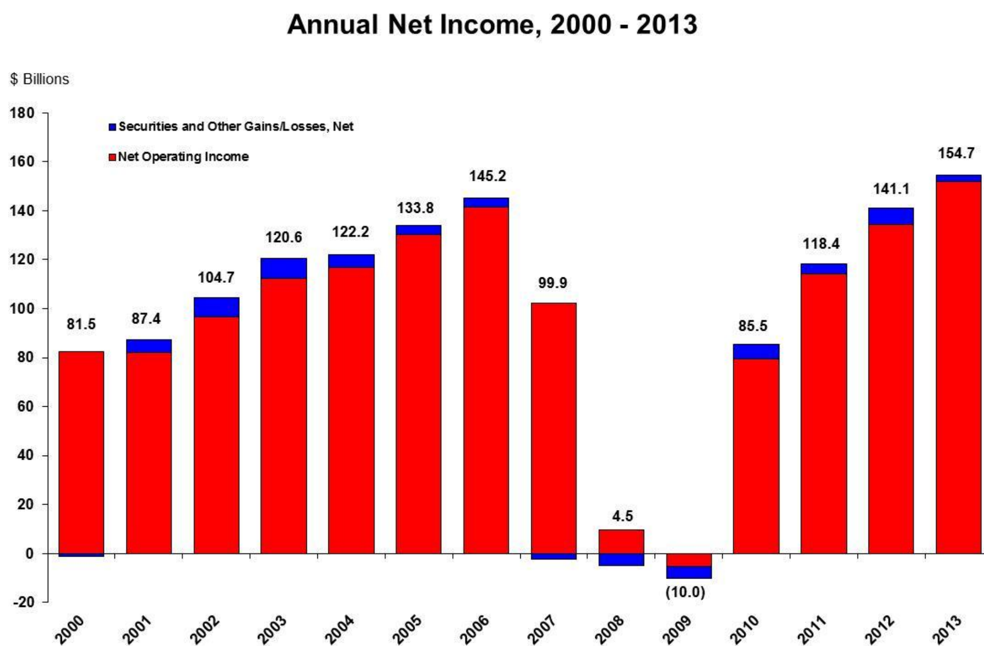
Opening Statement by FDIC Chairman Martin J. Gruenberg on the Fourth Quarter 2013 Quarterly Banking Profile
February 26, 2014

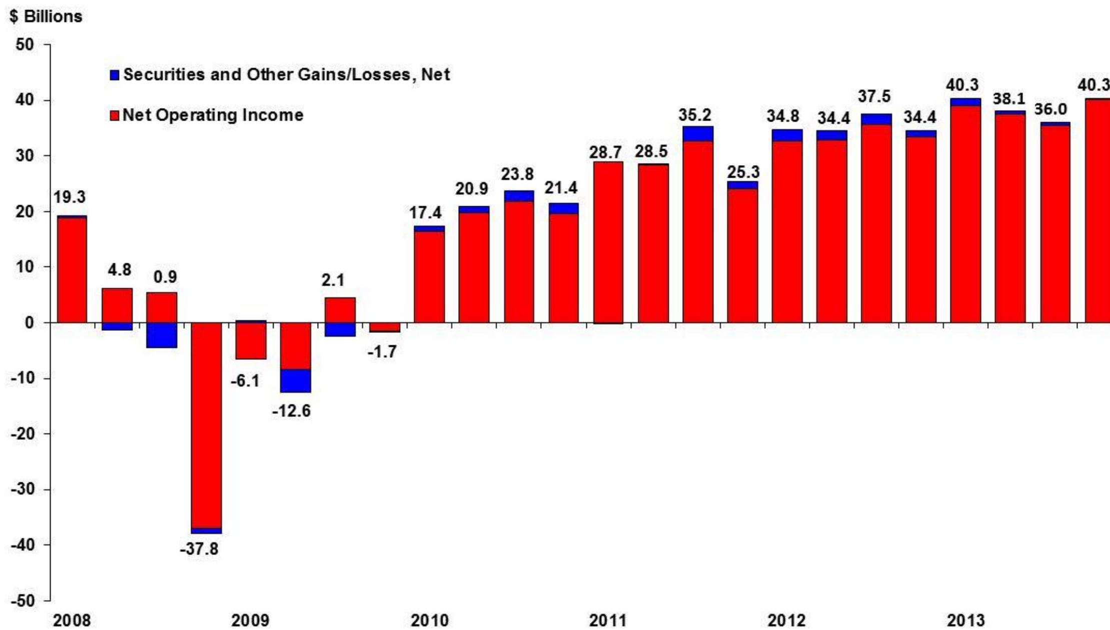
Good morning, and welcome to our release of fourth quarter and full year 2013 results for FDIC-insured institutions.

