Office of the
Comptroller of the Currency

MDIAC Meeting

September 21, 2021

State of MDIs

Financial Information as of June 30, 2021

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MDIAC Agenda

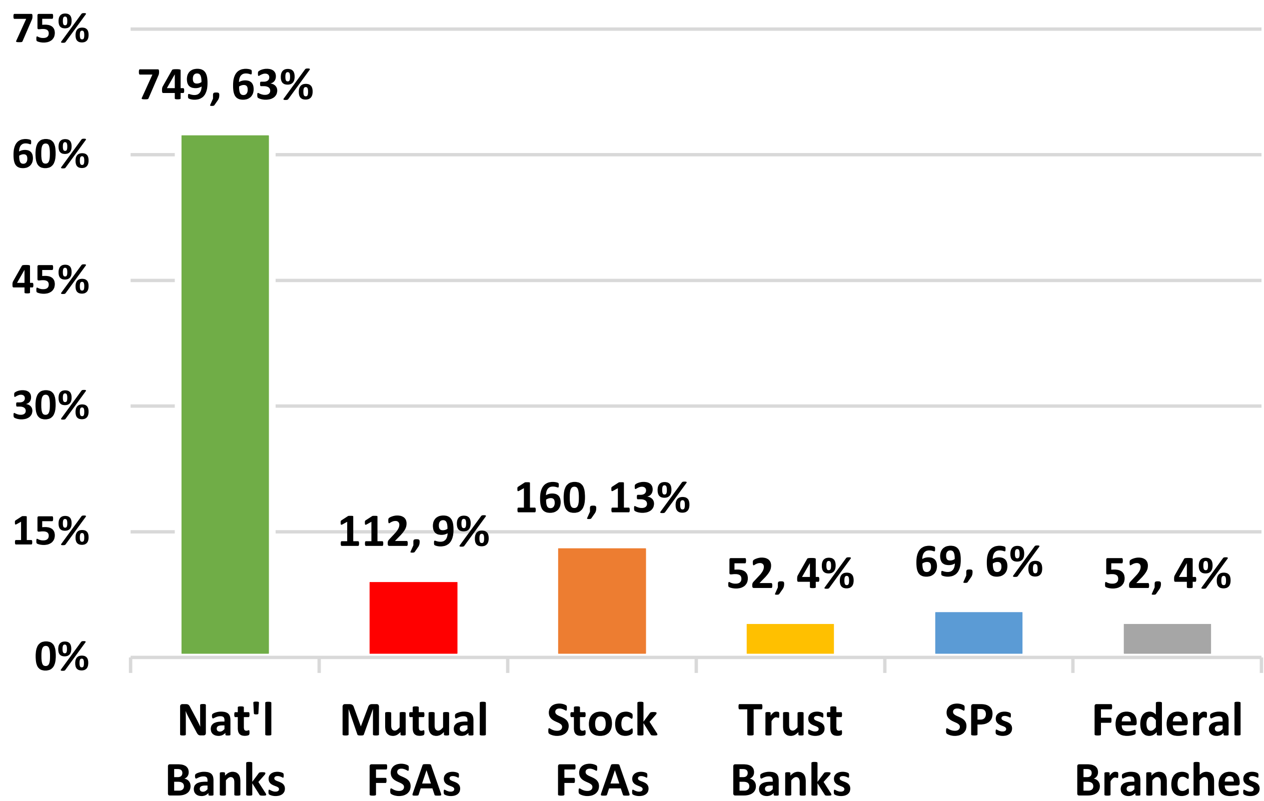
This presentation will focus on:

- **Portfolio Demographics**
- **Financial Performance and Component Ratings**
- **Supervisory Information**

Preface: Financial trend charts start in 2007. The current bank population as of June 30, 2021, is “held constant.” All federal savings associations (FSAs) have filed the commercial bank call report since 2012. Some charts use the median; others use weighted averages.

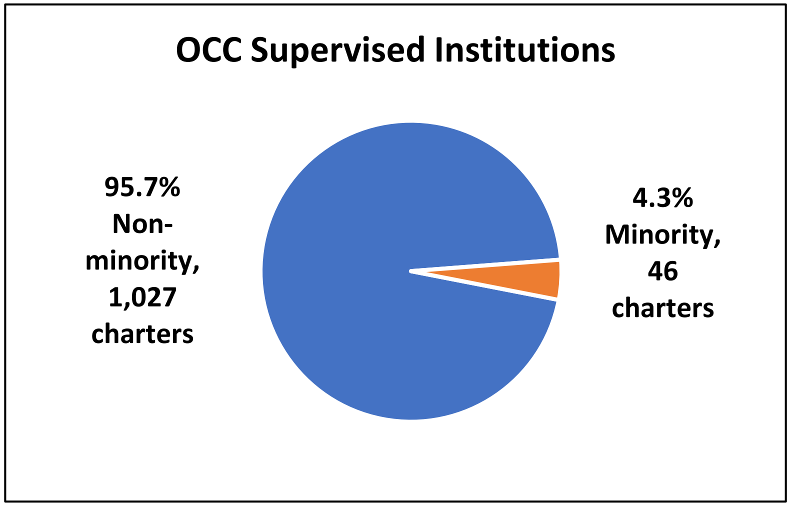
OCC Charters by Institution Type

OCC supervised 1,194 institutions as of June 30, 2021.

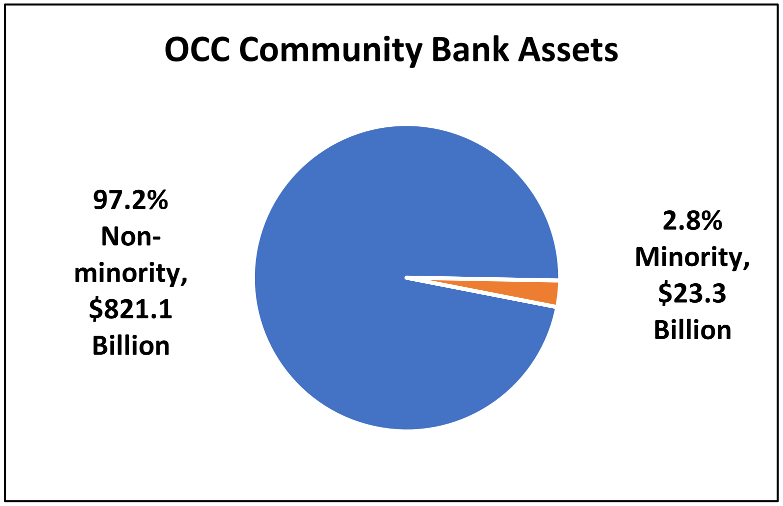


Minority Charters and Total Assets

- Minority Depository Institutions (MDIs) represent 46 or 4.3 percent of total OCC bank charters as of June 30, 2021.

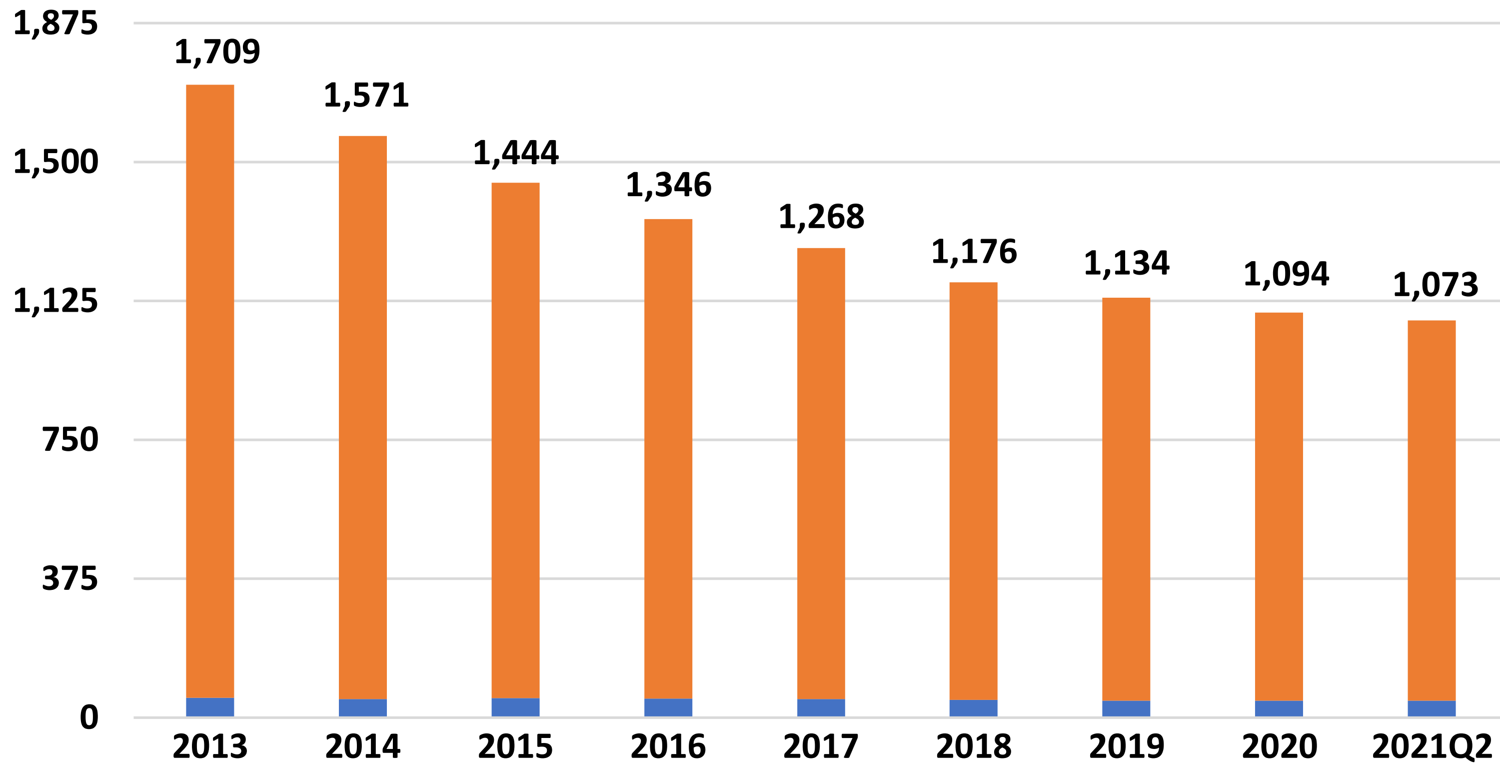


- Minority Depository Institutions represent $23.3 billion or 2.8 percent of total OCC supervised community bank assets as of June 30, 2021. (This chart does not include Trust, Midsize, or Large Bank charters.)



Trends in OCC and MDI Charters

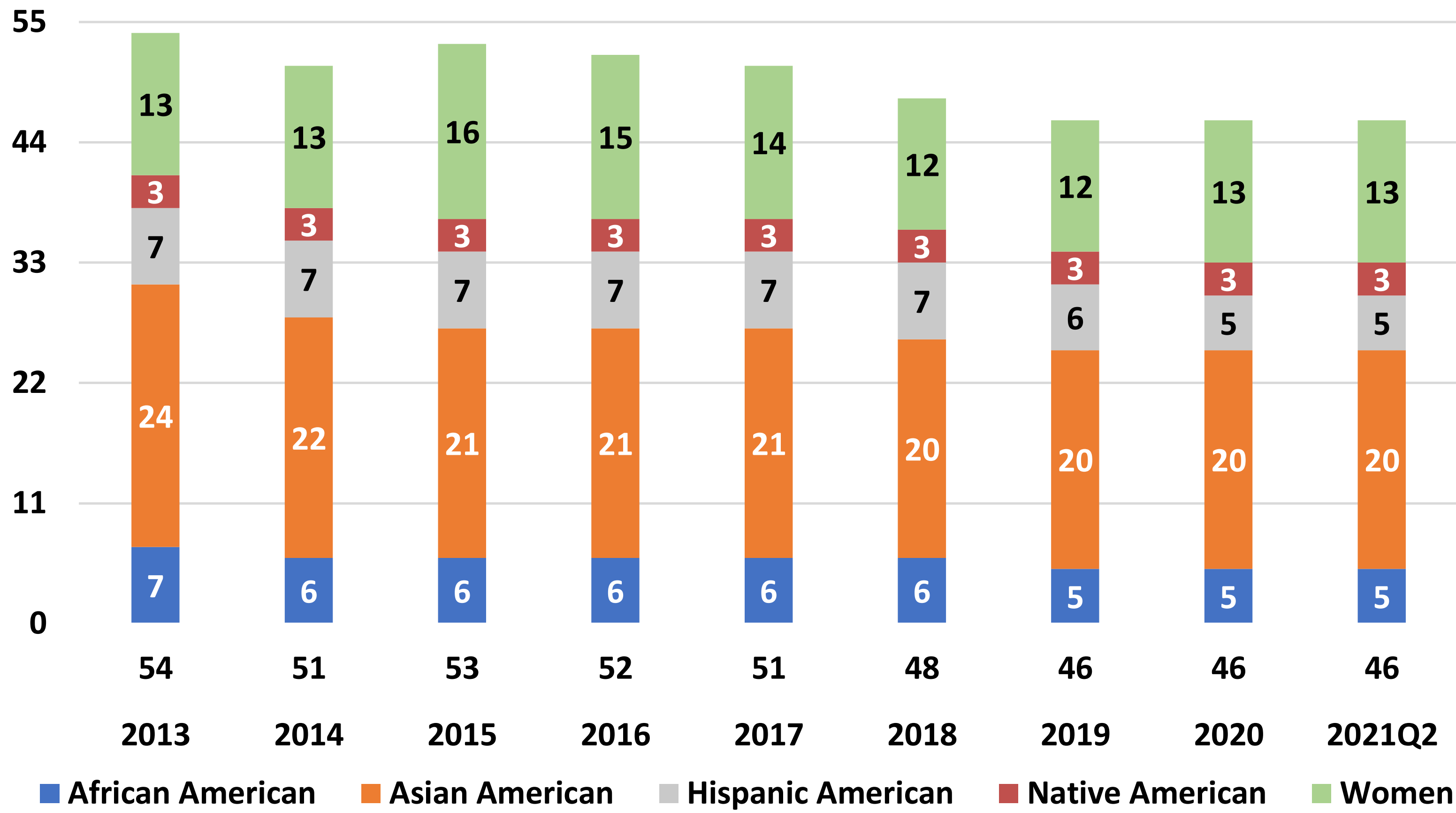
The net number of OCC charters decreased by 636 or 37 percent since 2013 due primarily to mergers and acquisitions.



