December 2018

Data for this report were collected Nov. 6–Nov. 14, and 67 financial institutions—11 credit unions and 56 banks—responded.

Over the past six weeks, the Eleventh District financial sector has shown some mixed signals. According to respondents, loan volume continued to increase, but at a slower pace, with the index moving from 30.4 to 20.9. Loan demand, however, declined over the past six weeks, falling from an index of 32.3 to –1.5.

Survey respondents suggest that nonperforming loans decreased over the past six weeks. Loan pricing increased, with the index at 50, slightly down from 50.7. Overall, credit standards and terms tightened, 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 23.9, down from 39.1.

Increases in loan volume were seen across all categories, but the overall rise in loan volume was mainly driven by gains in CRE lending. 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, cost of funds and noninterest income all point to expansion but at a slower pace over the last six weeks. Net interest margins, however, declined, moving from an index of 5.8 to –3.0.

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 pace. Nonperforming loans are also expected to continue declining over the next six months and at an increasing rate.

Next Release: Jan. 16, 2019

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	30.4	43.3	34.3	22.4
Loan demand	−1.5	32.3	30.3	37.9	31.8
Nonperforming loans	−8.0	−1.5	6.5	79.0	14.5
Loan pricing	50.0	50.7	56.1	37.9	6.1

Indicator	Current index	Previous index	Percent reporting eased	Percent reporting no change	Percent reporting tightened
Credit standards and terms	−11.5	−12.5	1.6	85.2	13.1

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	3.3	9.9	25.0	53.3	21.7
Nonperforming loans	−8.9	−3.4	3.6	83.9	12.5

Indicator	Current index	Previous index	Percent reporting eased	Percent reporting no change	Percent reporting tightened
Credit standards and terms	−10.3	−12.3	0.0	89.7	10.3

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	18.9	26.2	37.9	43.1	19.0
Nonperforming loans	−3.7	−1.7	5.7	84.9	9.4

Indicator	Current index	Previous index	Percent reporting eased	Percent reporting no change	Percent reporting tightened
Credit standards and terms	−12.1	−14.8	1.7	84.5	13.8

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	6.8	16.6	28.8	49.2	22.0
Nonperforming loans	−7.3	0.0	1.8	89.1	9.1

Indicator	Current index	Previous index	Percent reporting eased	Percent reporting no change	Percent reporting tightened
Credit standards and terms	−3.5	−1.7	0.0	96.5	3.5

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	7.8	7.5	17.2	73.4	9.4
Nonperforming loans	−1.7	−1.5	3.3	91.7	5.0

Indicator	Current index	Previous index	Percent reporting eased	Percent reporting no change	Percent reporting tightened
Credit standards and terms	−4.9	−3.1	1.6	91.9	6.5

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	8.9	15.9	32.8	43.3	23.9
Cost of funds	79.1	87.0	82.1	14.9	3.0
Net interest margin	−3.0	5.8	32.8	31.3	35.8
Noninterest income	9.1	11.7	19.7	68.2	10.6

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	25.7	36.8	34.8	56.1	9.1

Indicator	Current index	Previous index	Percent reporting more	Percent reporting no change	Percent reporting fewer
Nonperforming loans	−19.7	−8.8	4.5	71.2	24.2

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	23.9	39.1	29.9	64.2	6.0
Six months from now	23.9	36.7	38.8	46.3	14.9

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.

- As we approach the end of the year and the beginning of 2019, I believe loan demand will slow down and gradually pick up in second quarter 2019 after holiday bills are paid and taxes are completed.
- Cost of funds continues to be a concern. As the rate environment increases, we are seeing our competitors adjust their funding costs, which is leading to a tight competition for deposits. Even though this is the case, our institution continues to have a strong liquidity position. Management still has concerns over compliance and IT costs. Smaller institutions seem to continue to struggle to manage expenses related to compliance and IT costs. Also, management is having difficulty finding younger skilled employees who would be well-suited for officer-level positions, especially in rural areas. With the aging of our board, it is prudent to have a firm management succession plan in place and have it executed well.
- Home affordability, escalating property values and tech employers are concerning to our institution.
- Internet banks, financial institutions that provide credit cards and other banks that have a primary focus on commercial real estate loans have been very aggressive on paying higher rates for money market accounts and certificates of deposit. These interest rate increases will cause more pressure on the net interest margin for community banks.
- It is discouraging to read news about misleading and deceptive advertising and disclosure practices by online marketplace lenders, only to have a slap-on-the-wrist consequence without any monetary fees or penalties. If our newly empowered lawmakers seek opportunities to expand regulation, then the online marketplace lending industry (and fintech industry) would be a great place to start.
- Our bank has a concentration of agricultural loans. The weather the last two months has been a detriment to our farmers. Most cotton will not be harvested, and planting of wheat will not be accomplished. Commodity prices continue to suffer, and tariffs are not helping either. Most farmers will have to depend on insurance and preventive planning. Cattle prices also continue to suffer. We will continue to support our customers to the best of our abilities. We are not seeking any additional agricultural loans unless they have a USDA guarantee.
- Our primary issue of concern is increased competition from credit unions who continue to increase CD rates far in excess of the national average and continue to drive up our cost of funds in our local market area. A secondary area of concern is regulatory compliance. Regulatory compliance requirements continue to cause delays that are bothersome to

consumers who do not understand or appreciate the needless delays caused by these requirements. In addition, the costs associated with regulatory compliance continue to negatively impact our net income.

- Regulations and the increased cost of compliance and the Bank Secrecy Act are pain points for our institution.
- We are concerned about regulations and in particular Matters Requiring Attention (MRA) related to supervisory guidance.
- The current rising rate environment is concerning for our institution.
- The general level of business activity in southeast New Mexico is heavily dependent upon the oil and gas extraction industry. The recent New Mexico gubernatorial election resulted in a new governor being elected who will take office in January 2019. The new governor and the new state land commissioner have indicated they will not be as supportive of the oil and gas industry as the previous governor. This may have an effect on the level of economic activity in our area. Time will tell.