Chart 1



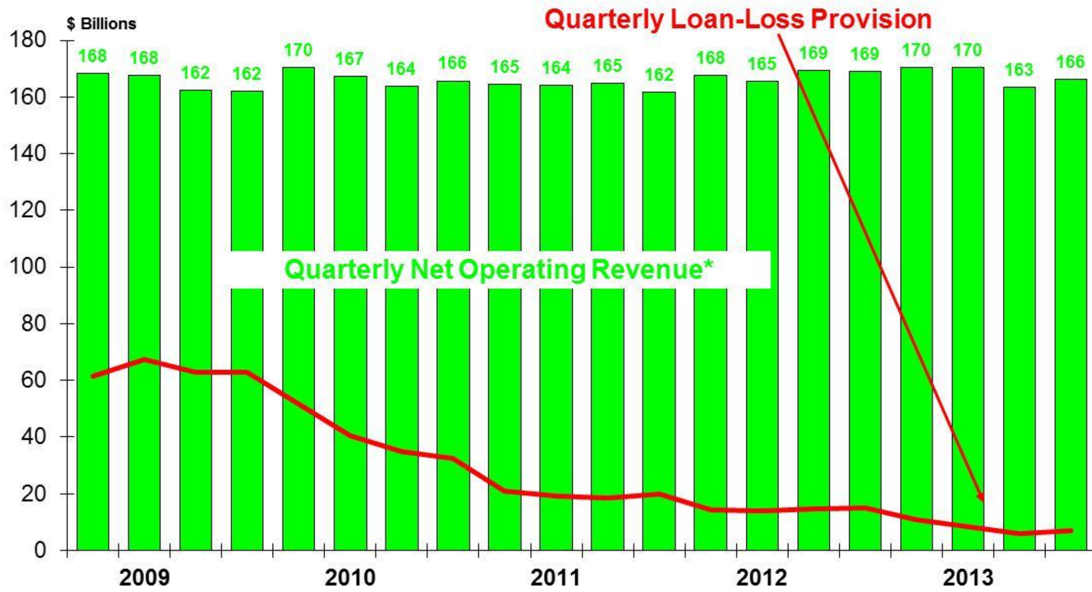
Our first chart shows annual net income in the banking industry from 2000. The improvement in the performance of banks since the financial crisis is evident in this chart, as annual net income totaled 155 billion dollars in 2013.

