Office of the
Comptroller of the Currency

RMA New England Chapter

February 28, 2023

State of the Banking Industry

Financial Information as of December 31, 2022

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State of the Industry

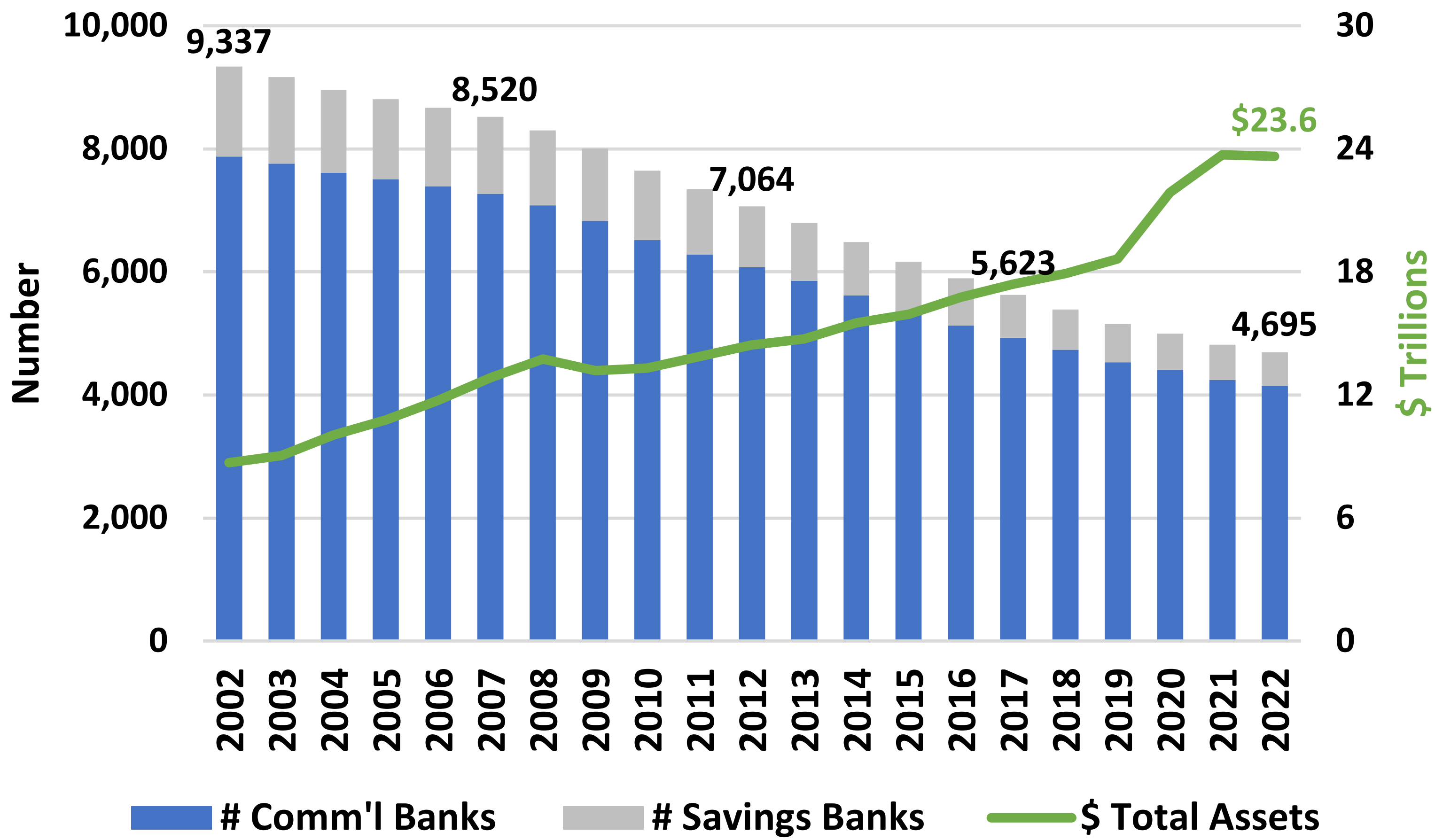
Banking during Tight Monetary Policy

- Portfolio Demographics
- Financial Performance
- Supervisory Information
- Outlook and Challenges

Preface: This presentation analyzes federally insured banks active as of December 31, 2022. For many of the performance metrics, this population is "held constant." Most charts use the median and others use weighted averages.

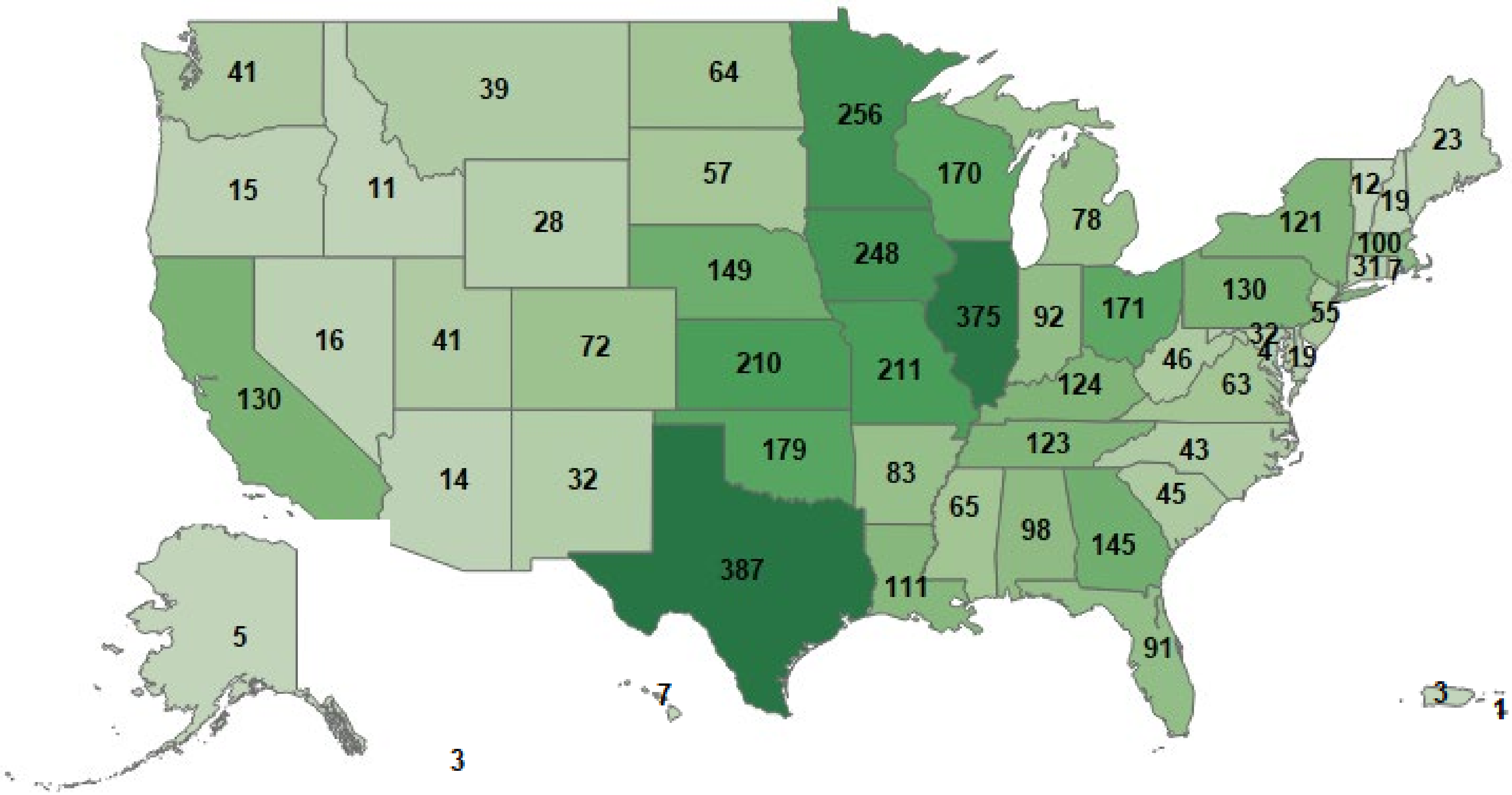
Trends in Bank Charters

The banking industry continues to consolidate. The total number of charters declined by 49.7 percent since 2002 and 2.6 percent in 2022. Total assets fell 1.4 percent in 2022 after two years of strong growth during the pandemic.



Banks by State and Territory

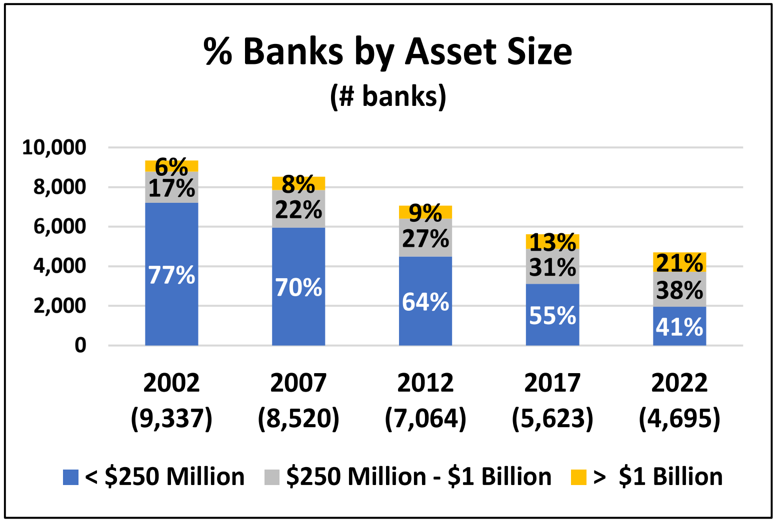
Insured banks are concentrated in the Midwest and Texas. There are six states - Texas, Illinois, Minnesota, Iowa, Missouri, and Kansas - with 200 or more charters. These states are home to 36 percent of all insured banks.

