

## FIRST QUARTER RECAP

by [Steve Brown](#)

First quarter 2011 data came out over the weekend and the summary is that banking is beginning to return to normal. We want to highlight a couple of trends from this preliminary data, as it may be instructive.

The most obvious trend of the 1Q is that banks returned to a moderate level of profitability. ROE for the industry came in at 7.50%, up from its 5.84% level last quarter and better than the 5.09% level for the same period last year. Here, performance was correlated to size, as large banks over \$25B and in the \$3B to \$5B range did the best. Most community banks under \$1B produced a 5.00% ROE and under \$100mm averaged 4.45%.

Net interest margin for the industry came in at 3.68%, about the same as last quarter. Banks in the \$10B to \$25B range did the best at a 5.05% NIM, followed by banks under \$100mm that produced a 4.07% margin. The yield on earning assets decreased 3 to 23bp for most banks, as loan competition heated up. The exception here were banks in the \$10B to \$25B range, which increased NIM back to the 6% level by extracting greater value through loan structuring. On the other side of the equation, cost of funds dropped for most banks below \$5B, but the industry average came in at 0.78%, for a decrease of 10bp since last quarter. Banks below \$5B came in around a 1.10% COF, largely unrelated to asset size. One interesting note on the trends is that if you ever wondered if your bank is more sensitive to deposit or loan pricing, the answer is usually deposit pricing "since fewer variables makes COF more correlated to both NIM and earnings."

In looking at non-interest income, there were no major changes, as the total level and associated ratios were largely unchanged. One trend that did stick out were lower service charges on checking accounts from last quarter, but we are not sure yet what to attribute that to.

The largest contributor to increased earnings was a reduction of asset quality problems. Here, non-current loans to total loans fell 18bp to 4.76%. Banks below \$300mm are still experiencing loan issues, as are banks in the \$10B to \$25B range. However, every other asset class reported an improvement not correlated to size, but correlated to geography. Other asset quality categories such as OREO, ALLL and Texas Ratios followed similar trends.

Lower leverage is a major trend of the quarter, as loan-to-deposit ratios dropped from 74.3% in 4Q to 67.8%. Interestingly, large banks (\$10B to \$25B) employed the lowest deposit leverage at 49.3%, followed by banks below \$100mm at 65.7%. Capital leverage also was also lower, as the industry came in with a Tier 1 capital ratio of 12.6%, up from 12.4%. Banks under \$100mm are the best capitalized at 17.1%.

As we finish up the major indicators of the industry, operating expenses were stable, as the efficiency ratio was largely unchanged at 61.3%. The number of employees in the industry was also largely unchanged even as salary/benefit expenses increased 4% for the quarter.

Tomorrow we highlight more trends, as we look at changes in the balance sheet, composition, ALM positions and geography.

# BANK NEWS

## Leaving

The FDIC announced Sheila Bair will officially step down effective July 8th, 2011.

## Money Market Mutual Fund Future

Something that we are closely following today is the outcome of the President's Working Group roundtable for the Financial Stability Oversight Council on the fate of money market mutual funds. Fluctuating NAV, emergency liquidity fund, assessments and transparency will all be hot topics today. The outcome of today's meeting will have far ranging consequences on bank deposits, as we expect money funds to become less competitive.

## Overdraft OK

Bank of America is testing a program that will allow customers to approve debit card purchases that exceed their balances by text message. The bank no longer allows transactions that overdraw accounts, but may do so once again through a program where customers give specific permission.

## Small Biz Taxes

A survey by the National Small Business Association finds 66% of small business owners say economic uncertainty is their top challenge, followed by: a decline in customer spending at 39%; health insurance costs at 35% and regulatory burdens at 32%.

## Biz Operating Systems

A survey of computer operating systems by Zoomerang of small to mid-sized businesses finds 45% use Windows XP, 30% use Windows 7 and 16% use Windows Vista (91% use some form of Windows operating system). Meanwhile, 5% use Apple's OS X and 1% use Linux.

## Biz Technology

A survey of small to mid-sized businesses by Zoomerang finds 78% of companies have in house technology support, while 22% outsource. Of those doing IT inside their company, the survey found 30% of their staff did other functions; 15% were involved in business development and 11% were in customer support.

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