November 2017

Data for this report were collected Oct. 31– Nov. 8, and 71 financial institutions—10 credit unions and 61 banks—responded.

Over the past six weeks, the Eleventh District financial sector has strengthened but at a slower pace compared with the previous period. Banking leaders indicated that loan volume continued to expand but at a slower pace; loan demand has remained the same over the past six weeks. The loan volume index was 14.0, down from 19.7. The loan demand index fell to 0.0 from 7.0.

The survey suggests that nonperforming loans decreased over the past six weeks overall. Residential real estate lending was the only category surveyed that experienced an increase in nonperforming loans. Loan pricing continued to increase but at a faster pace, with an index of 15.7, up from 13.9. Overall, credit standards and terms continued to tighten; most of this tightening was seen in commercial real estate (CRE) lending. All loan categories experienced tightening with the exception of residential real estate and consumer loans, with respondents suggesting that standards and terms have remained the same for these areas. General business activity expanded over the past six weeks but at a much faster rate compared with the previous period, with a reading of 21.4, up from 8.7.

The gains in loan volume were driven by CRE and commercial and industrial (C&I) loans. CRE loan volume continued to increase but at a slower rate, with an index of 10.8, down from 21.5. For C&I loans, loan volume increased and at a faster pace, moving from an index value of 3.0 to 6.2. Consumer loans were the only loan class that experienced a decrease in loan volume over the past six weeks.

Core deposit volumes continued to expand over the past six weeks. Cost of funds also increased and at a quicker rate, up to 45.7 from 39.4. According to the respondents, net interest margins have increased compared with the previous period. Noninterest income declined over the past six weeks, with an index reading of –4.3, down from 11.4.

The outlook for the Eleventh District financial sector is slightly more optimistic. Expectations for total loan demand points to expansion but at a slower rate compared with the previous period, and nonperforming loans are still expected to decline six months from now, but at a slower pace. Expectations for general business activity, however, were very optimistic, with an index value of 52.2, up from 30.4.

Next Release: January 17, 2018

The Federal Reserve Bank of Dallas conducts the Banking Conditions Survey twice each quarter to obtain a timely assessment of activity at banks and credit unions headquartered in the Eleventh Federal Reserve District. CEOs or senior loan officers of financial institutions report on how conditions have changed for indicators such as various loan types, deposits and loan pricings. Respondents are also asked to report on their banking outlook and how they perceive broader economic conditions to have changed (general business activity).

The answers serve a dual function: They provide supplemental anecdotal information for the Eleventh District Beige Book and supply timely information on banking conditions in preparation for monetary policy deliberations before the eight Federal Open Market Committee meetings each year.

Participants are asked whether they are seeing changes in a series of indicators. In addition, participants are given the opportunity to submit comments on current issues that may be affecting their business.

Survey responses are used to calculate an index for each indicator. Each index is calculated by subtracting the percentage of respondents reporting a decrease (or tightening or worsening) from the percentage reporting an increase (or easing or improvement). When the share of firms reporting an increase exceeds the share of firms reporting a decrease, the index will be greater than zero, suggesting the indicator has increased over the prior reporting period. If the share of firms reporting a decrease exceeds the share reporting an increase, the index will be below zero, suggesting the indicator has decreased over the prior reporting period. An index will be zero when the number of firms reporting an increase is equal to the number reporting a decrease. Note: Percentages may not add to 100 due to rounding.

1. Total loans: Over the past six weeks, how have the following changed?

Indicator	Current index	Previous index	Percent reporting increased	Percent reporting no change	Percent reporting decreased
Loan volume	14.0	19.7	39.4	35.2	25.4
Loan demand	0.0	7.0	31.0	38.0	31.0
Nonperforming loans	–8.9	0.0	9.0	73.1	17.9
Loan pricing	15.7	13.9	21.4	72.9	5.7

Indicator	Current index	Previous index	Percent reporting eased	Percent reporting no change	Percent reporting tightened
Credit standards and terms	–1.7	–6.3	4.8	72.9	6.5

2. Commercial and industrial loans: Over the past six weeks, how have the following changed?

Indicator	Current index	Previous index	Percent reporting increased	Percent reporting no change	Percent reporting decreased
Loan volume	6.2	3.0	23.1	60.0	16.9
Nonperforming loans	–6.7	–6.4	5.0	83.3	11.7

Indicator	Current index	Previous index	Percent reporting eased	Percent reporting no change	Percent reporting tightened
Credit standards and terms	–3.3	–7.8	3.2	90.3	6.5

3. Commercial real estate loans: Over the past six weeks, how have the following changed?

Indicator	Current index	Previous index	Percent reporting increased	Percent reporting no change	Percent reporting decreased
Loan volume	10.8	21.5	30.8	49.2	20.0
Nonperforming loans	–6.8	–12.9	3.4	86.4	10.2

Indicator	Current index	Previous index	Percent reporting eased	Percent reporting no change	Percent reporting tightened
Credit standards and terms	–6.7	–12.5	3.3	86.7	10.0

