

Banking CONDITIONS

Providing Tenth District insights on regional and national banks

Third Quarter 2021 Banking Conditions

By Chris Summers

The Federal Reserve Bank of Kansas City dedicates staff to monitor banking trends nationally and across our seven-state region.

Bank earnings continue to remain strong, though quarterly return on average assets (ROAA) declined at district banks. Earnings improvement has been driven by decreased provisions, as well as a decline in overhead expenses. In the third quarter, banks both nationally and at the District level realized net reverse provisions after having built up allowance levels throughout 2020. While ROAA has improved from year-ago levels, net interest margins (NIM) remain compressed as inflated balance sheets coupled with the low interest rate environment and depressed loan demand has placed downward pressure on asset yields. Yields on both loans and securities continue to decline, with yields decreasing more than cost of funds. In response, banks have extended durations in the securities portfolio to help achieve higher yields. Given the current challenges to NIMs, and when considering an eventual return to normal provision levels, the sustainability of this elevated level of earnings is uncertain.

Balance sheets across banks remain flush with liquidity. Pandemic-induced influxes of funds have been placed in liquid yet low-yielding assets, primarily investment securities and interest-bearing bank balances. Loan balances are decreasing, driven by declines in Paycheck Protection Program (PPP) loans, as these loans are being forgiven, while deposit levels continue to increase. As a result, loan-to-deposit ratios among District banks are at the lowest level in over 20 years. Also, partially contributing to depressed loan balances are decreases in agriculture loans and the slowing of 1-4 family loan growth, though CRE lending continues to fair well, particularly at the District level. Overall growth in balance sheets has outpaced capital growth. Leverage capital ratios have declined since the onset of the pandemic, but the decline steadied in the third quarter across District banks.

Credit conditions are stable with low levels of problem assets that approximate pre-pandemic levels. Noncurrent loans at District banks remain low and have declined across all major loan types, apart from commercial and industrial loans (C&I), over the past quarter. Loans modified under section 4013 of the CARES Act also continue to decline. Allowance for Loan and Lease Loss (ALLL) ratios have decreased due to net reverse provisions across banks during the quarter. While asset quality metrics generally appear positive, government stimulus and forbearance programs could be masking credit quality at some banks.

Chris Summers is a risk specialist in the Division of Supervision and Risk Management at the Federal Reserve Bank of Kansas City.

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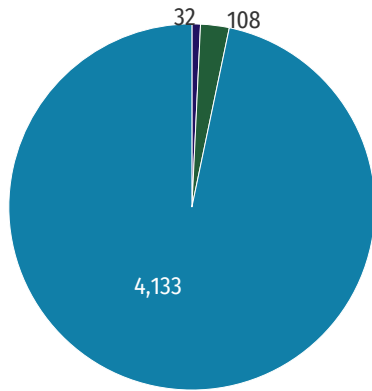
Select Ratios by Tenth District State

Banking Institutions Overview

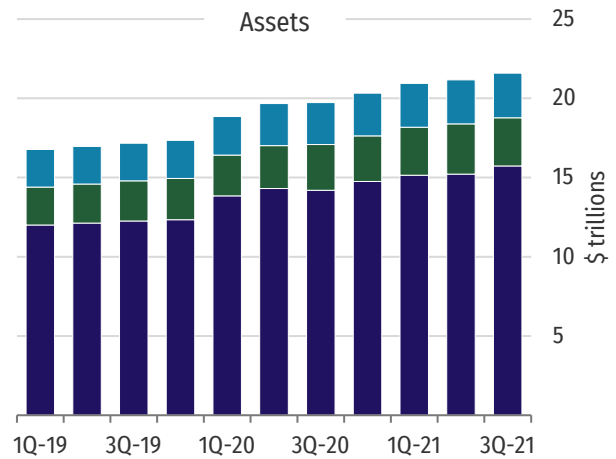
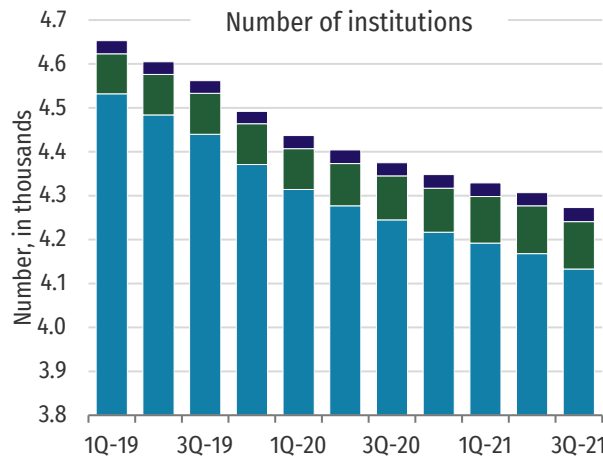
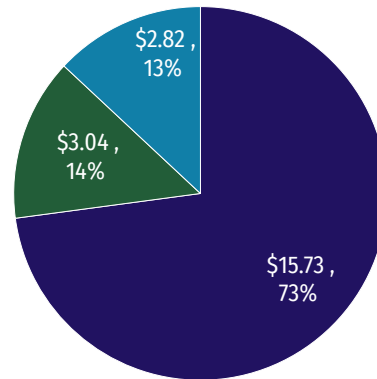
All U.S. Commercial Banks

