Chairman Martin J. Gruenberg's Opening Statement

First Quarter 2018 Quarterly Banking Profile

May 22, 2018

Good morning, and welcome to our release of first quarter 2018 results for FDIC-insured institutions.

The banking industry reported another positive quarter. Net income increased on higher net operating revenue and a lower effective tax rate. Loan balances continued to rise, net interest margins improved, and the number of "problem banks" continued to fall.

Community banks also reported another solid quarter. Their net income benefitted from higher revenue and a lower effective tax rate, and loan growth that was stronger than the overall industry.

While the performance of the banking industry has been positive, the current economic expansion is now the second longest on record. It is important to remain vigilant to underlying risks in the latter stage of this economic cycle.

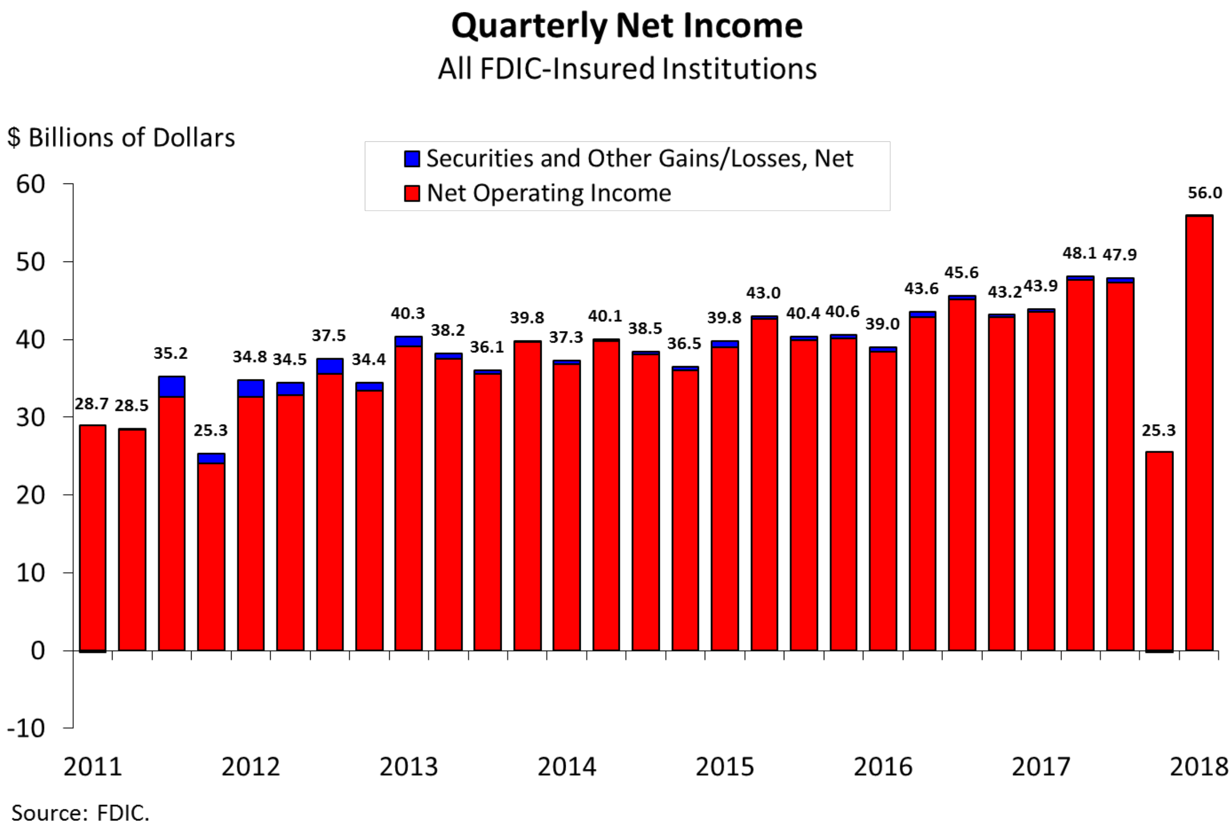
The interest-rate environment and competitive lending conditions continue to pose challenges for many institutions. Some banks have responded by "reaching for yield" through investing in higher-risk and longer-term assets.

Going forward, the industry must manage interest-rate risk, liquidity risk, and credit risk carefully to continue to grow on a long-run, sustainable path. The industry also must be prepared to manage the inevitable economic downturn, whenever it comes, smoothly and without undue disruption to the financial system.

