Joint Release

Board of Governors of the Federal Reserve System
Federal Deposit Insurance Corporation
Office of the Comptroller of the Currency
Office of Thrift Supervision

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Data Show Continued Improvement in Credit Quality, Slight Increase in CreditT[1] Commitment Volume

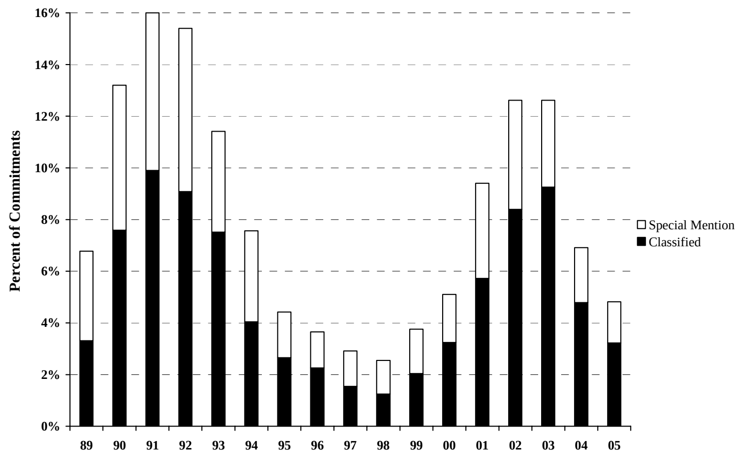
The quality of syndicated bank credits showed continued improvement this year, according to the Shared National Credit (SNC)[2] review released today by federal bank and thrift regulators. The review, which encompassed credits of at least $20 million that are shared by three or more financial institutions, also found that most industries exhibit much improved credit quality from peak problem levels experienced only a few years ago.

The results--reported by the Board of Governors of the Federal Reserve System, the Office of the Comptroller of the Currency, the Federal Deposit Insurance Corporation, and the Office of Thrift Supervision--are based on analyses prepared in the second quarter of 2005 and reflect business and economic conditions at that time.

Total classified credit commitments (those rated as either substandard, doubtful or loss) fell by $21.5 billion, or 29 percent, from the previous year, compared with a net decrease of $78.2 billion, or 51 percent, the year before. Commitments rated special mention decreased by $7.0 billion, or 21 percent, in contrast to 2004 when they fell by $22.4 billion, or 41 percent. None of these figures includes the effects of hedging or other techniques that organizations often employ to mitigate risk.

The ratio of classified credit commitments to total commitments fell to 3.2 percent, the lowest level since 1999. Total adversely rated credits[3] (classified and special mention combined) also fell considerably, to 4.8 percent of total commitments (see Chart 1 below).

Chart 1: Adversely Rated Credits



Overview

In aggregate, the 2005 SNC Program covered 6,817 credits totaling $1.6 trillion in credit commitments to 4,579 borrowers. Total commitments were up by 5.3 percent from the prior year, the first increase since 2001. However, the current level is 21 percent below the 2001 peak of $2.0 trillion. The increase in 2005 total commitments is consistent with market data pointing to higher customer demand and increased competition among a variety of lenders to provide new funds. Total outstandings, or drawn amounts, of $522 billion were up 4 percent from the prior year.

For the 2005 review, total credit commitments classified as substandard fell $10.9 billion, or 20 percent from the prior year, while doubtful credits dropped by $6.9 billion or 55 percent (see Table 1 below). Commitments classified as loss fell $3.7 billion, down 58 percent from the prior year. The portion of outstanding nonaccrual[4] classified credits fell to $19.3 billion.

Table 1 SNC Classifications ($ billions)

	% Change	Total Commitments				
	2004-2005	2005	2004	2003	2002	2001
Substandard	-20%	44.2	55.1	112.2	112.0	86.9
Doubtful	-55%	5.6	12.5	29.3	26.1	22.6
Loss	-58%	2.7	6.4	10.7	19.1	7.8
Total Classified	**-29%**	**52.5**	**74.0**	**152.2**	**157.1**	**117.3**
Percent of Commitments		3.2%	4.8%	9.3%	8.4%	5.7%
Memo: Nonaccrual classified	-36%	19.3	30.1	51.0	51.0	N/A
Special Mention	-21%	25.9	32.8	55.2	79.0	75.5
Total Criticized	**-27%**	**78.4**	**106.8**	**207.5**	**236.1**	**192.8**
Percent of Commitments		4.8%	6.9%	12.6%	12.6%	9.4%
Total SNC Commitments	5.3%	1,627	1,545	1,644	1,871	2,050