	2013	2014	2015	2016	2017	2018	2019	2020	2021Q2
Non-MDI	1,655	1,520	1,391	1,294	1,217	1,128	1,088	1,048	1,027
MDI	54	51	53	52	51	48	46	46	46

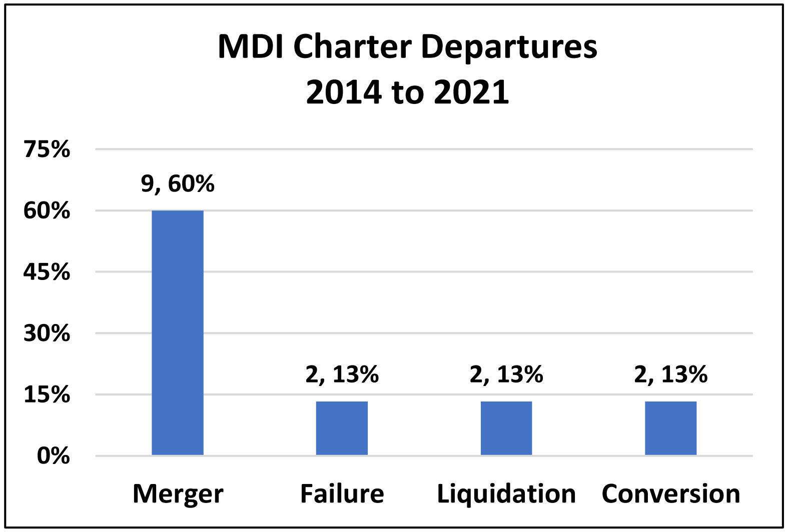
Trends in MDI Charters by Group

The net number of MDI charters decreased by eight or 15 percent since 2013. This departure rate compares favorably to the overall OCC departure rate of 37 percent for the same period.

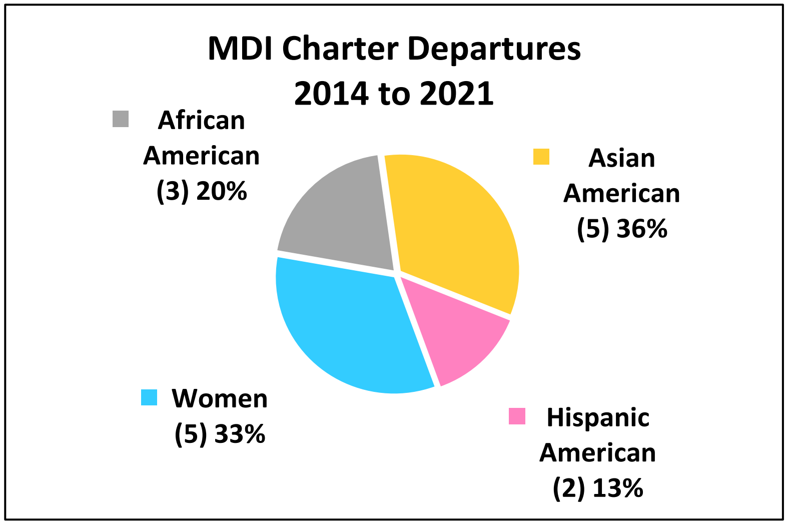


Disposition of Inactive MDI Charters

- Fifteen or 24 percent of total MDIs have gone inactive since 2014. Mergers and acquisitions were the primary reason for departure.

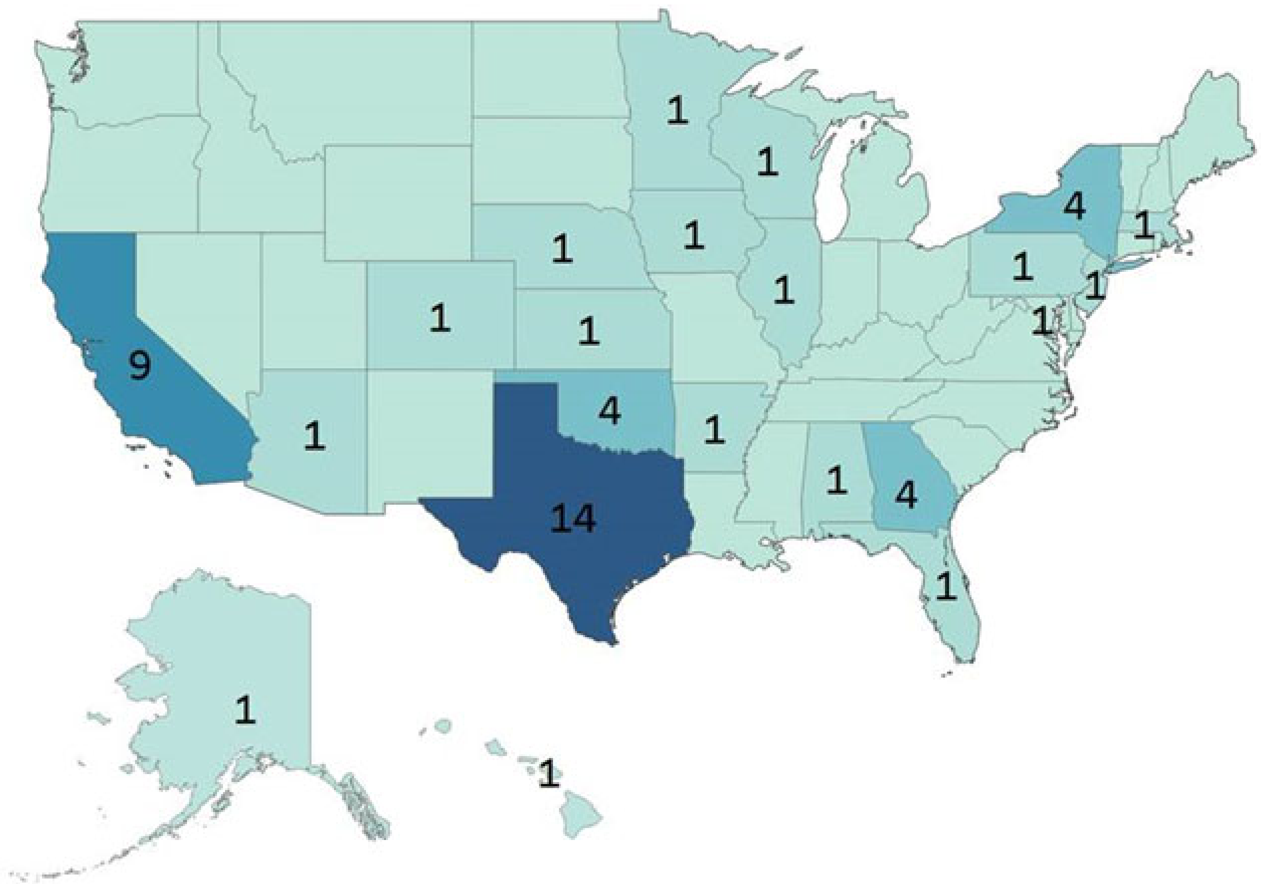


- Most MDI departures were from the Asian American and Women groups.



MDIs by State

OCC currently supervises 52 MDIs, including six that were designated as MDIs after June 30, 2021. MDIs are in 21 states and concentrated in Texas (14) and California (9). Three other states have multiple MDIs: Georgia (4), New York (4), and Oklahoma (4).

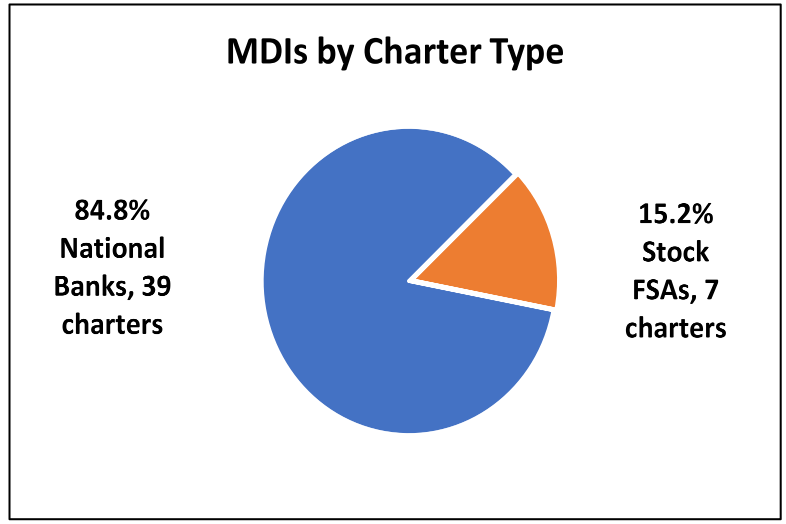


MDI Peer Groups

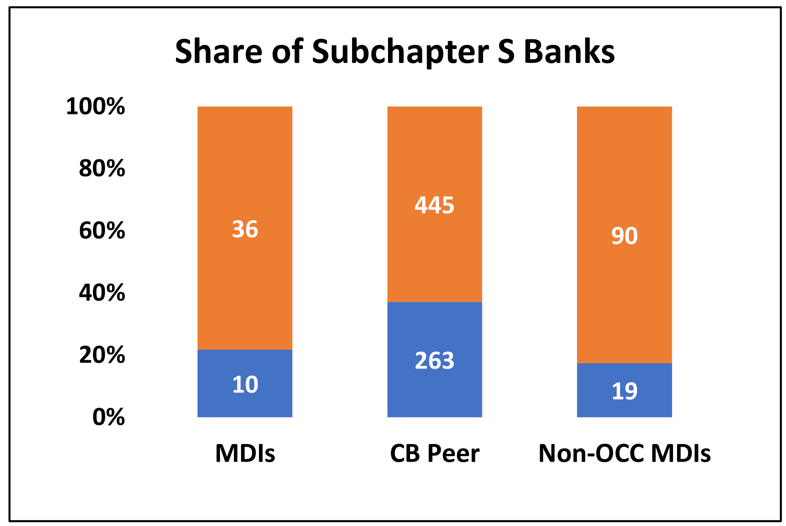
- As of June 30, 2021, the smallest MDI in assets was $27.9 million and the largest MDI was $2.9 billion.
- MDIs fall into two institution type categories – national banks or stock FSAs.
- There are no mutual FSA MDIs or trust company MDIs.
- No MDI is supervised by Midsize or Large Bank Supervision.
- As such, the MDI peer group referenced throughout this presentation is community banks with total assets less than $3 billion and not mutually-owned (CBs<$3B).
- We will also compare OCC-supervised MDIs to MDIs supervised by the FDIC and Federal Reserve.

MDIs by Charter Type and Sub S Status

- The majority or 84.8 percent of MDIs are national banks.



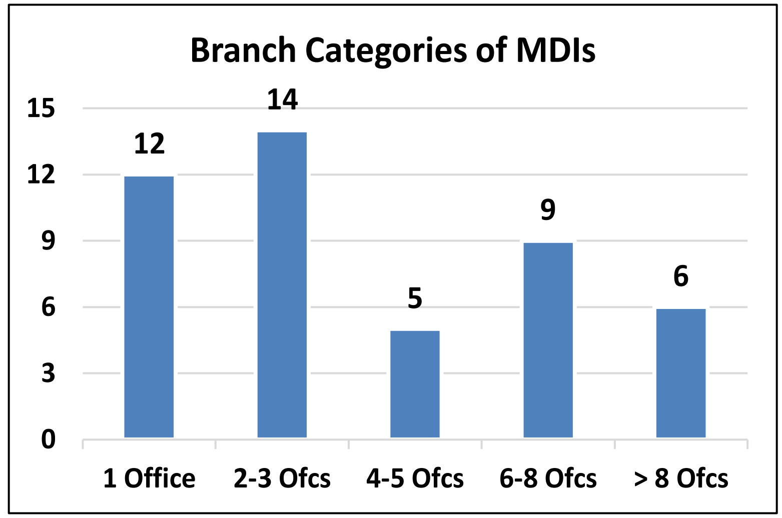
- Twenty-two percent of MDIs have elected Subchapter S status versus 37 percent for the community bank peer. Sub S banks may pass income (along with other credits, deductions, and losses) directly to shareholders, without paying federal corporate taxes.