The long-term objective for banks should be to position themselves during periods of good economic and banking conditions, as exist today, to be able to sustain lending through the economic cycle so that the industry can play a counter-cyclical role, and not a pro-cyclical role as occurred during the financial crisis.

These challenges facing the industry will remain a focus of supervisory attention.

Chart 1:

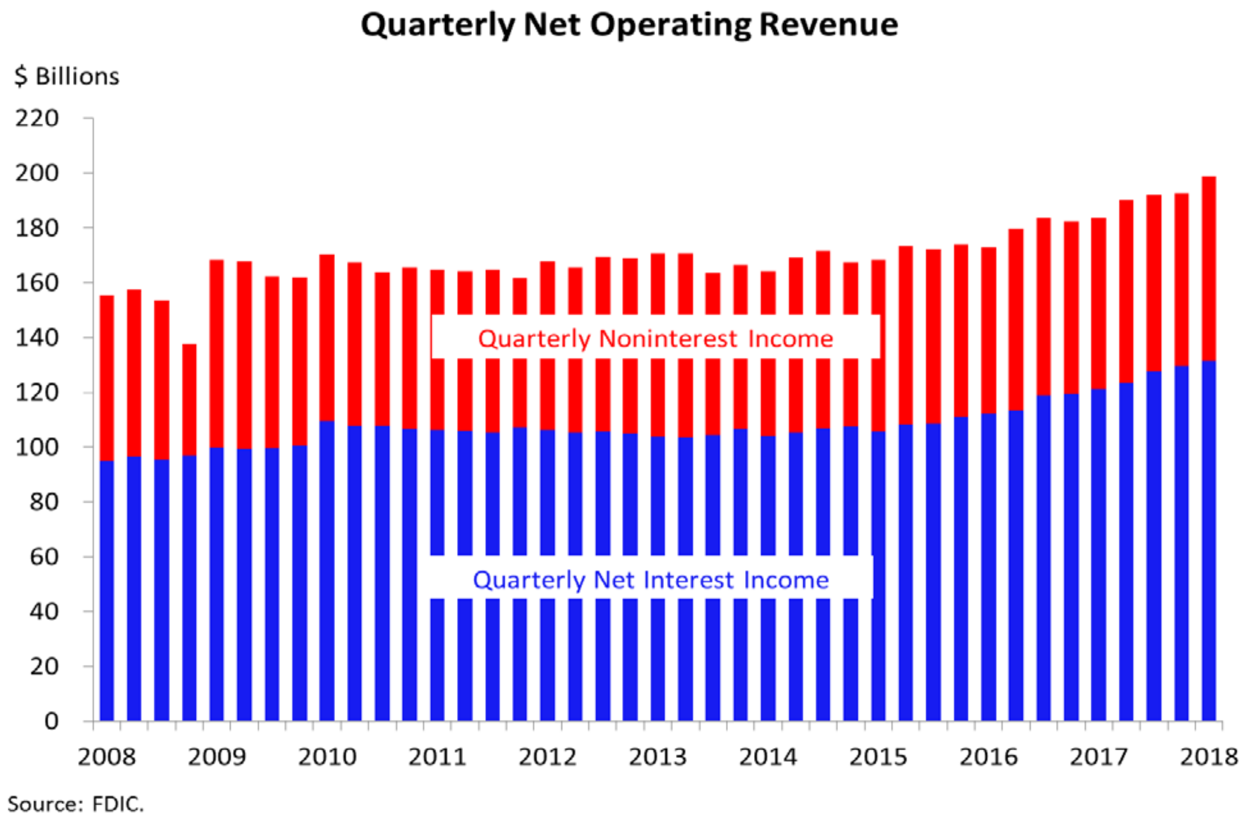


Our first chart shows that net income for the industry was 56 billion dollars in the first quarter, up 27.5 percent from a year ago. The improvement in net income was due to higher net operating revenue and a lower effective tax rate.

Assuming the effective tax rate for the banking industry prior to the new tax law, we estimate that quarterly net income would have been 49.4 billion dollars, or 12.6 percent higher than first quarter 2017.

Community banks reported net income of 6.1 billion dollars in the first quarter, an increase of 17.7 percent from a year earlier. Assuming the effective tax rate for community banks prior to the new tax law, we estimate that quarterly net income would have been 5.6 billion dollars, an increase of 9.2 percent over first quarter 2017.

