points between third quarter 1999 and third quarter 2002; however, the rate of unemployment in North Carolina more than doubled to 6.4 percent during the same period (see **Chart 2**).
- The performance of the North Carolina economy during the recent recession has been shaped by the industrial mix. Manufacturing remains a greater component of the state's economy than the nation's, representing nearly 20 percent of the workforce, compared to 13 percent nationally. Traditional industries, such as furniture, textiles, and apparel production, continue to play an important role in many local economies. The state's high-tech sector also expanded during the 1990s. In addition, banking is an important component of the ***Charlotte*** and ***Greensboro*** MSA economies. Typically, a relatively high level of economic diversity may insulate economies during downturns. However, because of the specific mix of industries, this has not been the case for the North Carolina economy. Job losses have increased in the state's traditional and high-tech industries, and employment growth has declined in the financial services sector during the past few years (see **Chart 3**). The ***Hickory*** MSA is a good example of this trend as employment shifted from the traditional industrial base, for example, furniture manufacturing, into fiber optic cable manufacturing during the 1990s. The jobless rate increased in the telecommunications industry (see **Chart 4**), diluting what may have been positive effects of industrial diversification.
- Housing markets appear to be weakening in the ***Raleigh***, Hickory, Charlotte, Greensboro, and ***Greenville*** MSAs where home price appreciation has moderated substantially. Earlier this year, builders in the Raleigh metro area

Chart 1: Employment Conditions in North Carolina Remain Weak



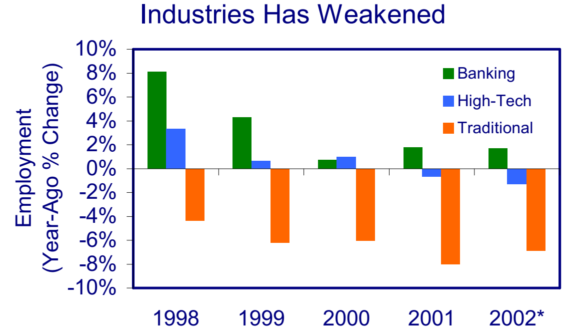
Source: Bureau of Labor Statistics/Haver Analytics

Chart 2: The Deterioration in Labor Market Conditions Varied Across North Carolina Metropolitan Areas



Source: Bureau of Labor Statistics/Haver Analytics

Industries Has Weakened

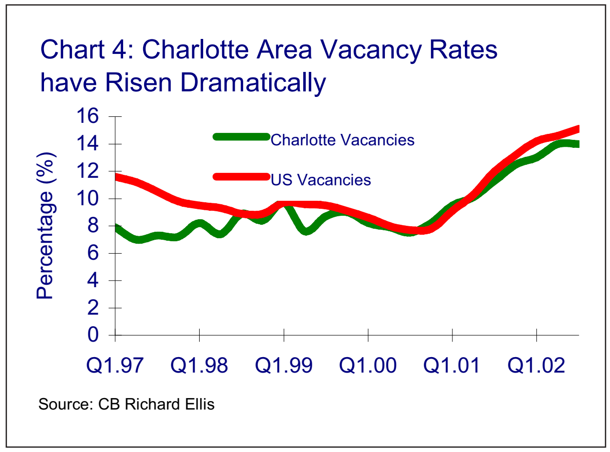


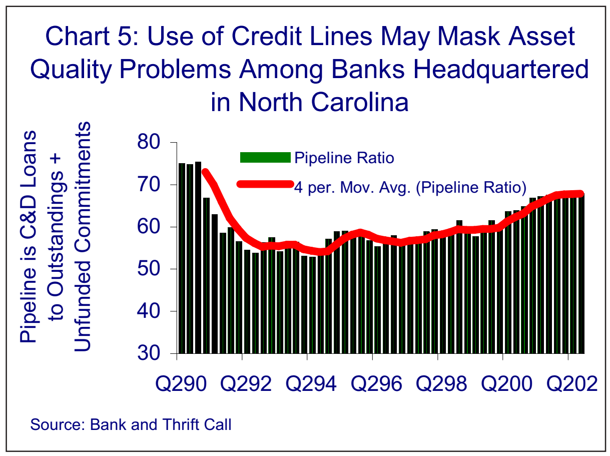
*Forecast (May 2002)
Source: Global Insights, Inc.

increased inventories in expectation of a late year recovery. Continued weak economic growth, however, has cooled demand, and builders have cut prices to reduce inventories.

Community banks headquartered in North Carolina[1] report sound conditions, but heightened balance sheet risk combined with economic weakness could lead to asset quality concerns.

- Overall performance among community banks headquartered in North Carolina improved during the year ending September 30, 2002. After reporting negative income growth in the third quarter of 2001, merger-adjusted net income growth at September 30, 2002, rose 42 percent as higher net interest margins (NIMs) contributed to the increase. NIMs improved for thirty-eight banks compared to fifteen a year earlier.
- Although lowering funding costs, aggressive interest rate cuts by the Federal Reserve helped to compress margins in 2001 as core deposits were slow to reprice at most of the state's community banks. Continued use of noncore funding, combined with the repricing of some core deposits in 2002, however, was instrumental in driving NIMs higher at these institutions during the first nine months of the year.
- Rapid loan growth has continued even as the economy has weakened. Total loans grew 16 percent year-over-year with the majority of the increase occurring in commercial real estate (CRE) loans. Among community banks headquartered in North Carolina at September 30, 2002, CRE loans comprised 19 percent of assets, up from 17 percent a year ago.
- Loan portfolio earnings were augmented by a shift into higher-yielding CRE loans as the average return on assets increased to 1.07 percent, up from 0.84 percent a year earlier. While the increased exposure has bolstered profitability, community banks headquartered in the state also may have heightened the level of balance sheet risk. The average CRE exposure among community banks headquartered in the Raleigh, Charlotte, and Hickory MSAs[2] was significant with each MSA reporting at least 20 percent of assets held in CRE loans, increasing the vulnerability of institutions headquartered in these areas to rising vacancy rates. Banks headquartered in the Charlotte MSA, however, had not reported asset quality problems as of September 30, 2002, despite a 14 percent office vacancy rate. The vacancy rate in this MSA has risen steadily, tracking the increase in the nation's rate, since December 2000 (see **Chart 4**). Noncurrent CRE loan levels among community banks in the Raleigh MSA have improved. However, nonperforming CRE loans held by community banks in the Raleigh MSA have trended higher.