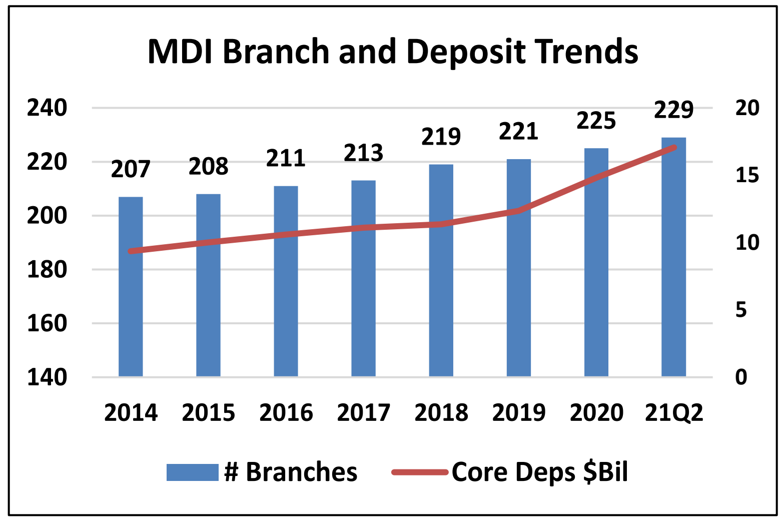


MDI Branches

- Twenty-six percent of MDIs operate from one location, and 57 percent have three locations or less. Nineteen MDIs or 41 percent have changed their branch configuration since 2014. Five MDIs reduced their branch network since 2014.

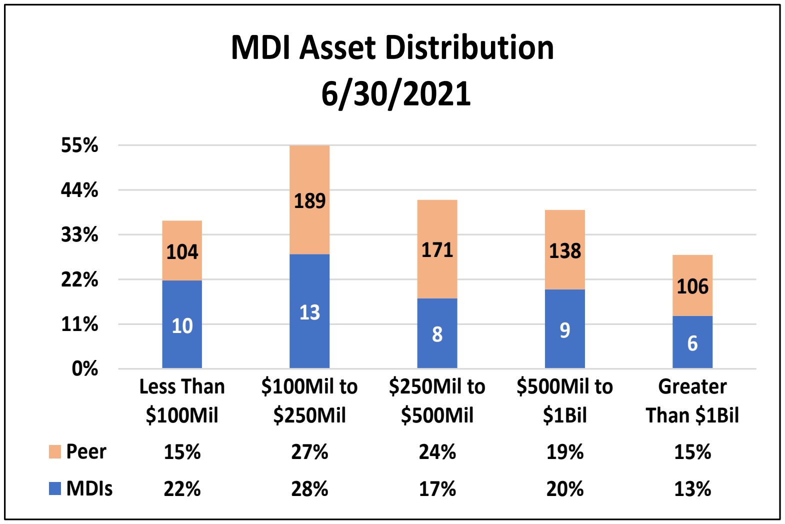
- Since 2014, the number of MDI office locations has grown 11 percent but core deposits have grown 82 percent (32 percent through 2019 or pre-pandemic).



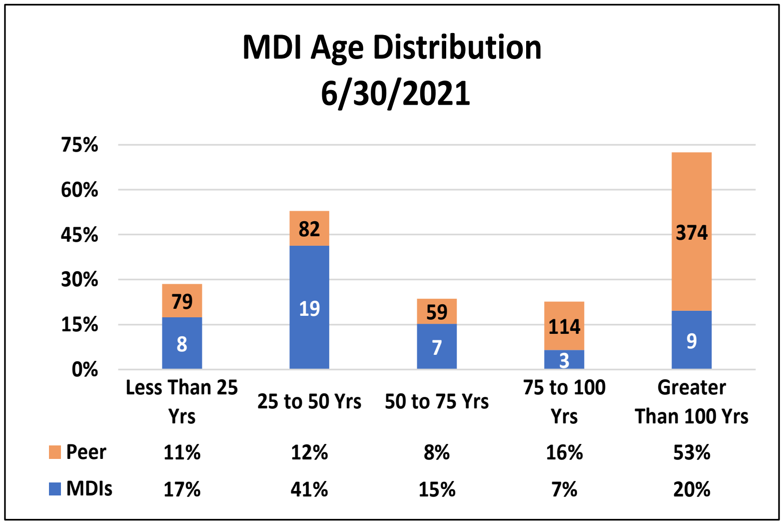


MDIs by Asset Size and Age

- MDIs are generally smaller in size than the community bank peer group. Fifty percent of MDIs have total assets less than $250 million versus 42 percent for the community bank peer.

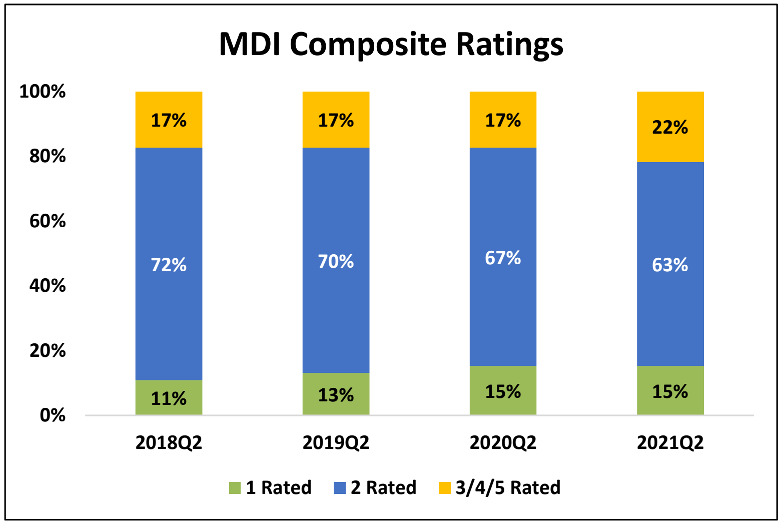


- MDIs have been operating for fewer years than the community bank peer. Fifty-eight percent of MDIs have operated for less than 50 years compared to 23 percent for the community bank peer. Only 20 percent of MDIs were formed more than **100** years ago.

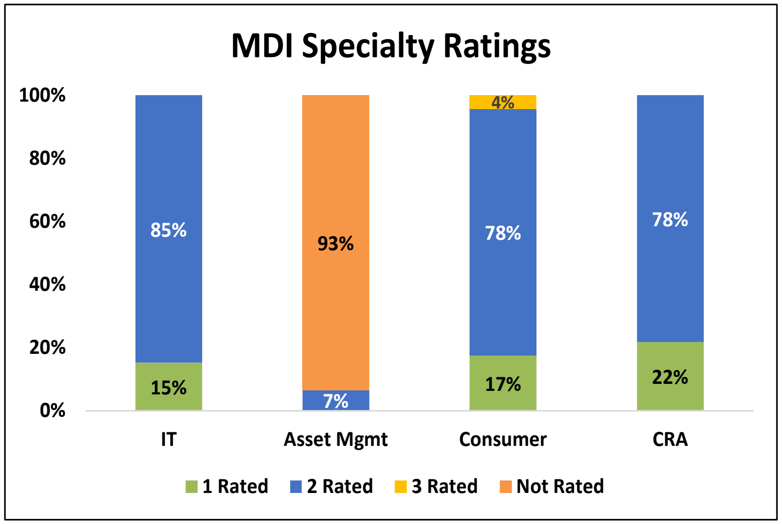


MDI Composite and Specialty Ratings

- Seventy-eight percent of MDIs have composite ratings of 1 or 2. The number of 1-rated charters remains stable.

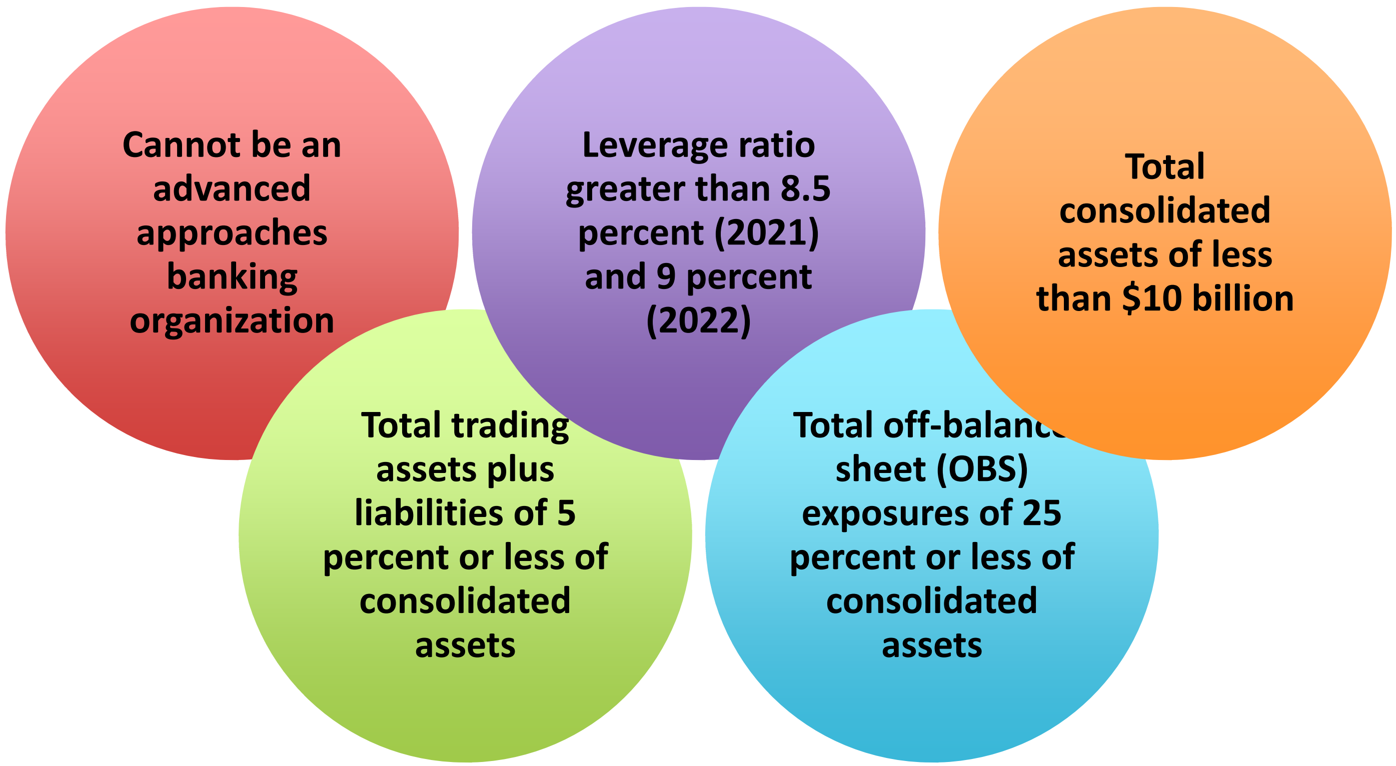


- Specialty ratings are satisfactory. No IT rating is worse than 2. Only three MDIs have trust powers. Two MDIs are rated 3 for consumer compliance. No CRA rating is worse than satisfactory.



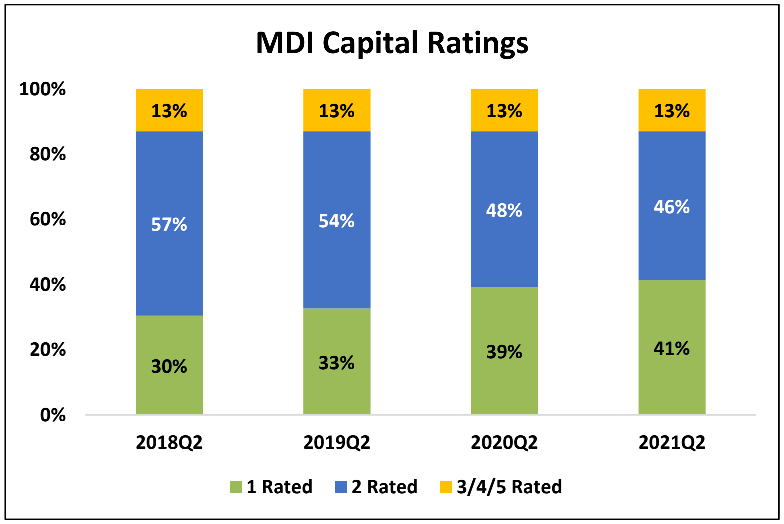
CBLR Framework-Now Being Phased In

The Community Bank Leverage Ratio (CBLR) is an optional simple leverage capital measure that became effective January 1, 2020. The CARES Act provided temporary relief and a gradual phase-in through 2021 due to the pandemic.

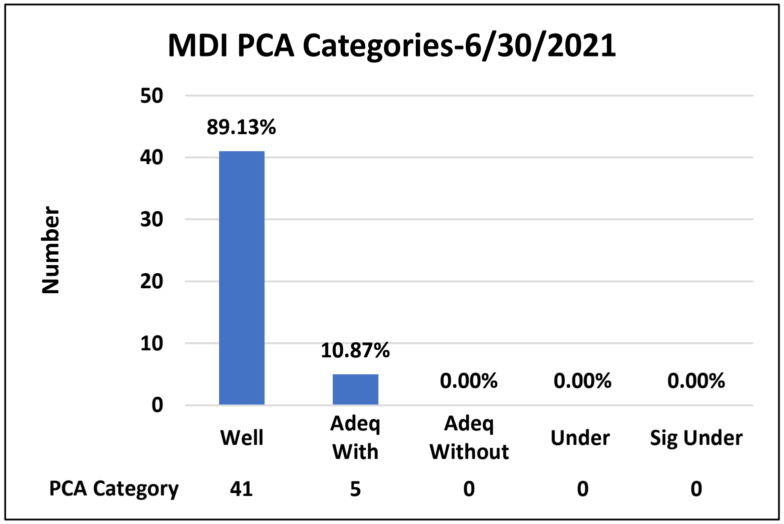


MDIs are "Well-Capitalized"

- MDI capital ratings remained stable. Eighty-seven percent of MDIs are rated 1 or 2 for capital with more MDIs rated 1 this year.