Chart 2



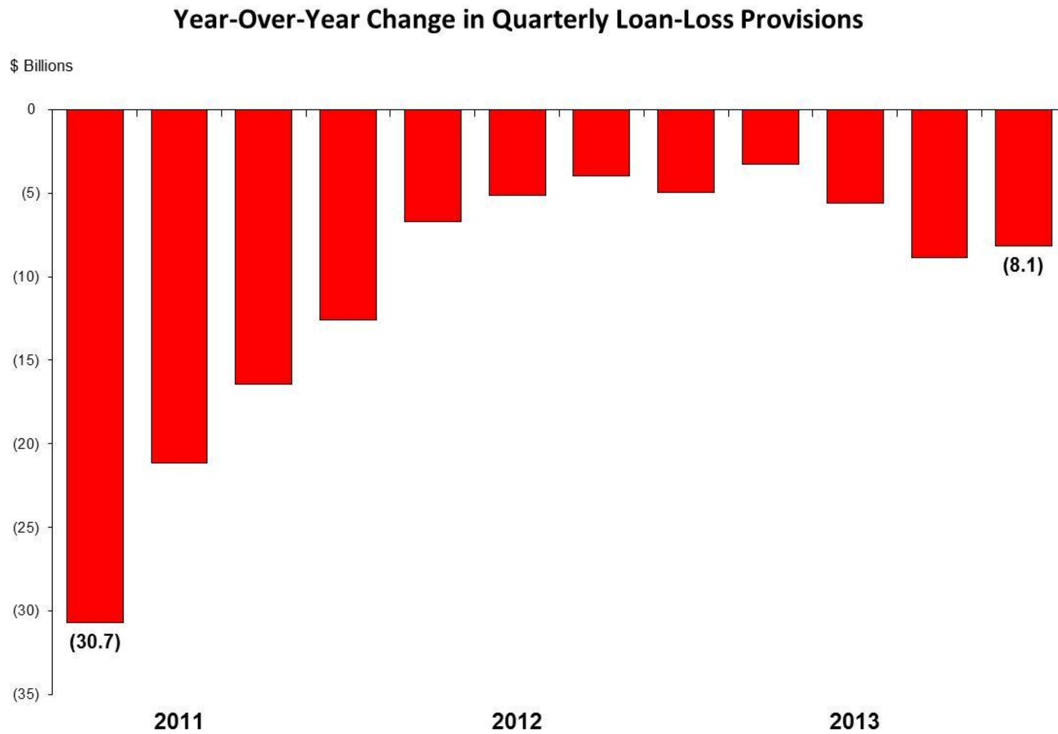
The second chart shows the trend in quarterly earnings over the past six years. Fourth-quarter net income totaled 40.3 billion dollars, nearly 6 billion dollars more than a year ago. Over half of all banks reported higher earnings from a year ago, and industry earnings have posted a year-over-year increase in 17 of the last 18 quarters.

Chart 3



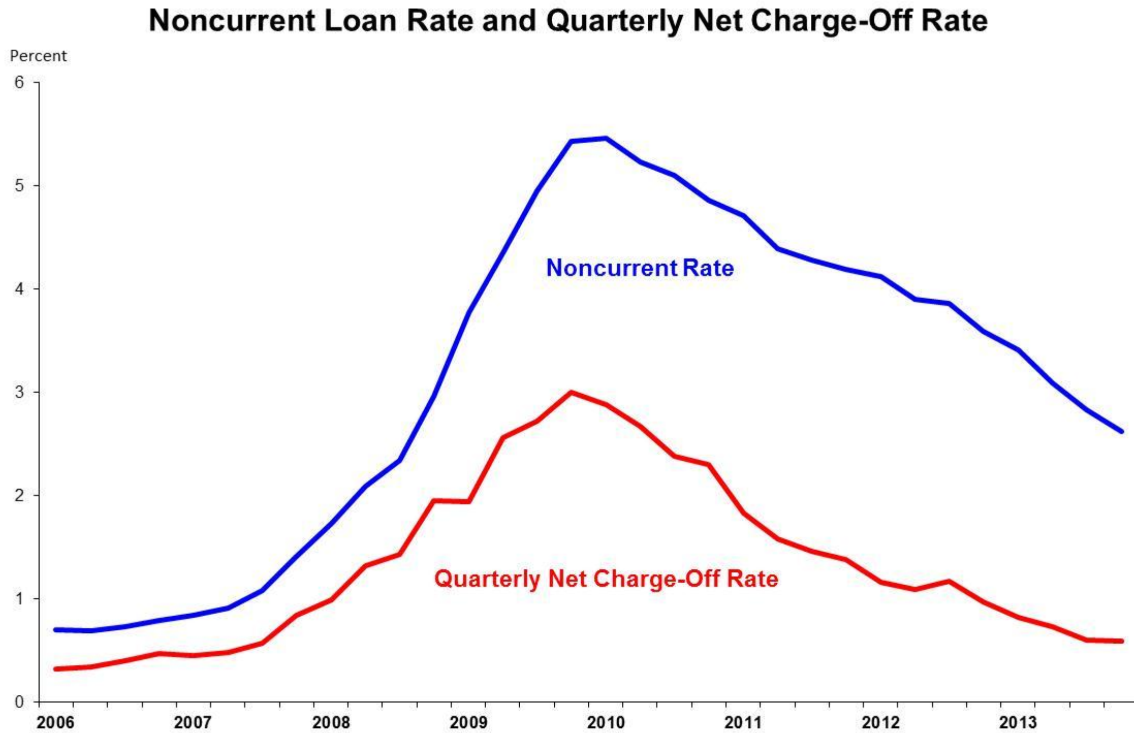
However, the industry continues to experience difficulty growing revenue. The next chart shows that quarterly net operating revenue—which is net interest income plus non-interest income—was lower than a year ago for a second consecutive quarter. Like last quarter, reduced mortgage refinancing activity resulted in a sharp drop in year-over-year non-interest income from mortgage sales, securitization, and servicing. In contrast, net interest income posted a year-over-year increase for the first time in five quarters due to an increase in loan balances and other interest-bearing investments. However, the increase was not enough to make up for the decline in mortgage refinancing activity.

