Member Bank Income – 1968

NET PROFITS at member banks in the Eighth Federal Reserve District rose moderately in 1968. Net income after taxes (net profits) was up about 5 per cent for the year, compared with increases of 8 and 14 per cent in 1967 and 1966 respectively and an average annual rate of 7 per cent in the eleven-year 1957-68 period.[1]

Operating revenue rose 16 per cent in 1968, reflecting both a larger volume of earning assets and a higher average rate of return on assets. Expenses were up 18 per cent, rising more rapidly than revenue, although by a smaller dollar amount. Net current earnings (operating revenue less operating expenses) climbed 11 per cent compared with 4 per cent a year earlier. However, the net effect of additions due to recoveries, transfers from reserves, and profits, and deductions due to losses, charge-offs and transfers to reserves, was a deduction from net current earnings of $25.6 million, or 16 per cent, compared with a deduction of $19.6 million, or 13 per cent in 1967.

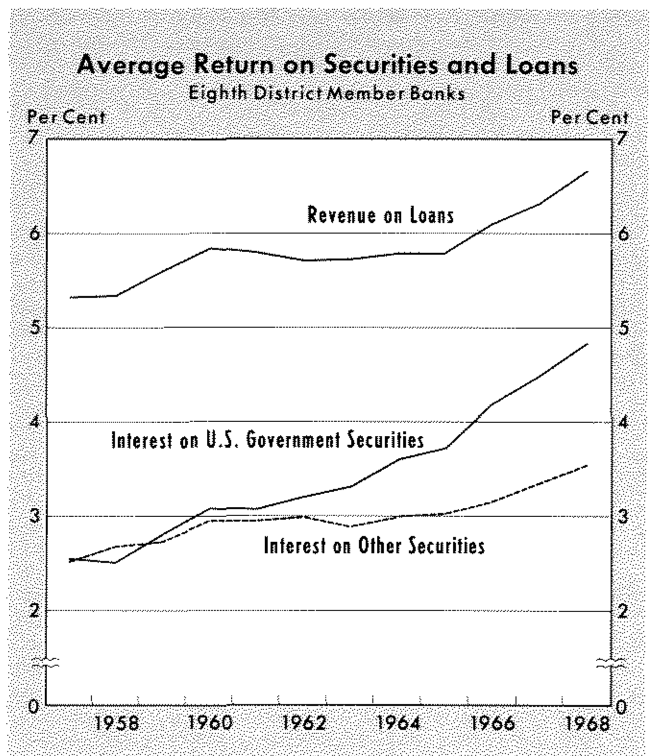
Net profits at all member banks in the nation were 7.5 per cent higher in 1968 than in 1967, somewhat more than for district member banks. Operating revenue rose slightly faster in the nation than in the district, and expenses increased more slowly. The net effect of security transactions and other profit and loss adjustments on loans and other assets at member banks in the nation was a reduction from net current earnings of $1.2 billion, or 24 per cent in 1968, compared with a reduction of $0.7 billion, or 17 per cent in 1967.

Revenues

Operating revenue at district member banks totaled $655 million in 1968, or 16 per cent above the previous year. The $428 million revenue on loans represented an increase of 14 per cent. Interest on Government securities of $97 million was up 18 per cent and that on other securities rose 22 per cent to $65 million in 1968. Revenue from all other sources totaled $66 million, an increase of 18 per cent from the previous year.

Loans rose from an average of $5.9 billion in 1967 to $6.4 billion in 1968, an increase of 8 per cent. This increase is similar to the trend growth in loans from 1957 to 1968 of 8 per cent per year. Holdings of U.S. Government securities rose 9 per cent in 1968, compared with a trend growth of only 1 per cent annually since 1957, and other securities rose 15 per cent, somewhat above their 13 per cent trend rate.

The rate of return on all types of earning assets increased. Returns on loans in 1968 averaged 6.7 per cent, compared with 6.3 per cent in 1967. Returns on U.S. Government securities averaged 4.8 per cent and



[1]Throughout this article 1957 is used as the base year in calculating trend rates, since that year was more typical of bank operations than 1958.