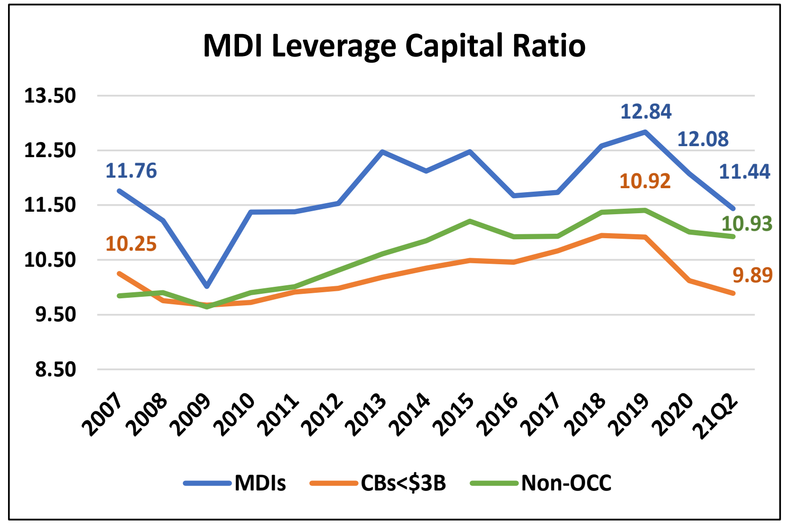


- Eighty-nine percent of MDIs met the "well-capitalized" definition contained in Prompt Corrective Action as of June 30, 2021. Five MDIs – with formal actions requiring higher minimums – are "adequately-capitalized."

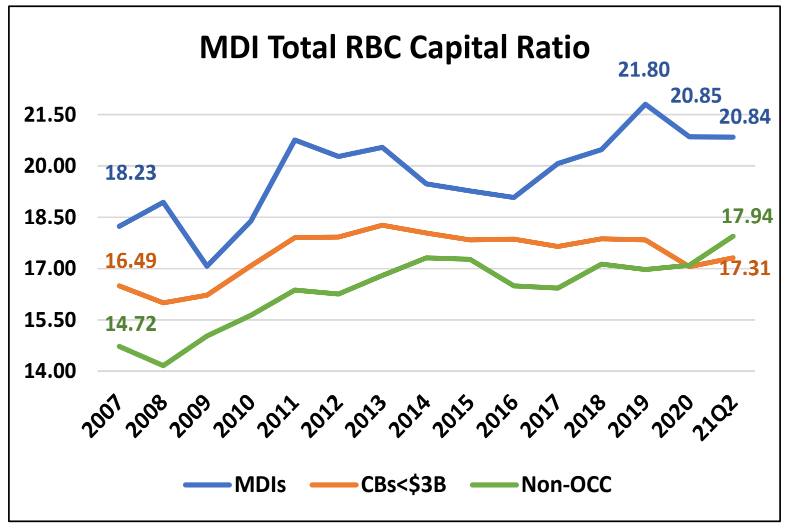


Capital Levels are Satisfactory but Lower

- The median MDI leverage ratio declined 140 basis points since 2019. MDI charters are better capitalized today versus pre-crisis when you adjust for the PPP.

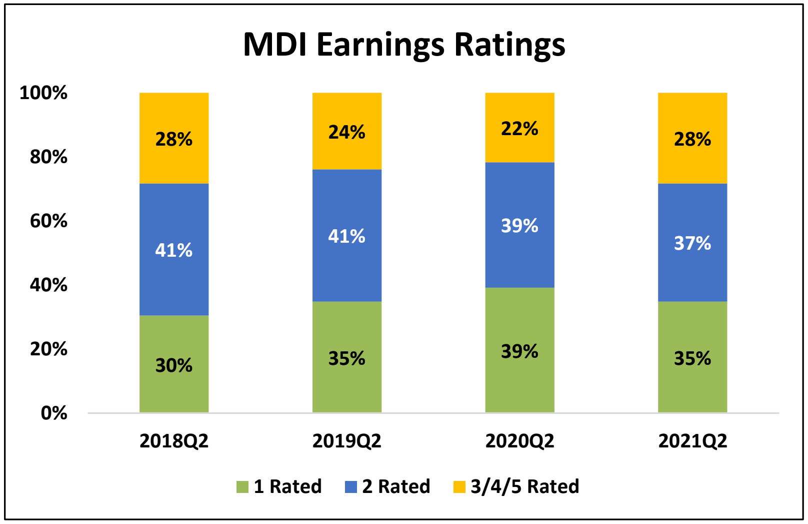


- MDI total risk-based capital levels remain stable at 20.84 percent this year. The gap between OCC MDIs and non-OCC MDIs narrowed to 290 basis points. Eighteen or 39 percent of MDIs have opted into the CBLR framework.

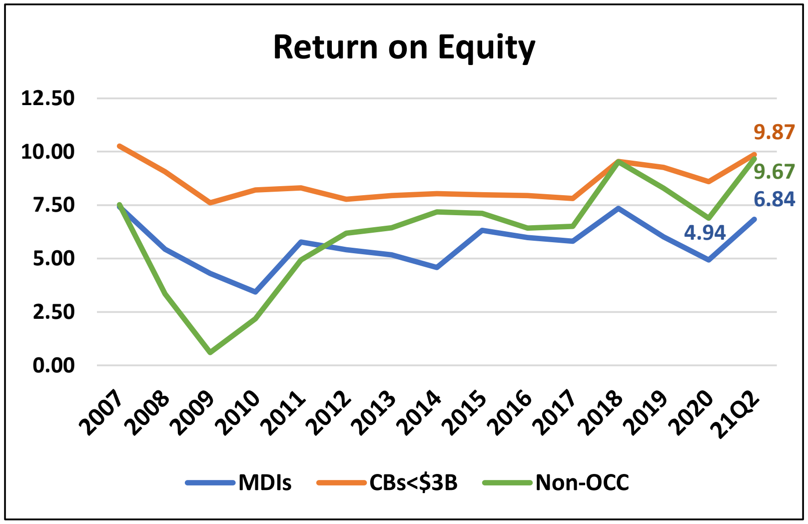


Earnings Ratings Lower in 2021

- Earnings ratings are stable but lag ratings in other safety and soundness areas. Only 72 percent of MDIs are rated 1 or 2 for earnings.

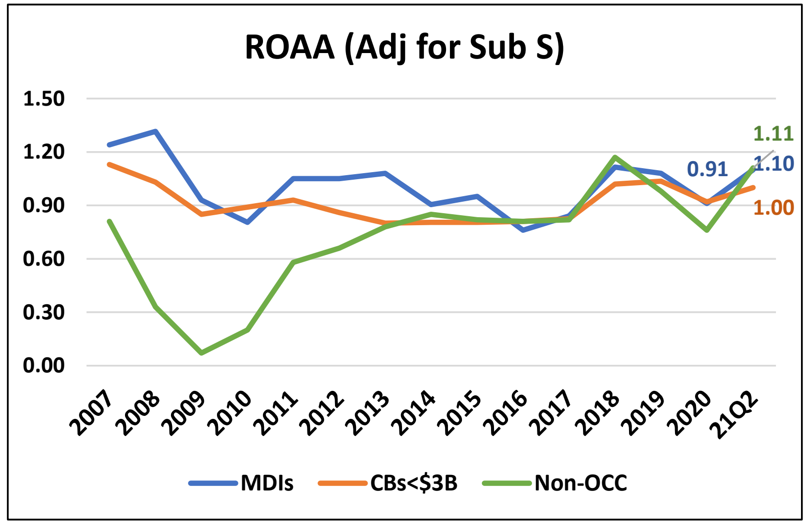


- MDI return on equity increased 190 basis points in 2021 but lags the other peer groups.

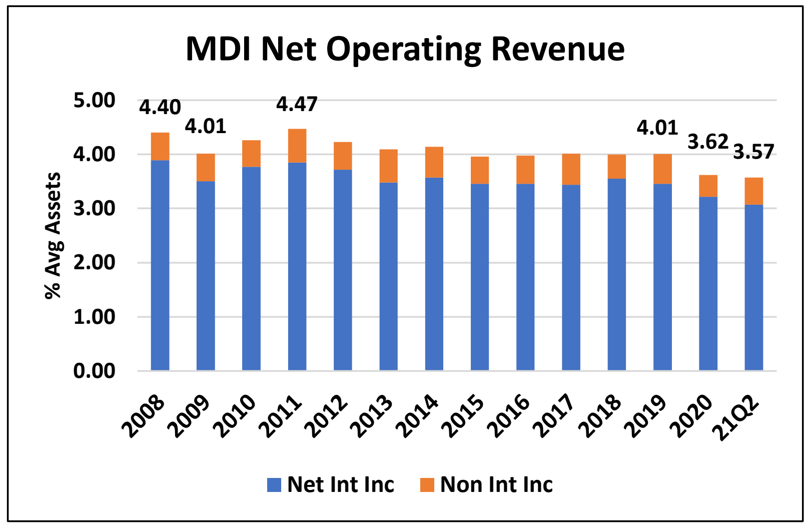


ROAA Increased This Year

- MDI ROAA increased 19 basis points to 1.10 percent in 2021. It is in line with Non-OCC MDIs and much higher than the community bank peer.



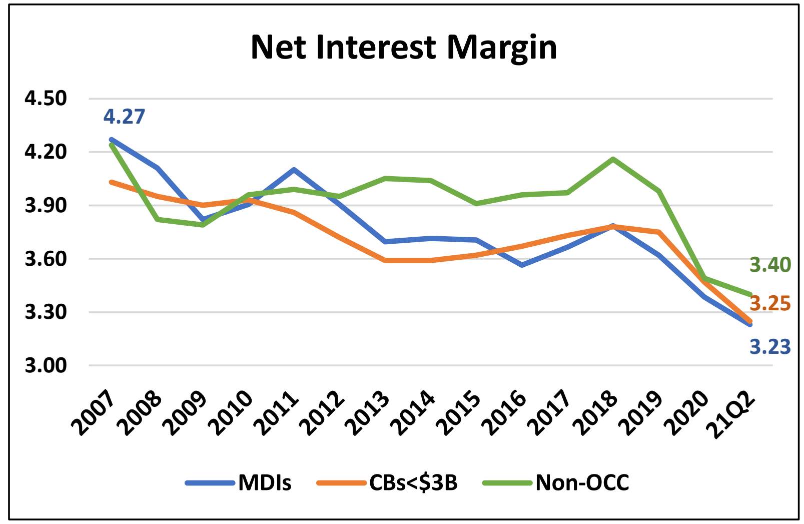
- MDI net operating revenue fell 44 basis points since 2019 to 3.57 percent. Net interest income fell 39 basis points to 3.07 percent. Fee income fell five basis points to 0.50 percent. Higher fee income remains a key distinction between smaller and larger banks.



NIM Sharply Lower

- Net interest margins (NIM) continue to compress. NIMs fell 16 basis points since 2020 and 11 basis points since last quarter.

- Margin compression is felt more by the smallest banks and usually leads to more industry consolidation and cost cutting by banks of all sizes.



Net Interest Margin - June 30, 2021

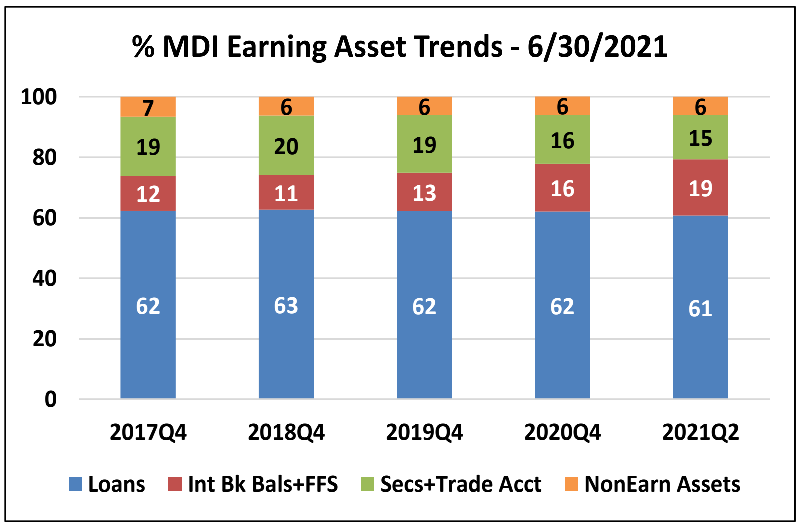
Asset Category	CBs<$3B	MDIs
Under $50MM	2.78	2.20
$50MM - $100MM	3.15	2.79
$100MM - $250MM	3.30	3.41
$250MM - $500MM	3.31	3.16
$500MM - $1B	3.19	3.86
Greater than $1B	3.26	3.57
Median	**3.25**	**3.23**

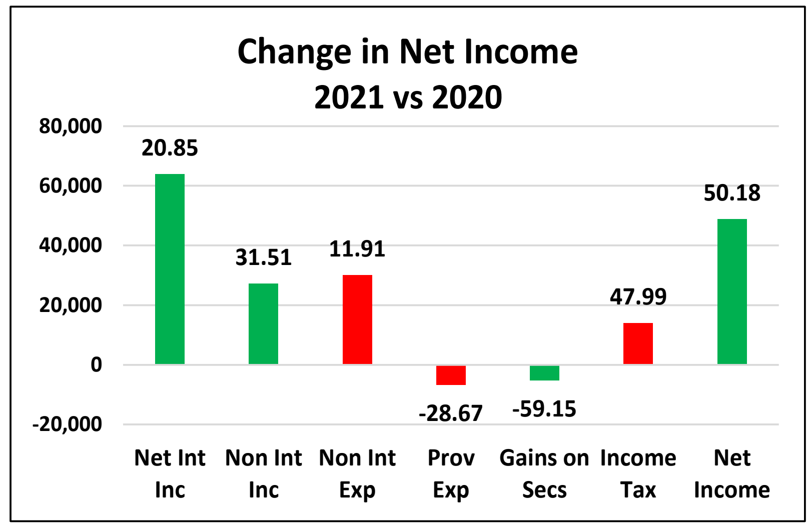
MDI Net Income Up 50.2 Percent in 2021

- Despite margin compression, MDI net income rose sharply in 2021 due to higher net interest income, strong growth in fee income, and lower provision expenses.