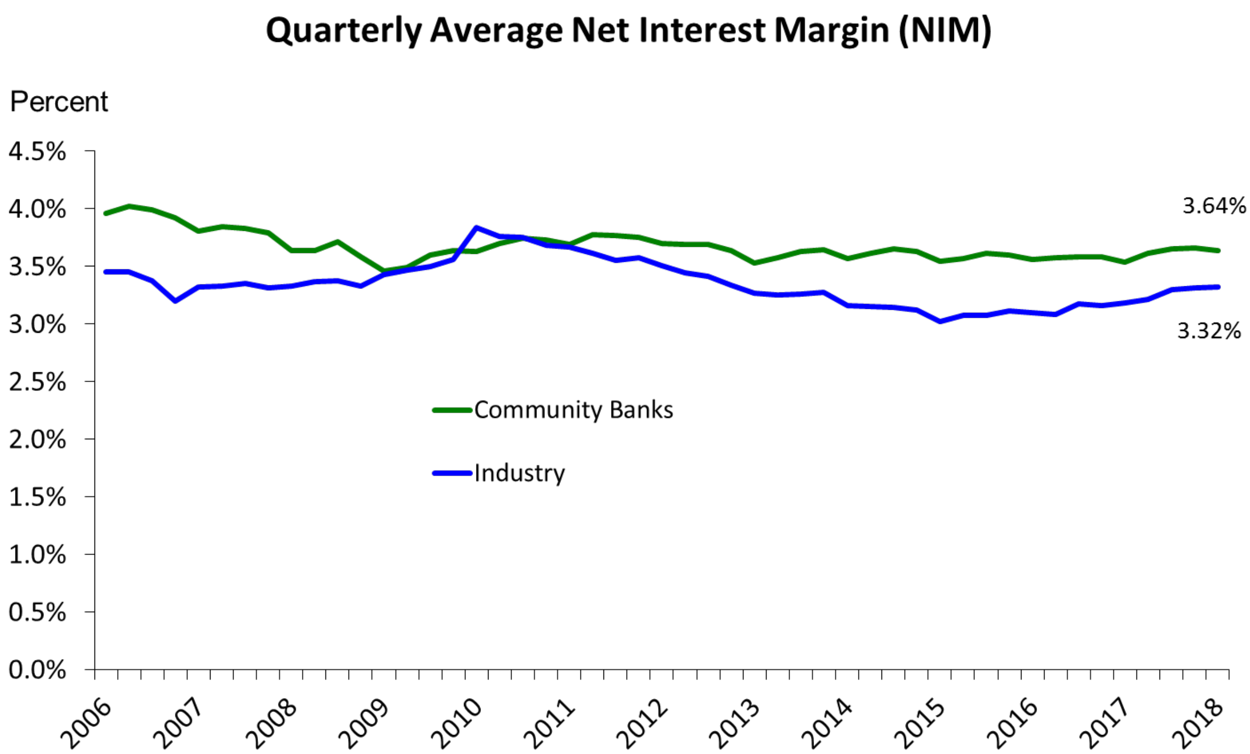
Chart 2:



Our next chart shows that net operating revenue totaled 198.8 billion dollars in the first quarter, an increase of 8.3 percent from a year ago. The increase in revenue was broad-based across the industry, as over 80 percent of all banks reported higher revenue from a year earlier.

The growth in revenue was driven by higher net interest income and higher noninterest income. Net interest income grew by 8.5 percent from a year ago due to loan growth and improved net interest margins. Noninterest income rose by 7.9 percent from a year ago due to higher trading revenue and other noninterest income.

Chart 3:

