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Derivatives Volume Grows to \$25 Trillion in 3rd  
Quarter;  
Quarterly Derivatives Revenue is Record \$2.5 Billion

WASHINGTON, D.C. -- The amount of derivatives activity at commercial banks increased by \$1.7 trillion in the third quarter to a record \$25 trillion, the Office of the Comptroller of the Currency (OCC) reported today. Since the beginning of 1997, the notional amount of derivatives activity has increased by 25 percent.

In its quarterly report of derivatives activity, the OCC said third quarter revenues of commercial banks from cash instruments and off-balance sheet derivatives increased to a record \$2.5 billion -- up \$509 million or 26 percent from the second quarter. For the year, revenues from trading cash instruments, such as Treasury bonds, and off balance sheet trading activities, such as swaps, futures, forwards and options, stood at \$6.8 billion. Cash instruments are traded along with derivatives, and they are not separated in revenue reports.

As a percentage of total revenue, derivatives trading accounted for an average of nearly 3 percent for all banks and more than 7.5 percent for the eight banks that are the industry's leading derivatives dealers. One bank, Morgan Guaranty Co. of New York, derived nearly 18 percent of its revenues from trading during the quarter. These eight banks accounted for 85 percent of the industry's third quarter trading revenues.

The increase of \$509 million in trading revenue during the quarter can be attributed to an across the board increase in revenues from positions in interest rates, foreign exchange, equities and commodities.

The third quarter report does not reflect the volatility of global debt and equity markets or the currency devaluations in some Asian nations that have occurred since October 1.

"On balance, the market volatility will probably reduce trading revenue in the final quarter of the year," said Mike Brosnan, the OCC's director of treasury and market risk.

"On the one hand, banks benefitted as customers became more interested in risk management products and as the volatility presented proprietary trading opportunities," he said.

"However, to date, those benefits were more than offset by losses that resulted at some banks from the sudden and severe shifts in equity values, currency rates and debt prices at the end of October." The fourth quarter report will be issued in March, 1998.

The notional amount of credit derivatives more than doubled to \$39 billion from \$19 billion since the first quarter of 1997 when banks first reported using the instrument. Nineteen banks

reported using credit derivatives during the quarter, an increase of five from the previous quarter.

"Credit derivatives are seen as an effective way for banks to reduce their credit risk, and I would look for this activity to continue to grow in the coming years," said Mr. Brosnan.

The OCC's third quarter derivatives report also shows:

The number of commercial banks holding derivatives increased by 11 in the quarter to 475.

Approximately 69 percent of the notional amount of derivative positions was comprised of interest rate contracts with an additional 29 percent represented by foreign exchange contracts. Commodity and equity contracts accounted for 2 percent of the total.

Eight commercial banks accounted for 94 percent of the total notional amount of derivatives in the banking system, with 99 percent accounted for by the top 25 banks.

Over-the-counter contracts, which accounted for 86 percent of the notional holdings in the third quarter, tend to be more popular with banks and bank customers because they can be tailored to meet firm-specific risk management needs. However, OTC contracts tend to be less liquid than exchange-traded contracts.

Relative to risk-based capital, total credit exposures for the top eight banks increased slightly to 6.4 percent of risk-based capital in the third quarter, up from 6.2 percent in the second quarter.

Nonperforming contracts remained at nominal levels. For all banks, the book value of contracts 30 days or more past due totaled only \$8.1 million, or .003 percent of total credit exposure from derivatives contracts. Since the beginning of the year, banks with derivative contracts reported \$59 million in credit losses from off-balance sheet derivatives. This relatively small loss figure reflects both the current healthy economic environment and the generally high credit quality of counterparties and end-users with whom banks presently engage in derivatives transactions, as well as the increased use of collateral.

The value of derivatives positions in which the bank has a gain is relatively balanced with the value of those positions with a loss. This indicates a controlled level of market risk taking at the major banks.

A copy of the OCC Third Quarter 1997 Derivatives Data Fact Sheet and the accompanying tables and graphs may be obtained by: writing to Comptroller of the Currency, Public Reference Room (Mail Stop 1-5), Washington, DC 20219; calling the OCC Information Fax Line at (202) 479-0141 and requesting document

number 797114 under news releases; faxing a request to (202) 874-4448; ordering by phone (202) 874-5043; or visiting the OCC's Public Reference Room at 250 E Street, S.W. in Washington, D.C. (9 a.m. - noon and 1 - 3 p.m., Monday - Friday). The document will be available on the OCC's web page at <http://www.occ.treas.gov>.

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The OCC charters, regulates and supervises more than 2,600 national banks and 66 federal branches and agencies of foreign banks in the United States, accounting for 56 percent of the nation's banking assets. Its mission is to ensure a safe, sound and competitive national banking system that supports the citizens, communities and economy of the United States.