Industry Trends

The quality of syndicated credits improved in most industries (see Appendix B).[5] The strongest improvement in dollar terms occurred in the Oil, Gas, Pipelines and Utilities, with a $10.2 billion, or 42 percent, decline in classified commitments. However, the level of classified credits in this segment remains significantly elevated, with 7.5 percent of commitments classified. Telecommunications and Cable was the only segment to exhibit an increase in classification levels, largely due to the migration of credits previously criticized into the classified categories. Well-documented problems facing the airline industry continue to drive classifications in the Lodging and Transportation segment. The remaining segments showed modest classification rates that were below the average those for the entire SNC program.

Credits identified for special mention fell by $7.0 billion, or 21 percent, with strong declines experienced in most industries except Manufacturing. This segment experienced a notable increase in special mention volume due to problems in the automotive manufacturing sector. Of total loss classifications in 2005, $1.1 billion, or 42 percent, were directly attributable to the energy sector, most of which is related to outcomes of bankruptcy filings. The remaining losses were spread across a variety of industries.

Trends by Entity Type

During 2005, the share of SNC commitments held by U.S. banks edged down 1 percentage point to 45 percent. Over the past several years, lenders not affiliated with banks, such as brokerage firms, mutual funds, insurance companies, and hedge funds, have taken on larger positions in the SNC program. These nonbank[6] entities have increased their share to 13 percent compared to 8 percent four years ago. Compared to last year, the share held by foreign banking organizations (FBOs) held steady at 42 percent in 2005 (see Table 2). U.S. banks and FBOs showed a decrease in classified assets, while nonbank classifications increased from the prior year. The quality of holdings also varied among entity types, with classifieds amounting to 1.6 percent of total commitments at U.S. banks, compared with 2.3 percent at FBOs and 11.7 percent at nonbanks. Total nonaccrual outstandings improved for all entity types. Most notably, U.S. banks experienced a 42 percent decline.

Table 2 Exposures By Entity Type

Share of Total Commitments	**2005**	**2004**	**2003**	**2002**	**2001**
U.S. Banks	45%	46%	45%	45%	46%
FBOs	42%	42%	44%	45%	46%
Nonbanks	13%	12%	11%	10%	8%
Total Classifications ($ Bil.)					
U.S. Banks	11.9	18.8	43.6	54.4	48.7
FBOs	15.5	31.3	65.0	61.7	44.3
Nonbanks	25.1	23.9	43.6	41.1	24.5
Totals	52.5	74.0	152.2	157.2	117.5
Total Classifications (% Increase)					
U.S. Banks	-37.0%	-56.8%	-20.0%	11.8%	85.5%
FBOs	-50.5%	-51.8%	5.5%	39.2%	99.4%
Nonbanks	5.2%	-45.3%	6.2%	67.9%	76.0%
Totals	-29.1%	-51.4%	-3.2%	33.8%	88.3%
Classifieds as % of Commitments					
U.S. Banks	1.6%	2.6%	5.8%	6.4%	5.1%
FBOs	2.3%	4.9%	9.0%	7.3%	4.7%
Nonbanks	11.7%	12.9%	24.4%	23.0%	14.6%
Totals	3.2%	4.8%	9.3%	8.4%	5.7%
Total NonAccrual Outstanding ($ Bil.)					
U.S. Banks	3.3	5.7	13.3	15.5	n.a.
FBOs	6.6	13.4	22.8	19.8	n.a.
Nonbanks	9.4	11.0	15.0	15.7	n.a.
Totals	19.3	30.1	51.1	51.0	n.a.

Risk Management by Banks

Banking organizations remain vigilant in identifying problem credits and have generally reflected the appropriate risk rating in their internal ratings of credits in the SNC program. Although credit quality has improved, banking organizations must continue to carefully monitor the condition of their borrowers to ensure that they promptly identify and address any emerging weaknesses and adjust loan loss allowance levels appropriately.[7]

Appendix A

Committed and Outstanding Balances
(Dollars in Billions)