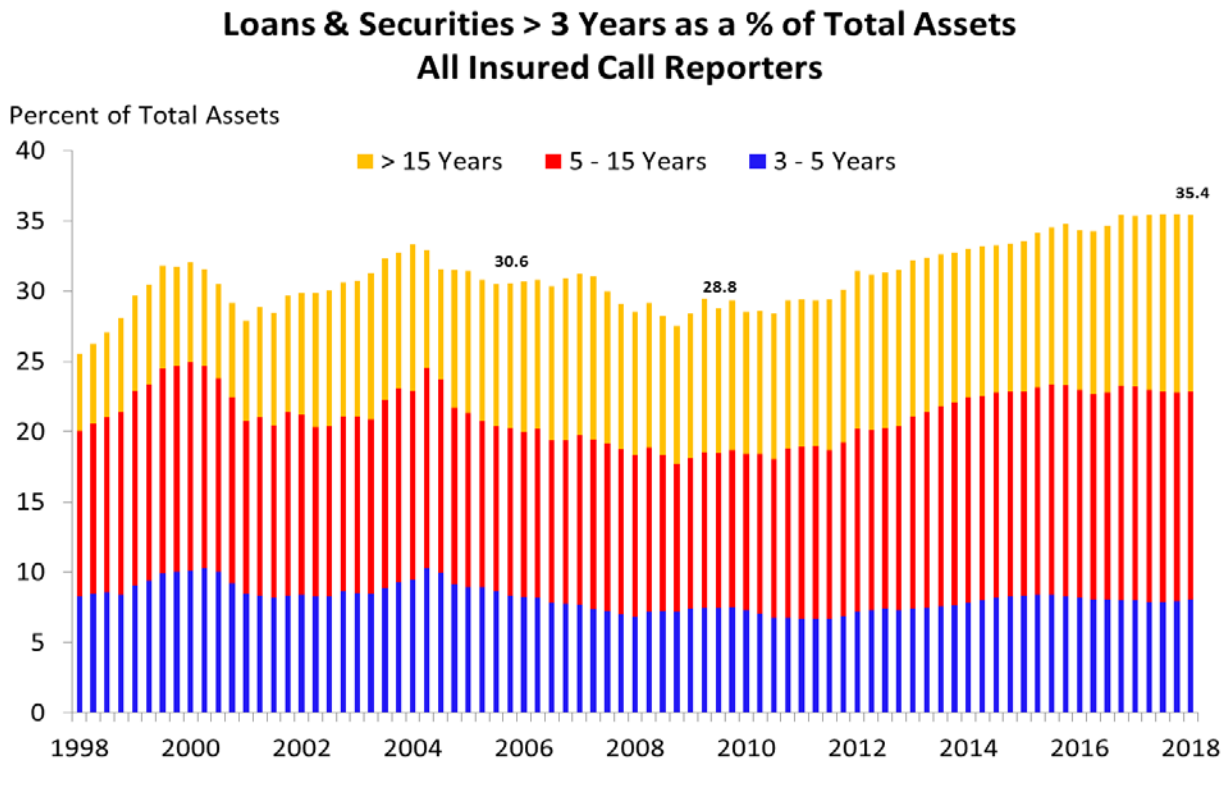


Source: FDIC.

Chart 3 shows that the average net interest margin for the industry was 3.32 percent in the first quarter, up from 3.19 percent a year earlier.

Community banks continue to report a higher average net interest margin than the overall industry. However, the gap has been narrowing. Large institutions have benefitted more than community banks from rising short-term interest rates, as large institutions have a greater share of assets that reprice quickly.

Chart 4:



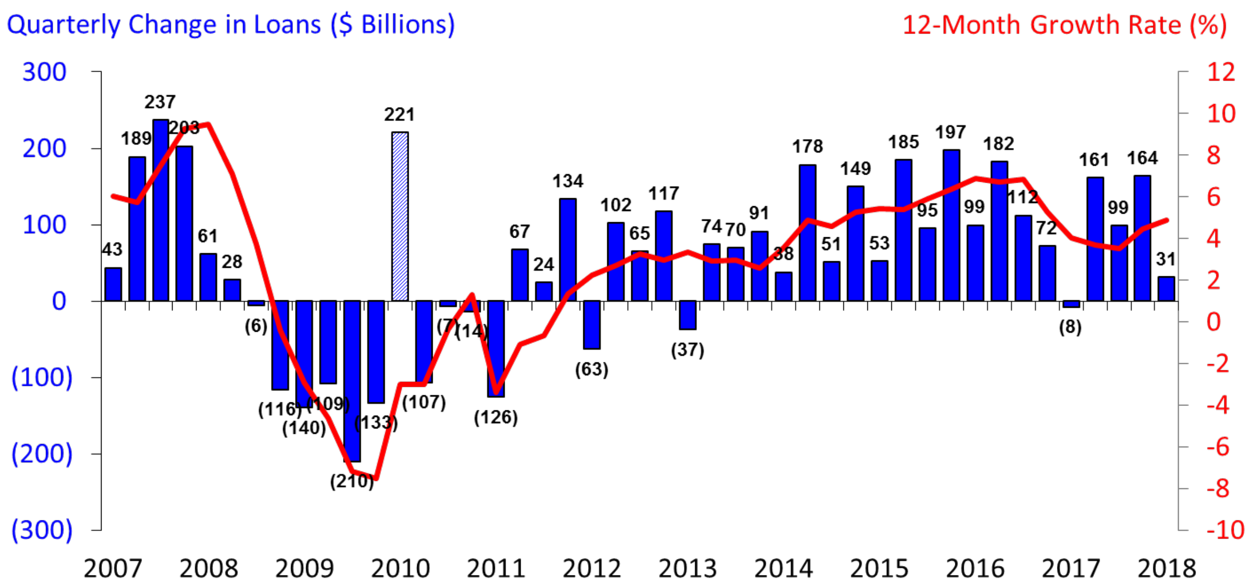
Source: FDIC.

