Through the first six months of 2001, FDIC-insured commercial banks reported record earnings of $39 billion, surpassing the first half of 2000 by $4.8 billion (14.1%), which translates into an annualized return on assets of 1.24%. Capital gains realized through security sales accounted for more than 5% of first-half earnings. Downward pressure on core earnings continued; the net interest margin fell to 3.86% at midyear, a drop of 9 basis points (bp) from the end of 2000 and 13 bp lower than the first half of 2000.

Return on equity through 2001:IIQ was 14.31%, compared to 14.07% for 2000. This improvement results from strong earnings performance: The 5 bp increase in ROA over the first half more than offset a slight decrease in leverage; core capital rose from 7.71% of total assets at yearend 2000 to 7.73% at the end of 2001:IIQ.

The economic slowdown of the past 12 months has yet to translate into serious asset quality problems in bank portfolios: Problem assets remained less than 1% of total assets. And, despite a 14 bp increase, net charge-offs remain below the levels experienced in the early 1990s.

While earnings for 2001:IIQ were higher than 2000 yearend numbers, the share of problem banks rose slightly (to 0.98%) in the first half of 2001. The share of banks that are unprofitable also rose slightly (from 7.06% at the end of 2000 to 7.10% at midyear).

Most of these changes in performance indicators are consistent with a strong banking sector, but the latest data are somewhat mixed. There does appear to be continued, albeit minimal, deterioration in asset quality.