FDIC State Profile

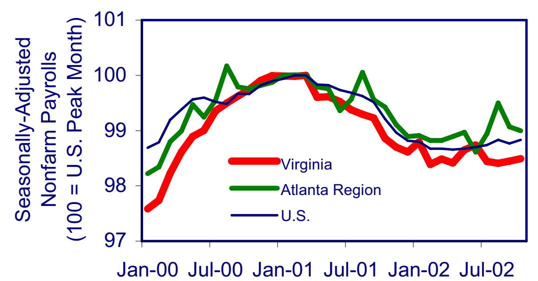
SPRING 2003

Virginia

Payrolls remain flat as Virginia struggles to emerge from the recession.

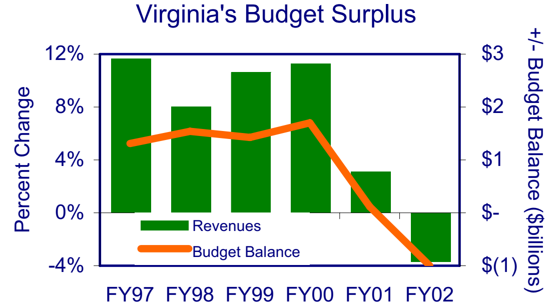
- Payrolls in Virginia, on a year-over-year basis, continued to contract through the first 10 months of 2002 (see **Chart 1**). Although the recent erosion in payrolls appeared to end, employment still remained 1.5 percent or over 50,000 jobs below its cyclical peak in March 2001.
- The transition from economic expansion to recession in Virginia was rapid and sharp. Between 1992 and 2000, Virginia's job growth averaged 2.7 percent annually compared to the third quarter 2002 year-ago decline of 0.8 percent. The change was even more pronounced in some metropolitan areas. In ***Northern Virginia,*** for example, job growth averaged above 4 percent annually between 1992 and 2000 but down 0.9 percent over the past year ending third quarter 2002—a difference of nearly 500 basis points.
- Although labor market conditions varied across the state, the highest county unemployment rates in third quarter 2002 continued to be found in south-central areas of the state where key manufacturing industries, such as textiles & apparel and furniture, have been hit hard by the recession. Although this region of the state has traditionally experienced high rates of unemployment, levels have risen by more than one percentage point in some areas over the past year ending third quarter 2002. In contrast, several southwestern counties in the state experienced significant declines in jobless over the past year. These declines, however, may not be the result of improving economic conditions but may be due labor force shrinkage as unemployed left the area to seek jobs elsewhere.
- The recent recession has had a substantial impact on Virginia's state finances. In FY-2001, tax revenue growth fell by more than half (see **Chart 2**). This was followed by a nearly 4 percent decline in revenue during FY-2002. After years of budget surpluses, the state now faces a deficit of nearly $1 billion. The magnitude of Virginia's budget difficulties was reflected in mid-October 2002 by Governor Warner's announcement of over $850 million in spending cuts, which would include the layoffs of 1,800 state employees.
- The recent recession had an adverse affect on Northern Virginia's commercial real estate markets where office absorption generally has declined since 2001, even as new completions remained at comparatively high levels (see **Chart 3**). Consequently, office vacancy rates increased sharply. Several submarkets saw vacancy rates climb well into the double-digits in third quarter 2002.

Chart 1: Employment in Virginia Remains Flat



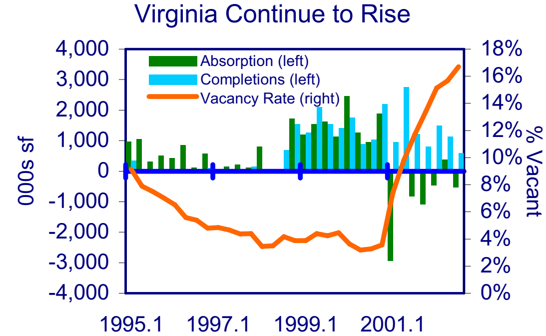
Source: Bureau of Labor Statistics/Haver Analytics

Chart 2: Tax Revenue Shortfalls Deflate Virginia's Budget Surplus



Note: Fiscal year runs June to June.
Source: Office of the Virginia Secretary of Finance

Chart 3: Office Vacancy Rates in Northern Virginia Continue to Rise

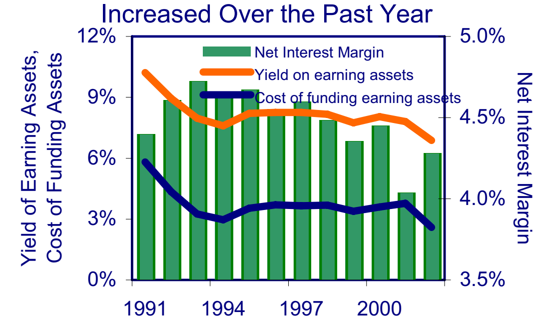


Source: Torto Wheaton Research

Banking conditions in the State of Virginia have remained solid throughout the current cycle, but commercial real estate lending is a particular concern.