Chart 4



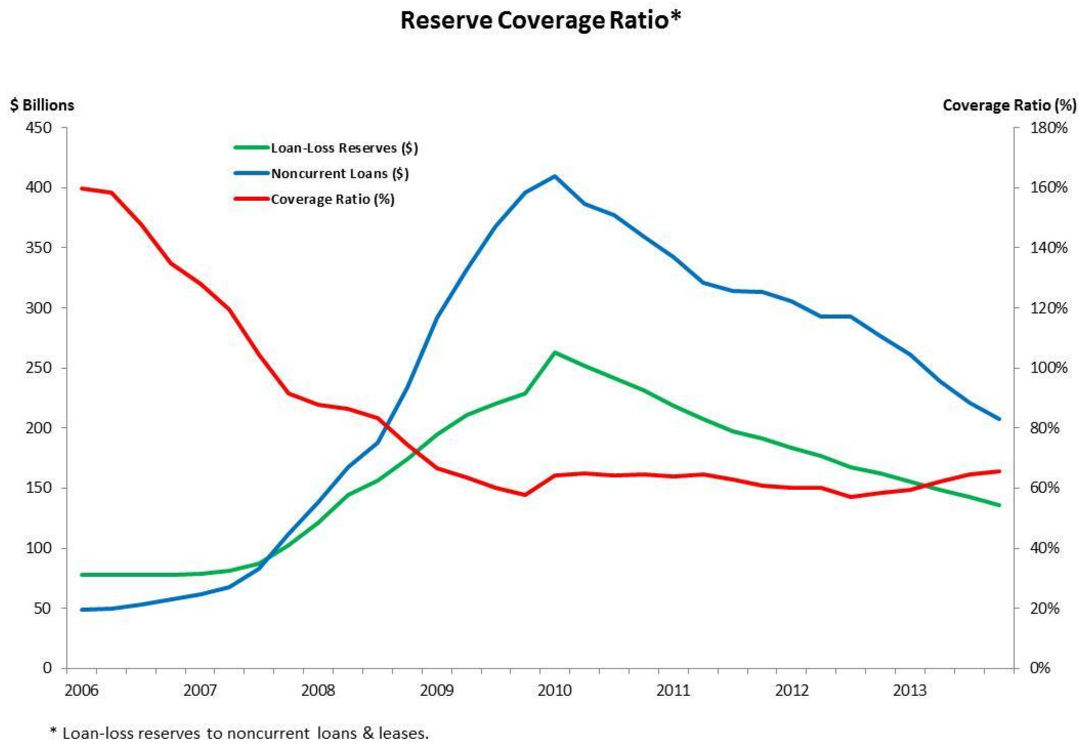
The industry remains dependent on declining loan-loss provisions to generate earnings improvement. Like previous quarters, a decline in loss provisions was the single largest component of the improvement in industry earnings. Banks set aside 7 billion dollars in loss provisions in the fourth quarter, which was over 8 billion dollars less than a year earlier.

