THRIFT INDUSTRY HIGHLIGHTS FIRST QUARTER 2006

Office of Thrift Supervision / May 19, 2006

SUMMARY

Strong earnings and profitability, solid loan growth, and healthy asset quality characterized thrift industry results for the first quarter of 2006. Although earnings and profitability for the industry were robust, thrift earnings are typically constrained in an interest rate environment that continues to be distinguished by a flat yield curve. The industry's aggregate net interest margin increased by one basis point from the prior quarter, but due to a regulatory reporting change, first quarter net interest margin is not directly comparable to that of prior periods.[1] Mortgage origination volume for the quarter was up two percent from the first quarter one year ago, but down 12 percent from the prior quarter as higher mortgage interest rates slowed the volume of existing and new home sales.

Thrift industry assets increased by 12 percent from the first quarter one year ago to $1.50 trillion. The number of thrifts supervised by OTS stood at 856 at the end of the first quarter. In addition, OTS supervised 481 holding company enterprises with approximately $7.2 trillion in U.S. domiciled consolidated assets. These enterprises owned 447 thrifts with total assets of $1.2 trillion, or 79 percent of total thrift industry assets.

Asset quality remained strong for all loan types over the first quarter and the overall level of credit quality in the thrift industry has remained good. While most noncurrent loan types showed improvement in delinquencies from one year ago, delinquencies of 1-to-4 family and multifamily mortgages were higher. Delinquencies of 1-to-4 family mortgage loans were higher chiefly because changes to accounting and regulatory reporting requirements for banks and thrifts now require loans repurchased, or eligible for repurchase, from Government National Mortgage Association (GNMA) mortgage pools to be included in past due loans[2]. Excluding these repurchased GNMA loans, troubled assets (defined as noncurrent loans and repossessed assets) were

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[1] Prepayment fees and other loan fees are required to be included with interest income rather than in "Other Fees and Charges" beginning with the first quarter 2006 regulatory reports. This change was made to match the regulatory reporting for the commercial banking industry.

[2] GNMA mortgage-backed securities are fully guaranteed by the U.S. Government. Individual loans repurchased from GNMA pools are fully or partially guaranteed or insured by agencies of the U.S. Government.

lower from one year ago, but up from the record low rate in the second quarter 2005. Loans past due by 30- to 89-days as a percentage of assets reached a record low at the end of the first quarter 2005, but have increased in subsequent quarters and were higher at the end of the first quarter 2006 from one year ago, but down from the prior quarter. The industry's equity capital level reached a record level at the end of the first quarter and, as a percentage of assets, its equity capital ratio was down slightly from the record ratio reached at the end of the prior quarter.

EARNINGS AND PROFITABILITY

Net income was $4.22 billion in the first quarter, up five percent from the year ago first quarter, but down two percent from a record $4.32 billion earned in the prior quarter. This was the fifth time and fifth consecutive quarter that quarterly income topped the $4 billion mark. The number of thrifts reporting losses in the first quarter was 80, up from 68 thrifts in the first quarter one year ago.

Profitability, as measured by return on average assets (ROA), was 1.14 percent in the first quarter, down from 1.22 percent in the comparable year ago quarter, and from 1.19 percent in the fourth quarter. The median ROA declined to 0.66 percent in the first quarter from 0.72 percent in the first quarter one year ago, and was down from 0.67 in the prior quarter.

Return on average equity (ROE) was 12.18 percent in the first quarter, down from 13.30 percent in the first quarter one year ago, and from 12.86 percent in the fourth quarter.

ANALYSIS OF ROA

The decrease in first quarter ROA from the prior quarter was driven by lower fee and other noninterest income and higher noninterest expense. Partially offsetting these negative impacts to quarterly profitability were a higher net interest margin (NIM) and higher mortgage loan servicing fee income, and lower loan loss provisions and taxes.

In the first quarter, NIM decreased to 277 basis points (or 2.77 percent of average assets) from 287 basis points in the comparable quarter a year ago, but was up from 276 basis points in the prior quarter.

Loan loss provisions decreased to 0.15 percent of average assets in the first quarter from 0.19 percent in the first quarter one year ago, and from 0.26 percent in the prior quarter. Loan loss provisions averaged 0.26 percent of average assets between 2001 and 2003, but have generally trended lower since the beginning of 2003 reflecting improved economic conditions.