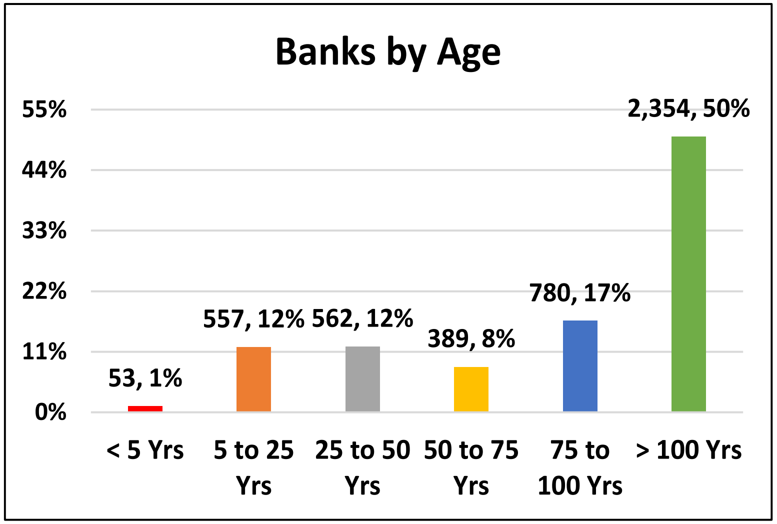


Banks by Asset Size and Age

- Growth in assets, fewer de novo charters, and mergers have resulted in a shift in mix toward larger institutions. In 2022, 41 percent of banks were less than $250 million in size versus 77 percent in 2002.

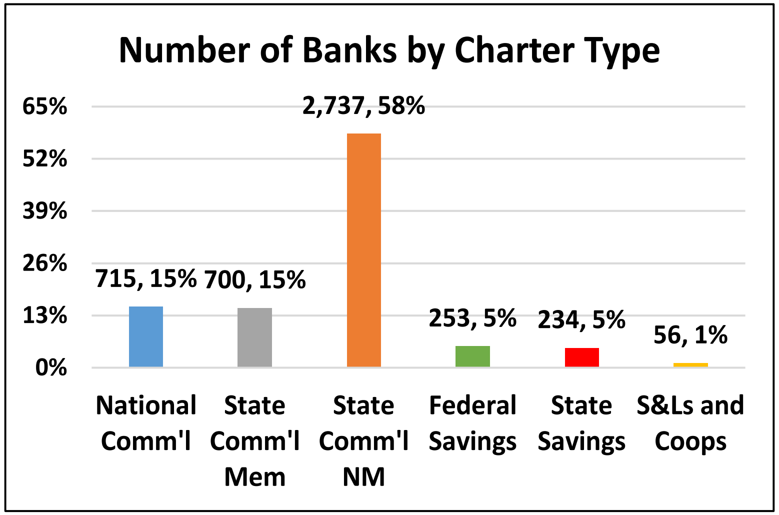
- Most insured banks or 50 percent have operated for over 100 years. Only 1 percent have been operating for less than 5 years.



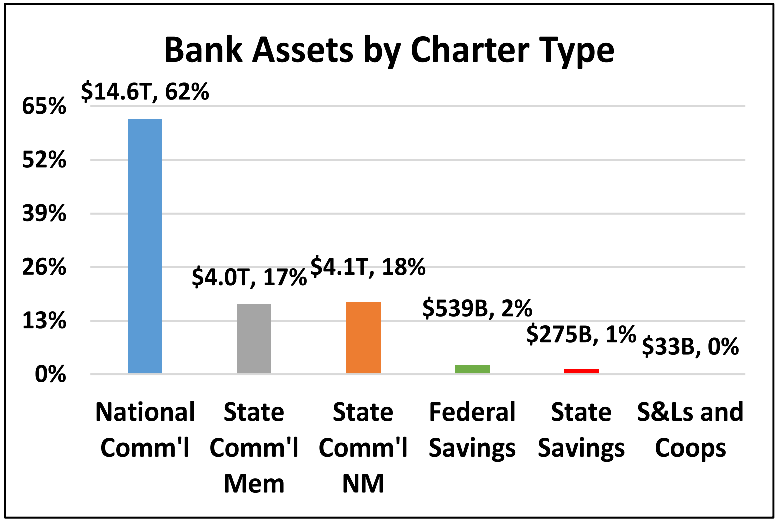


Banks by Charter Type

- There were 4,695 active insured banks as of December 31, 2022. Most charters or 58 percent are state commercial nonmembers of the Federal Reserve System.

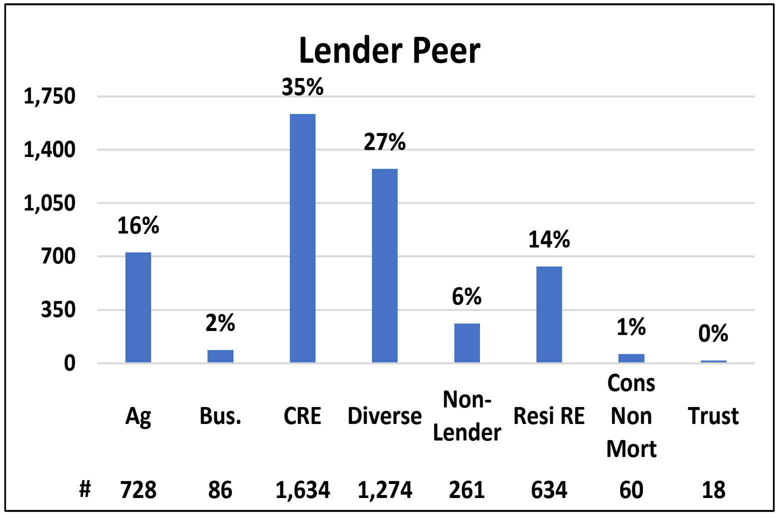


- Bank assets totaled $23.6 trillion as of December 31, 2022. Most assets or 62 percent are held by national commercial banks.

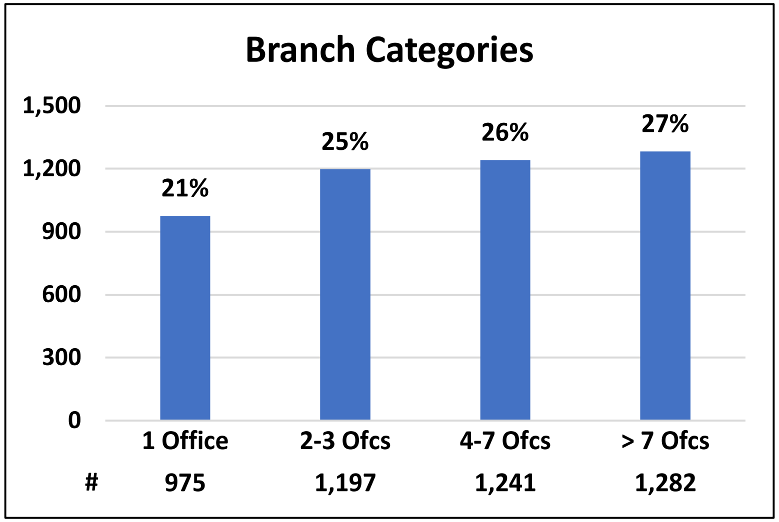


Banks by Lender Peer and Branch Network

- Thirty-five percent of banks are CRE lenders (up from 31 percent last year) and 27 percent are Diversified lenders (down from 29 percent last year).

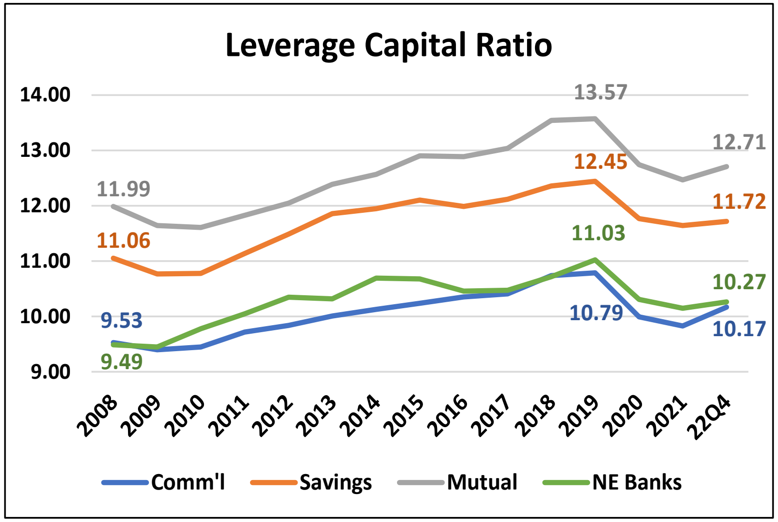


- Twenty-one percent of insured banks operate from one location, and 46 percent have three locations or less.



Capital Levels Remain Solid

- Banks are better capitalized today compared to 2008. Leverage ratios increased for all groups since 2021 and remain within 100 basis points from their cyclical peak in 2020.



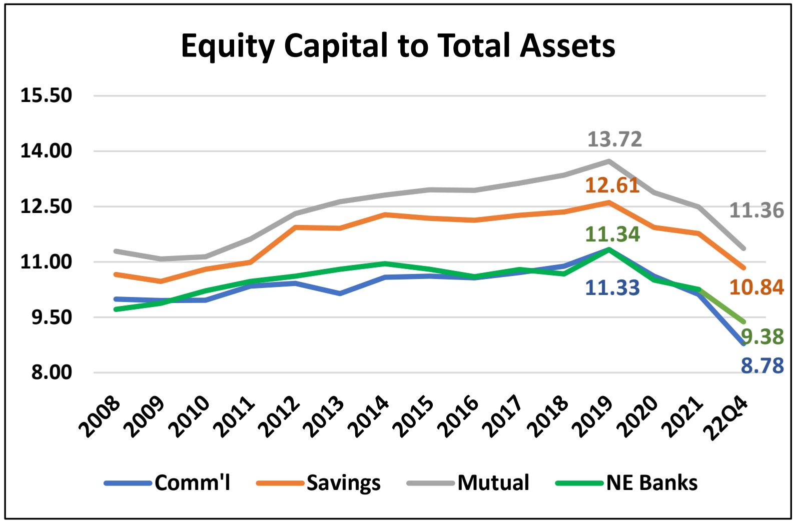
- In general, smaller banks hold higher levels of capital.