Chart 4 shows that the share of longer-term assets relative to total industry assets remains elevated, with over a third of industry assets maturing or repricing in three or more years. Banks have been extending asset maturities to increase yields and maintain net interest margins in a low interest rate environment. This has left some banks vulnerable to interest-rate risk, and is a matter of ongoing supervisory attention.

Community banks are particularly vulnerable to interest-rate risk, as nearly half of their assets mature or reprice in three or more years.

Chart 5:

Quarterly Change in Loan Balances



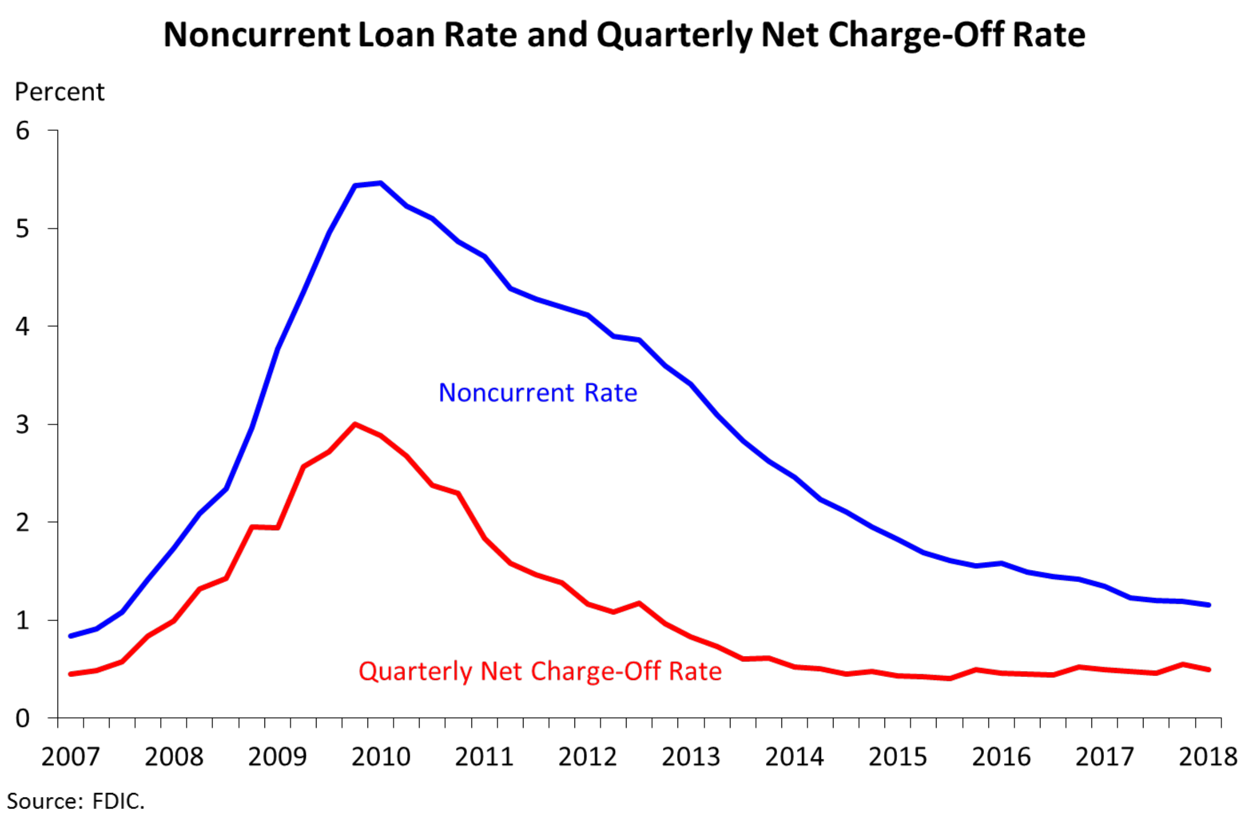
Source: FDIC.
Note: FASB Statements 166 and 167 resulted in the consolidation of large amounts of securitized loan balances back onto banks' balance sheets in the first quarter of 2010. Although the total amount consolidated cannot be precisely quantified, the industry would have reported a decline in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