MDI Income Statement ($000's)

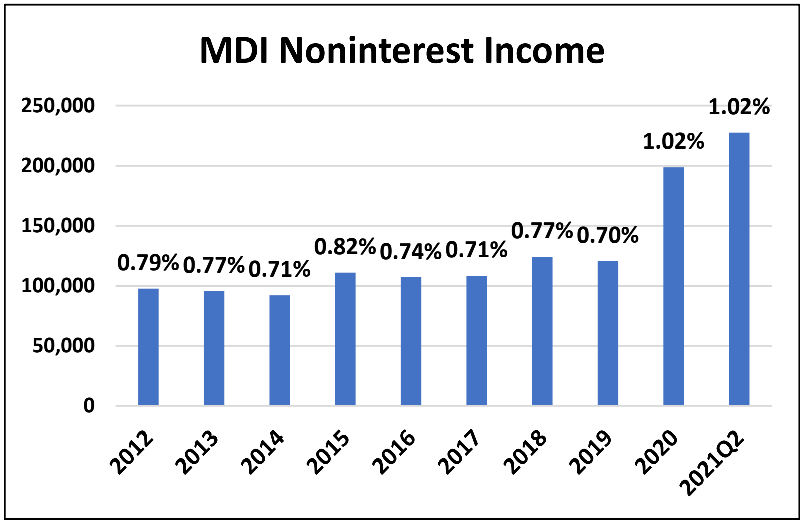
	2021Q2	2020Q2	Δ 1 Yr $	Δ 1 Yr %
Int Income	416,446	390,355	26,091	6.68
Int Expense	46,292	84,071	-37,779	-44.94
Net Int Inc	370,154	306,284	63,870	20.85
Non Int Inc	113,790	86,526	27,264	31.51
Non Int Exp	281,884	251,886	29,998	11.91
Prov Exp	16,753	23,487	-6,734	-28.67
Gains on Secs	3,580	8,764	-5,184	-59.15
Income Tax	43,016	29,067	13,949	47.99
Net Income	145,838	97,103	48,737	50.18



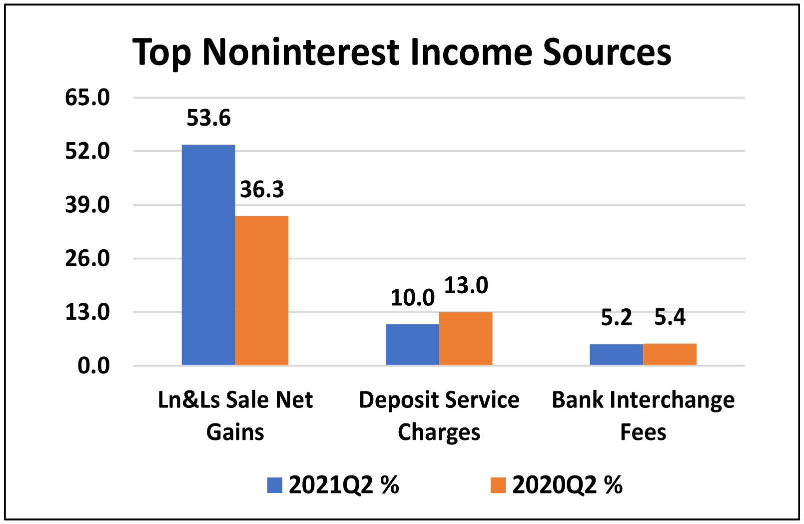


Noninterest Income Improving

- MDI noninterest income of $114 million is up 31.5 percent compared to one year ago. Eleven MDIs or 24 percent reported 0.25 percent of average assets or less this quarter. Lack of fee income diversity has hurt the smaller charters.



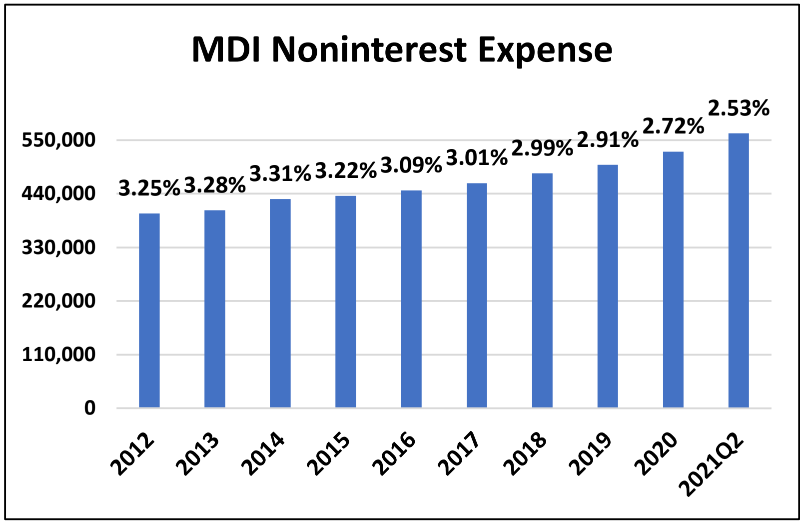
- At 53.6 percent loan and lease sales is the top noninterest income category in 2021. It has grown 94 percent over the last year. Deposit service charges is in second place and growing much slower at 2 percent.

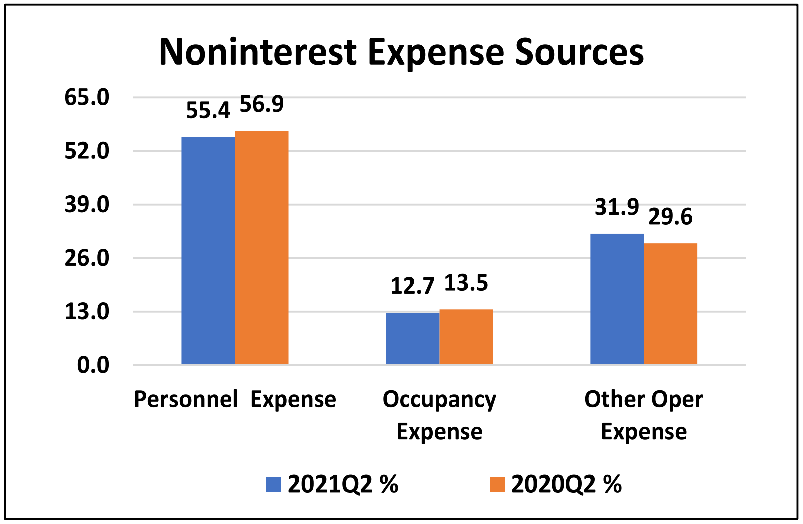


Noninterest Expense Increasing

- MDI noninterest expense of $282 million is up 11.9 percent compared to one year ago. Noninterest expense to average assets has decreased steadily since 2014. Five MDIs or 11 percent reported noninterest expense greater than 4 percent of average assets.

- At 55.4 percent, personnel expense is the top noninterest expense category. It has grown 9 percent over the last year. Occupancy expense is much lower at 12.7 percent of noninterest expense and growing slower at 5 percent.

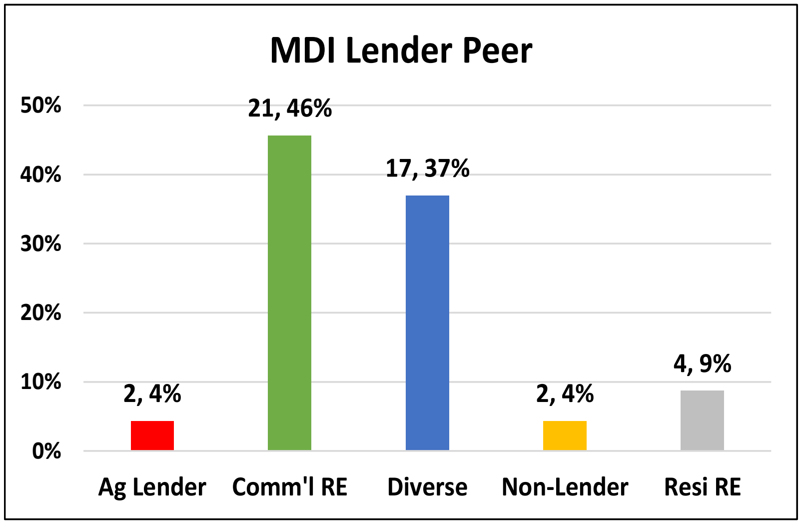


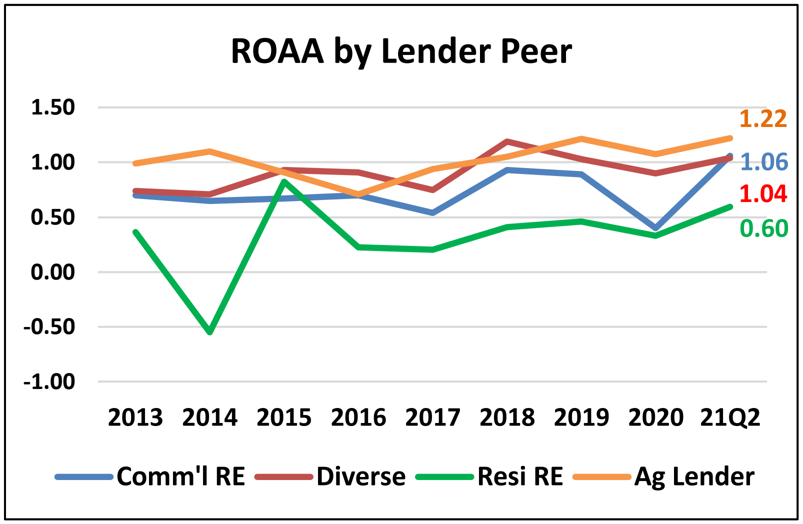


MDI ROAA by Lender Peer

- In addition to asset size and geography, OCC also analyzes bank performance by lender peer. Most MDIs or 46 percent are commercial real estate (CRE) lenders and 37 percent are diversified lenders.

- Ag lenders, CRE lenders, and diverse lenders have enjoyed ROAAs over 1 percent in 2021.

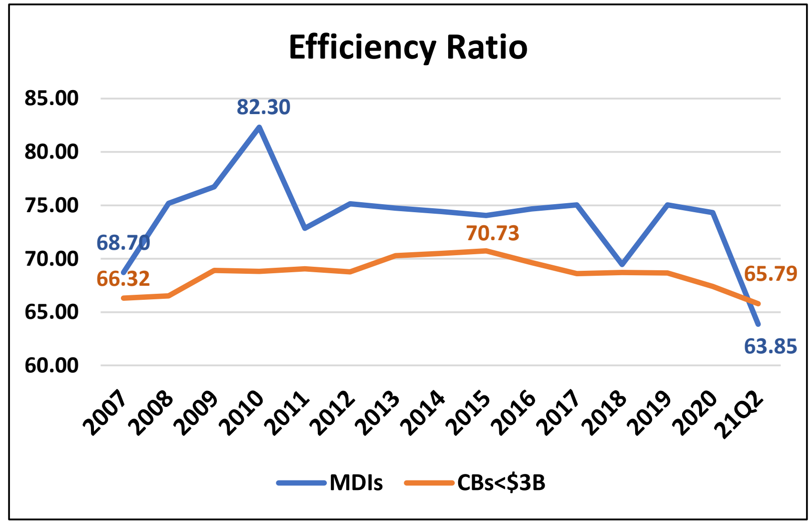




Efficiency Ratio Improving

- The MDI efficiency ratio improved in 2021 due to strong growth in adjusted operating revenue.

- If you stratify the efficiency ratio by asset size, you will find the larger the bank, the lower the efficiency ratio.

