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Trading Revenue Down Sharply In 4th Quarter

WASHINGTON, D.C. -- Derivatives activity at commercial banks increased slightly in the final quarter of 1997 to $25.1 trillion, even as trading revenues at these banks dropped 52 percent to $1.2 billion, according to the Office of the Comptroller of the Currency's (OCC) quarterly report on bank derivatives activities released today.

The drop in trading revenue from cash securities and off-balance sheet trading positions is attributed in part to the steep decline in global equity markets and emerging market debt during October.

"The fourth quarter report does not reflect the general rebound in global equity markets that has taken place so far in 1998," said Mike Brosnan, the OCC's director of the treasury and market risk division.

During the fourth quarter, banks' trading revenue from equity positions dropped $305 million largely as a result of volatility in some markets, particularly in Asia. Trading revenue from commodity and other positions declined $320 million, principally from emerging market debt trading. These declines came from eastern Europe, Asia and Latin America.

"OCC examiners in national banks are closely monitoring risk management practices for trading, with a focus on derivatives trading," said Mr. Brosnan.

The two largest areas of trading revenue come from interest rate and foreign exchange contracts. While revenue from foreign exchange activities increased $211 million to $1.3 billion from the previous quarter, revenue from interest rate positions fell to $534 million from $1.2 billion.

For all banks, quarterly trading revenue fell to 1.3 percent of gross revenue -- its lowest level since the OCC began reporting this data in early 1995. Three of the eight largest banks had a loss and the others showed smaller gains than in the previous quarter.

During the fourth quarter, the notional value of interest rate contracts fell by $185 billion to $17.1 trillion. Foreign exchange contracts increased by $162 billion to $7.4 trillion.
This figure excludes spot foreign exchange contracts, which decreased by $334 billion to $317 billion. Commodity and equity contracts rose by $42 billion to $494 billion.

Credit derivatives rose by $16 billion and now total $55 billion. Since the beginning of 1997 when banks first reported using this product, the notional value of credit derivatives has nearly tripled. Fifteen insured commercial banks reported using credit derivatives during the quarter, a decrease of two from the previous quarter.

Past due derivative contracts remained at nominal levels. For all banks, the book value of contracts past due 30 days or more aggregated only $28 million, or .008 percent of total credit exposure from derivatives contracts. Call report data, upon which the OCC derivatives report is based, do not show the volume of non-accrual assets attributable to derivative contracts.

During 1997, banks charged off $120 million in credit losses from off-balance sheet derivatives. "While credit-related losses have grown, 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 now engage in derivatives transactions," said Mr. Brosnan. "It also reflects the increased use of collateral in these deals."

The OCC's fourth quarter derivatives report also shows:

> The number of commercial banks holding derivatives decreased by 15 to 459 during the quarter.
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> Eight commercial banks accounted for 95 percent of the total notional amount of derivatives in the banking system, with 99 percent accounted for by the top 25 banks.
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> Total credit exposures for the top eight banks increased from 266 percent to 290 percent of risk-based capital.
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> Approximately 68 percent of the notional amount of derivative positions comprised interest rate contracts with an additional 30 percent made up of by foreign exchange contracts. Commodity and equity contracts accounted for 2 percent of the total.
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> Over the last two years, there has been a steady growth in interest rate contracts with a maturity of more than five years.

A copy of the OCC Fourth 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 79831 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.