Chart 5 shows that loan balances increased by 31 billion dollars during the first quarter. All major loan categories registered growth except for credit card balances, which showed a seasonal decline in the first quarter.

Over the past year, loan balances rose by 4.9 percent. This is up from 4.5 percent last quarter and is above nominal GDP growth.

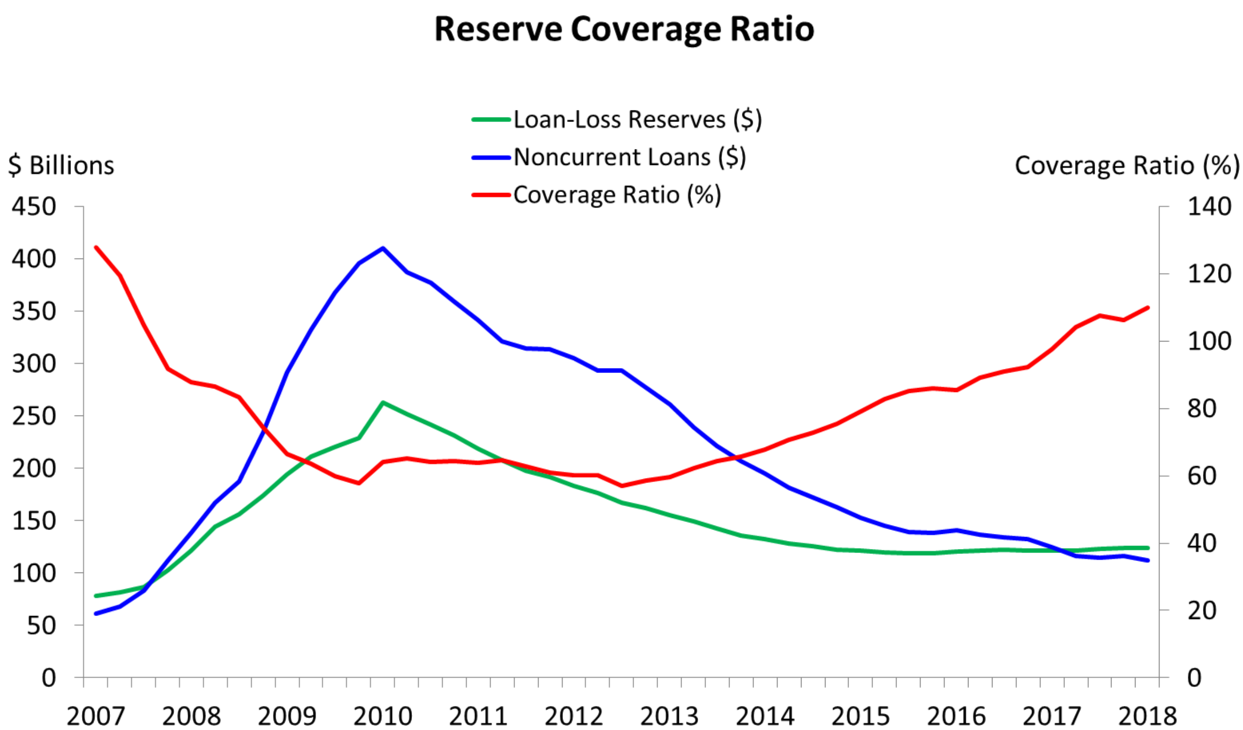
Loan growth at community banks was stronger than the overall industry. Loan balances at community banks grew 7.4 percent from a year ago, led by growth in commercial real estate loans, residential mortgages, and commercial and industrial loans.

Chart 6:



Our next chart shows that overall asset quality remained stable in the first quarter. The noncurrent rate declined modestly from the previous quarter, and the net charge-off rate remained stable from a year ago. Credit card balances registered the largest increase in net charge offs.

Chart 7:



Source: FDIC.
Note: Loan-loss reserves to noncurrent loans & leases.

