FDIC’s DIF Sinks To Negative Territory in Q3′09

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The U.S. government insurance fund, which is used to protect a huge portion of U.S. bank deposits, dropped to a balance of negative $8.2 billion in the third quarter, the FDIC said in its quarterly banking report on Tuesday.

The agency said its deposit insurance fund [DIF] declined by $18.6 billion at the end of September, primarily because of $21.7 billion in additional provisions for bank failures. Given the five-year forecast for bank closures, the fund is looking at an estimated $100 billion in costs. Also, unrealized losses on available-for-sale securities, combined with operating expenses, reduced the fund by $1.1 billion.

This is the second time in the agency’s history that the DIF balance fell into negative territory. At the end of the second quarter, the FDIC’s insurance fund had $10.4 billion. However, the FDIC has access to cash through a plan to have the banking industry prepay three years of assessments. This effort would provide the agency with approximately $45 billion in cash to satisfy its liquidity issues. In addition, the FDIC has also the option to tap a $500 billion line of credit with the Treasury Department.

The agency also said that fifty U.S. bank with combined assets of $68.8 billion failed in the third quarter of 2009, the largest number on record since 55 banks went bust during the second quarter of 1990. According to the report, the list of ‘problem’ banks rose from 416 to 552 during the quarter, and total assets of “problem” institutions jumped from $299.8 billion to $345.9 billion.

Fifty institutions failed during the third quarter, bringing the total number of failures in the first nine months of 2009 to 95.

Despite the turmoil in the industry, banks posted a modest $2.8 billion profit in the third quarter, driven by a recovery in bank securities portfolios. Bank profits were more than triple the $879 million they earned on a year-over-year basis (*last quarter, the industry lost $4.3 billion*). However, loan balances fell by the largest percentage since quarterly reporting began in 1984. Total loan and lease balances declined by $210.4 billion (2.8 percent) during the quarter. C&I loans fell by $89.1 billion (6.5 percent), residential mortgage loan balances declined by $83.7 billion (4.2 percent), and real estate C&D loans dropped by $43.6 billion (8.1 percent).

“Today’s report shows that, while bank and thrift earnings have improved, the effects of the recession continue to be reflected in their financial performance,” FDIC Chairman Sheila Bair said in a statement.

According to Bair, the credit adversity will persist for at least a couple more quarters before we see a meaningful improvement in that trend.

Bair said she was optimistic that if the banking industry addresses its problems head-on, it will see signs of improvement in earnings and lending in 2010.

We should point out that while the DIF’s balance came in negative $8.2 billion, that amount reflects a $38.9 billion contingent loss reserve that has been set aside to cover estimated losses over the next four q’s. Combining the fund balance with this contingent loss reserve shows total DIF reserves green at $30.7 billion.

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