



THRIFT INDUSTRY HIGHLIGHTS THIRD QUARTER 2010

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SUMMARY

The nation's thrift industry posted profits of \$1.77 billion in the third quarter 2010, or 0.77 percent of average assets (ROA). This was the fifth consecutive profitable quarter for the industry. Third quarter profits were up from \$1.49 billion in the prior quarter. In the third quarter one year earlier, thrifts reported profits of \$1.24 billion or 0.46 percent of average assets.

Though trending down from very high levels in 2008, loan loss provisions remained at elevated levels in the third quarter. The industry added \$2.12 billion (0.92 percent of average assets) to loan loss provisions in the third quarter. Provisions measured 0.98 percent of average assets in the prior quarter and 1.86 percent in the third quarter one year earlier. The substantial additions to loan loss reserves have bolstered the industry's reserve levels to at, or near, record levels.

Higher than average levels of loss provisioning are due to persistently high unemployment, continued housing market weakness, and spreading weakness to nonresidential commercial real estate markets. The need for loss provisions in upcoming quarters will largely depend on trends in employment, home prices and sales, and the commercial real estate markets.

The industry's financial fundamentals remained solid in the third quarter. The majority of thrifts – 93.1 percent – reported capital exceeding the “well-capitalized” regulatory standards. And these thrifts' combined assets represented 96.6 percent of industry aggregate assets.

To better gauge and assess earnings, many analysts are increasingly focusing attention on “core” or “operating” earnings. Operating earnings measures exclude volatile items and one-time events such as branch sale gains or acquisition charges. Operating earnings measures also exclude charges for provisions for loan losses.

The thrift industry's operating earnings for the first nine months of 2010 were 1.68 percent of average assets, compared with 1.70 percent for 2009 and 1.29 percent for 2008. The combination of solid capital, bolstered loan loss reserves and solid, stable operating earnings will help the industry weather the economic and housing market distress currently facing the nation.

Recent increases in problem assets are also a direct result of the continued housing market downturn and high unemployment. Troubled assets (noncurrent loans and repossessed assets) increased to 3.45 percent of assets from 3.35 percent in the prior quarter, but were down from 3.65 percent one year earlier.

The number of private sector thrifts supervised by OTS stood at 741 with assets of \$927.9 billion at the end of the third quarter. In addition, OTS supervised 436 holding company enterprises with approximately \$4.2 trillion in U.S. domiciled consolidated assets. These enterprises owned 398 thrifts with total assets of \$717 billion, or 77 percent of total thrift industry assets.

Other highlights include:

EARNINGS AND PROFITABILITY

- Net income was \$1.77 billion in the third quarter of 2010, up from \$1.24 billion in the third quarter one year earlier, and up from net income of \$1.49 billion in the prior quarter.
- Profitability, as measured by return on average assets (ROA), was 0.77 percent in the third quarter, up from 0.46 percent in the third quarter one year earlier, and up from 0.64 percent in the prior quarter. The median ROA in the third quarter was 0.44 percent, up from 0.33 percent in the third quarter one year earlier, and up from 0.41 percent in the prior quarter.
- Return on average equity (ROE) was 6.68 percent in the third quarter, up from 4.40 percent in the third quarter one year earlier, and up from 5.76 percent in the prior quarter.

ANALYSIS OF ROA

- Higher earnings in the third quarter were primarily due to higher net interest income as well as higher fee income. Also contributing to higher earnings was a decrease in loan loss provisions.
- Net interest margin in the third quarter improved to 313 basis points from 311 basis points in the third quarter one year earlier, and was up from 307 basis points in the prior quarter.
- Lower loan loss provisions in the third quarter had a positive impact on thrift earnings. In the third quarter, thrifts added \$2.1 billion, or 0.92 percent of average assets, to loan loss provisions. Provisions measured 0.98 percent of average assets in the second quarter and 1.86 percent in the third quarter one year earlier. Loan loss provisions averaged 0.26 percent of average assets

between 2001 and 2003, and generally trended lower from the beginning of 2003 through the first half of 2006, reflecting historically low levels of problem assets.

- Total fee income, including mortgage loan servicing fee income and other fee income, was 1.41 percent of average assets in the third quarter, up from 1.24 percent in the comparable quarter one year earlier, and up from 1.36 percent in the prior quarter.
- Other noninterest income improved to 0.51 percent of average assets in the third quarter from 0.43 percent in the third quarter of 2009, and was only down slightly from 0.52 percent in the prior quarter. Other noninterest income is typically volatile since it includes realized gains or losses on assets held for sale and the results of balance sheet restructuring activities.
- Noninterest expense increased to 2.91 percent of average assets in the third quarter from 2.10 percent in the third quarter one year earlier, and was up slightly from 2.90 percent in the prior quarter.
- Taxes increased to 0.45 percent of average assets in the third quarter from 0.35 percent in the third quarter one year earlier, and up from 0.41 percent in the prior quarter.

