Banking Conditions Survey

Federal Reserve Bank of Dallas

January 2018

Data for this report were collected Dec. 19–27, and 67 financial institutions—13 credit unions and 54 banks—responded.

Over the past six weeks, the Eleventh District financial sector has strengthened and at a faster pace compared with the previous period. Banking leaders indicated that both loan volume and loan demand continued to expand and at a faster pace over the past six weeks. The loan volume index was 20.9, up from 14.0. The loan demand index moved up to 13.6 from 0.0.

While the survey suggests that nonperforming loans decreased over the past six weeks overall, commercial and industrial (C&I) loans as well as consumer loans experienced an increase in nonperforming loans over the past six weeks. Loan pricing continued to increase but at a faster pace, with an index of 28.1, up from 15.7. Overall, credit standards and terms continued to tighten, with most of the tightening being seen in C&I and commercial real estate (CRE) loans. General business activity expanded over the past six weeks and at a faster rate compared with the previous period, with a reading of 34.9, up from 21.4.

The gains in loan volume were driven by CRE and residential real estate loans. CRE loan volume continued to increase but at a faster rate, with an index of 17.3, up from 10.8. For residential real estate loans, loan volume increased at a much faster pace, from an index value of 1.6 to 28.1.

Core deposit volumes continued to expand over the past six weeks. Cost of funds also increased and at a quicker rate, up to 49.2 from 45.7. According to the respondents, net interest margins have increased compared with the previous period. Noninterest income increased over the past six weeks, with an index reading of 3.1, up from –4.3.

The outlook for the Eleventh District financial sector is more optimistic compared with sentiments six weeks ago. Expectations for total loan demand point to expansion and at a much faster rate compared with the previous period; nonperforming loans are still expected to decline six months from now and at a quicker pace. Expectations for general business activity remain very optimistic, with an index value of 62.5, up from 52.2.

Next Release: March 7, 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	20.9	14.0	41.8	37.3	20.9
Loan demand	13.6	0.0	31.8	50.0	18.2
Nonperforming loans	–3.1	–8.9	16.9	63.1	20.0
Loan pricing	28.1	15.7	32.8	62.5	4.7

Indicator	Current index	Previous index	Percent reporting eased	Percent reporting no change	Percent reporting tightened
Credit standards and terms	–11.1	–1.7	1.6	85.7	12.7

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	7.0	6.2	22.8	61.4	15.8
Nonperforming loans	1.8	–6.7	8.9	83.9	7.1

Indicator	Current index	Previous index	Percent reporting eased	Percent reporting no change	Percent reporting tightened
Credit standards and terms	–10.5	–3.3	0.0	89.5	10.5

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	17.3	10.8	34.5	48.3	17.2
Nonperforming loans	–9.1	–6.8	3.6	83.6	12.7

Indicator	Current index	Previous index	Percent reporting eased	Percent reporting no change	Percent reporting tightened
Credit standards and terms	–12.3	–6.7	0.0	87.7	12.3

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	28.1	1.6	42.1	43.9	14.0
Nonperforming loans	–1.9	1.8	7.4	83.3	9.3

Indicator	Current index	Previous index	Percent reporting eased	Percent reporting no change	Percent reporting tightened
Credit standards and terms	–8.9	0.0	0.0	91.1	8.9

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	8.2	–3.0	21.3	65.6	13.1
Nonperforming loans	5.0	–1.6	10.0	85.0	5.0

Indicator	Current index	Previous index	Percent reporting eased	Percent reporting no change	Percent reporting tightened
Credit standards and terms	–6.6	0.0	1.7	90.0	8.3

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	38.9	32.9	49.3	40.3	10.4
Cost of funds	49.2	45.7	50.7	47.8	1.5
Net interest margin	12.0	11.5	26.9	58.2	14.9
Noninterest income	3.1	–4.3	12.5	78.1	9.4

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	61.2	31.9	65.7	29.9	4.5

Indicator	Current index	Previous index	Percent reporting more	Percent reporting no change	Percent reporting fewer
Nonperforming loans	–20.9	–14.5	9.0	61.2	29.9

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	34.9	21.4	39.4	56.1	4.5
Six months from now	62.5	52.2	62.5	37.5	0.0

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.

- 1. Consumer compliance regulations are a significant burden and not accomplishing their intent of helping consumers. 2. Ag commodity prices are causing significant consolidation in our market.
- A bit worried about the residential real estate market because the cost of new homes has increased so rapidly. The new tax plan is a variable that may spur some changes (up or down) in our loan demand from small-business customers.
- Although deposit rates remain competitive, deposit growth continues to be sluggish primarily due to a strong equities/stock market. Furthermore, an inverted yield curve appears to be on the horizon, which may be a precursor to a recession.
- As a company that pays taxes, our growing competition with the credit unions is beginning to affect our business. Their tax advantage along with their very liberal terms and interest rates are something that we just cannot compete with. Example: A consumer came into our bank with a nine-month-old delinquent credit union mortgage loan asking for a loan to "catch them up" on their mortgage payments—a nine-month-old past due loan and the credit union had not taken steps to collect the loan. Interesting credit standards are given by credit unions.
- Compliance and regulations are extreme and will soon cause more consolidation of community banks into megabanks.
- Concerns continue to be with compliance.
- Do not yet know if new 1/4 percent Fed rate increase will have impact on our financial institution.
- No current economic issues in addition to others mentioned in the past. Still dealing with Hurricane Harvey aftermath and related consequences for homeowners and business owners. Homes for sale inventory continues to decline to around three months. Christmas sales appear to have gone well, and employment is doing well. There are concerns for next year around availability of good staff; we've been fortunate to this point, but there are clearly fewer well-qualified individuals available. Also, there is the cost of keeping up with tech and advances in our industry across a broad spectrum of activities, technology, productivity enhancements and so forth.
- Regulatory burdens are affecting our business.
- Regulatory intrusions make operations and lending very difficult.
- So happy to have a president who understands the harm of government overreach and the burden of excessive regulations. Now, if politicians would become citizen advocates instead of "self" advocates, we might be able to get some work done in Washington that

would make this country great again; at least for now we appear to be on the right track despite all the hateful, negative push from the left.

- We are expecting an increase in general business activity as a result of the revision of the tax code. We have given employee bonuses and salary increases as a result. We expect this change to have a significant increase in the business environment. On the negative side, credit unions continue to loom as a large threat to the existence of community banks. Regulatory concerns have mitigated somewhat as a result of the Trump administration's order regarding the issuance of additional regulations.
- We have received some positive comments from a number of our corporate clients regarding the recently passed tax cuts and jobs act. These comments include paying higher salaries to employees as well as making additional capital expenditures. The results of this tax reform should be recognized at least by the second half of 2018. Other than what's expressed in the media, there seems to be a lot of buzz in the business community regarding this reduction in taxes.
- With the Fed continuing to tighten, we are preparing to start slowly increasing rates in 2018. Some of our competitors have started raising rates on deposit products, particularly CDs. We hope to start seeing some higher yields offered for municipal and mortgage-backed investments in 2018. Regulatory issues continue to weigh on the minds of the board and senior management. Costs that are incurred to stay in compliance are high, whether that is through additional personnel or external audits. Also, IT-related costs for additional equipment, continued IT operations or replacement of outdated equipment are high and increasing each year.

  With the potential for relaxed regulation oversight, we will be able to better serve our members.