Large banks Regional banks Community banks

Number of institutions



Assets, in trillions

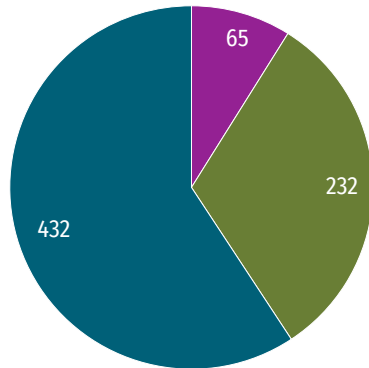


Banking Institutions Overview

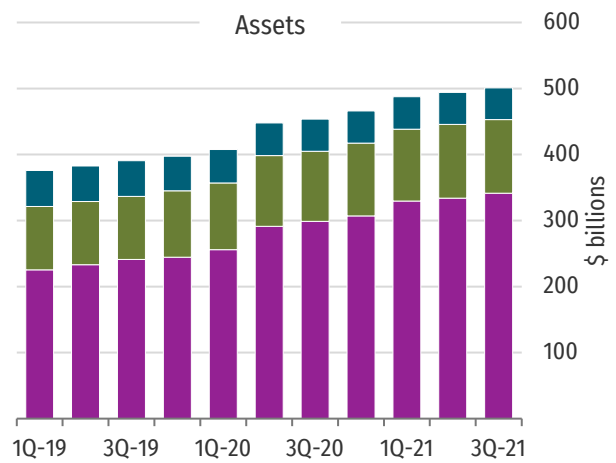
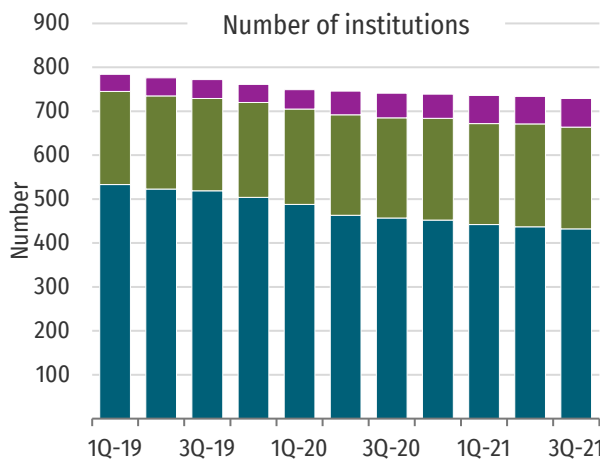
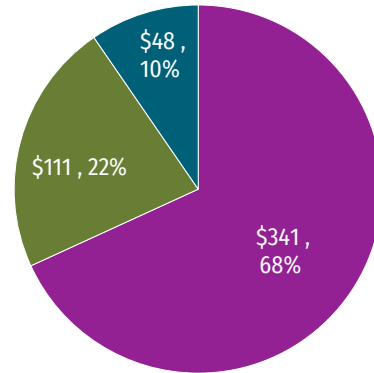
Tenth District Commercial Banks

Above \$1 bn \$250 mm - \$1 bn Under \$250 mm

Number of institutions



Assets, in billions



A. Capital and Earnings

- Capital levels steadied, whereas earnings performance decline in the third quarter.
- Balance sheet growth, driven by the Paycheck Protection Program, was the primary contributor to decreases in capital ratios since the onset of the pandemic.