Year	Special Mention	Sub-Standard	Doubtful	Loss	Total Classified	Total Criticized	Total Committed	Total Outstanding
1989	24.0	18.5	3.5	0.9	22.9	46.9	692	245
1990	43.1	50.8	5.8	1.8	58.4	101.5	769	321
1991	49.2	65.5	10.8	3.5	79.8	129.0	806	361
1992	50.4	56.4	12.8	3.3	72.5	122.9	798	357
1993	31.4	50.4	6.7	3.5	60.6	92.0	806	332
1994	31.5	31.1	2.7	2.3	36.1	67.6	893	298
1995	18.8	25.0	1.7	1.5	28.2	47.0	1,063	343
1996	16.8	23.1	2.6	1.4	27.1	43.9	1,200	372
1997	19.6	19.4	1.9	0.9	22.2	41.8	1,435	423
1998	22.8	17.6	3.5	0.9	22.0	44.8	1,759	562
1999	31.3	31.0	4.9	1.5	37.4	68.7	1,829	628
2000	36.3	47.9	10.7	4.7	63.3	99.6	1,951	705
2001	75.5	86.9	22.6	7.8	117.3	192.8	2,050	769
2002	79.0	112.0	26.1	19.1	157.1	236.1	1,871	692
2003	55.2	112.1	29.3	10.7	152.2	207.4	1,644	600
2004	32.8	55.1	12.5	6.4	74.0	106.8	1,545	500
2005	25.9	44.2	5.6	2.7	52.5	78.3	1,627	522

Appendix B[8]

Summary of Shared National Credit Industry Trends

(Dollars in Billions)

Industry	2005	2004	2003	2002	2001
Telecommunication & Cable					
Commitment	123.7	120.2	149.7	174.1	197.5
Classified	17.0	13.1	35.7	38.1	6.9
Special Mention	2.5	10.8	7.0	9.0	10.0
% Classified	13.7%	10.9%	23.8%	21.9%	3.5%
% Special Mention	2.0%	9.0%	4.7%	5.1%	5.0%
Manufacturing					
Commitment	409.7	400.1	424.4	494.8	540.5
Classified	10.7	19.6	42.6	60.9	58.1
Special Mention	16.6	6.9	22.8	26.2	27.0
% Classified	2.6%	4.9%	10.0%	12.3%	10.8%
% Special Mention	4.0%	1.7%	5.4%	5.3%	5.0%
Professional, Scientific, & Other Services					
Commitment	102.2	107.3	122.4	124.9	157.9
Classified	1.5	3.3	6.8	8.8	11.9
Special Mention	1.3	1.1	1.8	2.3	4.5
% Classified	1.5%	3.1%	5.5%	7.0%	7.5%
% Special Mention	1.3%	1.0%	1.5%	1.9%	2.8%
Oil, Gas, Pipelines & Utilities					
Commitment	186.4	175.7	200.5	229.5	222.8
Classified	14.1	24.2	38.1	17.1	4.3
Special Mention	1.9	10.1	12.3	15.5	7.0
% Classified	7.5%	13.8%	19.0%	7.4%	1.9%
% Special Mention	1.0%	5.8%	6.1%	6.8%	3.1%
Construction & Real Estate					
Commitment	107.9	90.2	87.5	96.7	100.1
Classified	0.7	2.5	3.6	4.1	4.7
Special Mention	0.3	0.9	2.3	3.2	1.9
% Classified	0.6%	2.8%	4.1%	4.2%	4.7%
% Special Mention	0.2%	1.0%	2.6%	3.3%	1.9%
Lodging & Transportation					
Commitment	76.5	74.1	74.8	82.9	99.1
Classified	3.7	5.2	7.7	6.6	3.1
Special Mention	0.8	0.7	1.8	5.3	6.7
% Classified	4.9%	7.1%	10.3%	7.9%	3.1%
% Special Mention	1.1%	1.0%	2.4%	6.4%	6.8%
Financial Services & Insurance					
Commitment	336.0	337.1	343.3	376.5	420.0
Classified	0.1	2.1	6.7	8.9	11.9
Special Mention	0.2	0.5	2.5	2.9	4.4
% Classified	0.0%	0.6%	1.9%	2.4%	2.8%
% Special Mention	0.1%	0.2%	0.7%	0.8%	1.1%
All Other					
Commitment	284.2	240.4	241.0	291.6	310.8
Classified	4.7	3.8	11.0	12.7	16.5
Special Mention	2.4	1.8	4.7	14.6	13.9
% Classified	1.6%	1.6%	4.6%	4.4%	5.3%
% Special Mention	0.8%	0.7%	2.0%	5.0%	4.5%
All Industries (Total)					
Commitment	1,626.7	1,545.2	1,643.5	1,871.0	2,048.9
Classified	52.5	72.4	152.2	157.1	117.5
Special Mention	25.9	32.8	55.2	79.0	75.4
% Classified	3.2%	4.7%	9.3%	8.4%	5.7%
% Special Mention	1.6%	2.1%	3.4%	4.2%	3.7%

[1] Credits include syndicated loans and loan commitments, letters of credit, commercial leases, as well as other forms of credit. Credit commitments include both drawn and undrawn portions of credit facilities. This release reports only the par amounts of commitments; these may differ from the amounts at which loans are carried by investors.

