

TEXAS RATIO - WORST 15 STATES/TERRITORIES

by [Steve Brown](#)

This week we are going to take a look at just how strained things remain in the banking system by examining the Texas Ratio. While this ratio can be calculated in many ways, for our purposes, we will be using the following formula: $\text{Texas Ratio} = (\text{all loans past due 30 days or more} + \text{nonaccrual loans} + \text{OREO}) / (\text{Tier 1 Capital} + \text{loan loss reserves})$. As we have previously written about, this ratio came from research done on Texas banks during the early 1980s (hence the name) and was tested again on New England bank failures during the 1990s. It has a reasonably high degree of accuracy when asset quality is the biggest issue in the industry and the research found that institutions tended to be severely stressed when this ratio climbed above 100%. While we inherently dislike using any singular metric to analyze banks (given complexities involved overall and certain issues that can occur related to combinations tied to FDIC assisted transactions), we felt the data was compelling enough to provide an update on industry conditions using 3Q data (unadjusted for failures since 9/30).

Based on this data, analysis reveals that Puerto Rico is the most strained of all the states or territories (FDIC insures banks in territories as well). In fact, it comes in with a weighted average ratio for all of its 10 banks of an amazing 122%. Showing just how strained this territory is, we also find that 70% of all banks have a ratio above 100%. Finally, the highest ratio for any bank in the territory is 259%, while the lowest comes in at 33%.

Taking the #2 slot in terms of stress is the state of FL. This state has just over an 85% weighted average Texas Ratio, pointing to a very difficult environment. Overall, its 295 banks have already seen 6 failures since 3Q, so it isn't surprising that FL also holds the #1 spot in terms of bank closures (tied with CA) since quarter-end. Unfortunately for those banks doing business in the Sunshine State, conditions will remain difficult for some time to come. In fact, the data shows 73 banks (about 25% of all banks in the state that haven't failed) are currently carrying a ratio at or above 100%.

Dropping into the 3rd toughest spot and just behind FL at 84% is WA. While this state hasn't seen any failures since the 3Q, the data shows that trend isn't likely to last much longer. In all, 8 banks have a Texas Ratio above 200%, while 23 (about 24% of all banks in the state) are above the 100% threshold.

Coming in at 4th and carrying a weighted average Texas Ratio of 73% is the state of MI. Battered by job losses and carrying the country's highest unemployment rate of 15.1%, the Wolverine State remains under pressure. Here, 15% of banks (excluding the 2 banks that failed since 3Q) have a ratio greater than 100%, with the highest one coming in at 349%.

In the 5th spot is the Sooner State of OK, which has an overall ratio of 69%. OK has only 5 banks of its 252 (about 2%) with a ratio greater than 100%, but as the data shows, many more banks in the state are at levels high enough to push OK into one of the top rankings in the country.

As for the rest of the top 15 states, here they are in order by weighted average ratio: GA (65% overall with 26% of banks >100%); AZ (63% overall with 21% of banks >100%); AK (63%, but skewed by Wells Fargo, Anchorage at 74%); SC (60%); MD (57%); OR (56%); DC (54%); AL (52%); OH (50%); and WI (50%).

Again, no single metric can capture everything going on in these states and territories, but given the heightened focus on asset quality; it is important to stay on top of industry trends and the Texas Ratio is certainly a decent tool to use.

BANK NEWS

Black Friday

According to the National Retail Federation, shopping traffic was up this year by 13% for Black Friday and total spending inched up 0.5%. However, the bad news is that the average amount spent fell nearly 8% to \$343.31 per person, the lowest level in 4Ys.

Gambling Compliance

The Fed announced a 6-month extension of the deadline (to 6/1/10) that would mandate banks comply with the Unlawful Internet Gambling Enforcement Act of 2006. Banks are still trying to figure out what exactly "Unlawful Internet Gambling" is (as there is no clear definition in the Act), let alone proper policies and procedures.

Large Bank Strain

Bank analyst Richard Bove indicates many large US banks would have to raise capital if the Treasury goes through with its stated goal of requiring TARP funds be paid back soon. Bove indicated in a research report that "only 3 of the top 30 banks would have an adequate Tier 1 Capital ratio if they redeemed these preferreds (TARP)."

Business Activity

An index that measures equipment leasing and financing activity measured in Oct. 2009 has fallen 33% from Oct. 2008 and nearly 9% from the prior month.

Corporate Profit

In a good news, bad news story, corporations in the 3Q increased profits by 10.6% QOQ, the biggest gain since 2004. Unfortunately, much of the improvement came by cutting costs and employees.

Office CRE

Jones Lang predicts office vacancies will rise to 19.5% late next year, as landlords struggle to fill empty space.

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