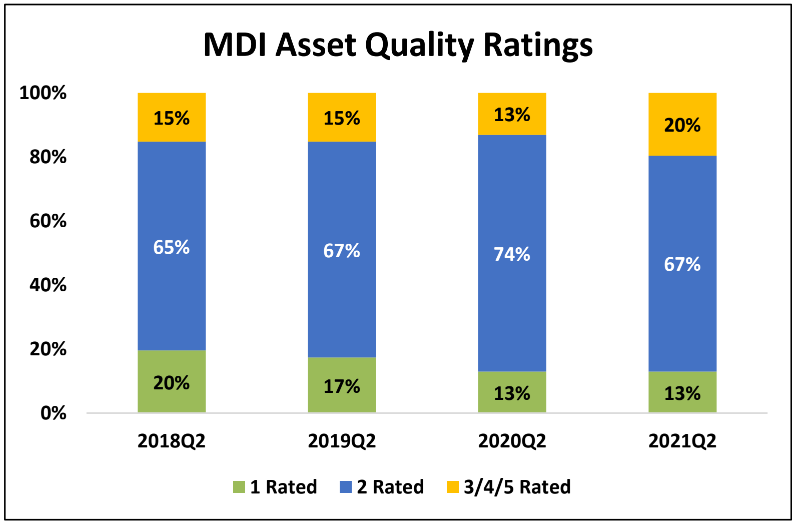


Efficiency Ratio - June 30, 2021

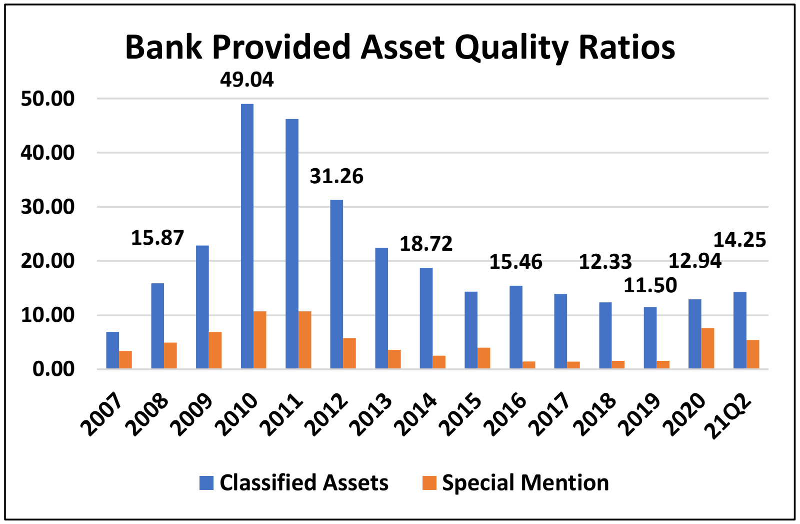
Asset Category	CBs<$3B	MDIs
Under $50MM	85.10	89.94
$50MM - $100MM	74.15	70.02
$100MM - $250MM	68.80	70.26
$250MM - $500MM	63.74	69.53
$500MM - $1B	63.75	53.22
Greater than $1B	61.64	50.43
Median	**65.79**	**63.85**

Asset Quality Ratings Worsened

- Asset quality ratings worsened in 2021 but remain satisfactory. Eighty percent of MDIs are rated 1 or 2 for asset quality.



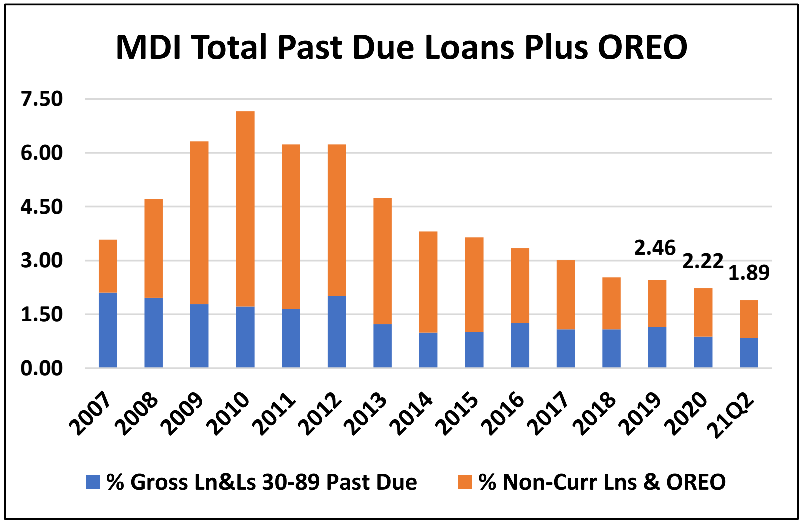
- MDI bank provided classified assets to tier 1 capital plus the ALLL ratios reached a cyclical low in 2019 and rose to 14.25 percent this year.

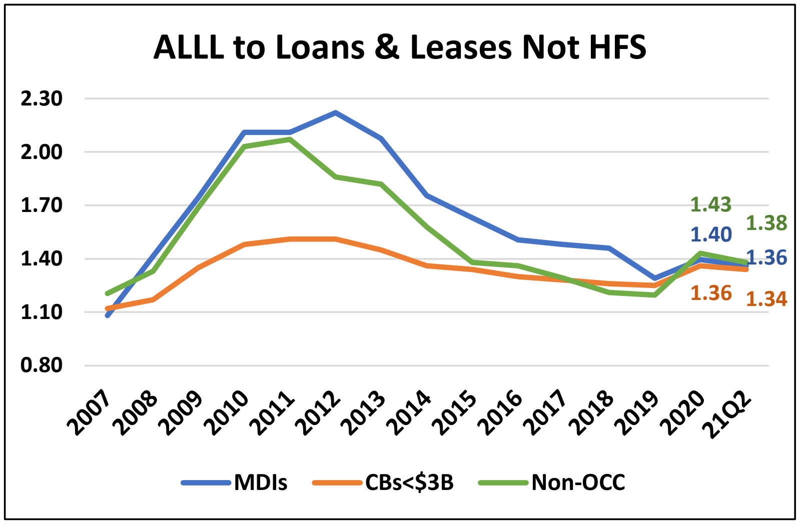


Noncurrent Loans Remain at Low Levels

- Past due loans plus OREO fell to a decade low of 1.89 percent. While past dues remain low, modification programs in the CARES Act are masking delinquencies for some credits. Fortunately, that pool of loans is declining.

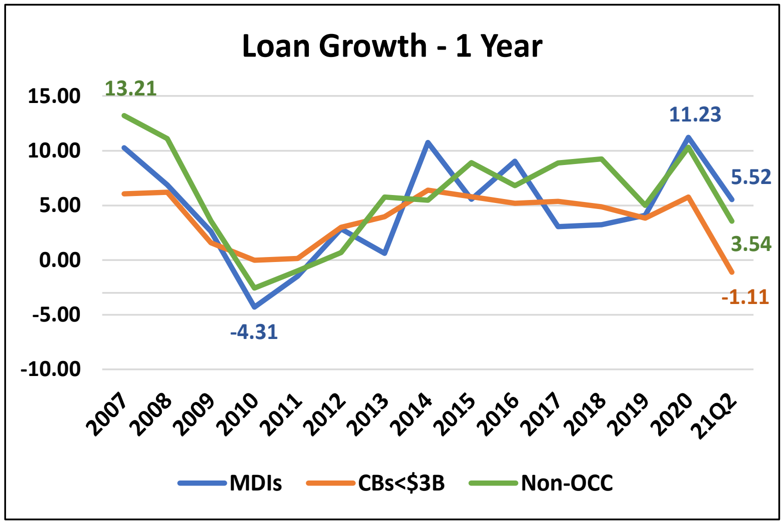
- Four MDIs or 9 percent have lower ALLL accounts in 2021. Only one MDI recorded a negative provision and three released reserves by losses exceeding the provision expense.





Loan Growth Weak

- After removing PPP loans, the adjusted MDI loan growth fell to 5.15 percent as of second quarter 2021.



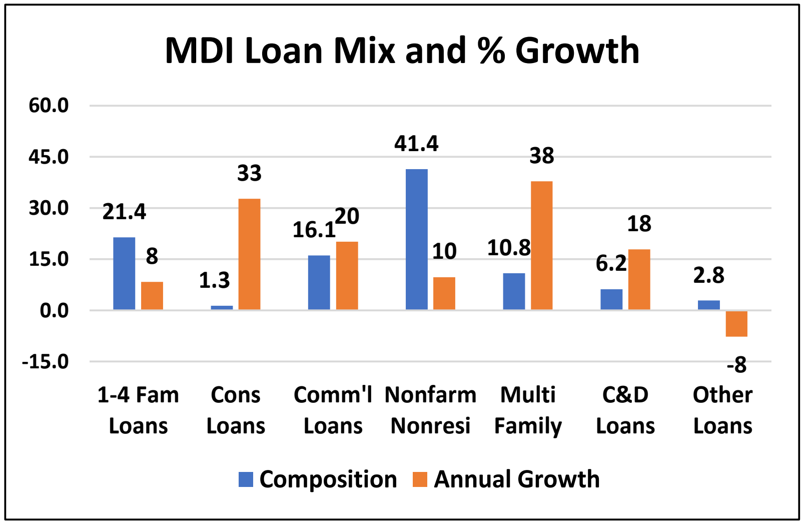
- Loan growth is normally highest for banks with total assets over $1 billion and lowest for banks with total assets under $50 million.

Loan Growth Ratio - June 30, 2021

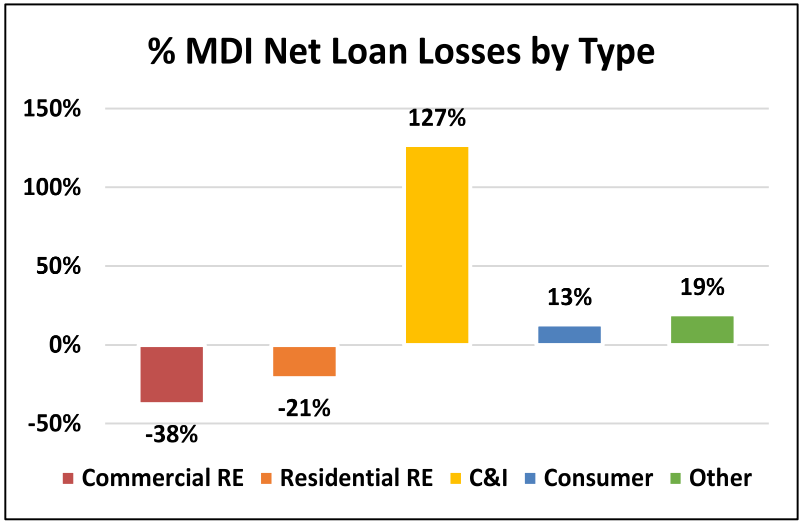
Asset Category	CBs<$3B	MDIs
Under $50MM	-6.64	-1.51
$50MM - $100MM	-1.48	3.12
$100MM - $250MM	-1.76	5.42
$250MM - $500MM	-1.17	-0.80
$500MM - $1B	0.09	7.53
Greater than $1B	0.01	18.36
Median	**-1.11**	**5.52**

MDI Loan Mix CRE-Heavy and Losses Low

- CRE at 58.4 percent is the largest MDI loan category. Loan growth for MDIs was highest for multifamily loans. Loan balances increased for all categories from last year except Other Loans.

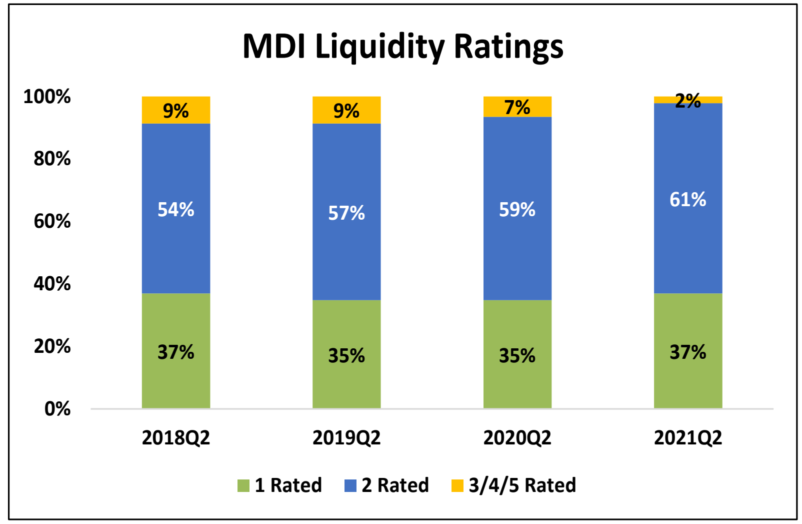


- MDI loan losses are at historically low levels or 0.03 percent in 2021. Most losses emanate from commercial loans. Consumer loans account for 1.3 percent of loans but 13 percent of net losses (auto-5 percent).

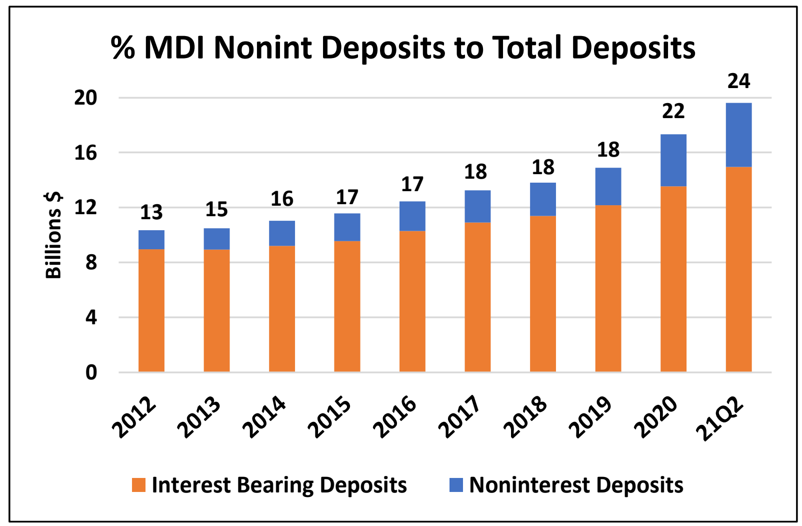


Liquidity is Strong; Deposits are Higher

- MDI liquidity ratings are strong and improving. Ninety-eight percent are rated 1 or 2.