Leverage Ratio - December 31, 2022

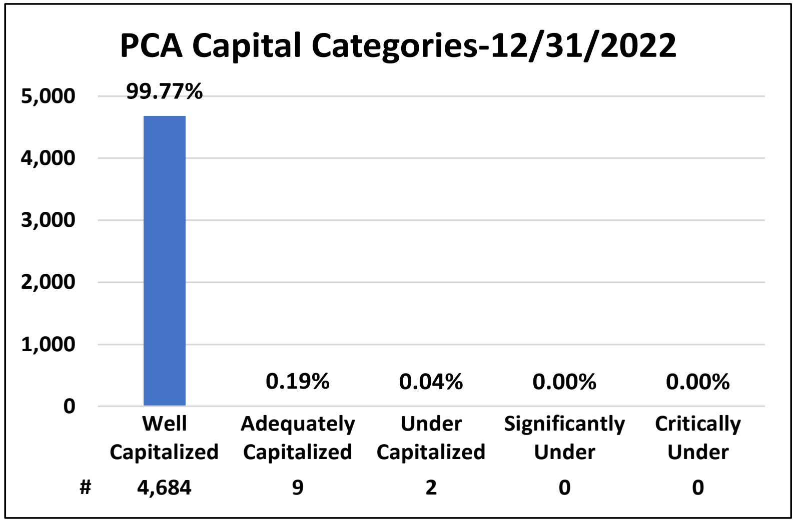
Asset Category	Savings	Comm'l
Under $50MM	19.17	11.77
$50MM - $100MM	13.79	11.05
$100MM - $250MM	12.11	10.54
$250MM - $500MM	12.04	10.11
$500MM - $1B	11.30	9.83
Greater than $1B	10.41	9.72
Median	**11.72**	**10.17**

Banks are "Well Capitalized"

- Equity capital to total asset ratios declined in 2020 and 2021 due to pandemic-related asset growth and fell more sharply in 2022 due to AOCI-related adjustments.

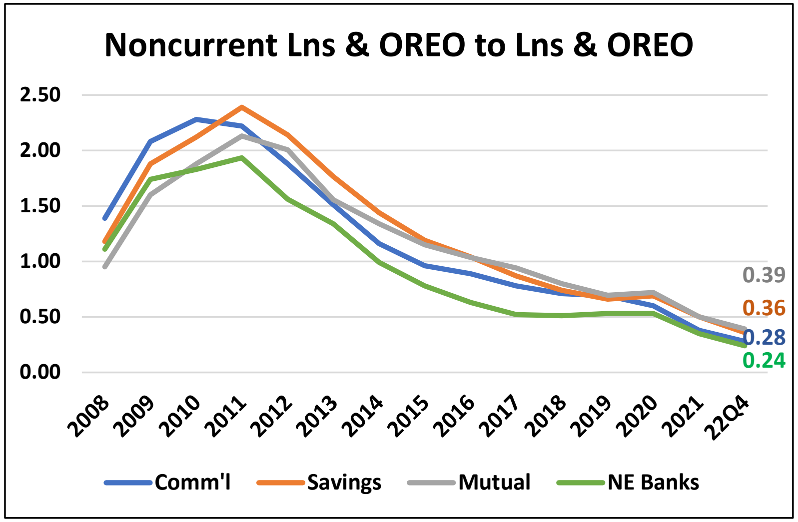


- Based on capital ratios, 99.8 percent of banks are "well capitalized" per Prompt Corrective Action as of December 31, 2022. Thirty-five percent of banks opted into the CBLR framework.

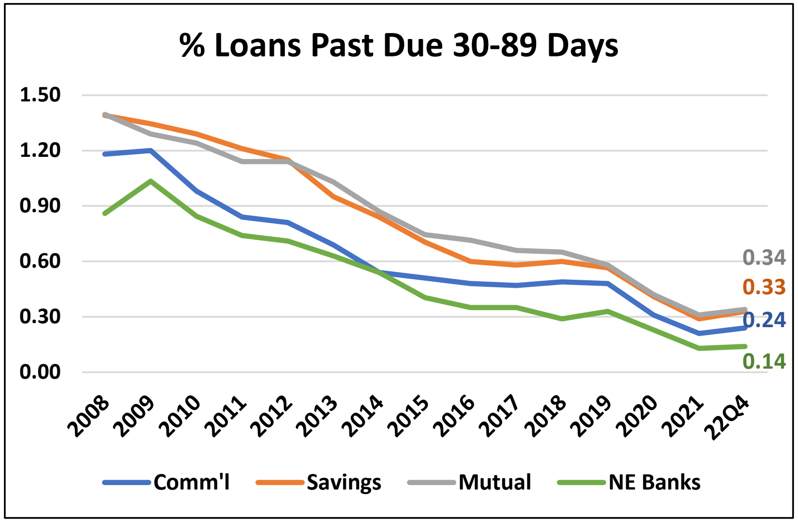


Delinquent Loans Low but Edge Higher

- Noncurrent loans continued to decline through the pandemic and reached new cyclical lows this year.

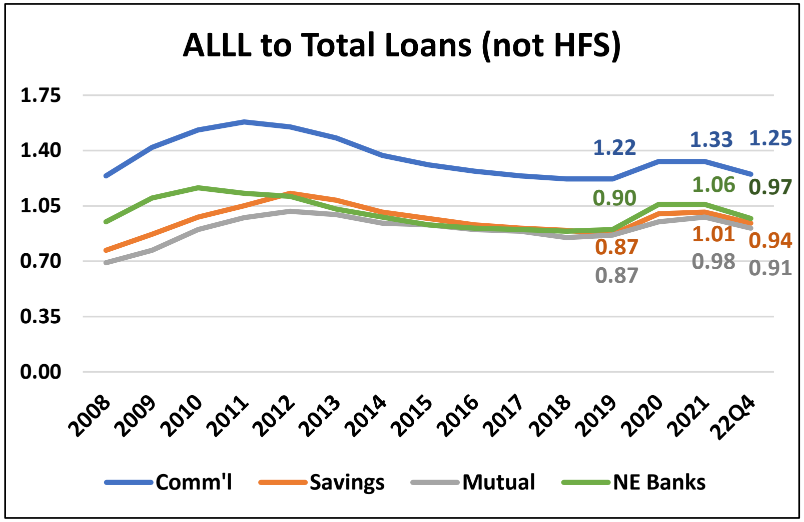


- Loans past due 30 to 89 days are also low but have up-ticked in 2022. NE banks have the lowest past dues at 0.14 percent.

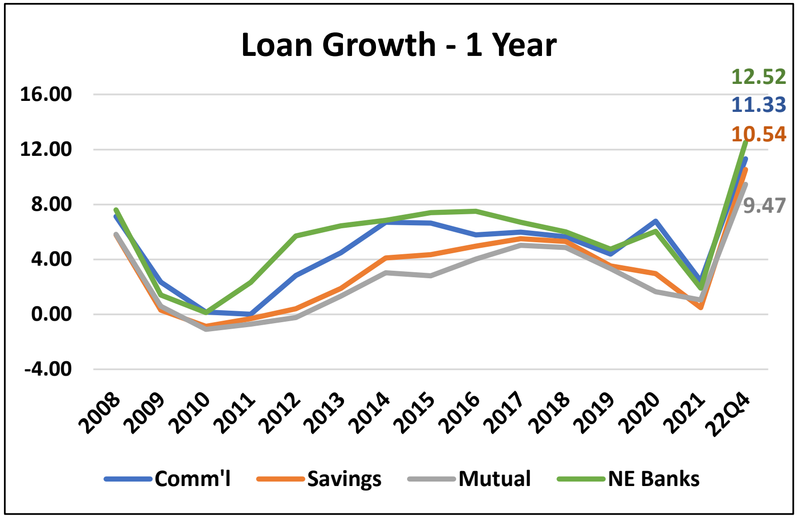


ALLL Lower and Loan Growth Jumps

- While 8 percent of banks recorded negative provisions and another 18 percent released reserves by losses exceeding provision expense, the ALLL to total loans ratio remained higher than the pre-pandemic levels.

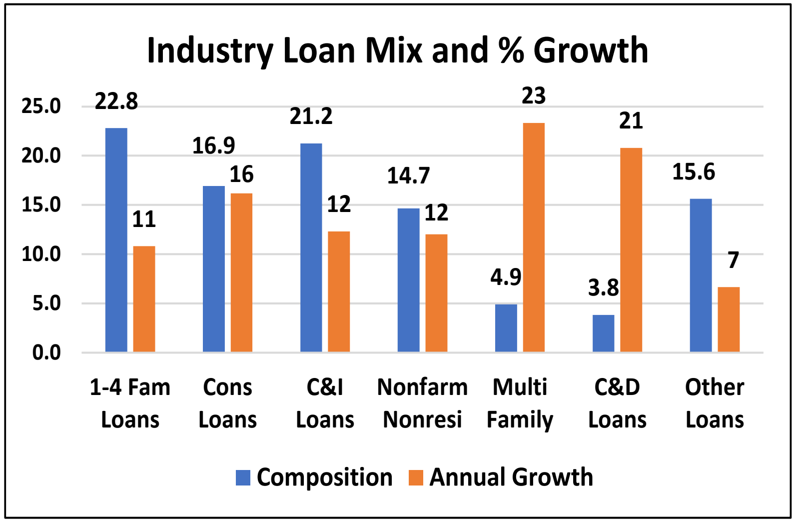


- Loan growth is more difficult to interpret due to the Paycheck Protection Program (PPP). After adjusting for the PPP, median loan growth picked up in fourth quarter and was 12.63 percent for commercial banks and 10.91 percent for savings banks.

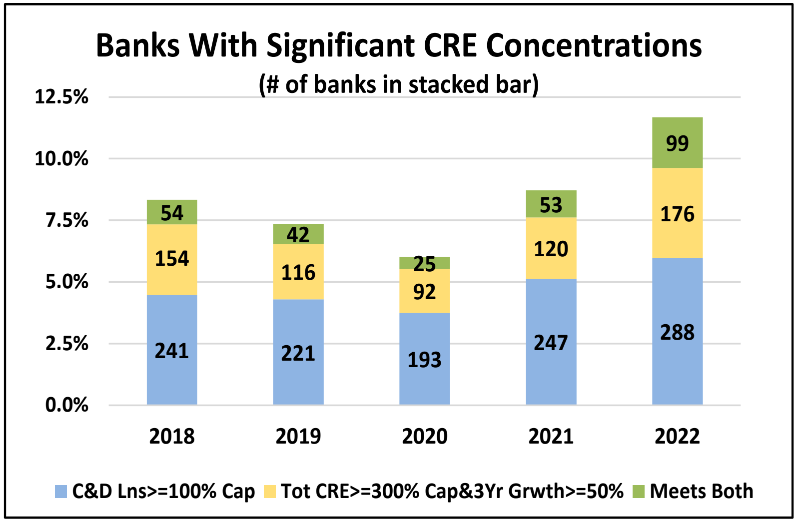


CRE Concentrations Increased

- Loan growth in absolute volume was centered in consumer loans ($289 billion or 16 percent) and commercial and industrial loans ($285 billion or 12 percent).

