1Q COMMUNITY BANK PERFORMANCE

by Steve Brown

After being accused of going "soft" when we wrote about Glee instead of highlighting the Kentucky Derby, we got all jacked up to write a testosterone-fueled piece featuring steak, cage fighting and Corvettes. The problem was that we got sidetracked when we read the reviews of the new movie, Babies and our softer side once again took over. Who wouldn't want to see an 80 minute movie, with no talking, about 4 babies? Since there is no sarcasm font, we will just say that we decided to compromise and highlight 1Q bank performance for all non-OTS banks under $25B instead.

While not smelling baby fresh, this group of banks saw their performance turn the corner for the first time in several quarters and ROE climbed above 3% - something that it hasn't done since Sep of 2008. ROE increased from -0.50% in 4Q, back to positive territory at 3.23%. On a pre-tax, pre-provision basis, ROE went from 14.23% to 16.15%. ROA followed suit and increased from -0.50% to 0.35%.

Earnings gains were driven both by improvement in core operations and abatement in relative credit deterioration. Net interest margin improvement was the source of most of the increase in earnings, as it went from 3.56% to 4.07% QoQ. Both yield on earning assets increased (5.25% to 5.53%) and cost of funds decreased (1.67% to 1.46%) - something that hasn't happened since the start of the decade. In addition to NIM improvement, the best news is that for the first time in many quarters, we have seen ALLL as a percent of non-current loans, improve (ALLL is now 2.5% of loans).

Unfortunately, this story also has some spit up in it, as while problem loan growth is slowing as a percent of capital; it is still getting worse, due to higher problem loan counts and more charge offs. The average Texas Ratio increased from 39% in 4Q to 43% in 1Q for this group. While both construction and development loans continued to decrease, CRE as a percent of Tier 1 capital moved up from 193% to 211%. That said; ALLL as a percent of non-current loans increased for the first time in many quarters, as it went from 53.97% to 54.59%.

Over the last year, next to asset quality changes, funding has also undergone a restructuring at many banks. Core deposits continued to grow and wholesale funding decreased. Most of the core growth was in interest-bearing money market accounts with some checking account strength. Part of this increase is from the current trend of banks to reduce their premiums on their CD structure (to the lowest absolute levels since recorded banking time). This has pushed balances away from core CDs and into other products. While good, repricing has also shortened the duration structure of most banks, creating more asset sensitivity. Loan-to-deposit leverage decreased from 84% to 82% and core capital leverage improved from 9.5% to 9.6%. In other good news, banks finally arrested growing operating expenses as the average efficiency ratio dropped from 66.2% to 63.3%.

If you are a subscriber to BIG Metrics, you now can see your 1Q bank performance compared to peers earlier than everyone else. For non-subscribers we will be hosting free dashboards of selected metrics and rankings throughout the week, so stay tuned. While the 1Q was not a great one for banks, we will take what we can get and are ecstatic over the general improvement of performance.

We are not sure if we will make it to Babies since we have already had our fill of cuteness; however look for another movie analogy soon, as we do have our eye on the manly Iron Man 2.

BANK NEWS

Closed (68 YTD)

On Fri, the FDIC closed: 1) The Bank of Bonifay ($243mm, FL) and sold it to First Federal Bank of Florida ($833mm, FL). First Federal adds 5 branches (no premium), all deposits and $78mm in assets (FDIC retains the remainder). 2) Access Bank ($32mm, MN) and sold it to Prinsbank ($57mm, MN). Prinsbank adds 2 branches, all deposits (0.02% premium) and all assets. 3) Towne Bank ($120mm, AZ) and sold to Commerce Bank of Arizona ($212mm, AZ). Commerce adds 1 branch, all deposits (0.3% premium) and all assets ($80mm under a loss share). 4) 1st Pacific Bank of California ($336mm, CA) and sold it to City National Bank ($20.7B, CA). City National adds 6 branches, all deposits (1.62% premium) and all assets ($276mm under a loss share). For more information click here.

TAG Update

The FDIC released information about banks that had opted-out of the TAG portion of the Temporary Liquidity Guarantee Program. The list breaks down as follows: 525 banks/thrifts opted out of the original program; 1,110 opted out of the program extension covering Jan 1 thru Jun 30 2010; 441 opted out of the most recent extension from Jul 1 to Dec 31 2010. All told, 2,075 financial institutions (about 1 in 4) has opted out of this program.

FHA Policy

The FHA will no longer certify mortgage brokers and lenders may be held responsible for losses, fraud or underwriting on loans guaranteed by the FHA. Instead, lenders will now need to sponsor brokers

Lena Horne

One of the most beautiful voices we have ever heard made even more beautiful by what this woman accomplished. She will be missed.