Chart A1. Leverage Ratio, All U.S. Commercial Banks

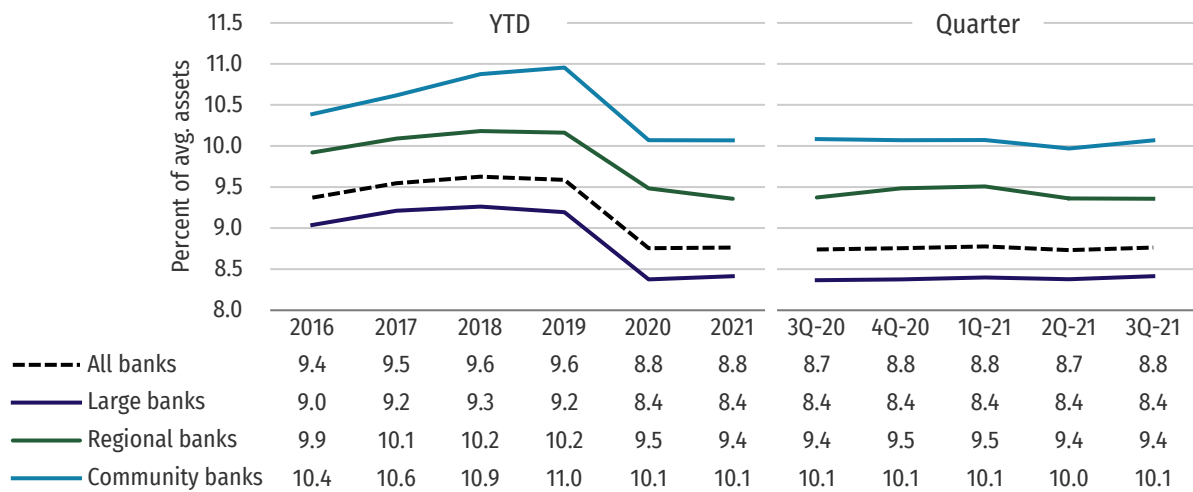


Chart A2. Leverage Ratio, Tenth District Commercial Banks

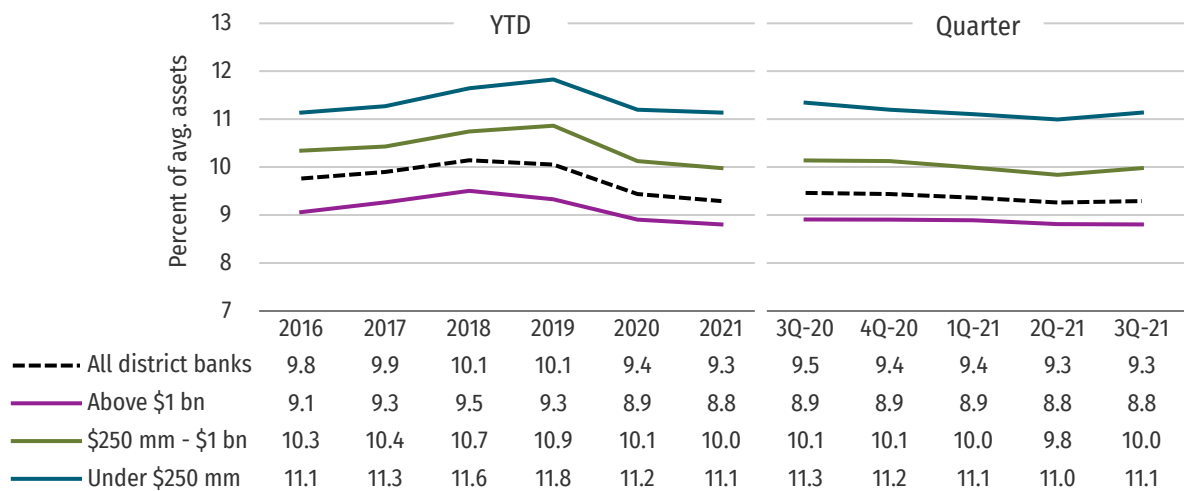


Chart A3. Quarterly Dividend Trends

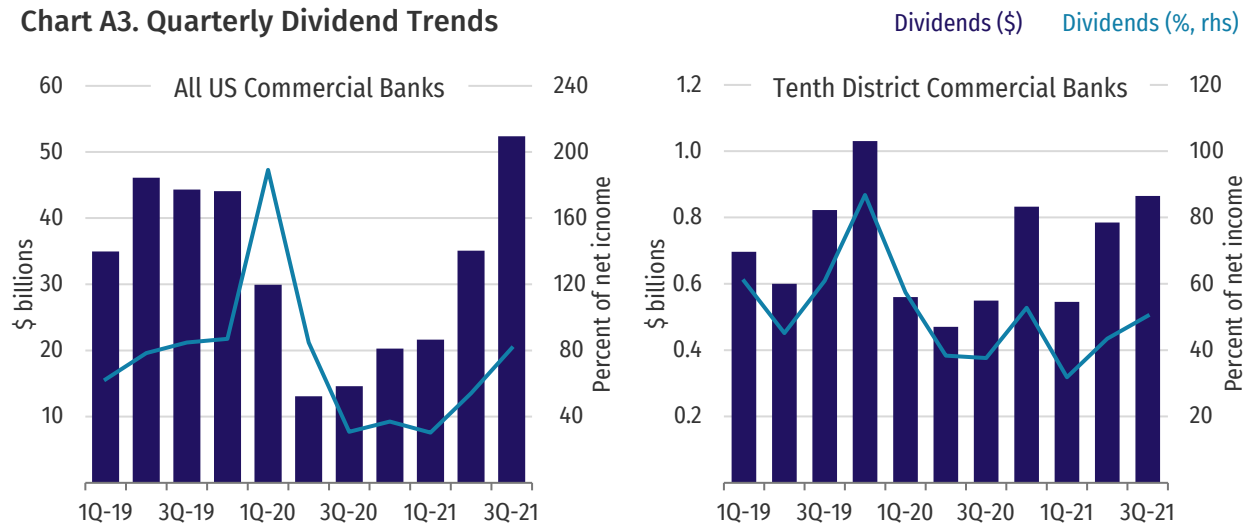


Chart A4. Return on Average Assets Summary

	All US Commercial Banks				y/y change	q/q change	Tenth District Commercial Banks				y/y change	q/q change
	4Q-18	4Q-19	4Q-20	3Q-21			4Q-18	4Q-19	4Q-20	3Q-21		
Net interest income	3.04	3.00	2.53	2.28	▼ (0.09)	▲ 0.07	3.57	3.54	3.22	3.04	▼ (0.08)	▼ (0.01)
Noninterest income	1.56	1.51	1.38	1.37	▼ (0.04)	▼ (0.02)	1.13	1.21	1.30	1.19	▼ (0.27)	▼ (0.05)
Total revenue	4.60	4.51	3.90	3.65	▼ (0.14)	▲ 0.05	4.70	4.75	4.52	4.23	▼ (0.35)	▼ (0.06)
Provisions	0.26	0.29	0.64	(0.18)	▼ (0.34)	▲ 0.12	0.22	0.24	0.40	0.01	▼ (0.24)	▲ 0.01
Noninterest expense	2.64	2.61	2.43	2.24	▼ (0.11)	▲ 0.01	2.90	2.96	2.77	2.52	▼ (0.26)	▼ (0.00)
Total expenses	2.90	2.90	3.07	2.05	▼ (0.45)	▲ 0.13	3.12	3.20	3.17	2.53	▼ (0.50)	▲ 0.01
Pre-tax operating income	1.70	1.61	0.83	1.60	▲ 0.31	▼ (0.08)	1.58	1.54	1.35	1.70	▲ 0.15	▼ (0.07)
Net Income	1.35	1.29	0.70	1.28	▲ 0.24	▼ (0.03)	1.36	1.30	1.20	1.43	▲ 0.08	▼ (0.09)