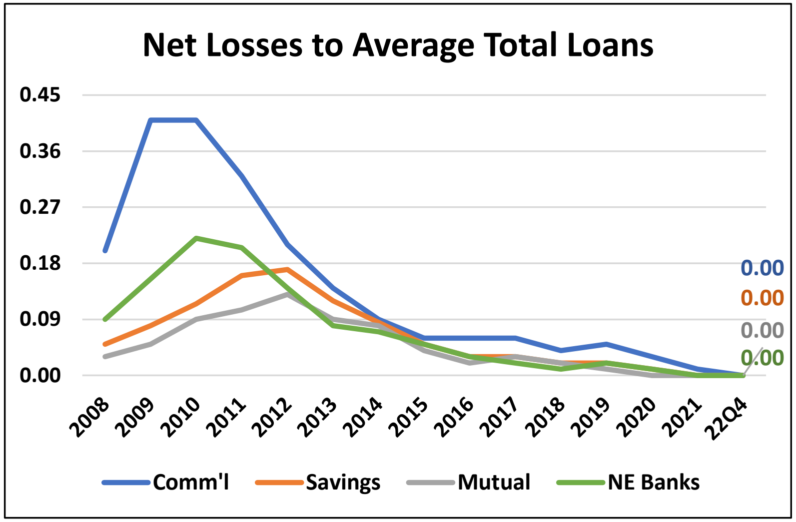


- About 12 percent of banks exceed the supervisory thresholds in the Interagency CRE Guidance (Dec 2006). Banks have a **significant** CRE concentration if C&D loans > 100 percent of capital or Total CRE > 300 percent of capital **and** CRE loans grew more than 50 percent in the prior three years.

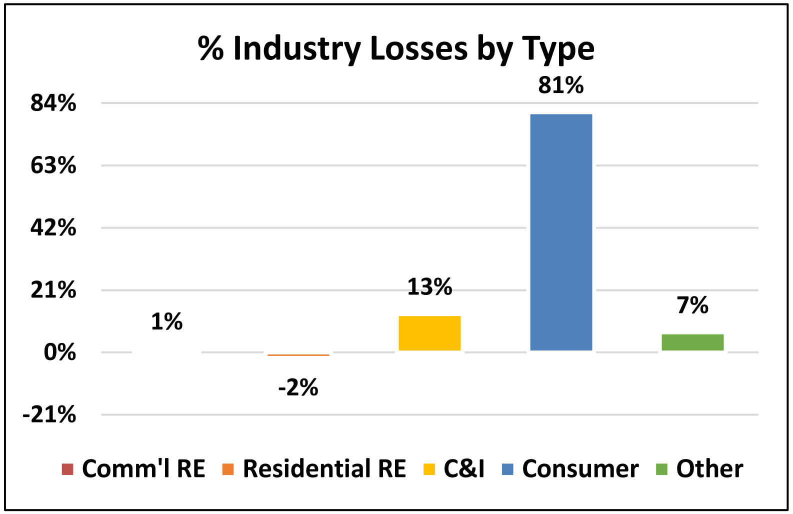


Loan Losses Low

- Loan losses remain low and increased slightly to 0.26 percent of total loans on a weighted average basis in 2022.

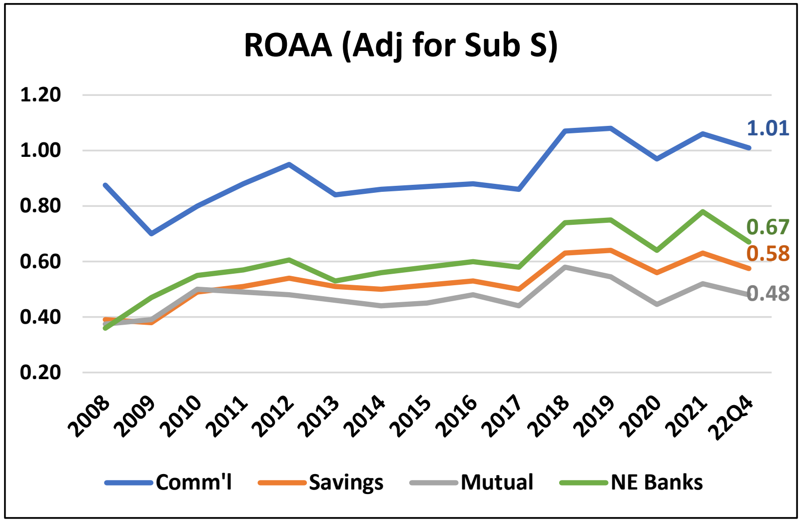


- Consumer loans account for 16.9 percent of loans and 81 percent of losses. On the other hand, 1-4 family real estate loans account for 22.8 percent of loans and show a net recovery.

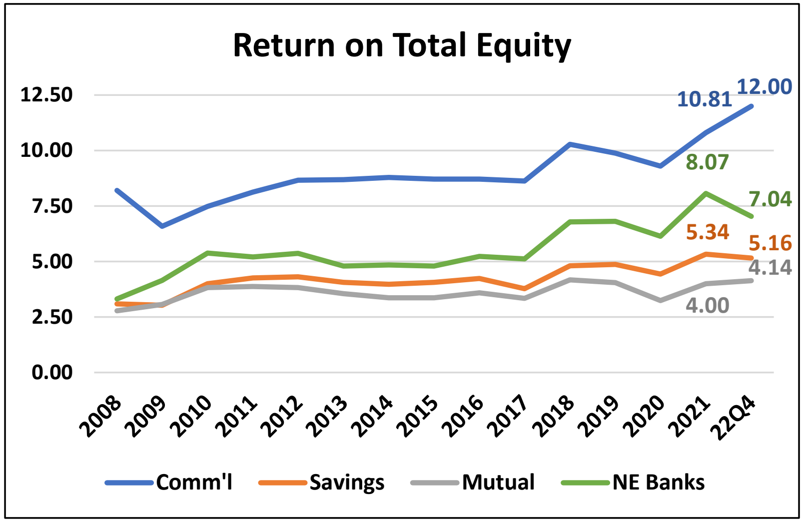


ROAA and ROE Lower in 2022

- ROAA declined five basis points for commercial and savings banks in 2022.



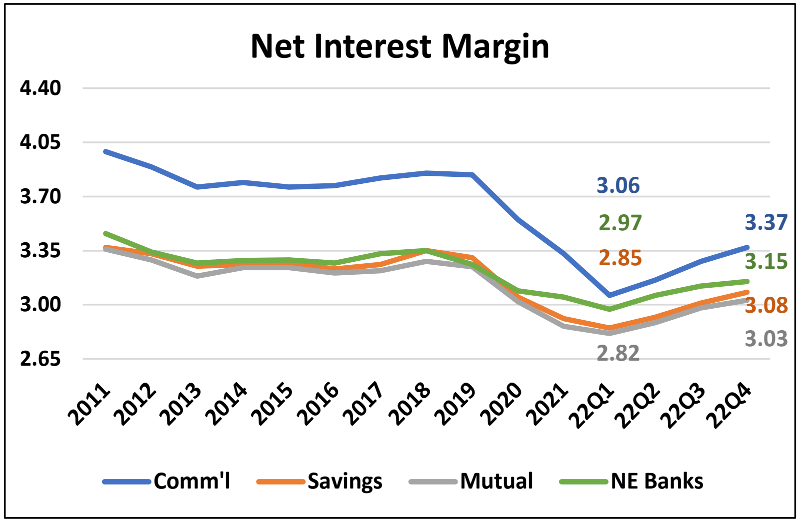
- Return on equity was up this year for commercial banks and mutual banks due to a high negative level of other comprehensive income that reduced total equity capital by 3.6 percent in 2022.



Net Interest Margin Rebounded

- Net interest margins plummeted to a new record low in first quarter 2022. Since then, margins have rebounded 31 basis points for commercial banks and 23 basis points for savings banks.

- 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 - December 31, 2022

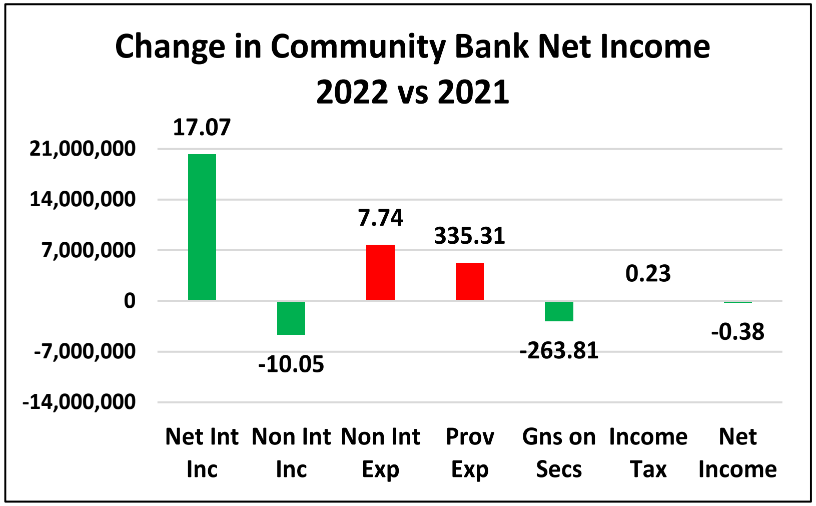
Asset Category	Savings	Comm'l
Under $50MM	2.92	3.13
$50MM - $100MM	3.00	3.32
$100MM - $250MM	3.08	3.35
$250MM - $500MM	3.10	3.41
$500MM - $1B	3.10	3.43
Greater than $1B	3.09	3.35
Median	**3.08**	**3.37**

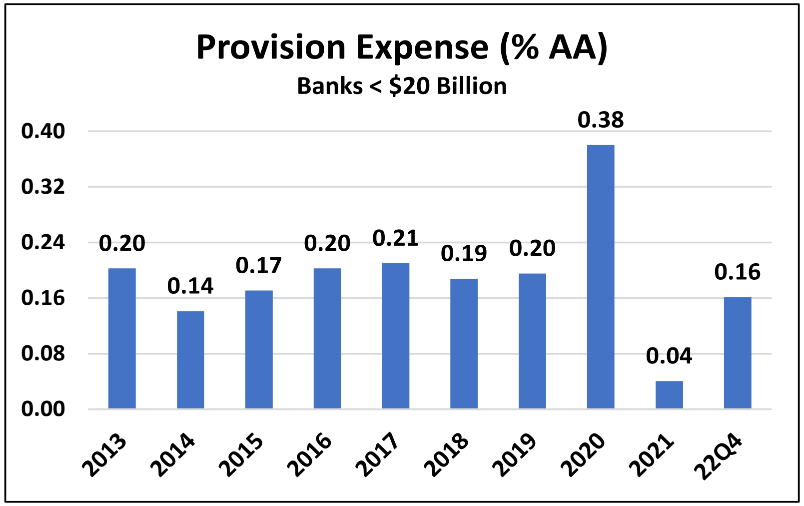
Net Income Edged Lower in 2022

ROAA fell due to a contraction in fee income and higher provision expenses.