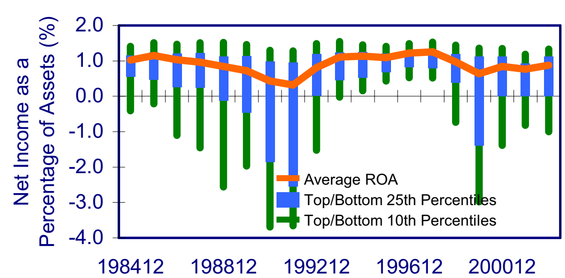
- Banking conditions in the State of Virginia have remained solid throughout the current cycle. On a merger adjusted basis, Net income rose 32 percent during the 12-months ending September 30, 2002, compared to only 11 percent growth in the year earlier period.
- Although lowering funding costs, aggressive interest rate cuts by the Federal Reserve helped to compress margins in 2001 as core deposits were slow to reprice at most 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 banks.
- Profitability measures for community banks improved year over year with the average return on assets (ROA) ratio rising 11 basis points to 0.88 percent for the first 9 months of the year (see **Chart 4**). However, the performance of the institutions operating in the bottom 10th percentile weakened slightly. These banks saw their average ROA fall to a negative 1.00 percent at period end, down slightly from a year earlier. About fifty percent of the banks in this group are de novos[1]; a group often expected to lose money.
- Loan growth at Virginia's community institutions has continued at a relatively brisk pace, averaging roughly 14 percent in the last two periods. However, growth is concentrated in the riskier lending category of commercial real estate (CRE), which may be inconsistent with current economic conditions. CRE now accounts for close to 18 percent of assets, up from 17 percent in the year earlier period.
- Among MSAs with at least five community institutions, the ***Norfolk, Roanoke,*** and ***Washington, DC-MD-VA-WV*** MSAs appear most vulnerable to a renewed downturn. As of third quarter 2002, institutions with concentrations in CRE (25 percent or more of total assets) accounted for at least 35 percent of the banks in these MSAs. Although noncurrent CRE loan levels were manageable, rising office vacancy rates, similar to those seen in the Northern Virginia market, could have a disproportionately negative affect on delinquency levels at community banks in these areas.

Chart 4: Margins at Virginia Community Banks Increased Over the Past Year



Source: Bank Call Reports (June 30 data)

Chart 5: The Average Community Bank[1] Return on Assets in Virginia



[1]Commercial banks with assets less $1 billion in assets.
Source: Bank Call Reports

[1] De novo institutions have been in operation no longer than 3 years.

Virginia at a Glance

General Information	Sep-02	Sep-01	Sep-00	Sep-99	Sep-98
Institutions (#)	116	129	133	127	134
Total Assets (in thousands)	29,487,817	29,327,546	26,389,242	23,482,696	24,119,068
New Institutions (# < 3 years)	9	18	21	14	8
New Institutions (# < 9 years)	32	31	30	24	15

Capital	Sep-02	Sep-01	Sep-00	Sep-99	Sep-98
Tier 1 Leverage (median)	8.77	8.59	9.20	9.20	9.28

Asset Quality	Sep-02	Sep-01	Sep-00	Sep-99	Sep-98
Past-Due and Nonaccrual (median %)	1.13%	1.58%	1.49%	1.65%	1.96%
Past-Due and Nonaccrual > = 5%	10	11	9	11	18
ALLL/Total Loans (median %)	1.19%	1.14%	1.16%	1.15%	1.20%
ALLL/Noncurrent Loans (median multiple)	2.64	2.75	2.73	1.80	1.84
Net Loan Losses/Loans (aggregate)	0.17%	0.19%	0.10%	0.19%	0.19%

Earnings	Sep-02	Sep-01	Sep-00	Sep-99	Sep-98
Unprofitable Institutions (#)	10	11	14	14	3
Percent Unprofitable	8.62%	8.53%	10.53%	11.02%	2.24%
Return on Assets (median %)	1.13	0.95	1.16	1.14	1.24
25th Percentile	0.82	0.56	0.80	0.86	0.98
Net Interest Margin (median %)	4.29%	4.07%	4.43%	4.35%	4.52%
Yield on Earning Assets (median)	6.81%	7.85%	8.22%	7.82%	8.25%
Cost of Funding Earning Assets (median)	2.60%	3.94%	3.86%	3.46%	3.75%
Provisions to Avg. Assets (median)	0.21%	0.18%	0.18%	0.14%	0.15%
Noninterest Income to Avg. Assets (median)	0.58%	0.58%	0.60%	0.58%	0.60%
Overhead to Avg. Assets (median)	2.88%	2.98%	2.96%	2.94%	2.91%

Liquidity/Sensitivity	Sep-02	Sep-01	Sep-00	Sep-99	Sep-98
Loans to Deposits (median %)	76.11%	78.81%	79.35%	75.68%	73.71%
Loans to Assets (median %)	66.21%	66.63%	66.73%	64.87%	63.21%
Brokered Deposits (# of Institutions)	18	15	9	7	7
Bro. Deps./Assets (median for above inst.)	2.25%	5.39%	4.21%	4.07%	2.04%
Noncore Funding to Assets (median)	15.20%	14.59%	14.52%	11.44%	10.92%
Core Funding to Assets (median)	74.17%	74.64%	75.04%	77.72%	77.92%

Bank Class	Sep-02	Sep-01	Sep-00	Sep-99	Sep-98
State Nonmember	18	18	19	19	20
National	31	32	30	28	24
State Member	67	79	84	80	90
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	55	12,247,700	47.41%	41.53%
Washington DC-MD-VA-WV PMSA	21	7,205,404	18.10%	24.44%
Richmond-Petersburg VA	12	2,399,207	10.34%	8.14%
Norfolk-Virginia Bch-Newport News VA-NC	10	3,171,174	8.62%	10.75%
Roanoke VA	5	1,176,147	4.31%	3.99%
Lynchburg VA	4	557,477	3.45%	1.89%
Danville VA	4	1,157,521	3.45%	3.93%
Charlottesville VA	3	459,261	2.59%	1.56%
Johnson City-Kingsport-Bristol TN-VA	2	1,113,926	1.72%	3.78%