4. Residential real estate loans: Over the past six weeks, how have the following changed?

Indicator	Current index	Previous index	Percent reporting increased	Percent reporting no change	Percent reporting decreased
Loan volume	1.6	11.5	25.4	50.8	23.8
Nonperforming loans	1.8	–1.7	3.6	94.6	1.8

Indicator	Current index	Previous index	Percent reporting eased	Percent reporting no change	Percent reporting tightened
Credit standards and terms	0.0	–8.2	4.8	90.3	4.8

5. Consumer loans: Over the past six weeks, how have the following changed?

Indicator	Current index	Previous index	Percent reporting increased	Percent reporting no change	Percent reporting decreased
Loan volume	–3.0	–6.0	16.4	64.2	19.4
Nonperforming loans	–1.6	3.0	3.3	91.8	4.9

Indicator	Current index	Previous index	Percent reporting eased	Percent reporting no change	Percent reporting tightened
Credit standards and terms	0.0	–6.1	3.0	93.9	3.0

6. Other banking developments: Over the past six weeks, how have the following changed?

Indicator	Current index	Previous index	Percent reporting increased	Percent reporting no change	Percent reporting decreased
Volume of core deposits	32.9	21.1	44.3	44.3	11.4
Cost of funds	45.7	39.4	47.1	51.4	1.4
Net interest margin	11.5	0.0	22.9	65.7	11.4
Noninterest income	–4.3	11.4	10.0	75.7	14.3

7. Banking outlook: What is your expectation for the following items six months from now?

Indicator	Current index	Previous index	Percent reporting better	Percent reporting no change	Percent reporting worse
Total loan demand	31.9	38.9	42.0	47.8	10.1

Indicator	Current index	Previous index	Percent reporting more	Percent reporting no change	Percent reporting fewer
Nonperforming loans	–14.5	–16.7	10.1	65.2	24.6

8. General business activity: What is your evaluation of the level of activity?

Indicator	Current index	Previous index	Percent reporting improved	Percent reporting no change	Percent reporting worsened
Over the past six weeks	21.4	8.7	34.3	52.9	12.9
Six months from now	52.2	30.4	56.7	38.8	4.5

9. Issues of concern: Please feel free to comment on any issue that may be affecting your business.

These comments are from respondents' completed surveys and have been edited for publication.

- Following the aftermath of Hurricane Harvey, our expectation was to have potential losses in real estate and some commercial business. We have extended and deferred a number of payments for these customers; however, we have not recognized any measurable loss to the loan portfolio. There may be losses as a result of the hurricane; however, they have not been identified at this time. Based on conversations with other bankers in the Houston market, we all seem to share the same position. We also anticipate an uptick in loan demand related to storm damage.

- I am concerned about the regulatory guidance limitations on construction and development loans when these loans are the main source of loan opportunities for community banks and are underwritten with prudent and conservative credit requirements.

- We still struggle with unnecessary regulatory burdens, especially being a small institution. Consumer Financial Protection Bureau overreach and the current expected credit loss replacement of a "just fine" allowance for loan and lease losses program are just more government intervention and control that is totally unneeded.

- Regulatory burden is still weighing heavy on community bank resources. The promise to reduce regulatory burden coming from Washington appears to be put on hold as other topics such as tax reform take center stage. Coming up on one year of the new administration being in office has some positives but mostly results in frustration to get any sweeping reforms done. Daily back and forth about whether something will be passed makes it difficult to judge the outlook for the next year. We are finding it difficult to retain young talent who want to start their career in banking or join our organization. This is especially true in the areas of information technology and compliance. Management succession planning is difficult and is on the minds of senior management. Bankers have to deal with so many audits and examinations that real meaningful customer relationships are being hurt. To stay in compliance, the bank must either hire additional resources due to workload or provide additional training, both of which increase expenses and hurt our bottom line. We recently have seen an influx of deposits; however, they appear to be noncore in nature. Liquidity is improving. With the Fed most likely increasing rates another 25 basis points in December, we will need to seriously consider raising deposit rates. We have seen a few of our competitors already start to raise rates.

- Failure of Congress to pass meaningful tax reform will likely have a significant negative effect on general business activity, loan demand and equity valuations.

- We are still dealing with aftereffects of Hurricane Harvey and associated flooding. Deposit flows have been huge for this time of year due to insurance and disaster recovery proceeds. Consumer loans have also been in demand especially for replacement automobiles and smaller consumer loans for immediate living needs, alternative living quarters, repairs to homes that were not a total loss or were uninsured and so forth. Expenses continue to rise in general. Regulations have held back recovery relief even more than they would in normal times. We have a few members complaining about steps we took to alleviate pressure on most of our members such as deferring loan payments, no-fee ATM usage, etc.

- Cybersecurity—constantly worrying about it. Small banks need regulatory relief soon.

- The heated commercial real estate market, especially retail, in Plano, McKinney and Allen is concerning.

- General business activity will depend on the outcome of tax reform, if any.

- Continuing improvement in the overall economy and in our market area will continue to depend upon the price of crude oil.

- Continue to be concerned about compliance—Fair Lending and Community Reinvestment Act.

- We continue to be concerned by increased compliance costs.

- We are concerned about the next Federal Reserve rate increase expected in December.