FDIC State Profile

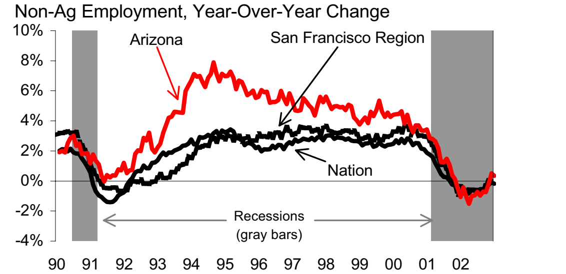
SPRING 2003

Arizona

Nonfarm employment in Arizona was flat during the year ending December 2002 after falling during the previous year.

- Payroll jobs rose 0.2 percent during 2002 (see **Chart 1**) in contrast to the state's strong growth in the 1990s.
- The manufacturing, transportation and public utilities, and finance, insurance, and real estate sectors experienced the greatest declines in employment. Job growth in the government sector helped to mitigate these declines.
- However, a looming budget deficit for fiscal year 2004 has prompted layoffs in the state government sector.

Chart 1: Arizona's Employment Rebounded in Late 2002

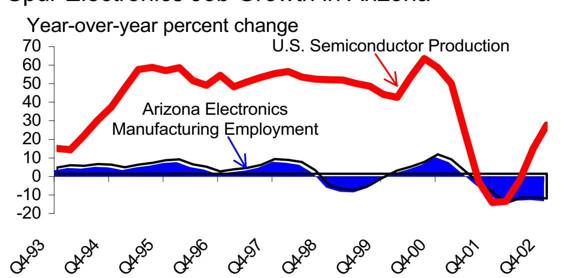


Source: Bureau of Labor Statistics

Employment in the state's high-tech sector has declined significantly, reflecting the recent downturn in this industry.

- Employment in the electronics manufacturing sector declined 13.3 percent during the past year (see **Chart 2**).
- According to Economy.com, Arizona faces increasing competition from other states for these high-tech manufacturing operations because of the state's relatively high labor costs.
- High-tech manufacturing in the ***Tucson*** metropolitan statistical area (MSA) depends more on demand for defense-related products than does the ***Phoenix*** area. As a result, the Tucson economy may rebound faster in response to increased U.S. military spending. The recent increase in national security spending, however, has not yet affected manufacturing jobs in this metropolitan area.

Chart 2: Rising Semiconductor Output Did Not Spur Electronics Job Growth in Arizona



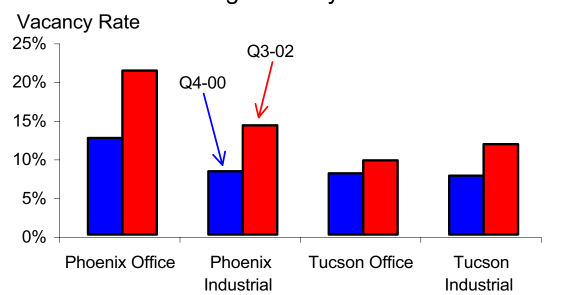
Note: Electronics manufacturing employment includes Standard Industrial Classifications 35 and 36

Sources: Bureau of Labor Statistics, Federal Reserve Board

Office and industrial vacancy rates have risen somewhat in the Tucson MSA, but more significantly in the Phoenix MSA (see Chart 3).

- According to Torto Wheaton Research (TWR), the Phoenix MSA office and industrial vacancy rates now exceed the national averages. In addition, TWR reports that the office space rental rate in the Phoenix MSA as of third quarter 2002 declined 9.9 percent from the peak in 2000. The rental rate in the Tucson MSA rose 8 percent during the same period.
- Property and Portfolio Research, LLC (PPR) data indicate that, with the exception of hotels, vacancy rates in these MSAs remain below those experienced during the serious real estate downturn during the late 1980s and early 1990s.