Chart 5



This chart illustrates the ongoing improvement in asset quality that has coincided with the downward trend in loss provisions. The noncurrent loan rate and the quarterly net charge-off rate both have been trending down along a similar path. While banks continue to remove nonperforming loans from their balance sheets, noncurrent loan balances remain elevated.

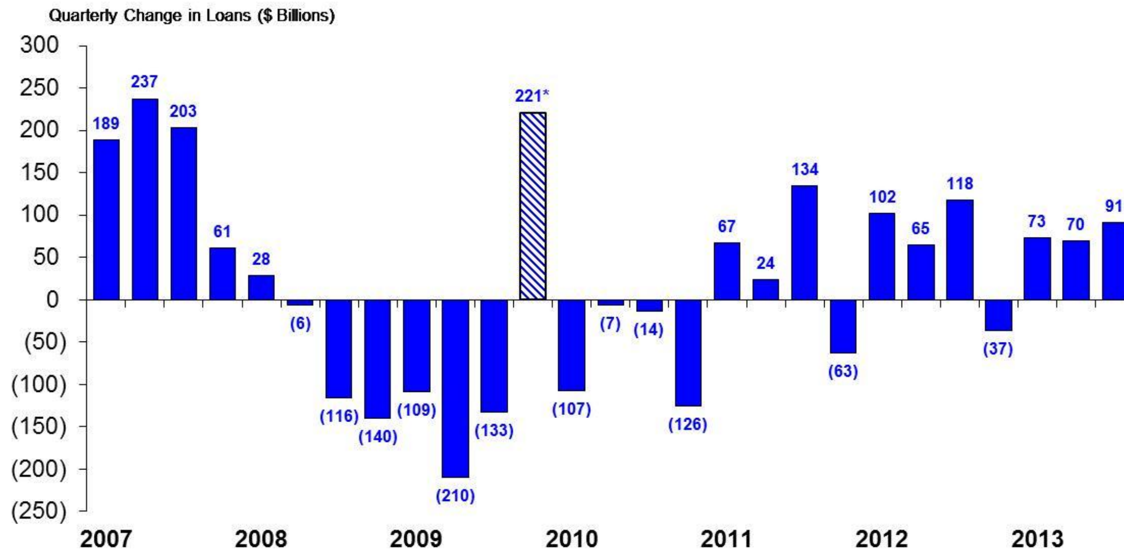
Chart 6



Lower provisions have contributed to a decline in loan-loss reserves. As the next chart shows, reserves have been declining for more than four years. However, over the last five quarters, noncurrent loan balances have fallen more rapidly than reserves. As a result, the coverage ratio—which is reserves to noncurrent loans—has been rising, although it remains below pre-crisis levels.