Chart A5. Return on Average Assets, All U.S. Commercial Banks

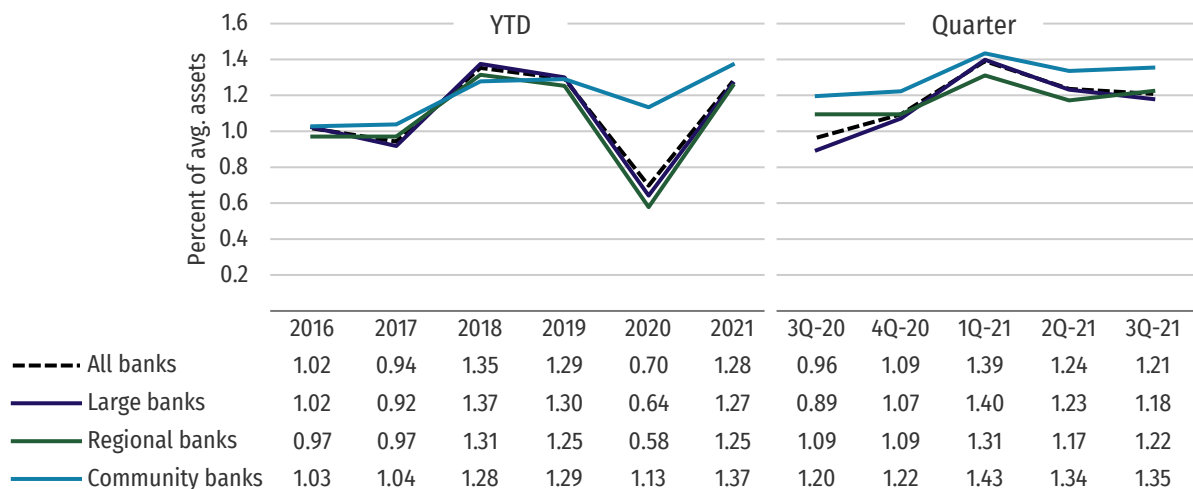


Chart A6. Return on Average Assets, Tenth District Commercial Banks

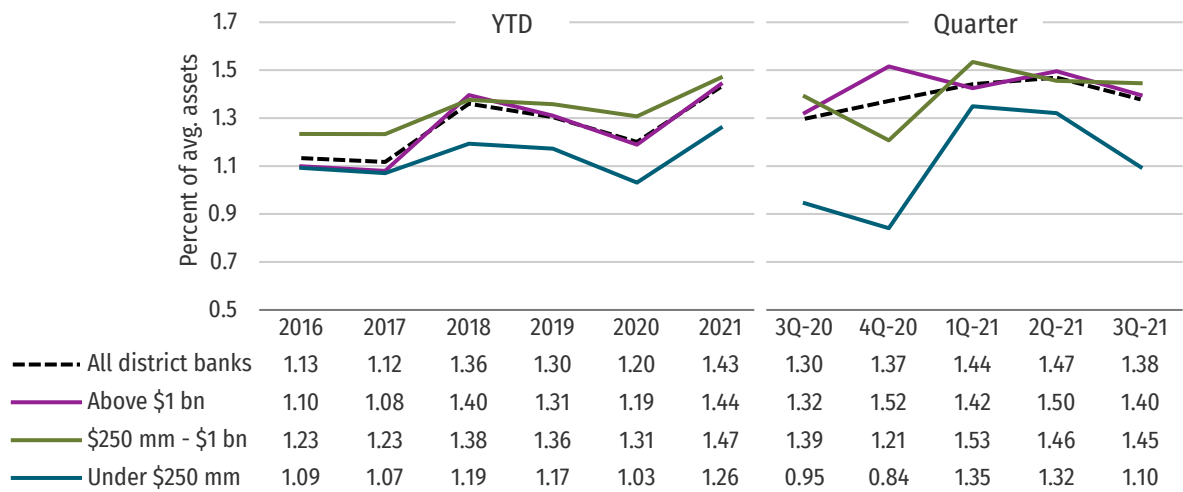


Chart A7. Quarterly Revenue Trends

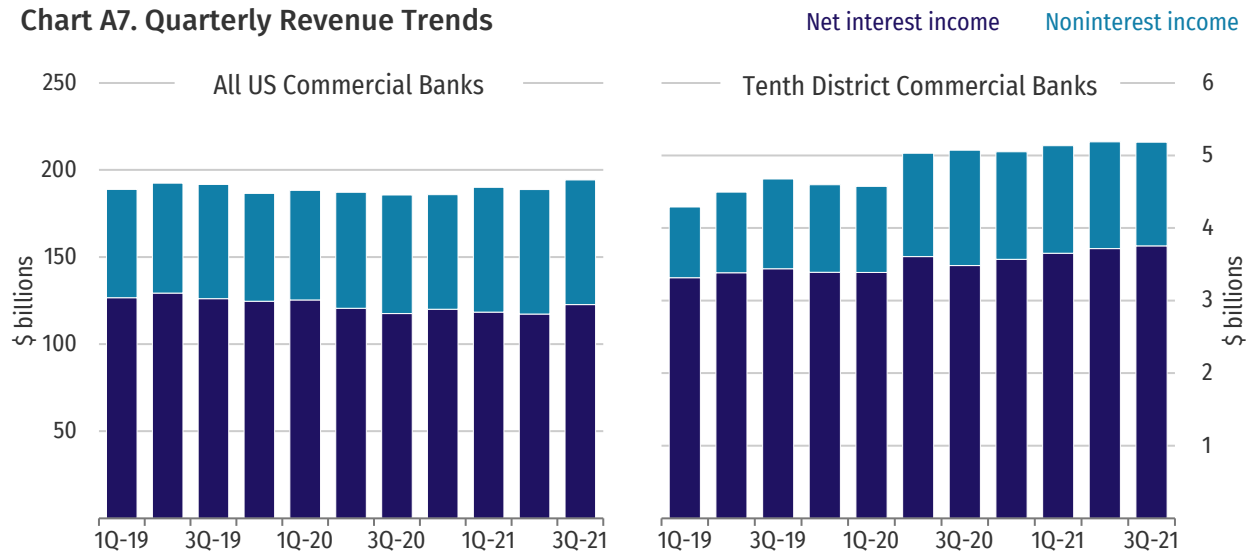


Chart A8. Year-Over-Year Change in Income & Expense Items, All U.S. Commercial Banks

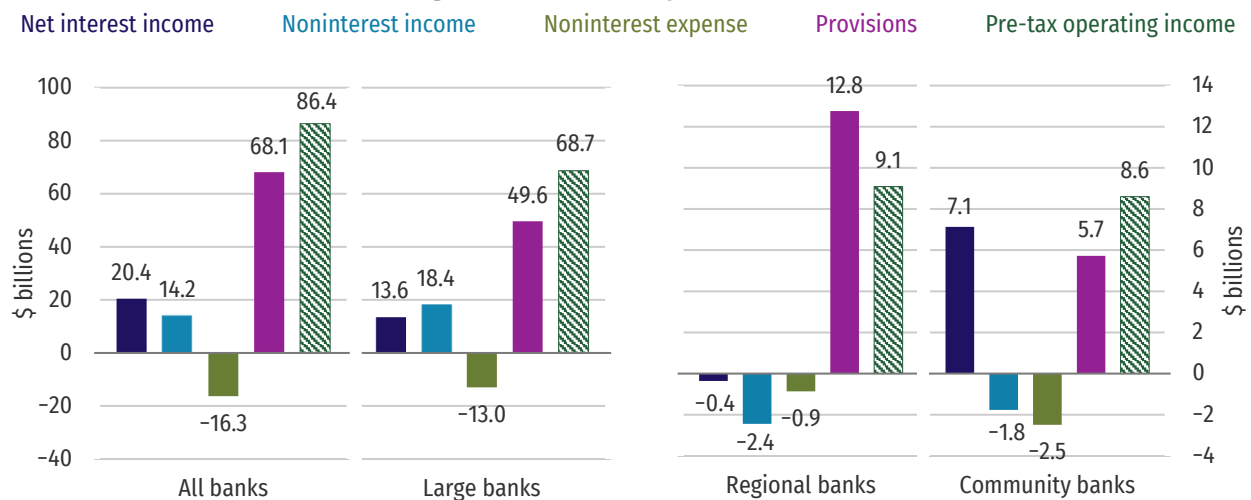


Chart A9. Year-Over-Year Change in Income & Expense Items, Tenth District Commercial Banks