Banks < $20 Billion (000's) Income Statement	2022	2021	Δ 1 Yr %
Tot Int Inc	156,947,515	129,038,726	21.63
Tot Int Exp	18,259,443	10,574,469	72.67
Net Int Inc	138,688,072	118,464,257	17.07
Non Int Inc	41,845,226	46,518,241	-10.05
Non Int Exp	107,553,711	99,827,416	7.74
Prov Exp	6,803,549	1,562,909	335.31
Gns on Secs	-1,727,968	1,054,856	-263.81
Income Tax	13,359,611	13,329,128	0.23
Net Income	51,088,459	51,317,901	-0.38

ROAA Decomposition - as of Dec 31st	2022	2021	Δ 1 Yr
Tot Int Inc	3.72	3.35	
Tot Int Exp	0.43	0.27	
Net Int Inc	3.29	3.08	0.21
Non Int Inc	0.99	1.21	-0.22
Non Int Exp	2.55	2.59	0.04
Prov Exp	0.16	0.04	0.12
Gns on Secs	-0.04	0.03	-0.07
Income Tax	0.32	0.35	-0.03
ROAA	1.21	1.33	-0.12

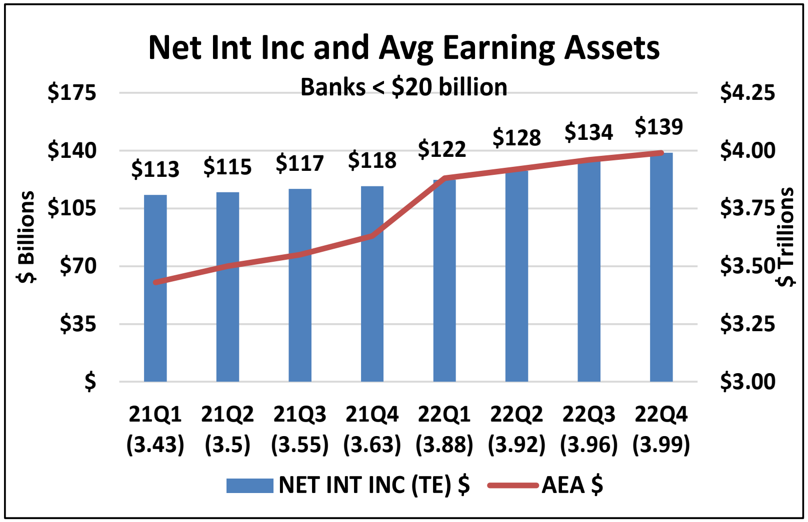


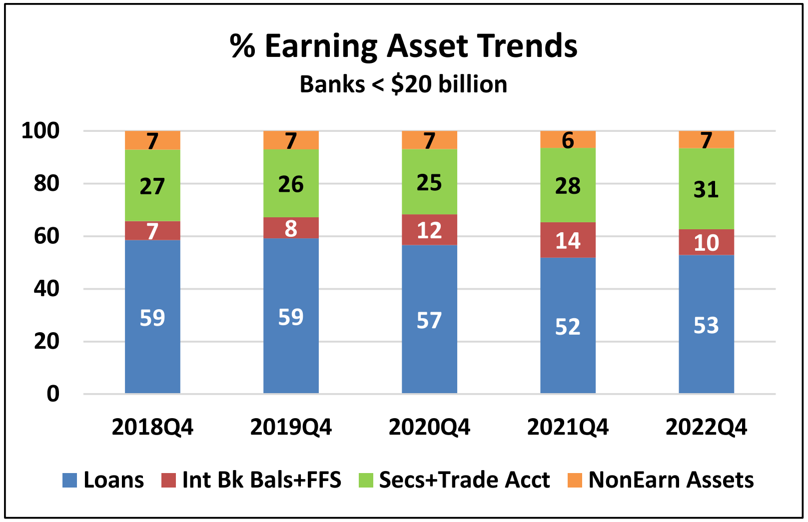


Net Interest Margin Detail

- The weighted average net interest margin expanded 21 basis points this year to 3.47 percent due to net interest income growth of $20.2 billion or 17.1 percent outpacing average earning asset growth of $368 billion or 10.2 percent.

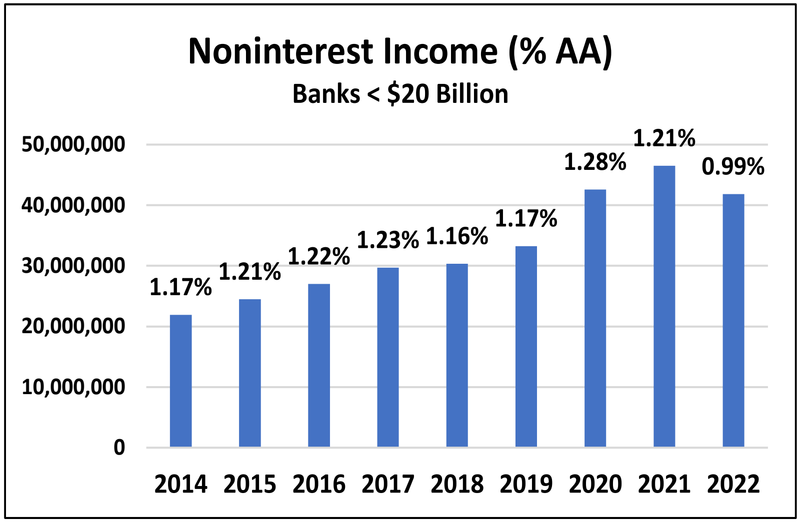
- The shift in the earning asset mix from interest-bearing bank balances to loans and securities also boosted the net interest margin.



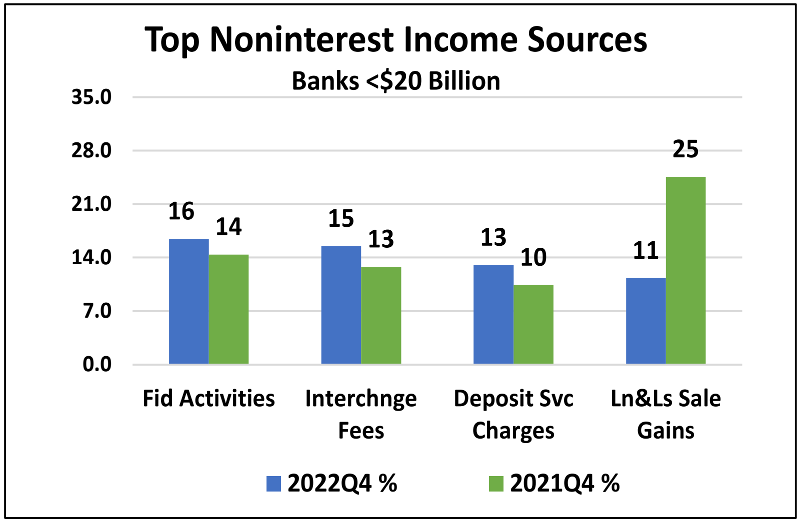


Noninterest Income Declined

- Fee income contracted by 10.0 percent in 2022 due to a 59 percent decline in gains on loan sales. About 23 percent or 1,079 charters reported 0.25 percent or less in fee income.

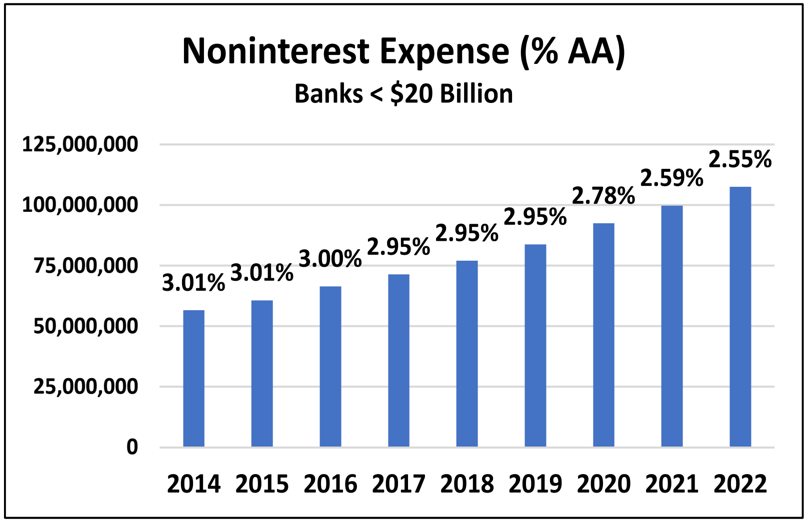


- For banks with assets of $20 billion or less, fiduciary activity income was the top noninterest income category and gains on loan sales fell to fourth place.

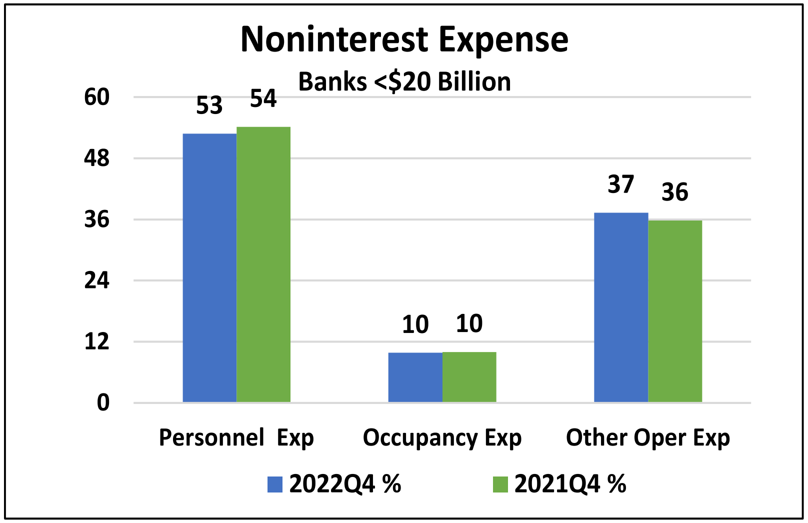


Noninterest Expense Increased

- Noninterest expense increased by 7.7 percent in 2022 and most of the increase was from other operating expenses.