Chart 7

Quarterly Change in Loan Balances

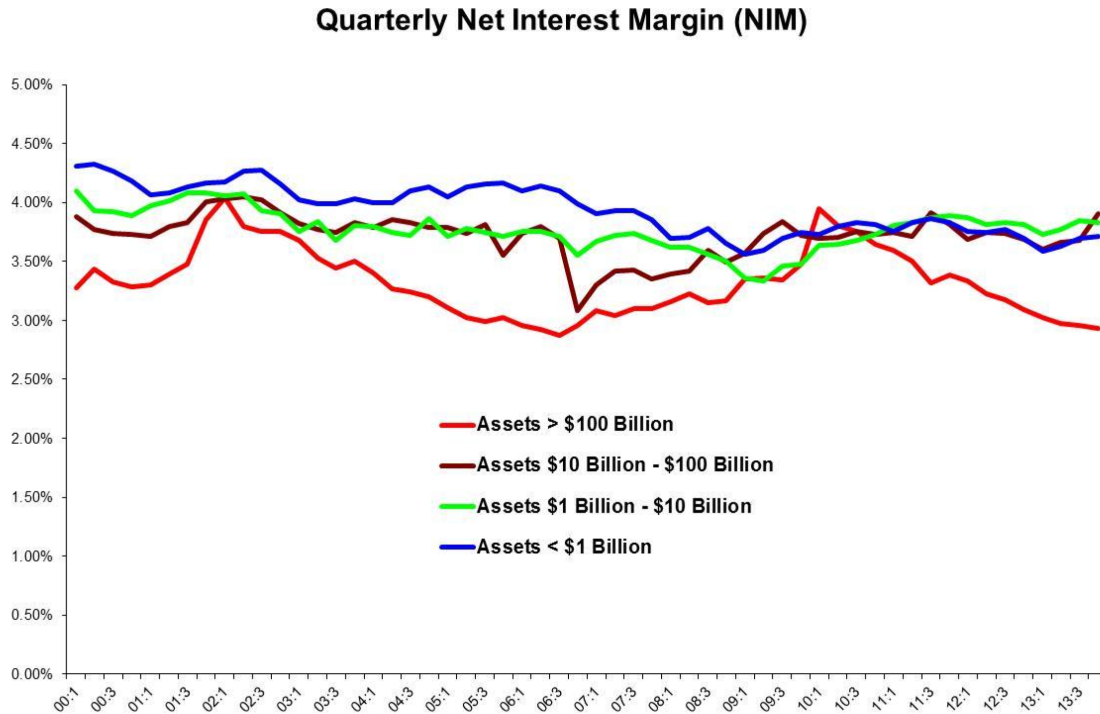


* FASB Statements 166 and 167 resulted in the consolidation of large amounts of securitized loan balances back onto banks' balance sheets in the first quarter of 2010. Although the total amount consolidated cannot be precisely quantified, the industry would have reported a decline in loan balances for the quarter absent this change in accounting standards.

We saw modest growth in loans during the fourth quarter, which was in line with prior quarters. Loan balances also grew in most major categories. A notable exception was 1-4 family residential real estate loans, where loan balances have fallen for the past five quarters.

In contrast to the overall industry, community banks showed an increase in all major loan categories, including 1-4 family residential real estate loans. Community banks also continued to support small businesses, accounting for 46 percent of the industry's small loans to farms and businesses.