Chart 7 shows that the industry's reserve coverage ratio, which measures loan-loss reserves relative to total noncurrent loan balances, increased to 110 percent at the end of the first quarter. This is the highest reserve coverage ratio since second quarter 2007.

Chart 8:

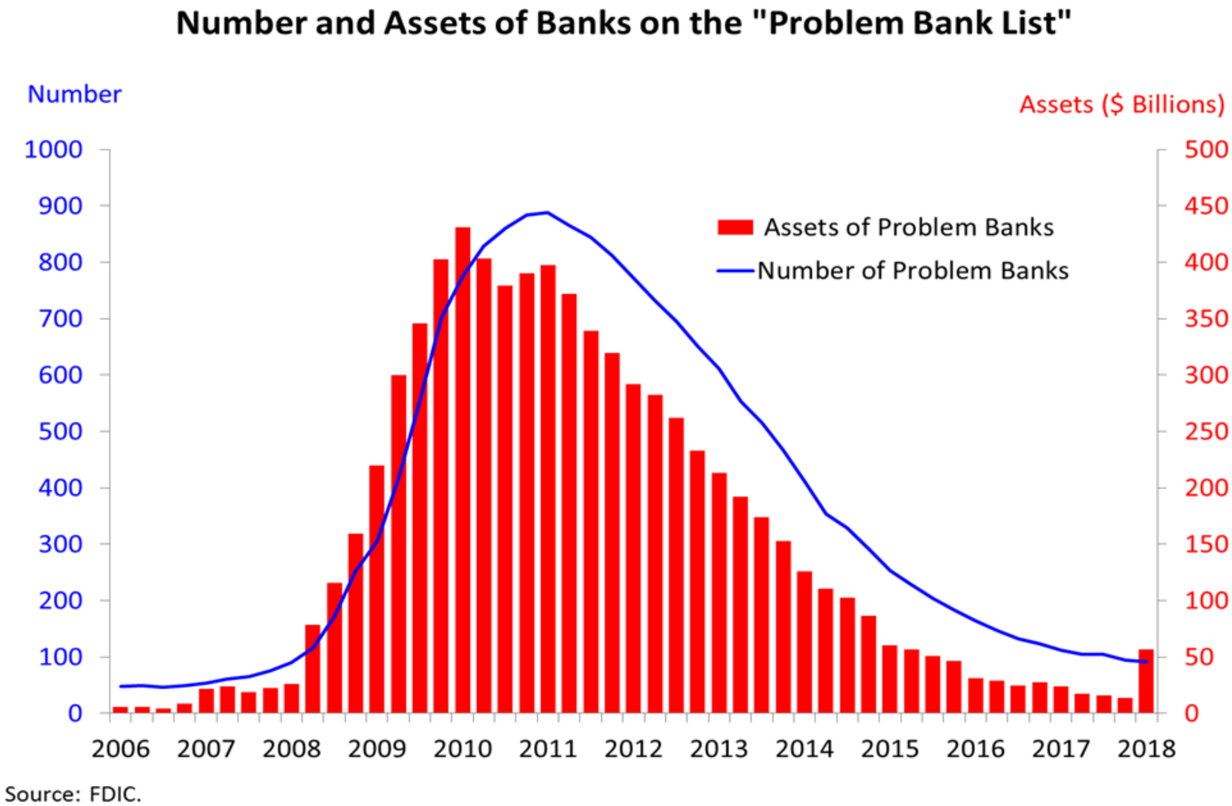
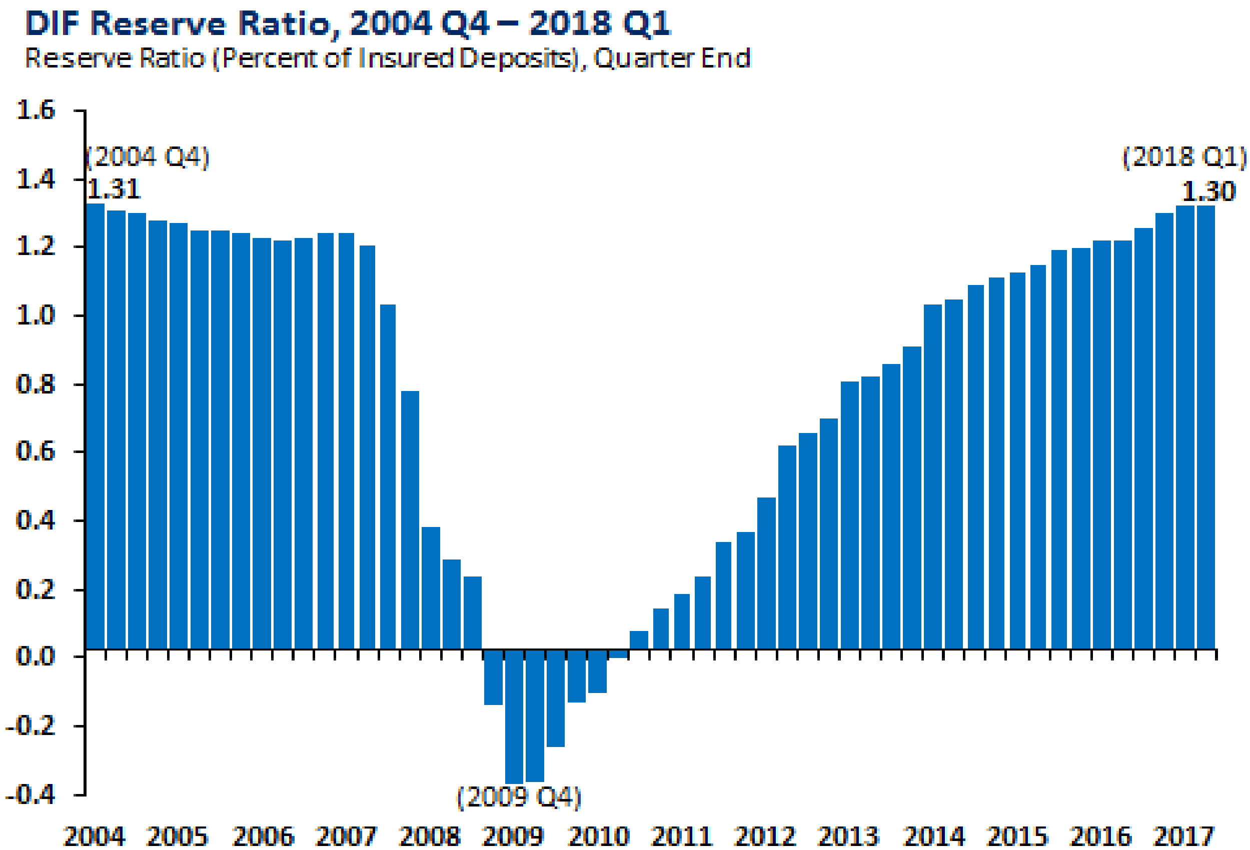