Chart 3: The Sluggish State Economy Contributed to Rising Vacancy Rates

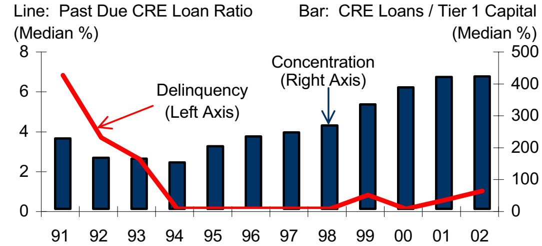


Source: Torto Wheaton Research

Weakening CRE market conditions could adversely affect the 18 established community institutions[1] headquartered in the Phoenix MSA that hold CRE loans.

- As of third quarter 2002, the median CRE loan-to-Tier 1 capital ratio among these institutions was 415 percent, more than twice the concentration reported ten years earlier (see **Chart 4**).[2] The group's median construction and development (C&D) loan-to-Tier 1 capital ratio more than quadrupled over the past ten years to 110 percent. Median CRE and C&D concentration measures far exceeded levels reported by MSA-based institutions nationwide.
- Increasing CRE vacancy rates pushed up CRE loan delinquencies among some of Phoenix's established community institutions (see **Chart 4**). However, past-due CRE loan ratios remained well below levels reported in the early 1990s, when rapid declines in CRE market conditions battered insured institution asset quality.

Chart 4: Community Institutions in the Phoenix Area Report High CRE Loan Exposures

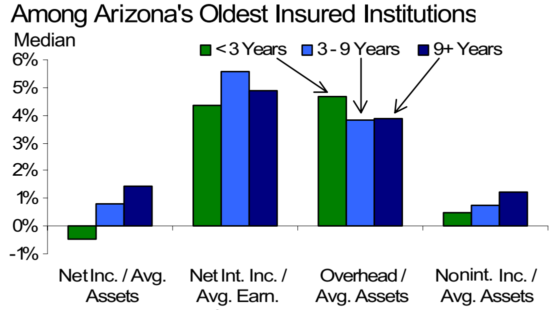


Notes: Includes insured institutions based in the Phoenix metropolitan area, open at least three years, with less than $1 billion in assets. CRE = commercial real estate.
Source: Phoenix Bank and Thrift Call Reports (September of each year)

Earnings among Arizona's insured institutions were weak through third quarter 2002, primarily because of the state's high proportion of relatively young institutions (i.e., less than 9 years old).

- The state's median annualized return on average assets (ROA) ratio declined year-over-year through September 2002 from 1.11 to 0.77 percent, and compared unfavorably to a 1.10 percent national median. Narrower net interest margins among the state's predominantly asset-sensitive institutions hampered earnings.
- ROA ratios were weaker among institutions less than nine years old, which accounted for 58 percent of the state's insured institutions (see **Chart 5**). Insured institutions in operation more than nine years reported strong ROA ratios, primarily because of the high proportion of specialty consumer lenders.

Chart 5: Earnings Performance Was Strongest Among Arizona's Oldest Insured Institutions

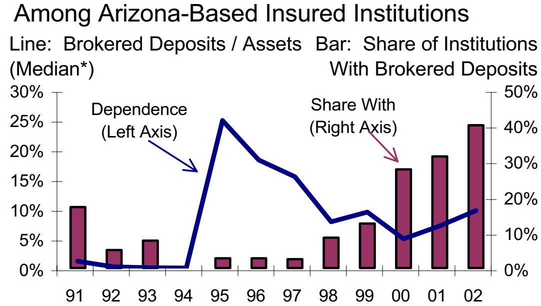


Source: Arizona Bank and Thrift Call Reports (September 30, 2002)

Insured institutions based in Arizona relied increasingly on non-core funding sources,[3] including brokered deposits.

- The median non-core funds-to-total asset ratio among Arizona's insured institutions increased from 8 to 18 percent during the past decade.
- Brokered deposits, traditionally one of the less stable components of non-core funds, now represent an important source of funding for many institutions. The share of Arizona-based institutions using brokered funds increased to 40 percent by September 2002 (see **Chart 6**). Brokered deposits now fund nearly 10 percent of these institutions' assets.

