

An Update on Emerging Issues in Banking

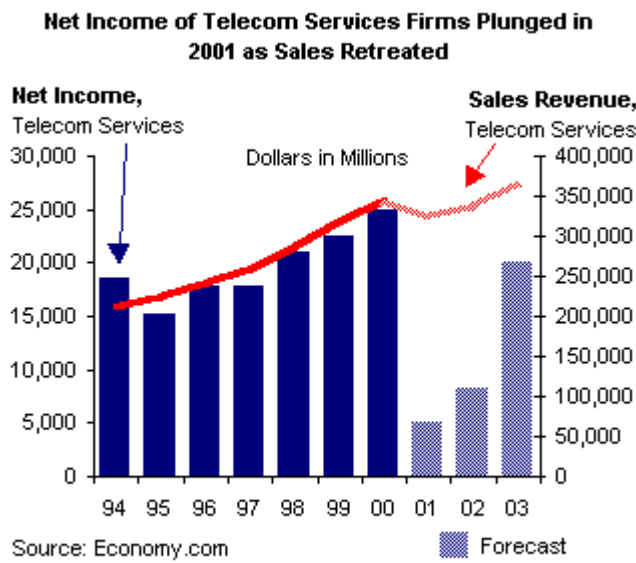
Telecommunications Sector, Bruised and Battered, Looks to a Brighter Future

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Summary

The FDIC actively monitors conditions in the economy and major industry sectors as part of its financial risk management activities. Since the middle of 2000, the telecommunications industry has been shaken by the convergence of several adverse forces, including the U.S. recession, the dot-com collapse, and a sudden scarcity of new capital market financing. An FDIC *Bank Trends* report issued today summarizes current conditions and future prospects in the telecommunications industry.

Chart 1



Commercial banks specialize in the management of credit risks, particularly those associated with commercial loans. Evaluating the prospects for an individual commercial borrower or an industry sector is a highly subjective art, requiring the lender or portfolio manager to gauge current conditions and to look ahead at how conditions may evolve over time. The telecommunications sector presents a particular challenge to lenders and analysts at the present time because current conditions are clearly weak and there is uncertainty over how and when a recovery in the sector may ultimately unfold.

The FDIC carefully follows trends in the general economy and in key industry sectors, and does so with three main goals in mind. First, to the extent that insured institutions have credit exposures to sectors such as telecommunications, the FDIC must incorporate an evaluation of those

exposures into its overall assessment of likely failures among insured institutions over the near term. Second, the FDIC has established processes to continually exchange information between its analysts and bank supervisors so that both can be better informed as to the prospects for the industry and the degree of risk in bank credit portfolios. Finally, the FDIC also communicates directly with lenders and outside industry analysts on emerging trends in the economy and credit portfolios in the belief that frequent dialog leads to better risk management on the part of all concerned.

Today, the FDIC published a *Bank Trends* report by Senior Financial Economist Stephen C. Gabriel that discusses current trends and future prospects in the telecommunications industry. Over the past two years the industry has been battered by forces ranging from a slowing economy and plunging stock prices to a withdrawal of primary sources of capital. The result has been rising credit risk, growing losses, and mounting bankruptcies and defaults. Although the long-term prospects in telecommunications are more encouraging, the more profitable times of the future will have to wait for the current scenario of stress and consolidation to run its course.

For the full *Bank Trends* report, entitled "Telecommunications Sector, Bruised and Battered, Looks to a Brighter Future," go to:
<http://www.fdic.gov/bank/analytical/bank/index.html>

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Chart 1

Net Income of Telecom Services Firms Plunged in 2001 as Sales Retreated

<u>Year</u>	<u>Telecom Services Net Income (Million \$)</u>	<u>Telecom Services Sales Revenue (Million \$)</u>
1994	18,473	213,399
1995	15,241	225,238
1996	17,728	242,040
1997	17,868	259,286
1998	20,921	288,695
1999	22,527	319,437
2000	24,904	346,141
2001F	5,008	325,374
2002F	8,198	338,325
2003F	20,048	368,378

F designates forecast figure.
Source: Economy.com