March 2018

Data for this report were collected Feb. 6–14, and 69 financial institutions—10 credit unions and 59 banks—responded.

Over the past six weeks, the Eleventh District financial sector has strengthened but at a slower rate compared with the previous period. Banking leaders indicated that both loan volume and loan demand continued to expand but at a slower pace over the past six weeks. The loan volume index was 13.3, down from 20.9. The loan demand index moved down to 5.9 from 13.6.

While the survey suggests that nonperforming loans decreased over the past six weeks overall, residential real estate loans as well as consumer loans experienced an increase in nonperforming loans over the past six weeks. Loan pricing continued to increase and at a faster pace, with an index of 39.4, up from 28.1. Overall, credit standards and terms continued to tighten, with most of the tightening being seen in consumer, commercial and industrial (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 37.7, up from 34.9.

The gains in loan volume were driven by CRE and residential real estate loans. CRE loan volume continued to increase but at a slower rate, with an index of 10.9, down from 17.3. For residential real estate loans, loan volume increased but at a slower pace, from an index value of 28.1 to 17.3.

Core deposit volumes continued to expand over the past six weeks, but at a slower pace. Cost of funds also increased and at a much quicker rate, up to 65.3 from 49.2. According to the respondents, net interest margins have continued to increase, but at a slower pace. Noninterest income increased over the past six weeks, with an index reading of 5.8, up from 3.1.

The outlook for the Eleventh District financial sector is slightly less optimistic compared with sentiments six weeks ago. Expectations for total loan demand point to expansion but at a slower rate compared with the previous period; nonperforming loans are still expected to decline six months from now but also at a slower pace. Expectations for general business activity are still optimistic, with an index value of 59.5, slightly down from 62.5.

Next Release: April 18, 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	13.3	20.9	41.2	30.9	27.9
Loan demand	5.9	13.6	30.9	44.1	25.0
Nonperforming loans	–4.7	–3.1	10.9	73.4	15.6
Loan pricing	39.4	28.1	42.4	54.5	3.0

Indicator	Current index	Previous index	Percent reporting eased	Percent reporting no change	Percent reporting tightened
Credit standards and terms	–12.1	–11.1	1.5	84.8	13.6

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	4.8	7.0	23.8	57.1	19.0
Nonperforming loans	–5.1	1.8	1.7	91.5	6.8

Indicator	Current index	Previous index	Percent reporting eased	Percent reporting no change	Percent reporting tightened
Credit standards and terms	–8.1	–10.5	1.6	88.7	9.7

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	10.9	17.3	32.8	45.3	21.9
Nonperforming loans	–8.5	–9.1	0.0	91.5	8.5

Indicator	Current index	Previous index	Percent reporting eased	Percent reporting no change	Percent reporting tightened
Credit standards and terms	–7.8	–12.3	3.1	85.9	10.9

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	17.3	28.1	39.7	37.9	22.4
Nonperforming loans	1.8	–1.9	3.7	94.4	1.9

Indicator	Current index	Previous index	Percent reporting eased	Percent reporting no change	Percent reporting tightened
Credit standards and terms	–3.4	–8.9	0.0	96.6	3.4

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	1.6	8.2	18.5	64.6	16.9
Nonperforming loans	6.6	5.0	8.3	90.0	1.7

Indicator	Current index	Previous index	Percent reporting eased	Percent reporting no change	Percent reporting tightened
Credit standards and terms	–9.7	–6.6	0.0	90.3	9.7

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	11.6	38.9	31.9	47.8	20.3
Cost of funds	65.3	49.2	66.7	31.9	1.4
Net interest margin	7.3	12.0	31.9	43.5	24.6
Noninterest income	5.8	3.1	13.2	79.4	7.4

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	52.2	61.2	59.4	33.3	7.2

Indicator	Current index	Previous index	Percent reporting more	Percent reporting no change	Percent reporting fewer
Nonperforming loans	–14.5	–20.9	5.8	73.9	20.3

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	37.7	34.9	39.1	59.4	1.4
Six months from now	59.5	62.5	63.8	31.9	4.3

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.

- I am concerned that the flat yield curve could lower net interest margins.
- Significant consolidation in the local agricultural markets should continue for the next several years.
- Compliance issues and regulations continue to be a great burden on community banks.
- We are specifically concerned about inflation and the market reaction to future rate increases.
- Items of concern are government regulations and competition from credit unions.
- The continued rancor in Washington, D.C., is beginning to cast a cloud on businesses, business expansion and the general business mood. It seems as if customers are pulling in expansion plans due to government instability.
- Volatility in publicly traded equity markets is likely to negatively impact business and consumer confidence and may serve to reduce business investment and, consequently, loan demand in the near term.
- Nothing major at this time. Still feeling aftereffects of Hurricane Harvey. Starting to see some of the huge dollars moving out of the institution to pay contractors, vendors, suppliers, etc. Savings are down slightly but not as much as usually experienced this time of year. Lending volume is also off a bit but, again, nothing too weird for this time of year. Do have concerns about the lawyers having a field day suing financial institutions for items mentioned by the Consumer Financial Protection Bureau such as Americans with Disabilities Act compliance, payday lending, overdraft programs and so on. Also, the inability of our governmental organizations to get a handle on cybercrimes and breaches or to punish offenders is troubling. Cybersecurity is probably the biggest risk we face and the losses associated with it. Finally, the card fraud taking place with no responsibility placed on vendors and merchants is taking a toll. This issue will only be resolved when the merchants pay the full freight on card fraud instead of dumping it all on financial institutions.
- Increased volatility in the stock market could have a spillover effect on business confidence.
- I am concerned with additional expenses incurred due to additional outside audits and reviews prescribed by regulators.
- Regulatory issues are a top concern.
- Washington appears to finally have made some progress on some issues that have been hanging over its head. It is nice to see tax reform being passed and businesses being able to forecast for the future. Of major concern is the Fed's proposed three rate

hikes by the end of 2018. The Fed appears to be much more aggressive than markets want to tolerate, and while the unemployment rate is low, inflation is hardly budging. Bond yields are on the rise, and while municipal metrics still appear strong, refunding of obligations will cost more. We are experiencing some difficulty in hiring young talent in our market who will stay at the bank for several years. This is particularly true in the areas of compliance and IT.

- We are experiencing a large number of longtime members facing difficulties causing losses in 2017, and we expect this will continue until the end of second quarter 2018. We do see it easing beginning third quarter 2018, but that is just an educated guess. It is affecting our bottom line. We are very grateful for the regulatory relief from the Trump administration!