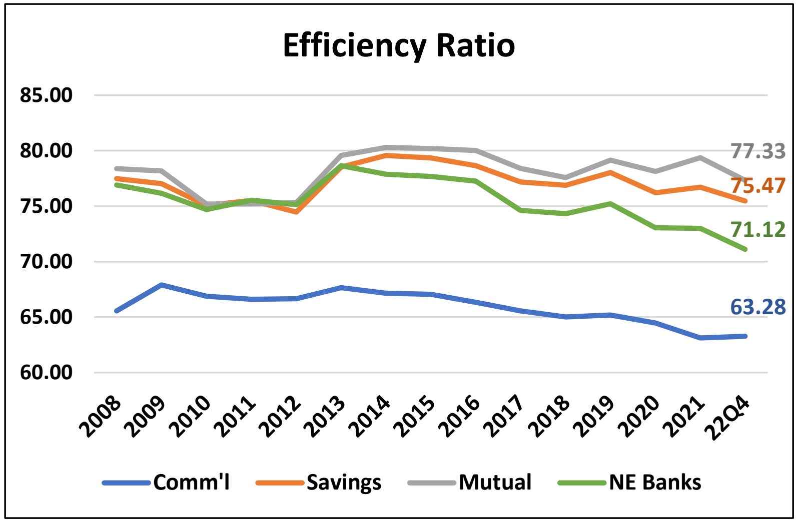
- For banks with assets of $20 billion or less, personnel expense at 53 percent is the top noninterest expense category. It increased 5.1 percent since last year. Higher data processing, marketing, and consulting fees pushed other operating expenses higher in 2022.



Efficiency Ratio Mixed

- The efficiency ratio has reduced in 2022 for savings, mutuals, and NE banks. About 3.1 percent or 146 banks reported efficiency ratios over 100 percent.

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



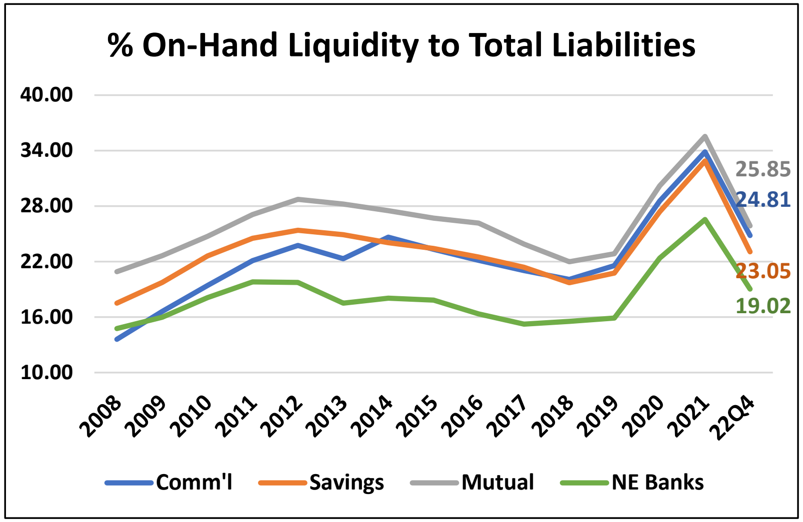
Efficiency Ratio - December 31, 2022

Asset Category	Savings	Comm'l
Under $50MM	92.68	78.34
$50MM - $100MM	81.89	69.63
$100MM - $250MM	81.06	65.79
$250MM - $500MM	76.01	62.64
$500MM - $1B	71.47	61.02
Greater than $1B	67.10	57.84
Median	**75.47**	**63.28**

On-Hand Liquidity Plummets in 2022

- After rising sharply in 2020 and 2021 due to pandemic-related deposits, on-hand liquidity levels fell in 2022 but remain above pre-pandemic levels.

- If you stratify the on-hand liquidity ratio by asset size, you will generally find the larger the bank, the lower the on-hand liquidity ratio.

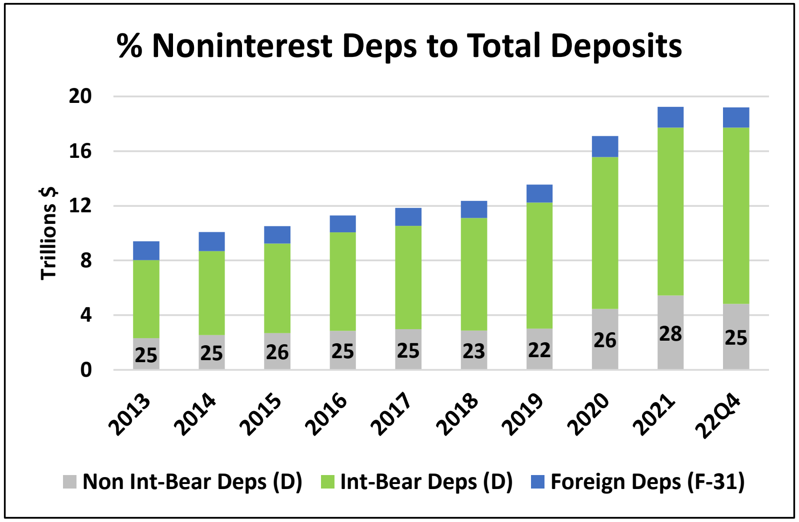


On-Hand Liquidity - December 31, 2022

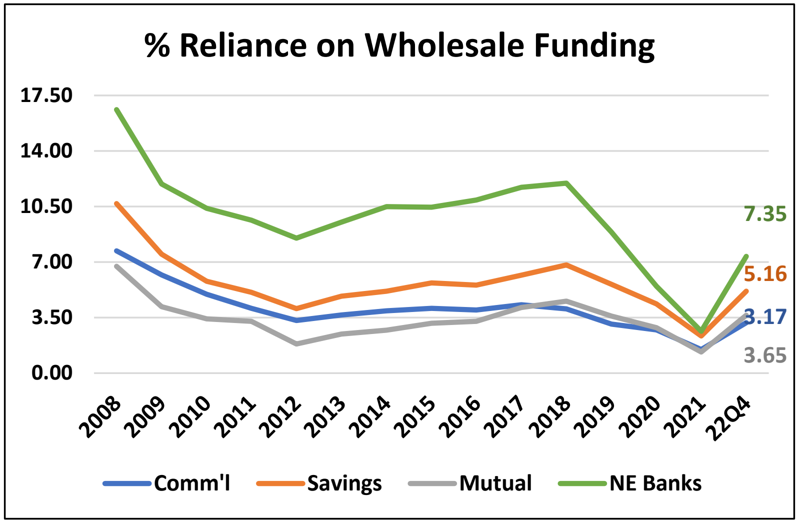
Asset Category	Savings	Comm'l
Under $50MM	36.66	45.66
$50MM - $100MM	34.82	34.53
$100MM - $250MM	26.80	28.53
$250MM - $500MM	26.41	23.58
$500MM - $1B	18.51	21.34
Greater than $1B	18.16	18.03
Median	**23.05**	**24.81**

Reliance on Wholesale Funding Higher

- Deposits remain above $19.2 trillion but shank -0.10 percent since last year. The share of noninterest-bearing deposits fell to 25 percent of total deposits.

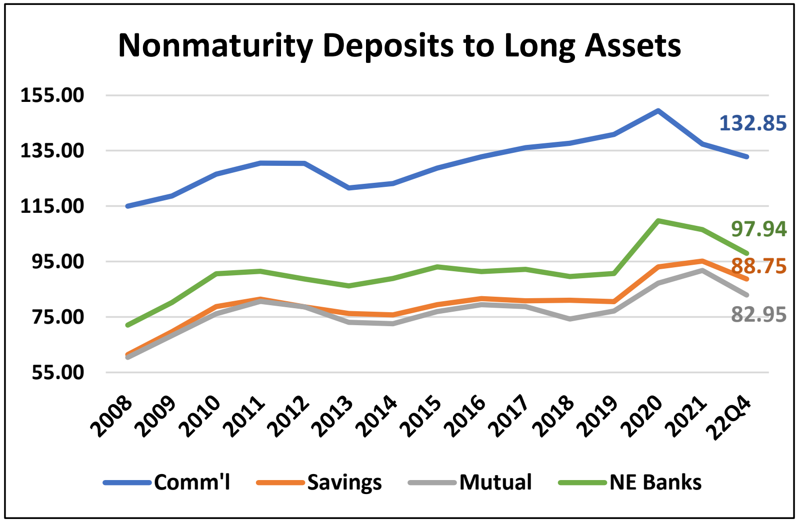


- Because of the decline in deposits, banks are relying more on wholesale funding sources this year.

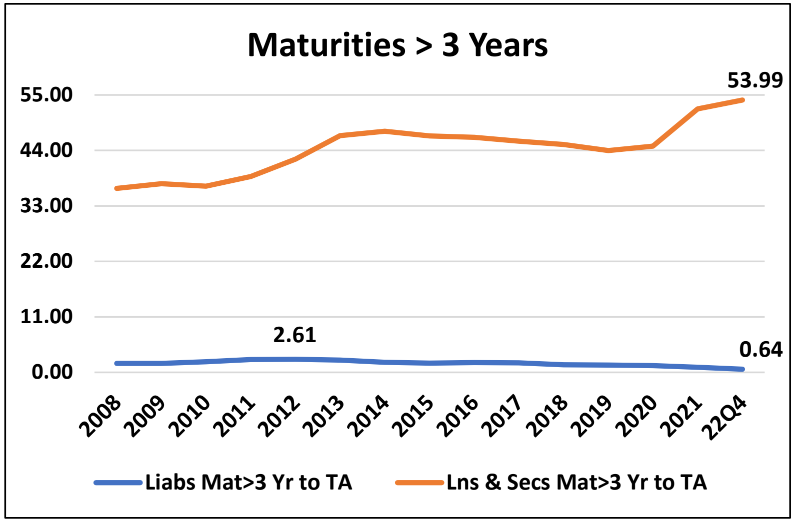


Nonmaturity Deposits Remain Good

- While nonmaturity ratios decreased this year for all groups, most levels are higher than pre-pandemic and all are well above their lows from 2008.