REVENUES AND EXPENSES OF EIGHTH DISTRICT MEMBER BANKS

	Millions of Dollars				Per Cent Change		
	1968	1967	1966	1957	1967-68	1966-67	Annual Rate 1957-68
Revenue on Loans	428.2	374.2	334.3	140.8	14.4	11.9	10.6
Interest on Securities							
U.S. Government	97.2	82.7	75.7	47.6	17.5	9.2	6.7
Other	65.3	53.4	43.5	12.7	22.3	22.8	16.1
Service Charges on Deposit Accounts	22.7	20.5	18.6	9.3	10.7	10.2	8.5
Trust Department	18.2	16.7	15.1	6.6	9.0	10.6	9.7
All Other Revenues	24.6	18.2	15.1	10.2	35.2	20.5	8.3
Total Operating Revenues	**655.2**	**565.7**	**502.3**	**227.2**	**15.8**	**12.6**	**10.1**
Salaries, Wages, and Benefits	149.5	132.4	118.8	63.7	12.9	11.4	8.1
Interest on Time Deposits	202.4	171.7	138.4	22.6	17.9	24.1	22.1
Other Expenses	139.8	113.8	102.8	50.7	22.8	10.7	9.7
Total Operating Expenses	**491.6**	**418.0**	**360.1**	**137.0**	**17.6**	**16.1**	**12.3**
Net Current Earnings	**163.6**	**147.7**	**142.3**	**90.2**	**10.8**	**3.8**	**5.6**
Recoveries, Transfers from Reserves, and Profits	14.0	15.9	20.2	5.2	−12.0	−21.3	9.4
Losses, Charge-Offs, and Transfers to Reserves	39.6	35.5	45.1	16.7	11.5	−21.3	8.2
Net Income (Before Income Taxes)	**138.0**	**128.1**	**117.3**	**78.7**	**7.7**	**9.2**	**5.2**
Taxes on Net Income	41.1	36.1	32.1	33.1	13.9	12.5	2.0
Net Income (After Income Taxes)	**96.9**	**92.0**	**85.2**	**45.6**	**5.3**	**8.0**	**7.1**
Cash Dividends on Common Stock	38.5	35.0	32.8	18.2	10.0	6.7	7.0
Interest on Capital Notes and Debentures[1]	2.2	2.0	1.9	*			
Number of Banks	474	478	480	491			

[1]Includes small amount of cash dividends on preferred stock
*Less than 0.05

4.5 per cent in 1968 and 1967, respectively, and those on other securities were 3.6 per cent and 3.4 per cent.

While total revenue increased more rapidly than loan revenue, the latter accounted for six-tenths of the increase in total revenue from a year earlier. Interest income from both U.S. Government securities and other securities (mostly issues of state and local jurisdictions) rose somewhat more rapidly than loan revenue during 1968. Revenue from securities accounted for about three-tenths of the rise in total revenues. Revenue from service charges on deposit accounts, up 11 per cent, and trust department revenue, up 9 per cent, rose more moderately than other sources of revenue.

