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OCC Reports Second Quarter Trading Revenue of \$7.3 Billion

WASHINGTON — Insured U.S. commercial banks and savings associations reported trading revenue of \$7.3 billion in the second quarter of 2013, \$0.2 billion lower (3 percent) than \$7.5 billion in the first quarter, the Office of the Comptroller of the Currency (OCC) reported today in the *OCC's Quarterly Report on Bank Trading and Derivatives Activities*.

Second quarter trading revenue was \$5.3 billion higher (268 percent) than \$2.0 billion in the second quarter of 2012.

"The decline in trading revenue was not a surprise, given the well-established seasonal pattern," said Kurt Wilhelm, Director of the Financial Markets Group. "What is a bit surprising, however, is how small the decline was." Mr. Wilhelm noted that trading revenue in the second quarter was the second highest of any second quarter, trailing only the \$7.4 billion in 2007. Regarding the seasonal pattern of trading revenue, he noted that it has fallen in the second quarter 11 times since 2000, with an average decline of \$1.3 billion. "There was strong demand for interest rate products, as investors increased their hedging and positioning activity after the Fed stated it may taper its bond purchases."

Credit exposures from derivatives fell in the second quarter. Net current credit exposure (NCCE), the primary metric the OCC uses to measure credit risk in derivatives activities, decreased \$19 billion, or 5 percent, to \$339 billion during the second quarter. "The rise in market interest rates during the second quarter caused a sharp decline in receivables on interest rate contracts," said Mr. Wilhelm, who noted that the gross fair value of interest rate contracts declined \$544 billion, or 16 percent, to \$2.9 trillion. Receivables on all other derivatives contracts increased \$46 billion, resulting in gross derivatives receivables falling by \$498 billion. Regarding credit performance, Mr. Wilhelm noted that charge-offs fell \$22 million during the second quarter to \$61 million. "Charge-offs of derivatives exposures usually result from swaps that are connected to defaulted loans." Mr. Wilhelm also noted some continued slippage in the quality of collateral held against derivatives exposures. "Collateral quality on derivatives exposures is very high, as 77 percent of it is cash. That explains why the charge-off rate on derivatives is so much lower than it is on loans." But, he noted that the percentage of collateral in cash was 81 percent at the end of the first quarter of 2012.

The report shows that the notional amount of derivatives held by insured U.S. commercial banks and savings associations rose \$2.2 trillion, or 1 percent, from the first quarter to \$233.9 trillion, a second consecutive quarterly increase. "The notional increase was due entirely to interest rate contracts," said Mr. Wilhelm, who noted that the \$3.4 trillion increase offsets declines in notionals for other asset classes. "After a long period of very low and stable rates, investors were reintroduced to interest rate risk in the second quarter, when the yield on the 10-year Treasury Note increased 66 basis points."

"Even with two consecutive quarterly increases, notionals have still fallen in five of the past eight quarters," said Mr. Wilhelm, who noted that banks have used trade compression to reduce notionals. Trade compression allows banks to reduce regulatory capital requirements, as well as operating and risk burdens in their derivatives portfolios, by aggregating a large number of trades with similar factors into fewer trades. The notional amount of derivatives peaked at \$249 trillion in the second quarter of 2011.

OCC also reported:

- Banks hold collateral to cover 75 percent of their NCCE. Collateral covers 88 percent of exposure from banks and securities firms, 325 percent of exposure from hedge funds, and 52 percent of exposure from corporates.
- Trading risk exposure, as measured by value-at-risk (VaR), averaged \$376 million across the top five dealer firms during the first quarter of 2013, down \$35 million (9 percent) from \$411 million in the first quarter.
- Derivatives contracts are concentrated in a small number of institutions. The largest four banks hold 93 percent of the total notional amount of derivatives, while the largest 25 banks hold nearly 100 percent.
- Derivative contracts remain concentrated in interest rate products, which represent 81 percent of total derivative notional values. On a product basis, swap products represent 61 percent of total derivatives notionals. Both measures moved 1 percentage point higher compared to the first quarter.
- Credit default swaps are the dominant product in the credit derivatives market, representing 97 percent of total credit derivatives. Credit derivative notionals fell \$519 million, or 4 percent, to \$13.4 trillion.
- The number of insured U.S. commercial banks and savings associations holding derivatives increased to 1,400, up 10 from the prior quarter.

A copy of the *OCC's Quarterly Report on Bank Trading and Derivatives Activities: Second Quarter 2013* is available on the OCC's Web site.

Related Link

- [OCC's Quarterly Report on Bank Trading and Derivatives Activities: Second Quarter 2013 \(PDF\)](#)

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