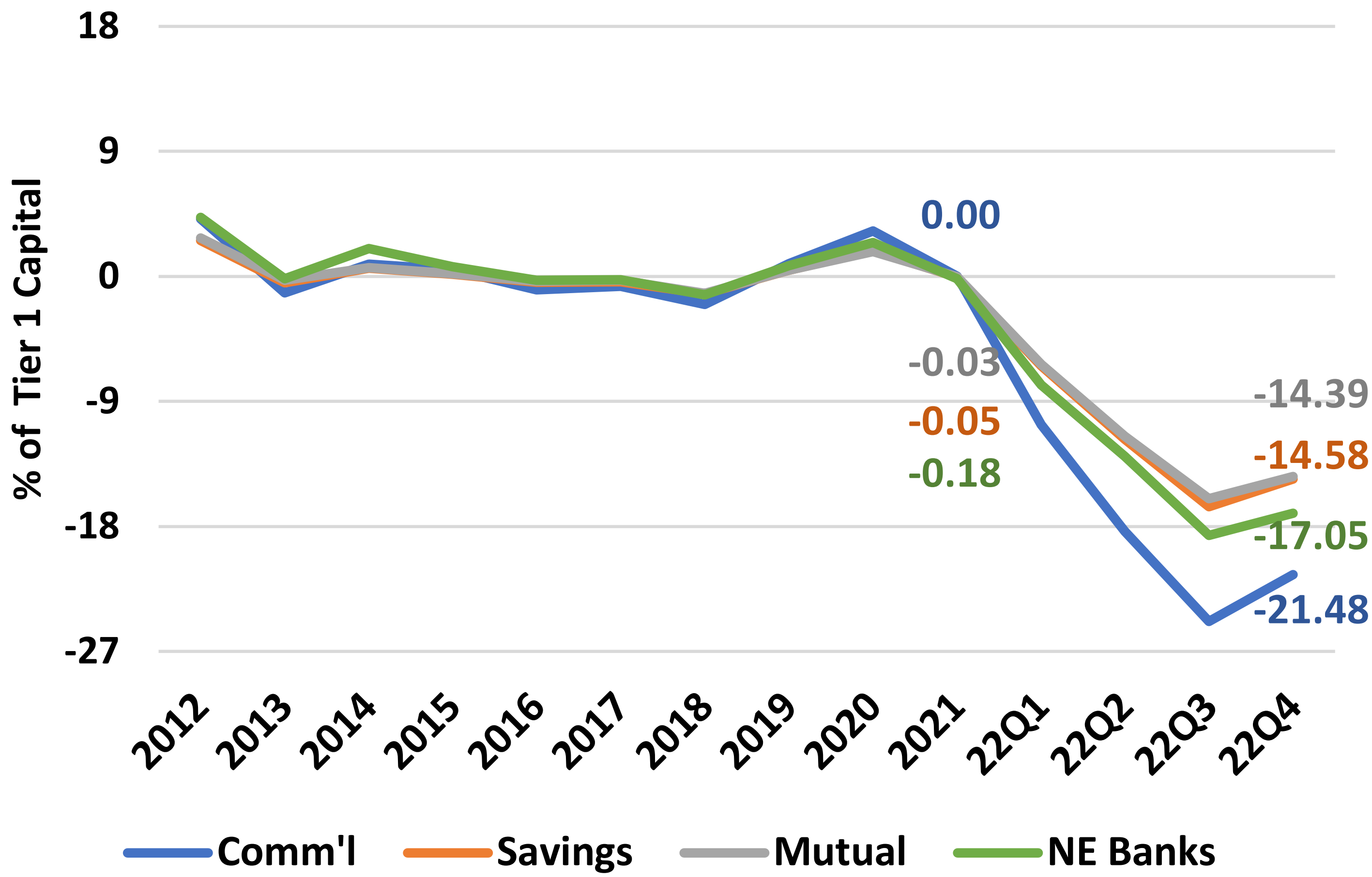


- After declining for five consecutive years, loans and securities greater than three years increased for the last three years. The high level of longer-term assets compared with the low level of longer-term liabilities represents a funding gap.



Investment Depreciation Significant

Investment portfolio depreciation to tier 1 capital has increased significantly this year due to the Fed raising interest rates and Quantitative Tightening.

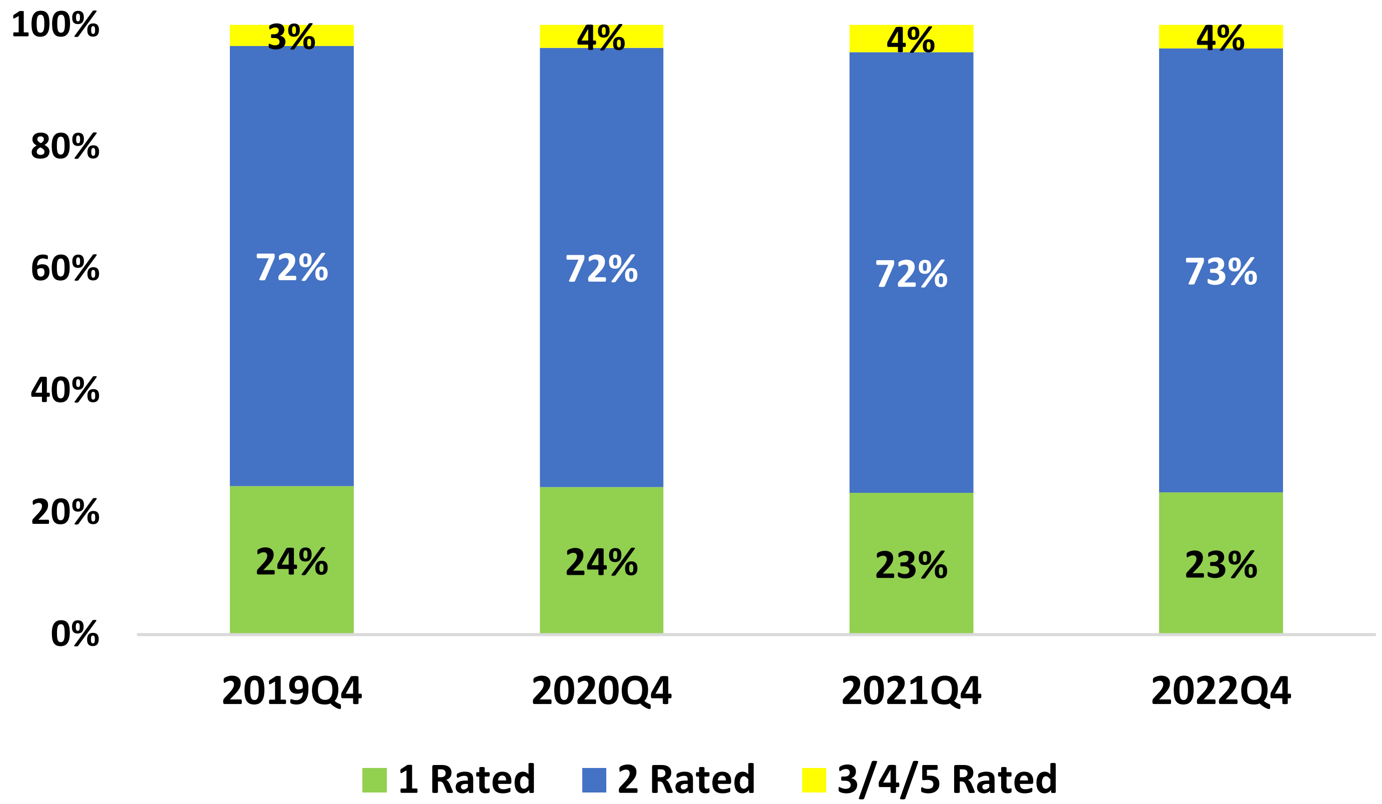


Summary of Condition-December 31, 2022

- The banking industry is comprised of a diverse group of 4,695 insured charters. The number of banks decreased 2.6 percent in 2022 due to mergers and acquisitions.
- **Capital is strong.** Leverage capital ratios are solid and increased in 2022; 99.8 percent of banks are "well capitalized" per Prompt Corrective Action.
- **Earnings are satisfactory.** Despite higher net interest income and expanding margins, ROAAs declined this year due to a contraction in fee income and higher provision expenses.
- **Asset Quality remains resilient.** Noncurrent loans and OREO remain low and stable but loans past due 30-89 days edged higher in 2022. The ALLL to Total Loan ratio remains adequate. Loan growth saw substantial improvement in 2022.
- **Liquidity is sufficient.** After rising sharply in 2020 and 2021 due to pandemic-related deposits, on-hand liquidity ratios fell in 2022 but remain above pre-pandemic levels.
- **Sensitivity to market risk is adequately controlled.** Investment portfolio depreciation to tier 1 capital has increased significantly this year due to the Fed raising interest rates and Quantitative Tightening.