Chart 6: Brokered Deposit Usage Increased Among Arizona-Based Insured Institutions



Note: * Median is calculated on insured institutions holding brokered deposits.
Source: Arizona Bank and Thrift Call Reports (September of each year)

[1] Established community institutions are defined as insured institutions holding less than $1 billion in total assets and open at least three years.

[2] CRE loans include mortgages secured by nonfarm-nonresidential, multifamily, and construction projects.

[3] Non-core funds include brokered deposits, jumbo time deposits, foreign office deposits, and other borrowed funds such as Federal funds purchased and reverse repurchase agreements.

Arizona at a Glance

General Information	Sep-02	Sep-01	Sep-00	Sep-99	Sep-98
Institutions (#)	45	48	47	48	47
Total Assets (in thousands)	46,836,634	65,313,389	57,725,458	47,792,146	38,753,345
New Institutions (# < 3 years)	11	14	14	15	14
New Institutions (# < 9 years)	26	26	26	26	23

Capital	Sep-02	Sep-01	Sep-00	Sep-99	Sep-98
Tier 1 Leverage (median)	9.05	9.72	9.21	9.67	9.84

Asset Quality	Sep-02	Sep-01	Sep-00	Sep-99	Sep-98
Past-Due and Nonaccrual (median %)	0.76%	1.40%	1.02%	0.45%	0.59%
Past-Due and Nonaccrual ≥ 5%	3	6	2	1	3
ALLL/Total Loans (median %)	1.23%	1.29%	1.21%	1.23%	1.36%
ALLL/Noncurrent Loans (median multiple)	2.46	2.01	2.81	2.74	4.27
Net Loan Losses/Loans (aggregate)	5.24%	2.49%	1.88%	2.53%	3.12%

Earnings	Sep-02	Sep-01	Sep-00	Sep-99	Sep-98
Unprofitable Institutions (#)	10	15	12	12	9
Percent Unprofitable	22.22%	31.25%	25.53%	25.00%	19.15%
Return on Assets (median %)	0.77	1.11	0.99	1.00	1.18
25th Percentile	0.11	-1.09	0.19	0.27	0.49
Net Interest Margin (median %)	4.84%	4.98%	5.59%	5.24%	5.40%
Yield on Earning Assets (median)	7.00%	8.50%	9.03%	8.24%	8.60%
Cost of Funding Earning Assets (median)	2.14%	3.57%	4.01%	3.02%	3.22%
Provisions to Avg. Assets (median)	0.23%	0.24%	0.22%	0.27%	0.21%
Noninterest Income to Avg. Assets (median)	0.87%	0.72%	0.64%	0.86%	0.83%
Overhead to Avg. Assets (median)	4.18%	4.47%	4.23%	4.24%	4.17%

Liquidity/Sensitivity	Sep-02	Sep-01	Sep-00	Sep-99	Sep-98
Loans to Deposits (median %)	85.11%	79.11%	82.04%	77.49%	64.86%
Loans to Assets (median %)	72.31%	66.85%	70.92%	61.72%	56.45%
Brokered Deposits (# of Institutions)	18	15	13	6	4
Bro. Deps./Assets (median for above inst.)	9.68%	7.08%	4.91%	9.42%	7.76%
Noncore Funding to Assets (median)	17.60%	16.17%	15.77%	13.73%	9.95%
Core Funding to Assets (median)	67.09%	62.27%	67.51%	73.26%	75.20%

Bank Class	Sep-02	Sep-01	Sep-00	Sep-99	Sep-98
State Nonmember	20	20	20	23	22
National	16	18	17	16	15
State Member	6	6	6	6	7
S&L	0	0	0	0	0
Savings Bank	3	4	4	3	3
Mutually Insured	0	0	0	0	0

MSA Distribution	# of Inst.	Assets	% Inst.	% Assets
Phoenix-Mesa AZ	32	42,648,509	71.11%	91.06%
Tucson AZ	5	3,073,821	11.11%	6.56%
Yuma AZ	3	143,548	6.67%	0.31%
Las Vegas NV-AZ	3	843,244	6.67%	1.80%
Flagstaff AZ	1	33,280	2.22%	0.07%
No MSA	1	94,232	2.22%	0.20%