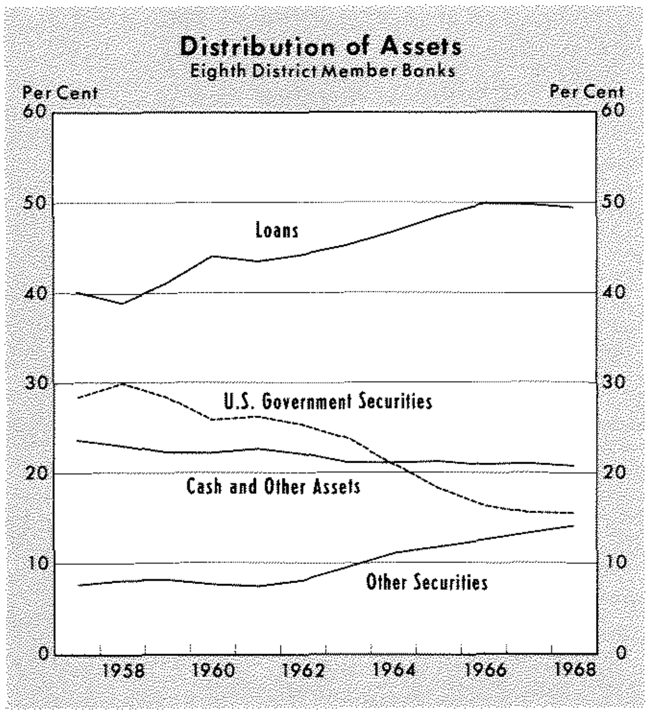
Although accounting for only a minor portion of the total, miscellaneous revenues were the most rapidly rising source, increasing from $18.2 million in 1967 to $24.6 million in 1968, or 35 per cent. This gain reflects the proliferation of nonlending services being offered by commercial banks in recent years. Some of the income items included in this category are rental of safe deposit boxes, income from leased property, and income from foreign departments.

Operating revenue at district banks has risen at an average 10 per cent annual rate during the past eleven years, from $227 million in 1957 to $655 million in 1968.[2] In addition to an increase in total assets, the growth in revenue reflects a marked rise in the general level of interest rates and a shift in the composition of assets to more of the relatively higher-earning types.

Total resources of district member banks grew from $6.6 billion in 1957 to $12.9 billion in 1968, an average annual increase of 6.3 per cent. Since the proportion of assets in the form of cash declined slightly, earning assets grew somewhat more rapidly, rising from $5 billion in 1957 to $10.3 billion in 1968, a 6.7 per cent rate.

The composition of banks' portfolios has changed sharply since 1957 to include proportionately more higher-earning assets. Holdings of U.S. Government securities dropped from 28 per cent of assets in 1957 to 16 per cent in 1968. Meanwhile, loans rose from

[2]These data are not adjusted for changes in total number of banks, resulting from new member banks or withdrawals from memberships. The effect of such changes on the total shown would be small.



40 per cent to nearly 50 per cent of assets, and securities, other than U.S. Governments, rose from 8 to 14 per cent.

The average rate of return on bank assets has trended upward. The average return on bank loans increased from 5.3 per cent in 1957 to 6.7 per cent in 1968, while the average return on Government securities rose from 2.6 per cent to 4.8 per cent during the same period.

Expenses

Operating expenses at district member banks totaled $492 billion in 1968, 18 per cent more than the previous year. As in most other recent years, expenses grew at a more rapid rate than revenue. Interest payments on time and savings deposits accounted for the largest dollar amount of increase in total expenses, but miscellaneous expense was the most rapidly rising item. Interest payments rose from $172 million in 1967 to $202 million in 1968, an increase of 18 per cent. Wages, salaries, and employee benefits rose from $132 million in 1967 to $150 million in 1968, or 13 per cent, as the number of officers and employees rose 6.4 per cent and average compensation per person increased 6 per cent. All other expenses rose 23 per cent from $114 million to $140 million.