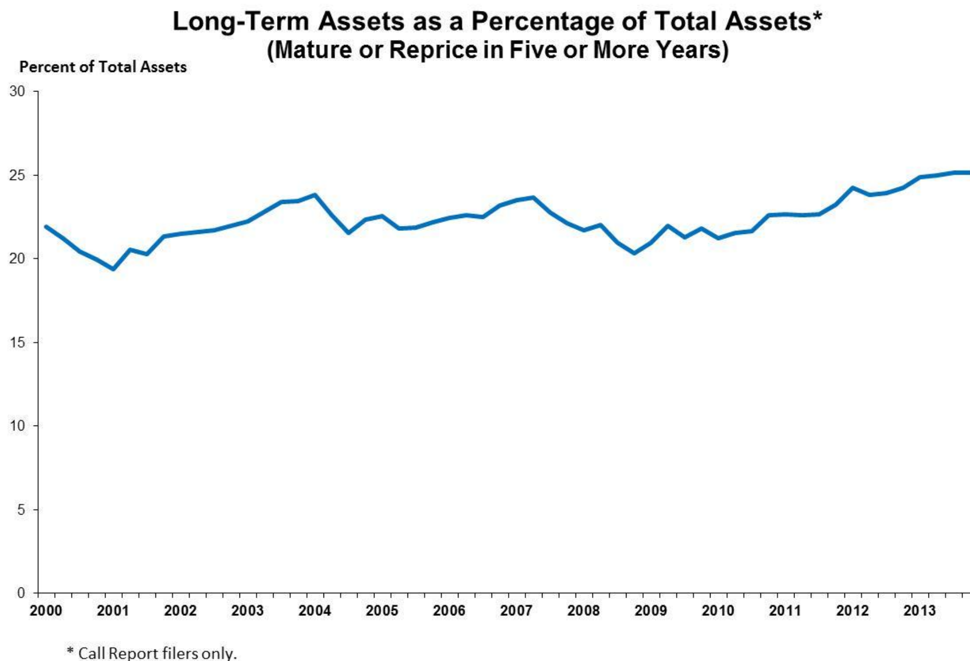
Chart 8



The steeper yield curve in 2013 helped net interest margins, as banks generally borrow short and lend for longer terms. Margins increased across all size groups in the fourth quarter except for the largest group of banks, where they generally have declined since 2010 due to growth in low-yield reserve balances held at Federal Reserve banks.

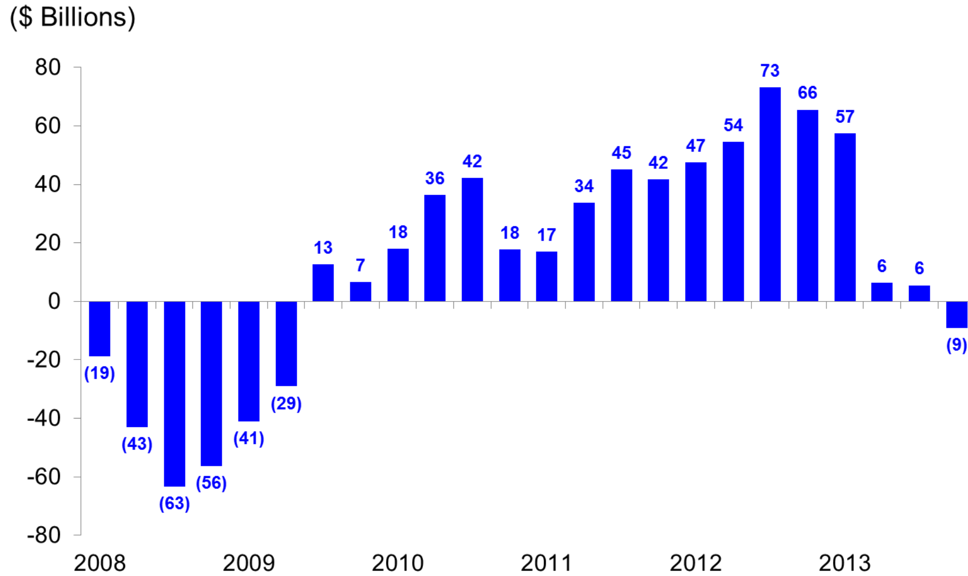
Community banks had an average margin of 3.65 percent. This was 37 basis points higher than the industry's average margin of 3.28 percent. Margin trends are especially important at community banks, since net interest income is a larger share of their overall revenue.