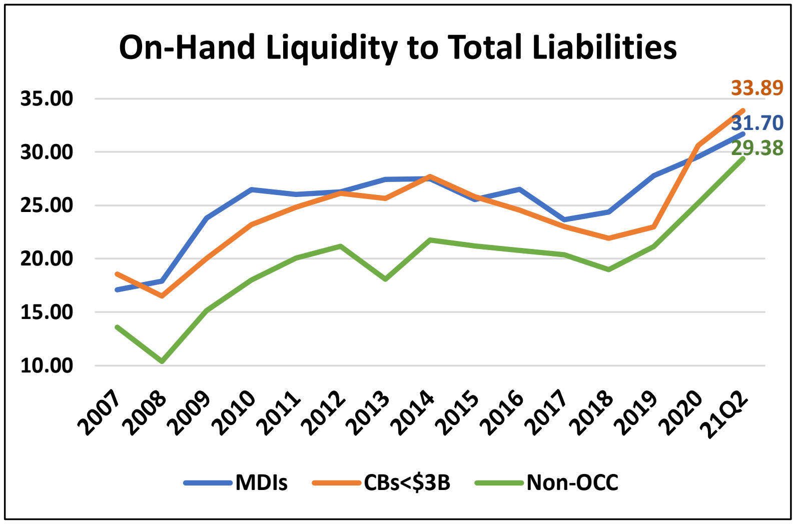


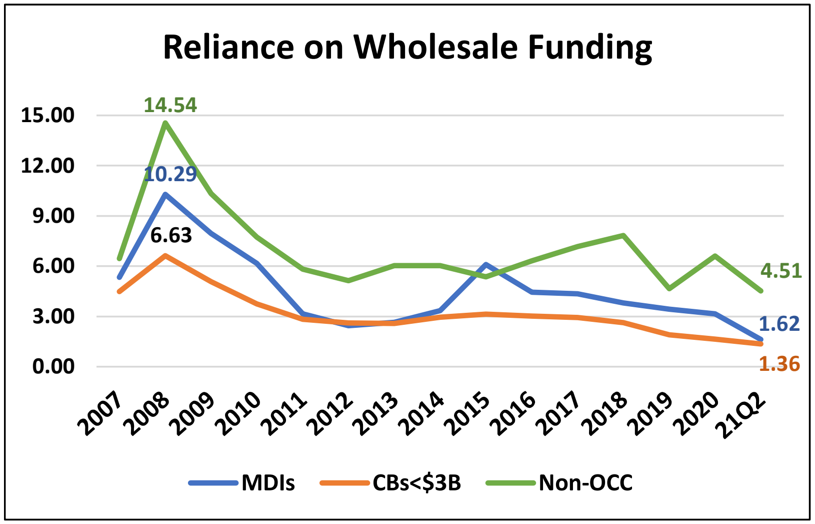
- Banks are flush with liquidity. MDI deposits grew 18.9 percent year-over-year due to pandemic-related deposits (stimulus checks, PPP funds) and a higher consumer saving rate.



On-Hand Liquidity Sharply Higher

- MDI on-hand liquidity ratios are sharply higher and above pre-crisis and pre-pandemic levels. Smaller banks have the highest levels of on-balance sheet liquidity. Because of the sharp rise in deposits, MDIs are relying less on wholesale funding sources.



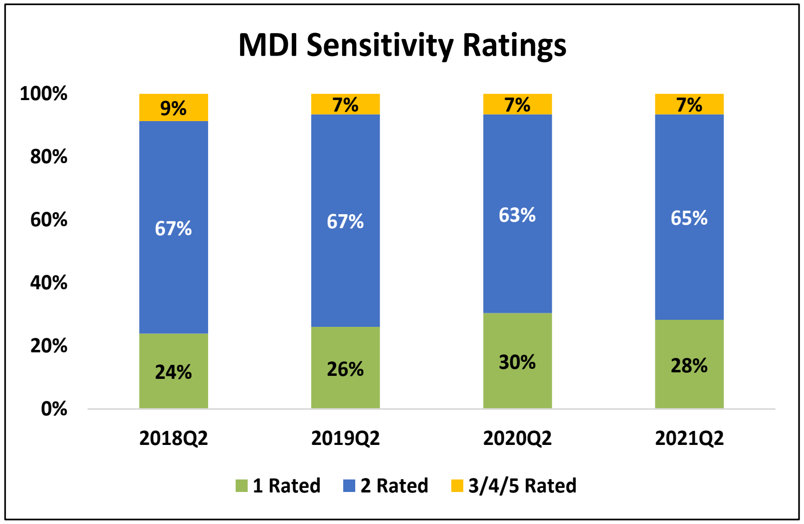


On-Hand Liquidity - June 30, 2021

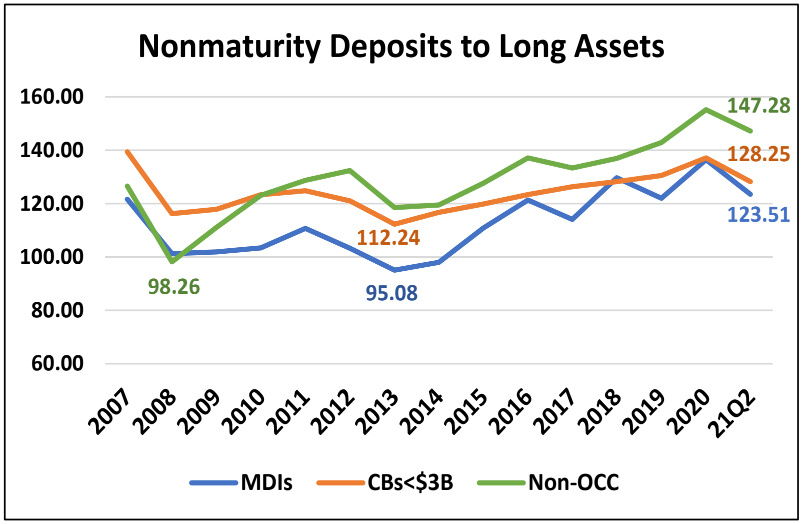
Asset Category	CBs<$3B	MDIs
Under $50MM	55.18	52.18
$50MM - $100MM	42.20	43.80
$100MM - $250MM	36.00	40.08
$250MM - $500MM	35.00	27.73
$500MM - $1B	32.12	20.31
Greater than $1B	26.83	19.80
Median	33.89	31.70

Sensitivity is Adequately Controlled

- MDI sensitivity to market risk ratings remain satisfactory. Ninety-three percent are rated 1 or 2.

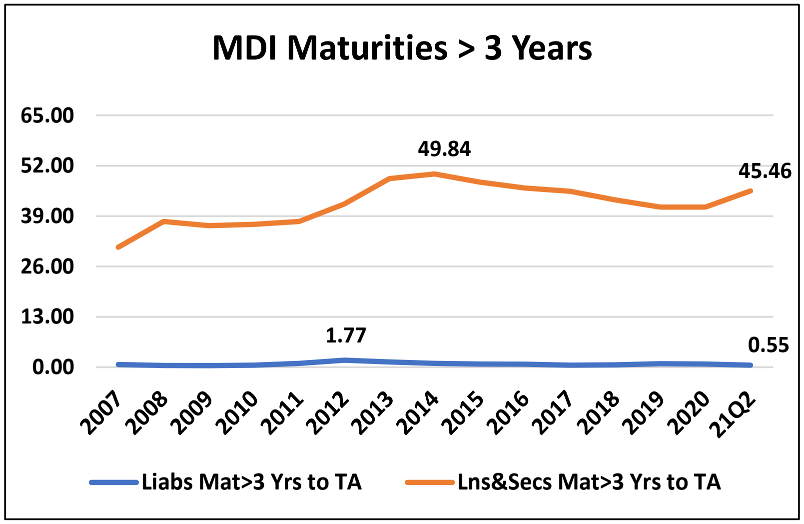


- Nonmaturity deposits to long-term assets have decreased for MDIs in 2021. However, they are up from their lows of 2013.

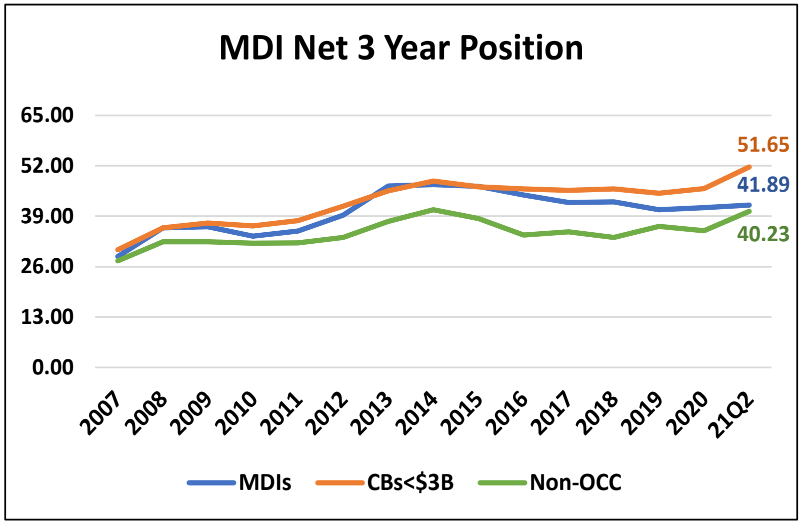


MDI Funding Gap Expanding

- After declining for six consecutive years, MDI loans and securities over three years increased to 45.46 percent. Only 0.55 percent of MDI liabilities mature or reprice in more than three years.

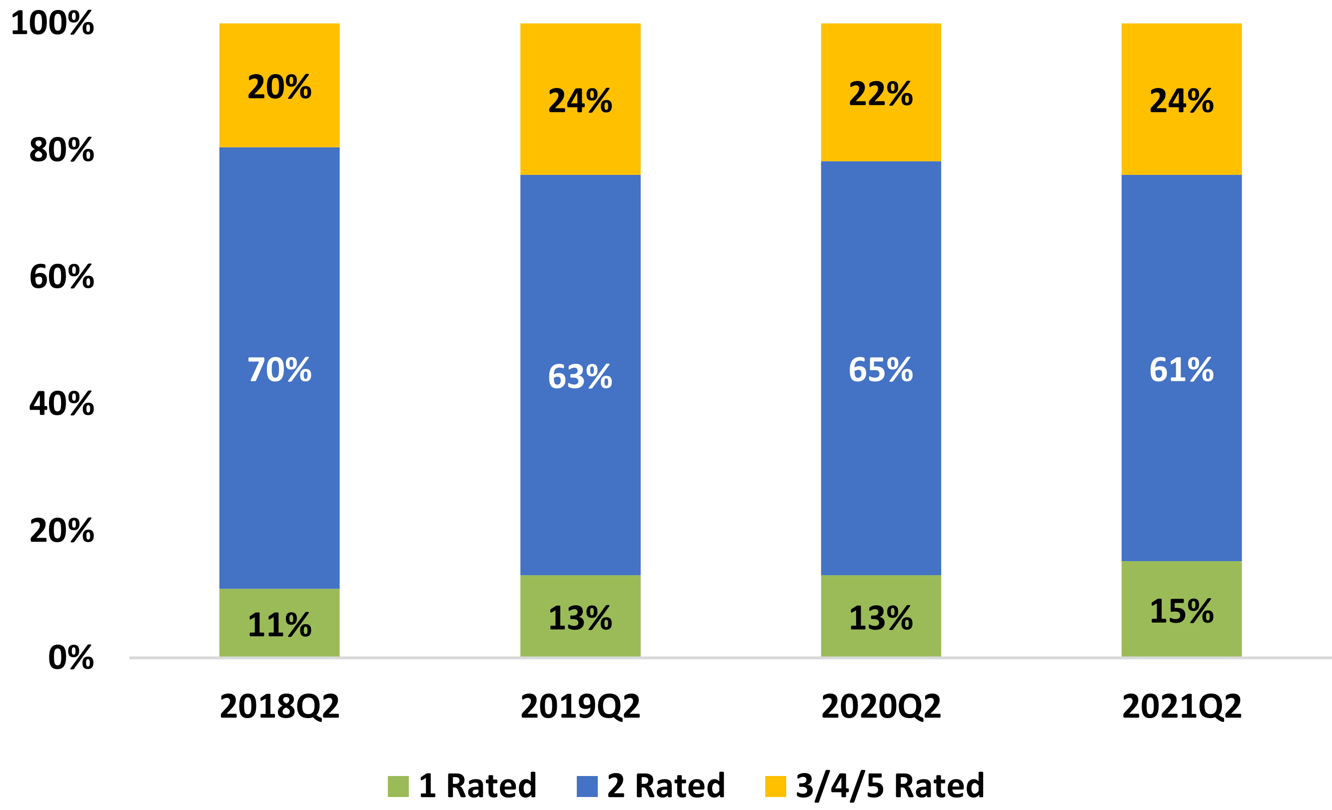


- The high level of longer-term assets compared with the low level of longer-term liabilities represents a significant funding gap. The funding gap is more pronounced for the community bank peer.