[2] The Shared National Credit (SNC) Program was established in 1977 by the Board of Governors of the Federal Reserve System, the Federal Deposit Insurance Corporation, and the Office of the Comptroller of the Currency. In 2001 the Office of Thrift Supervision became an assisting agency. With a few exceptions, the annual program, which seeks to provide an efficient and consistent review and classification of large syndicated loans, generally covers loans or loan commitments of at least $20 million that are shared by three or more financial institutions.

[3] Adversely rated credits (also known as criticized credits) are the total of credits classified substandard, doubtful, and loss – and credits rated special mention. Classified credits are only those rated substandard, doubtful, and loss. Under the agencies' Uniform Loan Classification Standards, classified credits have well-defined weaknesses, including default in some cases. Special mention credits exhibit potential weaknesses, which may result in further deterioration if left uncorrected.

Excerpt from Federal Reserve's SR Letter 79-556 defining regulatory classifications:
Classification ratings are defined as "Substandard," "Doubtful," and "Loss." A Substandard asset is inadequately protected by the current sound worth and paying capacity of the obligor or of the collateral pledged, if any. Assets so classified must have a well-defined weakness or weaknesses that jeopardize the liquidation of the debt. They are characterized by the distinct possibility that the bank will sustain some loss if the deficiencies are not corrected. An asset classified as Doubtful has all the weakness inherent in one classified Substandard with the added characteristic that the weaknesses make the collection or liquidation in full, on the basis of currently existing facts, conditions, and values, highly questionable and improbable. Assets classified as Loss are considered uncollectible and of such little value that their continuance as bankable assets is not warranted. This classification does not mean that the asset has absolutely no recovery or salvage value, but rather it is not practical or desirable to defer writing off this basically worthless asset even though partial recovery may be effected in the future.

Excerpt from June 10, 1993 Interagency Statement on the Supervisory Definition of Special Mention Assets:
A Special Mention asset has potential weaknesses that deserve management's close attention. If left uncorrected, these potential weaknesses may result in deterioration of the repayment prospects for the asset or in the institution's credit position at some future date. Special Mention assets are not adversely classified and do not expose an institution to sufficient risk to warrant adverse classification.

[4] Nonaccrual loans are defined for regulatory reporting purposes as **"**loans and lease financing receivables that are required to be reported on a nonaccrual basis because (a) they are maintained on a cash basis due to a deterioration in the financial position of the borrower, (b) payment in full of interest or principal is not expected, or (c) principal or interest has been in default for 90 days or longer, unless the obligation is both well secured and in the process of collection." In Table 1, nonaccrual classifieds are those funded or outstanding portions of loans classified as substandard and doubtful which are not accruing interest. For 2005, this consisted of $14.8 billion in loans rated substandard and $4.5 billion rated doubtful.

[5] Note that the current industry totals categorize borrowers using 2002 NAICS codes, in contrast to prior release of SNC data which categorized borrowers using 1997 NAICS codes.

[6] Nonbanks include a wide range of institutional investors.

[7] For further guidance, institutions should refer to the July 12, 1999 Joint Interagency Letter to Financial Institutions on the allowance for loan losses, as well as the July 2, 2001 Interagency Policy Statement on Allowance for Loan and Lease Losses (ALLL) Methodologies and Documentation for Banks and Savings Institutions.

[8] NAICS groupings of industries identified in Appendix B are as follows: Telecommunication & Cable - 5132 through 51339; Manufacturing - 31 through 33 and 5121 through 5131; Professional, Scientific, and Other Services - 54, 55, 56, 61, and 62; Oil, Gas, Pipelines, and Utilities - 21 (oil- & gas-related only), 22, and 486; Construction & Real Estate - 23 and 53; Lodging and Transportation - 48 (excluding 486), 49, and 72; Financial Services and Insurance - 52; and All Other - remaining NAICS codes. Prior year data has been restated to reflect industry categorizations using 2002 NAICS groupings rather than 1997 NAICS groupings used in prior data releases.

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