Federal Reserve Bank of Dallas

July 2018

Data for this report were collected June 19–27, and 73 financial institutions—12 credit unions and 61 banks—responded.

Over the past six weeks, the Eleventh District financial sector has continued to strengthen but at a moderately slower rate compared with the previous period. While the loan demand index moved up slightly to 32.8 from 30.3, the loan volume index was 34.3, down from 40.3.

Survey respondents suggest that the index of nonperforming loans decreased but at a slower pace over the past six weeks overall, with most of the decline seen in commercial real estate (CRE) loans. Loan pricing increased at a faster pace, with the index at 63.1, up from 43.1. Overall, credit standards and terms continue to tighten, mostly in commercial and industrial and CRE loans. General business activity has expanded over the past six weeks but at a slower rate than in the previous period, with a reading of 45.2, down from 55.2.

Increases in loan volume were seen across all loan categories, but only CRE and consumer loan volumes expanded at an increasing rate compared with last period. All other loan categories experienced growing loan volumes but at a decreasing rate.

According to respondents, the indexes of core deposit volumes, cost of funds, net interest margin and noninterest income have all continued to grow over the past six weeks, but only cost of funds is expanding at a quicker pace, with an index reading of 87.7 versus 71.2 the previous period.

The outlook for the Eleventh District financial sector is slightly less optimistic than it was six weeks ago. While expectations for total loan demand six months from now pointed to continued expansion at approximately the same rate projected last period, nonperforming loans were expected to continue declining but at a quicker pace. Expectations for general business activity were also slightly less optimistic, with an index value of 38.3, down from 53.0.

Next Release: Sept. 12, 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	34.3	40.3	54.8	24.7	20.5
Loan demand	32.8	30.3	47.9	37.0	15.1
Nonperforming loans	–5.7	–6.4	14.3	65.7	20.0
Loan pricing	63.1	43.1	65.8	31.5	2.7

Indicator	Current index	Previous index	Percent reporting eased	Percent reporting no change	Percent reporting tightened
Credit standards and terms	–13.7	–6.2	1.5	83.3	15.2

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	13.9	25.8	30.8	52.3	16.9
Nonperforming loans	–8.0	0.0	7.9	76.2	15.9

Indicator	Current index	Previous index	Percent reporting eased	Percent reporting no change	Percent reporting tightened
Credit standards and terms	–12.1	–6.5	0.0	87.9	12.1

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	35.9	32.3	49.3	37.3	13.4
Nonperforming loans	–14.0	0.0	1.6	82.8	15.6

Indicator	Current index	Previous index	Percent reporting eased	Percent reporting no change	Percent reporting tightened
Credit standards and terms	–14.9	–6.5	3.0	79.1	17.9

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	31.3	39.7	39.1	53.1	7.8
Nonperforming loans	–4.9	1.9	3.3	88.5	8.2

Indicator	Current index	Previous index	Percent reporting eased	Percent reporting no change	Percent reporting tightened
Credit standards and terms	–7.9	0.0	0.0	92.1	7.9

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	7.0	3.1	21.1	64.8	14.1
Nonperforming loans	–2.9	–12.9	7.2	82.6	10.1

Indicator	Current index	Previous index	Percent reporting eased	Percent reporting no change	Percent reporting tightened
Credit standards and terms	–2.8	–3.1	1.4	94.4	4.2

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	1.4	6.0	27.4	46.6	26.0
Cost of funds	87.7	71.2	87.7	12.3	0.0
Net interest margin	6.8	21.5	34.2	38.4	27.4
Noninterest income	15.3	15.1	23.6	68.1	8.3

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	46.6	47.0	54.8	37.0	8.2

Indicator	Current index	Previous index	Percent reporting more	Percent reporting no change	Percent reporting fewer
Nonperforming loans	–26.0	–19.7	5.5	63.0	31.5

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	45.2	55.2	47.9	49.3	2.7
Six months from now	38.3	53.0	49.3	39.7	11.0

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.

- The Bank Secrecy Act seems to be getting more burdensome and more costly to the bank and, therefore, our customers as we have to pass that cost on to them.
- Current expected credit loss continues to be an unnecessary burden, especially for small institutions with minimal delinquencies/charge-offs.
- Confusion exists regarding Home Mortgage Disclosure Act reporting rules for small banks. Are the rules in place on Jan. 1, 2018, still in place today after S.2155 [new regulatory relief legislation]?
- We continue to be very concerned about the TRID [financing disclosure] requirements for our bank. We get conflicting information from regulators and auditors. We do only a few each month in our small market. These regs are unproductive, do not protect the consumer and make the process unreasonably difficult.
- We are concerned with continued compliance requirements.
- Deposits will continue to be a challenge for all community bankers. Competition is picking up in regard to pricing. Commercial businesses are using their cash for working capital and capital investments. At the moment, depositors are sensitive to rate increases and will move for higher rates through various sources, whether it be another competitor, the internet or other financial depository sources.
- A flattening yield curve and ultimately an inverted yield curve will place pressure on the balance sheet when seeking loan alternatives, such as short-term investments. This will be more of a concern if loan demand and volume begin to decline over the next six to 12 months.
- We are concerned with gathering deposits.
- I don't have any particular concerns right now. The eventual increase in street rates for loans and deposits will eventually affect us, but we tend to fare well in periods of rising rates with only a short delay, so it is not a concern.
- Interest rates are very competitive in the marketplace. We find commercial banks still willing to fix rates for up to five years. We have moved more toward floating-rate and two- to three-year adjustables.
- It is discouraging to see nonbank/fintech [financial technology] entities employing "backdoor arrangements" to engage in banking activities without regulatory supervision/scrutiny by the bank regulatory agencies.
- We are currently concerned about lack of deposit growth to keep up with loan demand.
- We are concerned about potential pressure on net Interest margin due to flattening of the yield curve.

- Real estate prices seem to be increasing at a fairly rapid rate.
- We’re still concerned about increasing costs of regulation and the cost of combating risks of cybercrime.
- We are seeing an increase among institutions that are raising deposit interest rates to compete for deposits. Particularly in the realm of certificates of deposit, consumers are watching rates and moving funds to the best available rate they can find, regardless of previous relationships with the institution. Also, it seems as though we continue to struggle keeping up with compliance. Multiple audits and exams in a given year make it difficult for our institution to gather all necessary materials while also trying to focus on the customer.
- We are tightening credit standards and reducing loan volumes as we prepare our company for a recession—we are using 2020 as our time frame, so we’re making appropriate tightening now as well as looking at each borrower to assess “recession survivability.”
- We continue to have concerns about cybersecurity.
- We have a genuine concern that operational costs will significantly increase over time when compared to revenue-enhancement opportunities. This will eventually lead to bank consolidations and the elimination of small community banks. This may be the ultimate goal of our government, or more likely, an unintended consequence of “one-size-fits-all” banking laws and regulations.
- We are concerned that the yield curve could go inverted.