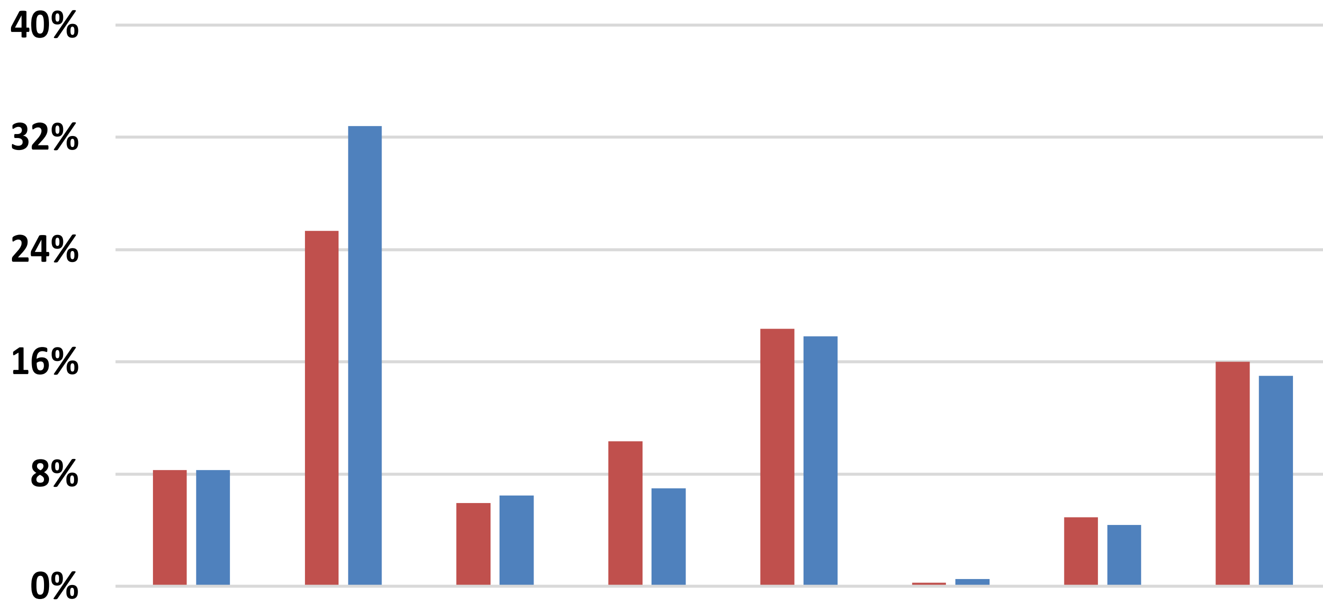
MDI Management Ratings are Stable

Management ratings are satisfactory. Seventy-six percent of MDIs are rated 1 or 2 for management.



High or Moderate/Increasing Risk Ratings

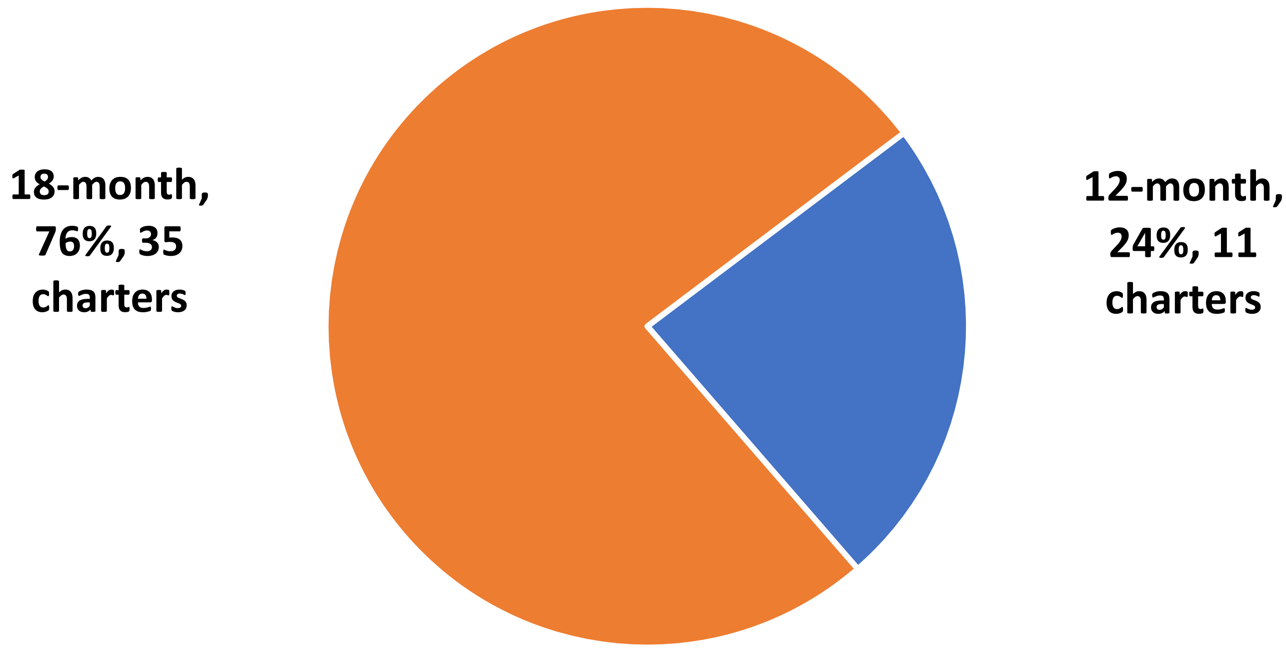
Below are the percentages of MDIs designated with either high or moderate and increasing risk. The top three risks are credit, operational, and strategic.



	COMP	CREDIT	IRR	LIQ	OPER	PRICE	REP	STRAT
2020Q2	8%	25%	6%	10%	18%	0%	5%	16%
2021Q2	8%	33%	6%	7%	18%	1%	4%	15%

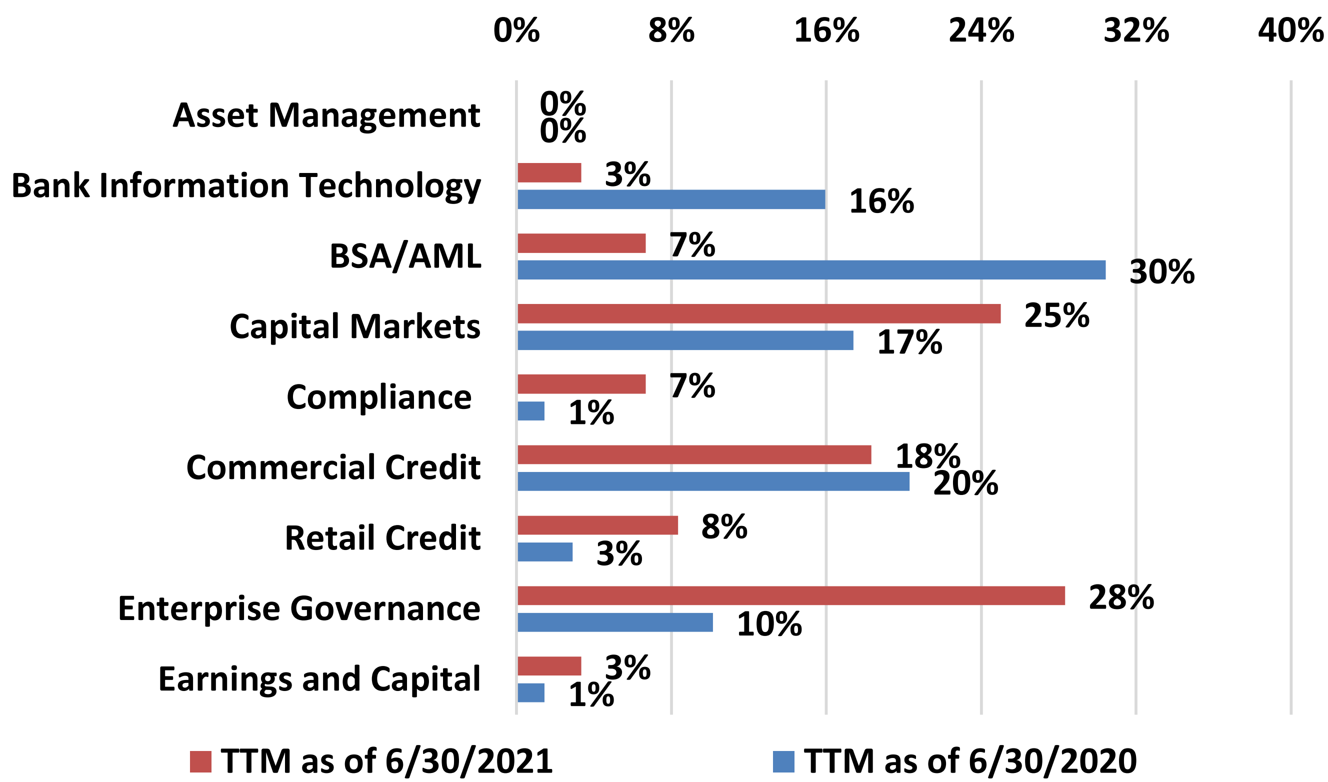
MDI Supervisory Cycles

Qualifying banks with less than $3 billion in total assets are eligible for an 18-month examination cycle. Seventy-six percent of MDIs are on the 18-month cycle.



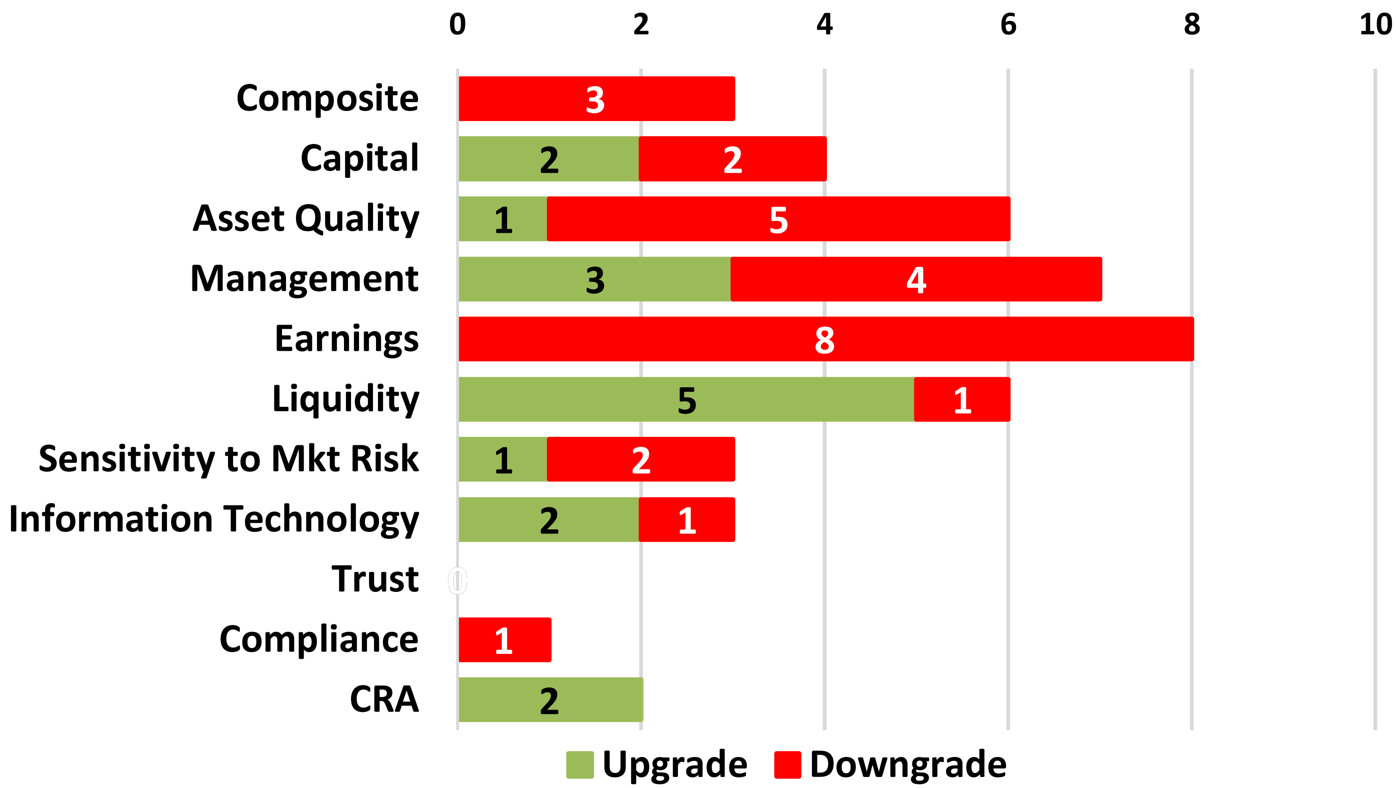
MDI MRAs by Examination Area

MRA volume is down by 9 percent in 2021. MRA concerns cited in the trailing twelve months ending June 30, 2021, were centered in Enterprise Governance, Capital Markets, and Commercial Credit. MRAs increased the most for Enterprise Governance and decreased the most for BSA/AML.



MDI Rating Changes

Over the last 4 quarters, rating downgrades exceeded upgrades. There were 16 upgrades and 27 downgrades, which translates to a net downgrade of 11. Most downgrades were for earnings and asset quality. Most upgrades were for liquidity and management.



Key Observations – June 30, 2021

- The number of MDIs continues to increase as a share of the community bank population.
- Composite ratings for MDIs remain satisfactory but are lower this year. Seventy-eight percent of MDIs are rated 1 or 2.
- **Capital remains strong**. After adjusting for the PPP loans, MDIs are better capitalized today versus pre-crisis.
- **Asset quality is satisfactory**. Total past due loans plus OREO fell to a decade low of 1.89 percent. Loan growth is weak. The ALLL is adequate and above pre-pandemic levels.
- **Earnings are adequate**. Despite NIM compression, MDI net income rose sharply this year due to higher net interest income, strong growth in fee income, and lower provision expenses. More MDIs are adversely rated for earnings than any other rating category.
- **Liquidity is strong**. MDIs are flush with liquidity due to pandemic related deposits and a higher consumer savings rate.
- **Sensitivity to market risk remains adequately controlled**. MDIs are holding higher levels of nonmaturity deposits relative to long-term assets making them less vulnerable to increases in interest rates.

Questions