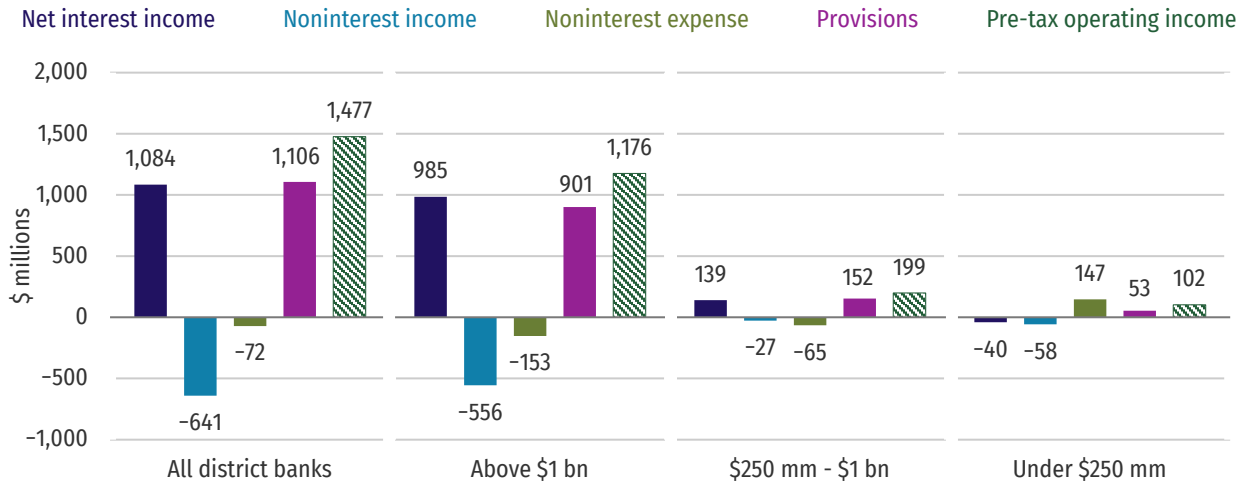


Chart A10. Net Interest Margin, All U.S. Commercial Banks

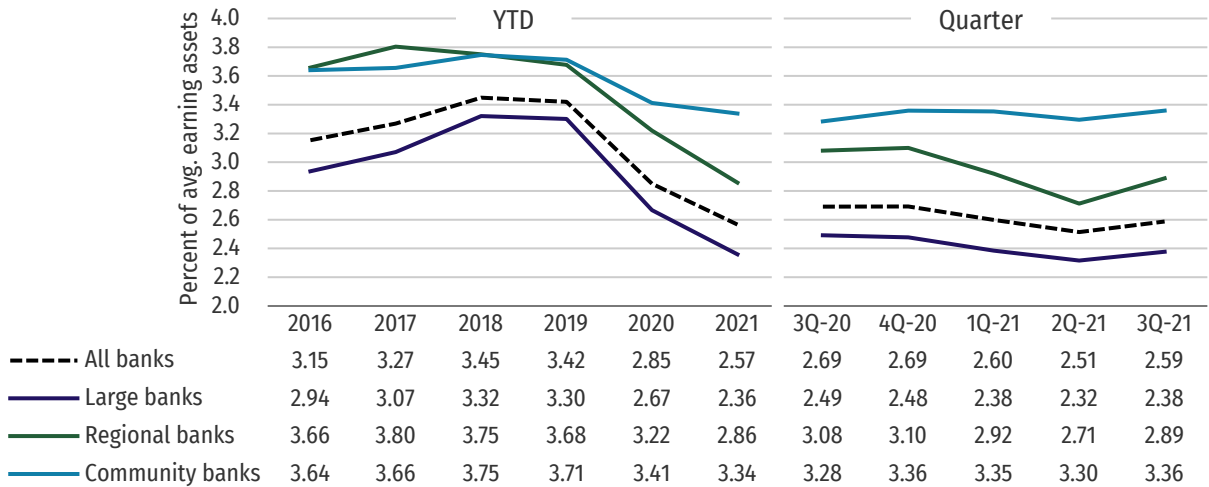


Chart A11. Net Interest Margin, Tenth District Commercial Banks

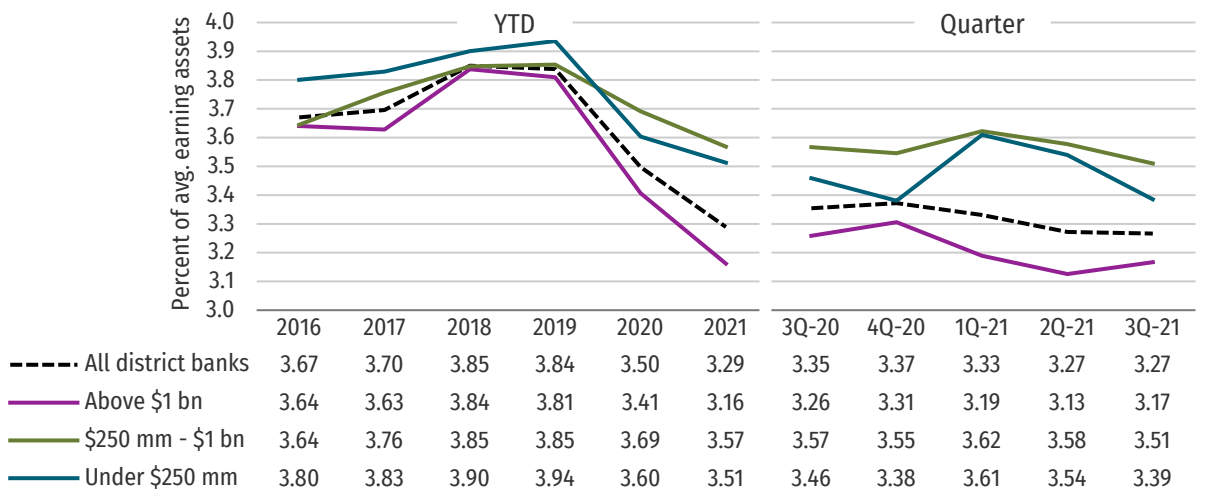


Chart A12. Interest Income, All U.S. Commercial Banks

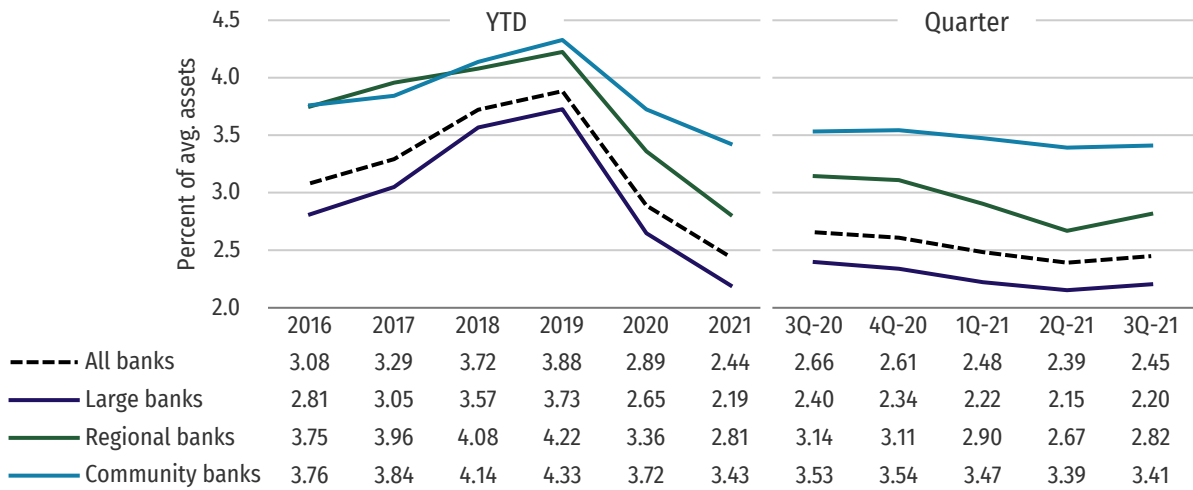


Chart A13. Interest Income, Tenth District Commercial Banks