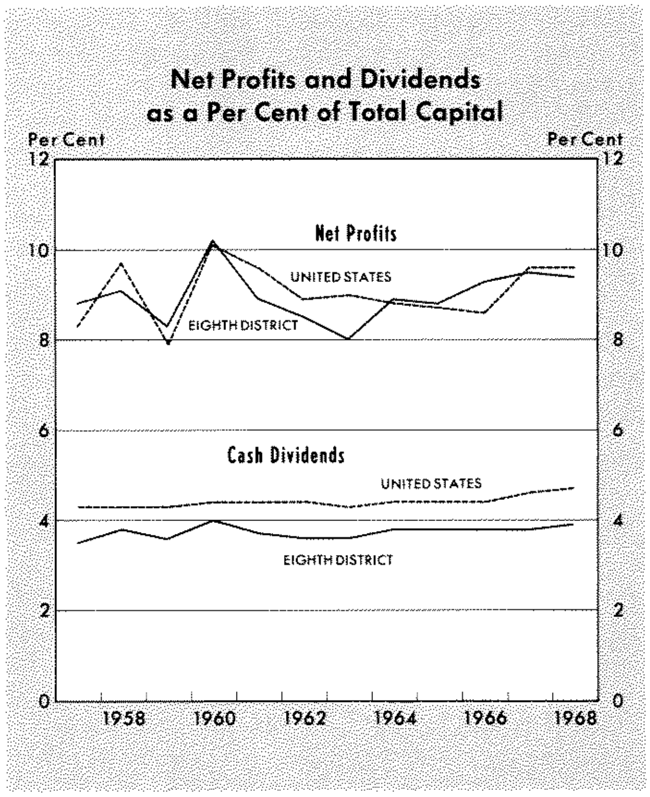
The rapid rise in miscellaneous expenses was largely due to larger payments for borrowed money and for furniture and equipment. At the interest rate relationships prevailing in much of 1968, banks found it profitable to increase their borrowings despite the rising rates paid on borrowed funds. During portions of 1968 market rates were above the rates which banks were permitted to pay on deposits under Regulation Q, and as a result banks relied more heavily on borrowings to meet their loan demand. The rapid increase in furniture and equipment expenses reflects increased mechanization and automation in commercial banking. Banks have been able to increase efficiency through increased use of data-processing equipment in performing the numerous clerical tasks associated with banking operations.

Since 1957 operating expenses of member banks in the district have risen from $137 million to $492 million, an average annual increase of 12 per cent. Reflecting a generally rising demand for loanable funds and competition among financial agencies to obtain such funds, interest paid by banks has increased sharply during the past decade. Interest expense rose from $23 million in 1957 to $202 million in 1968, an increase of 22 per cent per year. The volume of time and savings accounts rose from $1.3 billion in 1957 to $4.7 billion in 1968, or 12 per cent per year, while the average rate paid on these accounts rose from 1.7 per cent to 4.3 per cent. Other expense items have risen, but less rapidly than interest expense. Salaries, wages, and fringe benefits rose at an average annual rate of 8 per cent, and all other expenses rose at a 10 per cent rate.

Net Earnings and Income

Net current earnings of member banks in the Eighth District totaled $164 million in 1968, an increase of 11 per cent from a year earlier. This was about double the average annual increase of 5.6 per cent during the 1957-68 period. The net effect of adjustments for losses, charge-offs and transfers to valuation reserves in 1968, however, resulted in net income being $25.6 million less than net current earnings, compared with a $19.6 million difference in 1967. Much of this increase in the earnings/income differential resulted from losses on securities sold.

Net income after taxes at district member banks totaled $97 million in 1968, an increase of 5.3 per cent from a year earlier. This was somewhat below the trend rate of 7.1 per cent per year since 1957. In comparison, net income after taxes for all member banks in the nation rose 7.5 per cent last year and has risen at an 8.3 per cent rate since 1957.



Member banks distributed $38.5 million in dividends on common stock in 1968, an increase of 10 per cent from the previous year. Net retained earnings at these banks totaled $56 million. These undivided profits, of course, are the primary source of increased capital in banks. In addition, member banks in the district raised a net $6.7 million of other capital, for a total increase in capital of $63 million, 6.3 per cent above year-end 1967.

Since 1957, capital at district member banks has risen at a 6.5 per cent rate. In the late 1950's capital was rising more rapidly than either deposits or assets. As a result the capital-to-assets and capital-to-deposits ratios both rose. Since 1962, however, these ratios have had a downward trend. In comparison, the ratio of capital to loans has declined from about 20 per cent, prevailing in the 1957-62 period, to 16 per cent in 1968. Some analysts view these declining ratios as an increase in banks' exposure to risks, and viewed in this manner, risk exposure has increased somewhat in recent years.