Chart 9



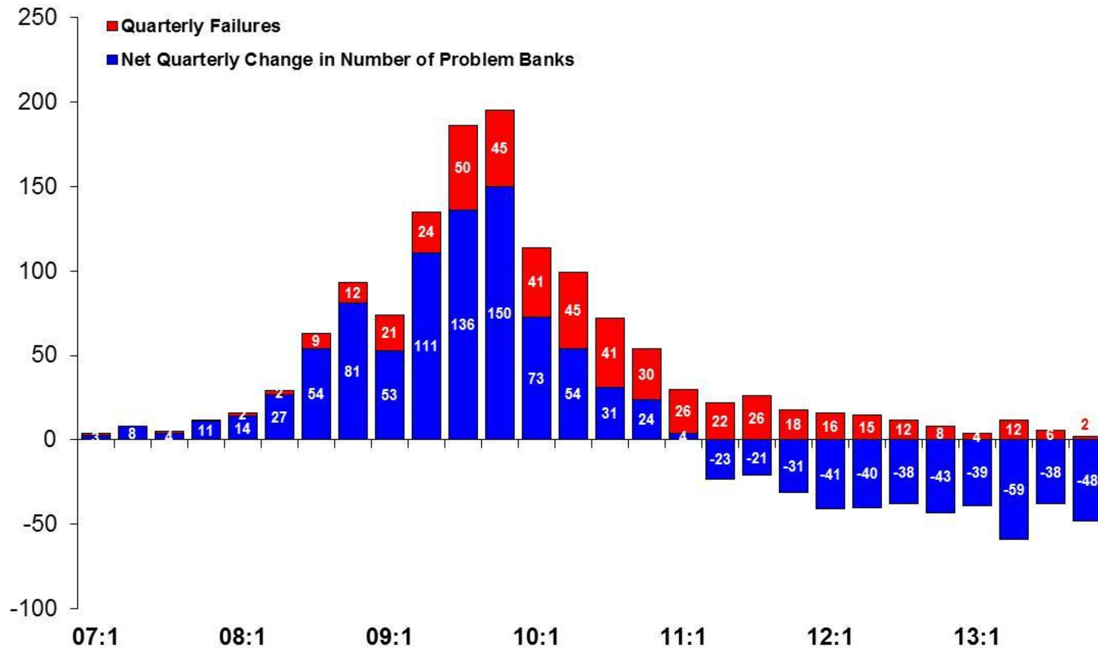
Many banks have sought to improve their margins by increasing the share of longer-term assets on their balance sheets. This is evident in the next chart. Banks are seeking higher asset returns in a low interest rate environment by going out further on the yield curve. This reach for yield has helped average asset yields, but it has left banks more vulnerable to interest rate risk as rates rise.

Chart 10



We saw the impact of rising longer-term rates in the second quarter when unrealized gains on available-for-sale securities fell by 51 billion dollars. At year-end 2013, the trend continued as banks reported 9 billion dollars in unrealized losses on their available-for-sale securities, down from 6 billion dollars in unrealized gains the prior quarter. Interest rate risk is an ongoing concern for bank regulators. And it will continue to be a focus of attention in our safety and soundness examinations.

Chart 11



The fourth quarter saw a further decline in the number of troubled institutions. The number of banks on the "problem list" declined from 515 to 467, the fewest since mid-year 2009 and nearly half of the peak of 888 institutions at first quarter 2011. There were two failures in the fourth quarter, the smallest quarterly total since second quarter 2008. And there were 24 failures in 2013, the fewest since 2007.

The Deposit Insurance Fund balance rose to 47.2 billion dollars as of December 31, up from 40.8 billion dollars at September 30. Assessment income and a reduction in estimated losses from failed institution assets drove the fourth quarter increase in the Fund balance.

Estimated insured deposits were 6 trillion dollars, up 0.7 percent over the quarter. The reserve ratio—which is the Fund balance as a percentage of estimated insured deposits—increased to 0.79 percent at December 31 from 0.68 percent at September 30. A year ago, the reserve ratio was 0.44 percent. As required by law, the Deposit Insurance Fund must achieve a minimum reserve ratio of 1.35 percent by 2020.

In summary, the trend of slow but steady improvement that has been underway in the banking industry since 2009 continued to gain ground. Asset quality improved, loan balances were up, and there were fewer troubled institutions. However, challenges remain in the industry. Narrow margins, modest loan growth, and a decline in mortgage refinancing activity have made it difficult for banks to increase revenue and profitability. Nonetheless, these results show a continuation of the recovery in the banking industry.

Thank you.

I am happy to take a few questions.