October 2018

Data for this report were collected Sept. 25–Oct. 3, and 69 financial institutions responded.

Over the past six weeks, the Eleventh District financial sector has continued to strengthen but at a slower pace compared with the previous period. The loan demand index moved down slightly to 32.3 from 33.3, and the loan volume index was 30.4, down from 38.3.

Survey respondents suggest that nonperforming loans decreased over the past six weeks but at a much slower rate. Loan pricing increased at a faster pace, with the index at 50.7, up from 46.7. Overall, credit standards and terms continue to tighten, mostly in commercial and industrial and commercial real estate (CRE) loans. Survey respondents indicated that general business activity has expanded over the past six weeks but at a slower rate than the previous period, with a reading of 39.1, down from 48.4.

Increases in loan volume were seen across all categories, but the overall increase in loan volume was mainly driven by gains in CRE and residential real estate loans. Consumer loans were the only loan category that experienced gains at an increasing clip. All other categories grew at a decreasing rate.

According to respondents, the indexes of core deposit volumes and net interest margins point to expansion but at a slower pace over the last six weeks. Cost of funds and noninterest income have all continued to grow as well over the past six weeks but at a faster rate, according to survey respondents.

The outlook for the Eleventh District financial sector is slightly less optimistic than it was six weeks ago. Expectations for total loan demand and general business activity six months from now are pointing toward continued expansion but at a slower rate. Nonperforming loans are expected to continue declining over the next six months but at a decreasing rate.

Next Release: Dec. 5, 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	30.4	38.3	47.8	34.8	17.4
Loan demand	32.3	33.3	44.1	44.1	11.8
Nonperforming loans	–1.5	–17.8	12.3	73.8	13.8
Loan pricing	50.7	46.7	53.7	43.3	3.0

Indicator	Current index	Previous index	Percent reporting eased	Percent reporting no change	Percent reporting tightened
Credit standards and terms	–12.5	–9.4	1.6	84.4	14.1

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	9.9	26.7	23.0	63.9	13.1
Nonperforming loans	–3.4	–9.8	6.8	83.1	10.2

Indicator	Current index	Previous index	Percent reporting eased	Percent reporting no change	Percent reporting tightened
Credit standards and terms	–12.3	–10.5	0.0	87.7	12.3

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	26.2	32.1	41.0	44.3	14.8
Nonperforming loans	–1.7	–15.1	5.1	88.1	6.8

Indicator	Current index	Previous index	Percent reporting eased	Percent reporting no change	Percent reporting tightened
Credit standards and terms	–14.8	–7.3	0.0	85.2	14.8

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	16.6	34.0	28.3	60.0	11.7
Nonperforming loans	0.0	–8.2	3.4	93.1	3.4

Indicator	Current index	Previous index	Percent reporting eased	Percent reporting no change	Percent reporting tightened
Credit standards and terms	–1.7	–1.9	1.7	94.9	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	7.5	1.8	22.4	62.7	14.9
Nonperforming loans	–1.5	–9.2	6.2	86.2	7.7

Indicator	Current index	Previous index	Percent reporting eased	Percent reporting no change	Percent reporting tightened
Credit standards and terms	–3.1	–5.6	3.0	90.9	6.1

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	15.9	25.5	39.1	37.7	23.2
Cost of funds	87.0	86.4	88.4	10.1	1.4
Net interest margin	5.8	20.4	30.4	44.9	24.6
Noninterest income	11.7	8.5	17.6	76.5	5.9

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	36.8	55.0	41.2	54.4	4.4

Indicator	Current index	Previous index	Percent reporting more	Percent reporting no change	Percent reporting fewer
Nonperforming loans	–8.8	–11.8	10.3	70.6	19.1

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	39.1	48.4	39.1	60.9	0.0
Six months from now	36.7	40.7	44.1	48.5	7.4

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.

- We are seeing very isolated increases in nonperforming loans and slower loan growth, but we are still positive.
- Competition for deposits is increasing substantially and, accordingly, interest rates on deposits are going up.
- We are concerned about the cost of deposits. The traditional definition of "core deposits" does not match new market realities. FDIC national rate cap methodology does not reflect reality/true prevailing market rate. There is an uneven playing field between community banks and fintech—no direct federal oversight of fintech, much looser consumer protection enforcement on fintech, little to no monitoring of fintech marketing (direct, affiliate and influencer channels). Community banks that want to innovate are held to much higher standards and requirements than fintech companies while serving the same end consumer with substantially similar products and services. Innovation inside an insured financial institution is contrary to much of the current federal regulatory oversight paradigm.
- Future business activity and loan demand are heavily dependent upon the price of crude oil remaining in the $60 to $70 per barrel range.
- I hope political issues do not get in the way of good business but am very proud our president is standing up for our country.
- We are concerned about irrational deposit pricing by banks with excessive loan-to-deposit ratios.
- Liquidity and costs of funding continue to be a primary focus of our institution.
- Mid-term election outcomes, trade wars and increases in the federal funds rate are factors that are contributing to an uncertain environment.
- Our bank is located in a growing market north of DFW. We are seeing an increase in both residential and some commercial real estate loans due to the continued price increases especially in Grayson and Collin counties. Also, the first lake to be built in Texas in over 30 years, Bois d'arc Lake, is being built by the North Texas Municipal Water District to serve Fannin, Collin and Rockwall counties. This event will have a major economic impact on Fannin County. The lake is to be completed by 2021.
- Our customers are optimistic about the economy.
- The competition for talent is a growing concern along with the lack of management succession.
- Uncertainty associated with trade relations and tarriffs has proven to be somewhat of a drag on business activity. Announcement of a tri-party agreement to replace NAFTA

(North American Free Trade Agreement) is positive, but business decision-makers will be cautious until the understanding is voted into law. The tri-party agreement is especially important to Texas, but for the country as a whole, it will be important to come to some resolution with China. Rising interest rates are already starting to create a drag on residential real estate. That business continues to be relatively strong, but as the Fed continues to push rates higher, the impact on home sales will become more pronounced. Resolution of trade concerns would likely prove to be a huge positive for equity markets that may be on shaky ground with current valuations without the benefit of incremental good news for business. Were the stock markets to falter, the impact on sentiment and business optimism could prove significantly negative for both consumer and business investment moving into 2019.

- We are seeing continued competition from surrounding institutions for deposits. Costs of funds seem to be slowly climbing, but adjustments are being made to new loan rates to keep our margin in line. Keeping pace with IT infrastructure changes to ensure our institution is competitive will be key when planning our budget for 2019.