Total fee income, including mortgage loan servicing fee income and other fee income, increased to 1.27 percent of average assets in the first quarter from 1.22 in the

first quarter one year ago, but was down from 1.38 percent in the prior quarter. Since 2001, total fee income has been depressed by lower mortgage loan servicing fee income as a consequence of impairment charges on mortgage servicing assets by a number of thrifts. These impairment charges resulted from higher mortgage prepayments, which decreased the duration and cash flow of servicing assets. Servicing fee income was 0.12 percent of average assets in 2005, an improvement of 13 basis points from the prior year. In the first quarter, servicing fee income was 0.20 percent of average assets, down from 0.23 percent in the first quarter one year ago, but up from 0.10 percent in the prior quarter.

Other fee income was up eight basis points from the first quarter one year ago to 1.07 percent of average assets, but was down from 1.28 percent in the prior quarter. Growth over the year came from increases in fee income from retail banking, trust activities, the sale of mutual funds and annuities, and loan servicing income from nonmortgage loans. Retail banking fees are generated from lending (activity fees, origination fees, insurance premiums, and penalty fees), and deposit taking (ATM charges, transaction account fees, and penalty fees).

Other noninterest income in the first quarter fell to 0.44 percent of average assets from 0.47 percent in the first quarter one year ago, and was down from 0.53 percent in the fourth quarter. Other noninterest income primarily includes gains on sales of assets and income from leasing office space. Other noninterest income is typically volatile since it includes realized gains and losses on assets held for sale and the results of balance sheet restructuring activities.

Noninterest expense increased to 2.56 percent of average assets over the first quarter, up from 2.46 percent in the first quarter one year ago, and from 2.54 percent in the prior quarter. General and administrative expense, the largest component of noninterest expense, increased by ten basis points to 2.52 percent of average assets in the first quarter from 2.42 percent in the comparable year ago quarter.

Taxes were down six basis points from the first quarter one year ago to 0.62 percent of average assets, and were down from 0.67 percent in the fourth quarter. Over the past two years, taxes have averaged 0.67 percent of average assets, or about 35 percent of pretax income.

MORTGAGE ORIGINATIONS

Total thrift industry mortgage originations (which include multifamily and nonresidential mortgages) in the first quarter increased to $164.6 billion from $161.0 billion in the first quarter one year ago, but were down from $187.1 billion in the prior quarter. First quarter 1-4 family mortgage originations by thrifts were $142.6 billion, up one percent from $141.5 billion in the first quarter one year ago, but down 13 percent from the $163.9 billion originated in the fourth quarter.

Thrifts accounted for approximately 26 percent of total 1-4 family originations nationwide in the first quarter of 2006,[3] up from 23 percent in the comparable year ago quarter and from 24 percent in the fourth quarter. An estimated 44 percent of thrift originations were ARMs in the first quarter, down from 50 percent in the prior and comparable year ago quarters. In contrast, the ARM share for all lenders was estimated at 30 percent in the first quarter, 33 percent in the first quarter one year ago, and 29 percent in the fourth quarter.[4]

The volume of mortgage refinancing was lower from the first quarter one year ago as longer-term interest rates increased. Refinancing activity accounted for 35 percent of thrift originations in the first quarter, down from 37 percent in the first quarter one year ago, but up slightly from 34 percent in the prior quarter.

ASSET QUALITY

Asset quality within the industry remained strong over the first quarter. OTS is closely monitoring thrift loan performance and asset quality since a significant proportion of thrift loan portfolios are recently originated, or unseasoned, loans. Moreover, newer loan types such as interest-only mortgages and the significant rise in home equity lines-of-credit are receiving additional supervisory scrutiny since these loans have not been stressed through different economic cycles. Troubled assets, which consist of noncurrent loans and repossessed assets, were unchanged from the prior quarter at 0.64 percent of assets, but were up from 0.47 percent in the comparable year ago quarter. Excluding repurchased GNMA loans, troubled assets were unchanged from one year ago at 0.47 percent of assets. Repossessed assets increased to 0.07 percent of assets from 0.05 percent of assets one year ago.