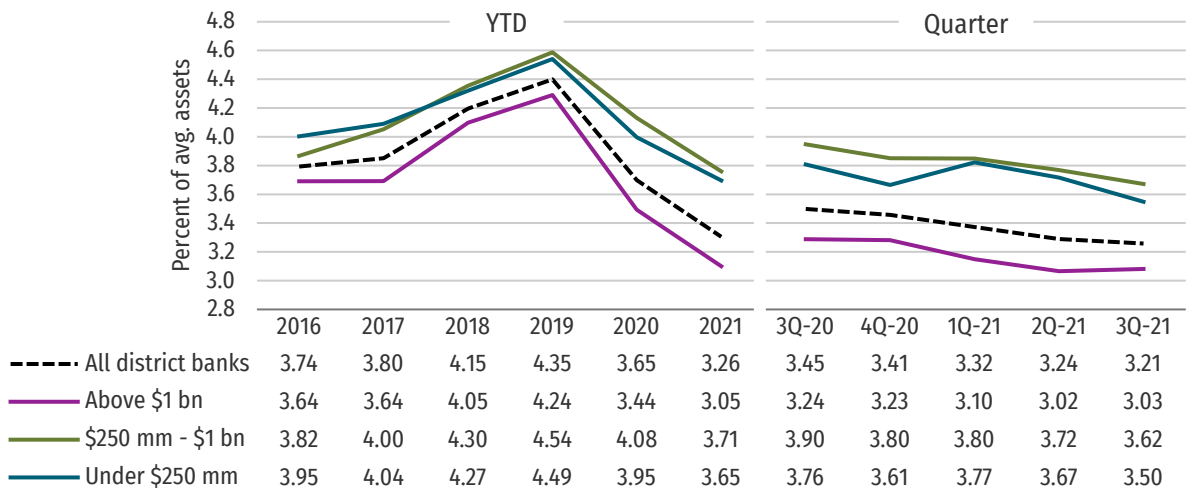


Chart A14. Noninterest Income, All U.S. Commercial Banks

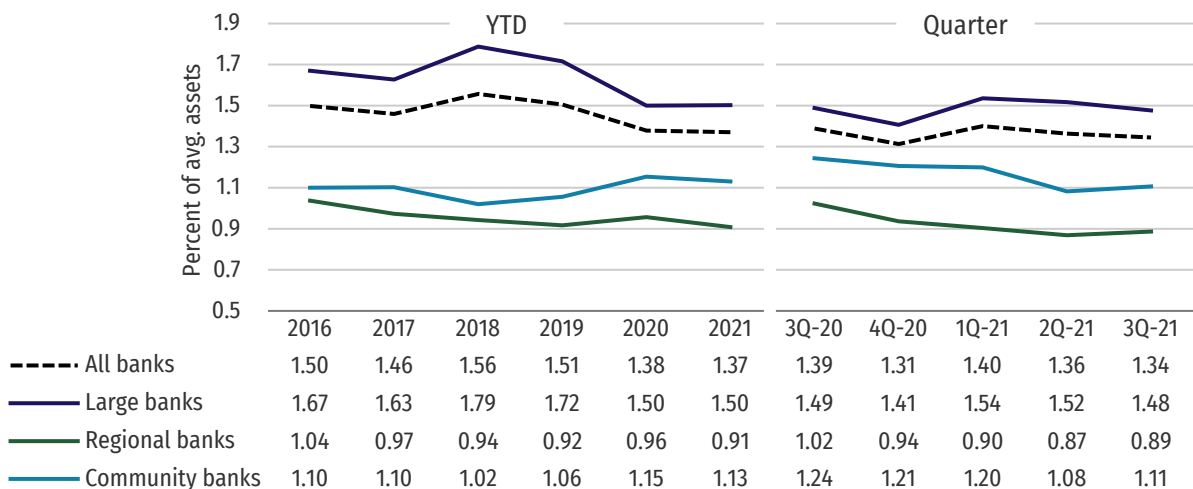


Chart A15. Noninterest Income, Tenth District Commercial Banks

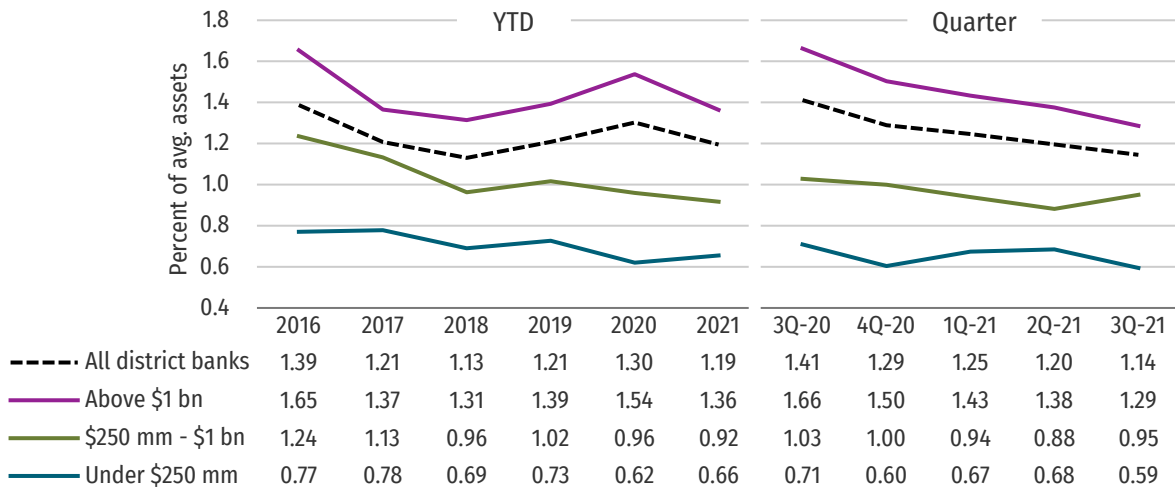


Chart A16. Noninterest Expense, All U.S. Commercial Banks

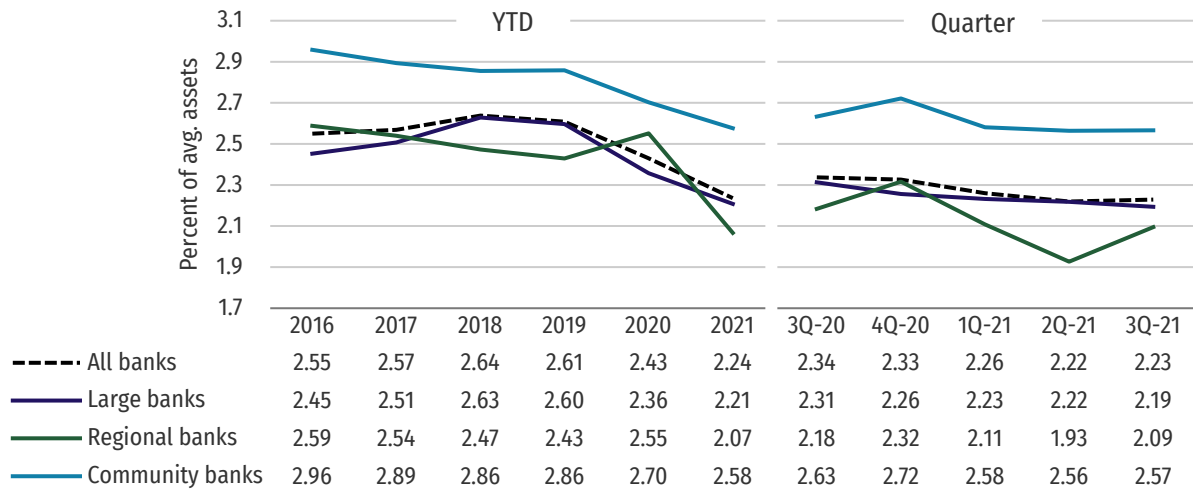
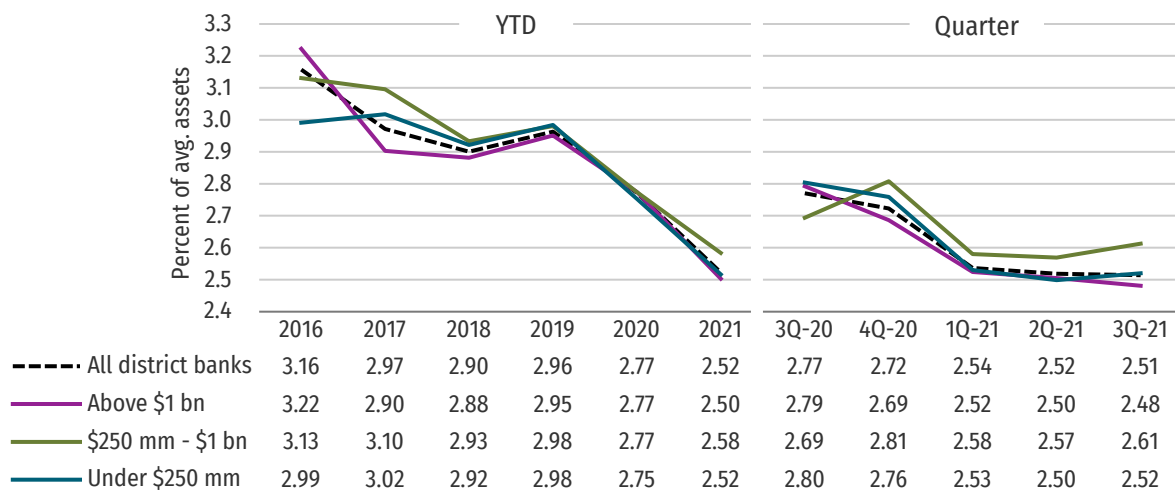


Chart A17. Noninterest Expense, Tenth District Commercial Banks



B. Loan Loss Reserves and Credit Conditions

- At the onset of the pandemic loan loss reserves were bolstered, particularly in the first half of 2020; however, with the improved economic outlook, some banks have started to release reserves.
- Credit conditions remained sound with problem assets continuing to decline.