Chart 8 shows that the number of banks on the FDIC's "Problem Bank List" declined from 95 to 92 during the quarter. This is the lowest number of problem banks since first quarter 2008. Three new charters were added, and no failures occurred in the first quarter.

Chart 9:



The Deposit Insurance Fund balance was 95.1 billion dollars on March 31, up 2.3 billion dollars from the end of last year. The increase in the fund was largely driven by assessment income. Estimated insured deposits totaled 7.3 trillion dollars at the end of March, increasing 2.6 percent in the first quarter and 3.7 percent over the past four quarters.

Chart 9 shows that the reserve ratio—the amount in the Deposit Insurance Fund relative to insured deposits—was 1.30 percent on March 31, unchanged from the end of last year, due primarily to strong first quarter growth in estimated insured deposits.

As required by law, the Deposit Insurance Fund must achieve a minimum reserve ratio of 1.35 percent by September 30, 2020.

We expect the reserve ratio to reach 1.35 percent this year, ahead of the statutory deadline.

In summary, the banking industry once again reported positive results for the quarter. Higher net operating revenue and a lower effective tax rate boosted net income. Loan balances grew, net interest margins improved, and the number of "problem banks" continued to fall.

Community banks also reported a solid quarter with net income benefiting from higher net operating revenue and a lower effective tax rate, and loan growth that exceeded the overall industry.

While results this quarter were positive, an extended period of low interest rates and an increasingly competitive lending environment have led some institutions to reach for yield. This has led to heightened exposure to interest-rate risk, liquidity risk, and credit risk.

In addition, with the current expansion in its latter stage, the industry needs to be prepared to manage the inevitable downturn, whenever it may occur, in order to avoid financial system disruption and sustain lending through the economic cycle.

These risks will remain a focus of supervisory attention.

Thank you.

I'll now be glad to respond to questions.