- Community bank construction and development (C&D) loans, which are primarily for residential construction, continued to represent a significant portion of total assets at 9.5 percent. Banks headquartered in North Carolina had not reported any deterioration in asset quality in this loan category as of third quarter 2002. In fact, noncurrent loan levels improved during the past year. However, debt restructurings and the use of credit lines may be keeping payments current, masking any weakening in C&D loan quality (see **Chart 5**).

[1] "Community banks" are defined in this article as insured institutions that hold less than $1 billion in assets. This definition excludes specialty institutions.

[2] Only MSAs with 4 or more banks were used.

North Carolina at a Glance

General Information	Sep-02	Sep-01	Sep-00	Sep-99	Sep-98
Institutions (#)	62	64	59	59	48
Total Assets (in thousands)	17,832,896	15,790,134	13,686,247	12,135,615	10,199,964
New Institutions (# < 3 years)	13	17	17	21	13
New Institutions (# < 9 years)	35	35	31	28	17

Capital	Sep-02	Sep-01	Sep-00	Sep-99	Sep-98
Tier 1 Leverage (median)	9.22	9.38	9.99	11.45	10.61

Asset Quality	Sep-02	Sep-01	Sep-00	Sep-99	Sep-98
Past-Due and Nonaccrual (median %)	1.16%	1.33%	0.87%	0.89%	1.06%
Past-Due and Nonaccrual > = 5%	2	1	3	1	2
ALLL/Total Loans (median %)	1.46%	1.40%	1.47%	1.45%	1.44%
ALLL/Noncurrent Loans (median multiple)	3.14	2.79	3.94	4.20	4.99
Net Loan Losses/Loans (aggregate)	0.21%	0.20%	0.12%	0.14%	0.25%

Earnings	Sep-02	Sep-01	Sep-00	Sep-99	Sep-98
Unprofitable Institutions (#)	9	11	12	15	8
Percent Unprofitable	14.52%	17.19%	20.34%	25.42%	16.67%
Return on Assets (median %)	0.78	0.74	0.88	0.86	0.97
25th Percentile	0.55	0.14	0.10	-0.84	0.42
Net Interest Margin (median %)	3.92%	3.85%	4.31%	4.36%	4.69%
Yield on Earning Assets (median)	6.58%	8.02%	8.65%	7.91%	8.49%
Cost of Funding Earning Assets (median)	2.44%	4.15%	4.21%	3.50%	3.75%
Provisions to Avg. Assets (median)	0.34%	0.36%	0.32%	0.25%	0.28%
Noninterest Income to Avg. Assets (median)	0.95%	0.82%	0.74%	0.74%	0.80%
Overhead to Avg. Assets (median)	3.04%	3.22%	3.44%	3.42%	3.51%

Liquidity/Sensitivity	Sep-02	Sep-01	Sep-00	Sep-99	Sep-98
Loans to Deposits (median %)	87.97%	86.55%	86.47%	83.33%	80.14%
Loans to Assets (median %)	72.72%	70.08%	71.44%	67.11%	66.11%
Brokered Deposits (# of Institutions)	26	17	12	8	3
Bro. Deps./Assets (median for above inst.)	6.88%	3.78%	2.46%	1.10%	0.27%
Noncore Funding to Assets (median)	24.67%	23.91%	21.33%	17.27%	15.68%
Core Funding to Assets (median)	63.16%	64.08%	65.65%	67.48%	69.90%

Bank Class	Sep-02	Sep-01	Sep-00	Sep-99	Sep-98
State Nonmember	51	54	53	52	41
National	5	5	5	5	5
State Member	6	5	1	2	2
S&L	0	0	0	0	0
Savings Bank	0	0	0	0	0
Mutually Insured	0	0	0	0	0

MSA Distribution	# of Inst.	Assets	% Inst.	% Assets
No MSA	21	6,297,215	33.87%	35.31%
Greensboro—Winston-Salem—High Point NC	13	4,306,840	20.97%	24.15%
Raleigh-Durham-Chapel Hill NC	8	2,774,612	12.90%	15.56%
Charlotte-Gastonia-Rock Hill NC-SC	8	1,312,579	12.90%	7.36%
Hickory-Morganton NC	4	1,598,382	6.45%	8.96%
Asheville NC	2	252,521	3.23%	1.42%
Wilmington NC	1	110,658	1.61%	0.62%
Rocky Mount NC	1	48,073	1.61%	0.27%
Norfolk-Virginia Bch-Newport News VA-NC	1	115,128	1.61%	0.65%
Greenville NC	1	20,697	1.61%	0.12%
Goldsboro NC	1	861,042	1.61%	4.83%
Fayetteville NC	1	135,149	1.61%	0.76%