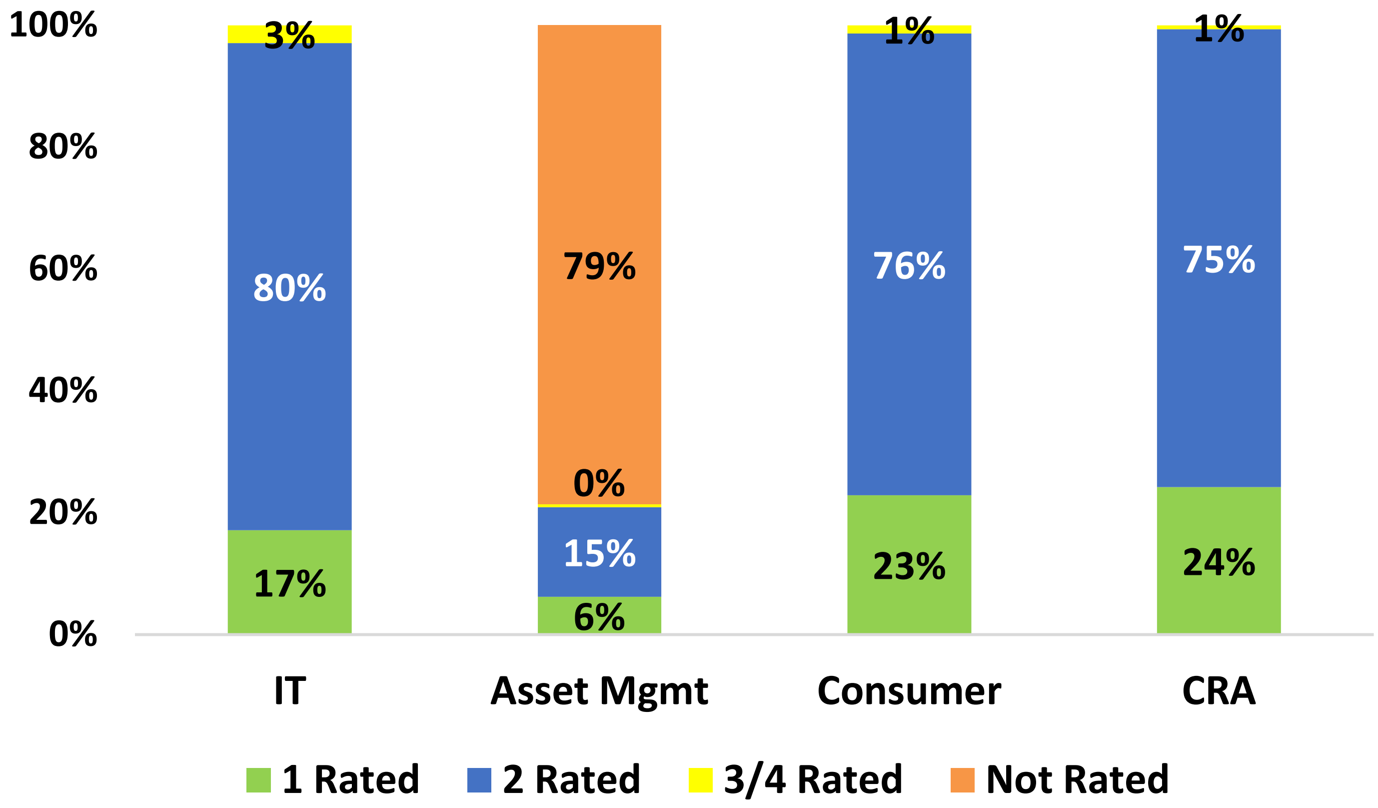
OCC Composite Ratings

Composite ratings are satisfactory and stable. Ninety-six percent of MCBS banks are rated composite 1 or 2.



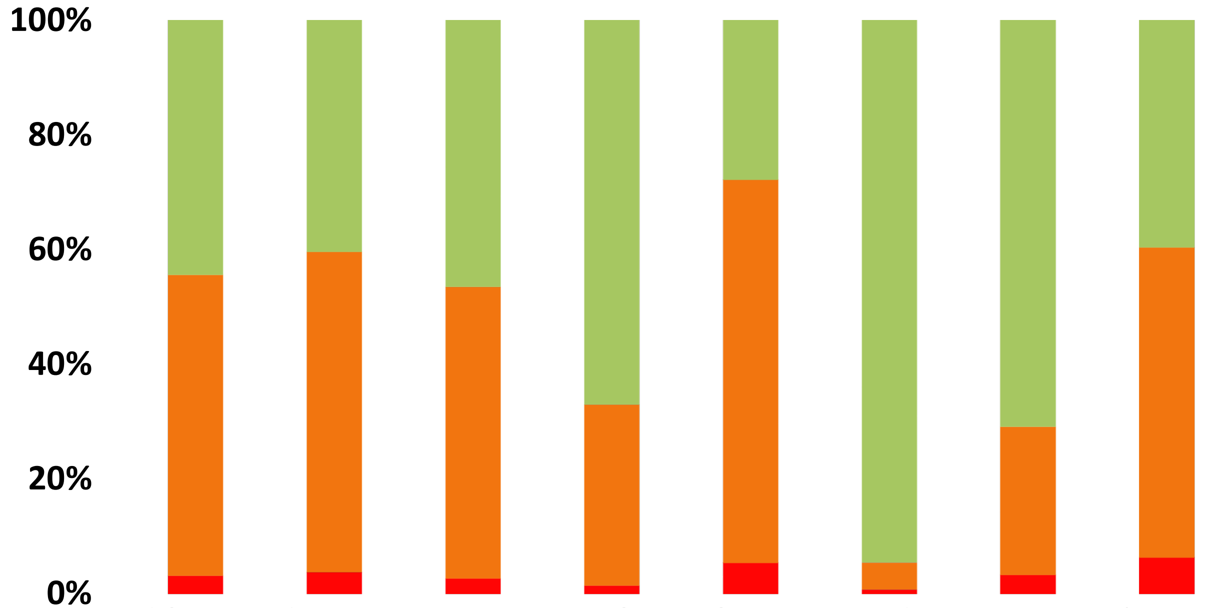
OCC Specialty Ratings

Specialty ratings are satisfactory. No specialty area is rated 5. About 21 percent of MCBS banks have trust powers. For purposes of this chart, a CRA rating of outstanding is 1, satisfactory is 2, and needs to improve is 3.



OCC Level of Risk Ratings

Most MCBS banks are designated with high risk for strategic, operational, and credit. Three of the eight risks are predominately rated as low.



	COMPL	CREDIT	IRR	LIQ	OPER	PRICE	REP	STRAT
Low	44%	40%	46%	67%	28%	94%	71%	40%
Moderate	52%	56%	51%	31%	67%	5%	26%	54%
High	3%	4%	3%	2%	5%	1%	3%	6%

Outlook and Challenges in 2023

- **Employment**
- **Inflation**
- **Consumer Spending**

Rate Hikes

The Fed raised the federal funds target rate 25 basis points to 4.50-4.75 percent at its Jan/Feb 31-1 meeting and the latest dot plot forecasts a 5.1 percent federal funds rate by year-end 2023. **Rates will be higher for longer.**

FOMC Meetings 2022	Rate Decision
Jan 25-26	0
Mar 15-16	+25 bps
May 3-4	+50 bps
Jun 14-15	+75 bps
Jul 26-27	+75 bps
Sep 20-21	+75 bps
Nov 1-2	+75 bps
Dec 13-14	+50 bps

FOMC Meetings 2023	Rate Decision
Jan/Feb 31-1	+25 bps
Mar 21-22	**+25 bps**
May 2-3	**+25 bps**
Jun 13-14	**+25 bps**
Jul 25-26	**0**
Sep 19-20	**0**
Oct/Nov 31-1	**0**
Dec 12-13	**0**

Summary of Economic Projections

In conjunction with the FOMC meeting held on Dec 13–14, 2022, meeting participants submitted their projections of the most likely outcomes for real gross domestic product (GDP) growth, the unemployment rate, and inflation for each year from 2022 to 2025 and over the longer run.

Percent

Variable	Median				
	2022	2023	2024	2025	Longer run
Change in real GDP	0.5	0.5	1.6	1.8	1.8
September projection	0.2	1.2	1.7	1.8	1.8
Unemployment rate	3.7	4.6	4.6	4.5	4.0
September projection	3.8	4.4	4.4	4.3	4.0
PCE inflation	5.6	3.1	2.5	2.1	2.0
September projection	5.4	2.8	2.3	2.0	2.0
Core PCE inflation	4.8	3.5	2.5	2.1	
September projection	4.5	3.1	2.3	2.1	
Memo: Projected appropriate policy path					
Federal funds rate	4.4	5.1	4.1	3.1	2.5
September projection	4.4	4.6	3.9	2.9	2.5

Employment

The Employment Situation Report is released 8:30am ET on the first Friday of the month (with few exceptions) by the Bureau of Labor Statistics. The White House - usually the President - speaks after the jobs report is released. The February 2023 Employment Situation Report is due to be released on March 3, 2023.

Jobs Report	Nov 2022	Dec 2022	Jan 2023
Release date	Dec 2, 2022	Jan 6, 2023	Feb 3, 2023
Payroll Change	**+256,000 (R)**	**+223,000**	**+517,000**
Estimate	+200,000	+200,000	+187,000
Net Revisions (prior month)			
Unemployment Rate-U3	**3.6%**	**3.5%**	**3.4%**
Unemployment Rate-U6	**6.7%**	**6.5%**	**6.6%**
Participation Rate	**62.1%**	**62.3%**	**62.4%**
Avg Hourly Earnings	**+5.1% Y/Y**	**+4.6% Y/Y**	**+4.4% Y/Y**

Inflation

The Fed views the PCE Price Index-the core rate in particular-as the most accurate measure of US inflation. As part of its price stability mandate, the Fed considers 2 percent to be healthy, though it will let the average go higher in the interest of promoting full employment.

PCE Price Index	Nov 2022	Dec 2022	Jan 2023
Release date	Dec 28, 2022	Jan 27, 2023	Feb 24, 2023
Core (x-food/energy)	**4.8%Y/Y**	**4.6%Y/Y**	**4.7%Y/Y**
Headline inflation	**6.2%Y/Y**	**5.0%Y/Y**	**5.4%Y/Y**

Consumer Price Index	Nov 2022	Dec 2022	Jan 2023
Release date	Dec 13, 2022	Jan 12, 2023	Feb 14, 2023
Headline inflation	**7.1%Y/Y**	**6.5%Y/Y**	**6.4%Y/Y**

Consumer Spending

Consumer spending makes up 70 percent of the US economy. Declining sentiment signals trouble if consumers pull back spending. The advance retail sales report is one of the timeliest economic reports because it provides data that is only a few weeks old. The Michigan Consumer Sentiment Index is a monthly survey of households on how consumers feel about the economy, personal finances, business conditions, and buying conditions.

Advance Retail Sales	Nov 2022	Dec 2022	Jan 2023
Release date	Dec 15, 2022	Jan 18, 2023	Feb 15, 2023
Retail Sales	-0.6% M/M	-1.1% M/M	3.0% M/M
Retail Sales (x-autos)	-0.2% M/M	-1.1% M/M	2.3% M/M

Consumer Confidence	Dec Final	Jan Final	Feb Final
Release date	Dec 23, 2022	Jan 27, 2023	Feb 24, 2023
Michigan Sentiment	59.7	64.9	67.0

Economic Challenges

- Fed will not pause rate hikes until they see clear and convincing evidence inflation is cooling. Powell, “Recession may be price to pay for crushing inflation.” It will be difficult to avoid recession to achieve 2 percent inflation.

- The disinflationary process has begun. The process will be bumpy and take a significant amount of time. We need ongoing rate hikes to a level that is sufficiently restrictive. We need softening in the labor market to reduce inflation.

- If the Fed keeps raising rates to reduce demand, the probability for overshooting and a hard landing is increased. Monetary policy is a blunt instrument. Inflation and employment reports are moving targets.

- Supply constraints that initially led to inflationary issues are not fully resolved. The Ukraine war has continued to cause global supply chain disruptions. Prices of essential commodities such as fuel and food have increased globally.

- Consumer confidence is key. If confidence holds up, we will not get a recession automatically rather, the Fed will raise rates to cool off demand and the economy will eventually slow, and inflation will reduce.

Questions?

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