MORTGAGE ORIGINATIONS

- Total thrift industry mortgage originations (which include multifamily and nonresidential mortgages) during the third quarter totaled \$41.8 billion, down 11 percent from \$46.8 billion in the third quarter one year earlier, but up 14 percent from \$36.6 billion in the prior quarter.
- Total originations of 1-4 family mortgages by thrifts during the third quarter were \$36.3 billion, down 8 percent from \$39.5 billion in the third quarter one year earlier, but up 18 percent from the \$30.8 billion originated in the second quarter. Much of thrifts' current 1-4 family mortgage production is being sold into the secondary markets. Sales of 1-4 family mortgages measured just over 100 percent of 1-4 family originations in the third quarter, up from 91 percent in the prior quarter.
- Refinancing activity accounted for 57 percent of thrift originations in the third quarter, up from 42 percent in the prior quarter, and from 45 percent in the third quarter one year earlier. The increase in third quarter refinancing activity was attributable to historically low mortgage interest rates. The record for thrift mortgage refinancing was 59.2 percent in the first quarter of 2003.

ASSET QUALITY

- Delinquencies for construction, land, nonresidential, and multifamily loans were higher over the year while 1-4 family mortgages and consumer and commercial loans were lower over the year.
- Troubled assets, which consist of noncurrent loans and repossessed assets, were 3.45 percent of assets at the end of the third quarter, down from 3.65 percent one year earlier, but up from 3.35 percent at the end of the prior quarter. Repossessed assets were up three basis points over the year from 0.48 percent of assets to 0.51 percent, and up from 0.46 percent at the end of the prior quarter.
- Noncurrent loan rates (loans over 89 days past due or in nonaccrual status) fell to 2.94 percent of assets at the end of the third quarter from 3.17 percent at the end of the third quarter one year earlier, but were up from 2.88 percent at the end of the prior quarter. Noncurrent loan rates for 1-4 family loans increased to 5.75 percent of all 1-4 family loans from 5.46 percent in the prior quarter, and were down slightly from 5.76 percent one year earlier. Noncurrent multifamily loans increased to 2.90 percent of all multifamily loans from 2.69 percent one year earlier. Noncurrent consumer loans decreased to 1.23 percent of all consumer loans in the third quarter from 1.68 percent at the end of third quarter one year earlier. Noncurrent nonresidential mortgages increased to 3.82 percent of all nonresidential mortgages from 2.79 percent one year earlier. Noncurrent construction and land loans were 16.01 percent of all construction and land loans at the end of the third quarter, up from 13.21 percent one year earlier. Noncurrent commercial loans decreased to 2.85 percent of all commercial loans at the end of the third quarter from 3.22 percent a year earlier.
- Loans past due by 30 to 89 days relative to total assets were lower over the year and from the prior quarter. Total loans past due by 30 to 89 days at the end of third quarter were \$10.0 billion, or 1.08 percent of assets, compared to \$16.1 billion, or 1.50 percent of assets, one year earlier, and were down from 1.13 percent of assets, in the prior quarter.

ASSETS, LIABILITIES, AND CAPITAL

- Industry assets decreased by 13 percent over the year to \$928 billion from \$1.1 trillion. Thrifts remain focused on residential mortgage lending, with 34.9 percent of assets invested in 1-4 family mortgage loans at the end of the third quarter, down from 39.2 percent one year earlier. The decline in the percent of residential loans was attributable to continued strong sales of loans into the secondary market and refinancing activity. Of total 1-4 family mortgage loans, 4.8 percent were home equity lines of credit, down from 5.0 percent one year earlier. Holdings of consumer loans increased to 8.6 percent of assets from 6.9

percent a year earlier. Multifamily mortgages increased over the year from 3.2 percent of assets to 3.3 percent at the end of the third quarter. Commercial loans increased from 4.8 percent of assets one year earlier to 5.4 percent.

- Deposits and escrows fell by five percent over the year to \$661 billion from \$699 billion. As a percentage of total assets, deposits and escrows increased to 71.3 percent from 65.3 percent one year earlier. Federal Home Loan Bank advances were down from 12.2 percent one year earlier to 8.6 percent of total assets at the end of the third quarter.
- Capital measures for the industry continue to be strong, stable and well in excess of minimum requirements. Equity capital at the end of the third quarter was 11.66 percent of assets, up from 10.70 percent one year earlier. At the end of the third quarter, 93.1 percent of the industry exceeded well-capitalized standards and 7 thrifts were less than adequately capitalized.

PROBLEM THRIFTS

- The number of problem thrifts – those with composite examination ratings of 4 or 5 – was up from 43 thrifts one year earlier to 53 thrifts at the end of the third quarter, and was down from 54 thrifts at the end of the prior quarter.

STRUCTURAL CHANGES

- A total of 13 thrifts left OTS regulation over the third quarter. One thrift converted to a bank charter over the quarter, three were acquired by a bank and nine thrifts failed. One thrift entered OTS regulation during the quarter.