Noncurrent loan rates (loans over 89 days past due or in nonaccrual status), excluding repurchased GNMA loans, fell to 0.40 percent of assets at the end of the first quarter from 0.41 percent one year ago, but were up from 0.39 percent in the prior quarter. Noncurrent loan rates for all loan types but 1-4 family and multifamily mortgages improved over the year. Mortgages on 1-4 family dwellings and multifamily mortgages are the mainstay of the thrift industry and together make up over half of thrift assets. The industry's concentration in this sector accounts for its overall strong credit quality. Noncurrent loan rates for 1-4 family loans, excluding repurchased GNMA loans, were up two basis points from one year ago and up one basis point from the end of the fourth quarter at 0.51 percent of all 1-4 family. Noncurrent multifamily loans increased to 0.14 percent of all multifamily loans from 0.08 percent one year ago.

Noncurrent nonresidential mortgages fell to 0.49 percent of all nonresidential mortgages from 0.68 percent one year ago. Noncurrent construction and land loans were 0.47 percent of all construction and land loans, down from 0.75 percent one year

[3] Total 1-4 family mortgage originations estimated by the Mortgage Bankers Association of America.

[4] Data are from the Federal Housing Finance Board's monthly *Mortgage Interest Rate Survey*.

ago. Noncurrent commercial loans fell to 1.07 percent of all commercial loans at the end of the first quarter from 1.30 percent a year ago. Noncurrent consumer loans decreased from 0.75 percent of all consumer loans one year ago to 0.67 percent at the end of the first quarter.

Similar to the year-over-year trends in noncurrent loan types, loans past due by 30 to 89 days were higher over the year for 1-4 family and multifamily mortgages. Rising delinquencies of loans 30 to 89 days past due can signal that thrifts may experience higher levels of troubled assets in the future. The highest past due rates occurred in consumer loans. Total loans past due by 30 to 89 days at the end of the first quarter, excluding repurchased GNMA loans, were $8.2 billion, or 0.55 percent of assets compared to $7.1 billion, or 0.53 percent of assets, one year ago, and $8.6 billion, or 0.59 percent of assets, in the fourth quarter.

ASSETS, LIABILITIES, AND CAPITAL

Industry assets increased by 12.0 percent over the year to $1.50 trillion from $1.34 trillion. Thrifts remain focused on residential mortgage lending, with 56.5 percent of assets invested in 1-4 family mortgage loans at the end of the first quarter, up slightly from 56.3 percent one year ago. Of these 1-4 family mortgage loans, 10.8 percent are home equity lines of credit, down from 11.0 percent of 1-4 family mortgages in the first quarter one year ago. Holdings of consumer loans decreased to 5.7 percent of assets from 5.8 percent a year ago, and multifamily mortgages were down over the year to 4.4 percent of assets from 4.7 percent. Commercial loans fell to 2.9 percent of assets at the end of the first quarter from 3.0 percent one year ago.

Deposits and escrows grew by 11 percent over the year to $867 billion from $785 billion. As a percentage of total assets, deposits and escrows decreased to 57.8 percent from 58.5 percent one year ago. Federal Home Loan Bank advances were unchanged from one year ago at 18.0 percent of total assets.

Capital measures for the industry continue to be strong, stable, and well in excess of minimum requirements. At quarter-end, over 99 percent of the industry exceeded well-capitalized standards. Equity capital at the end of the first quarter was 9.36 percent of assets, up from 9.18 percent one year ago. No thrift was less than adequately capitalized at year-end.

PROBLEM THRIFTS

As the thrift industry continued to perform at or near record levels over the past year, the number of problem thrifts has remained at a low level. Problem thrifts – those with composite examination ratings of 4 or 5 – decreased by two over the year to six. Assets of problem thrifts were lower at the end of the first quarter at $1.1 billion, down

from $1.6 billion at the end of the comparable year ago quarter and from $1.9 billion at the end of the prior quarter.

Thrifts with composite ratings of 3 remained were down by nine over the year to 44 at the end of the first quarter and were down by one from the fourth quarter. Thrifts with composite ratings of 3 exhibit some weaknesses that may range from moderate to severe in one or more of the ratings components. These institutions are more vulnerable to adverse conditions and require more supervisory attention. All of the 3-rated thrifts at the end of the first quarter were well capitalized, providing them with some degree of cushion to work through their problems.

STRUCTURAL CHANGES

Charter choice decisions resulted in five institutions choosing a thrift charter during the first quarter – three were “de novo” institutions and two were existing credit unions that converted to a federal thrift charter. Two thrifts converted to commercial bank charters over the first quarter. Also during the first quarter, two OTS-regulated thrifts merged with other OTS-regulated thrifts, and non-OTS regulated institutions acquired eight thrifts.