Chart B1. Loan Loss Provisions, All U.S. Commercial Banks

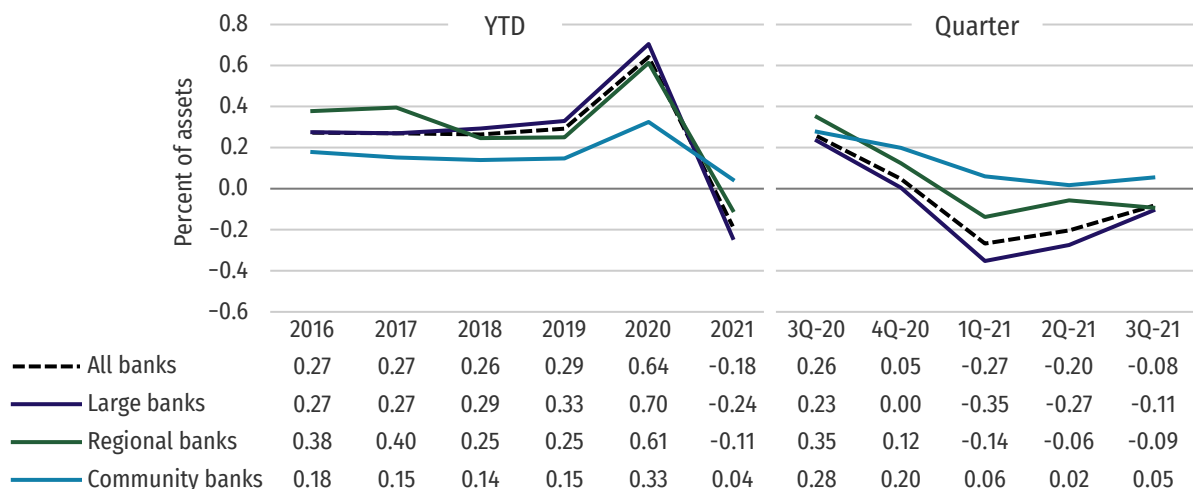


Chart B2. Loan Loss Provisions, Tenth District Commercial Banks

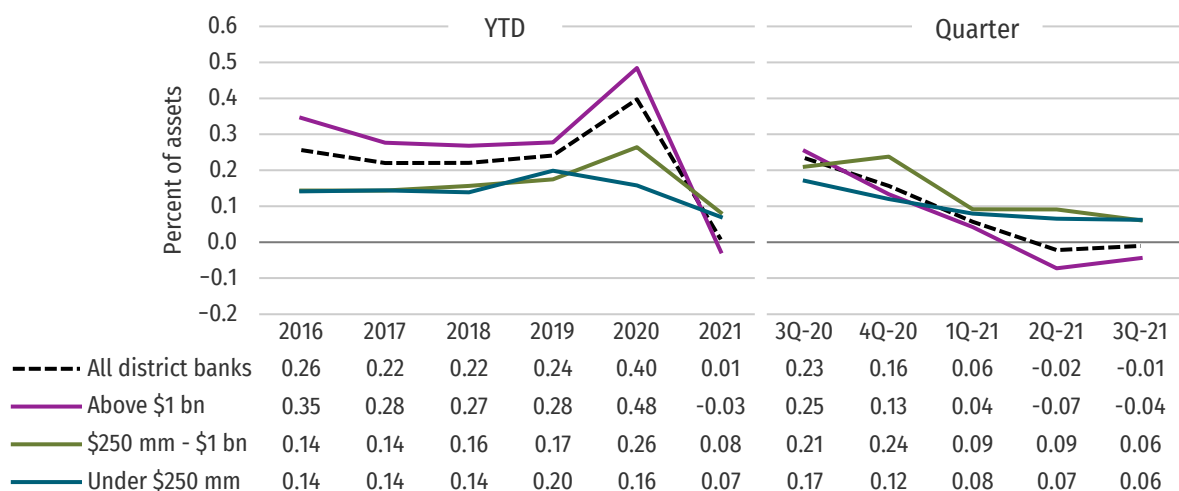


Chart B3. Quarterly Allowance for Loan and Lease Losses Trends

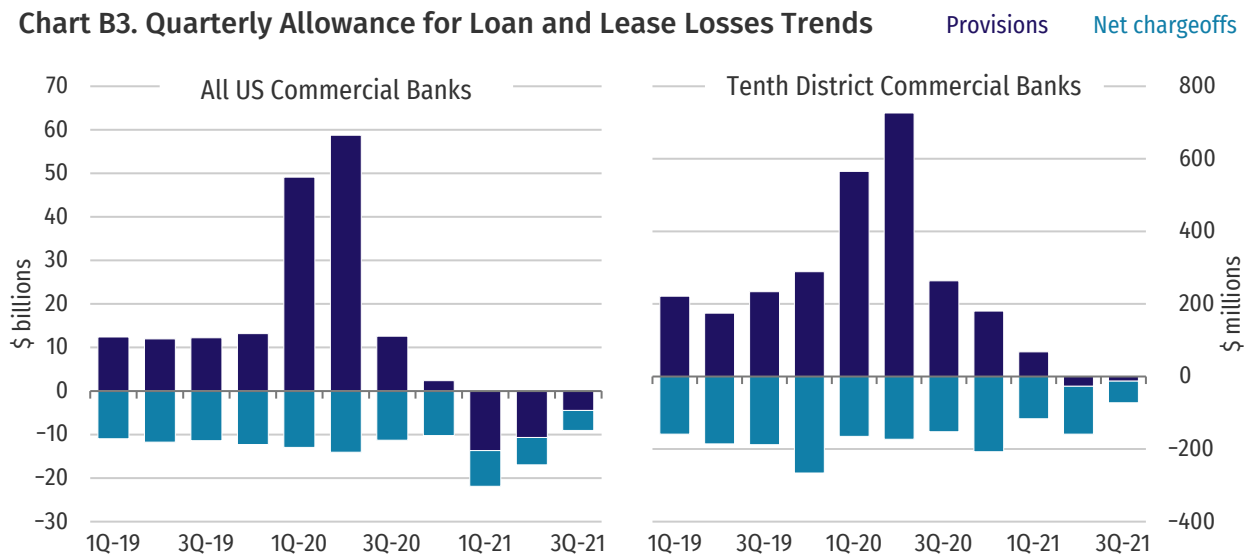


Chart B4. Problem Assets, All U.S. Commercial Banks

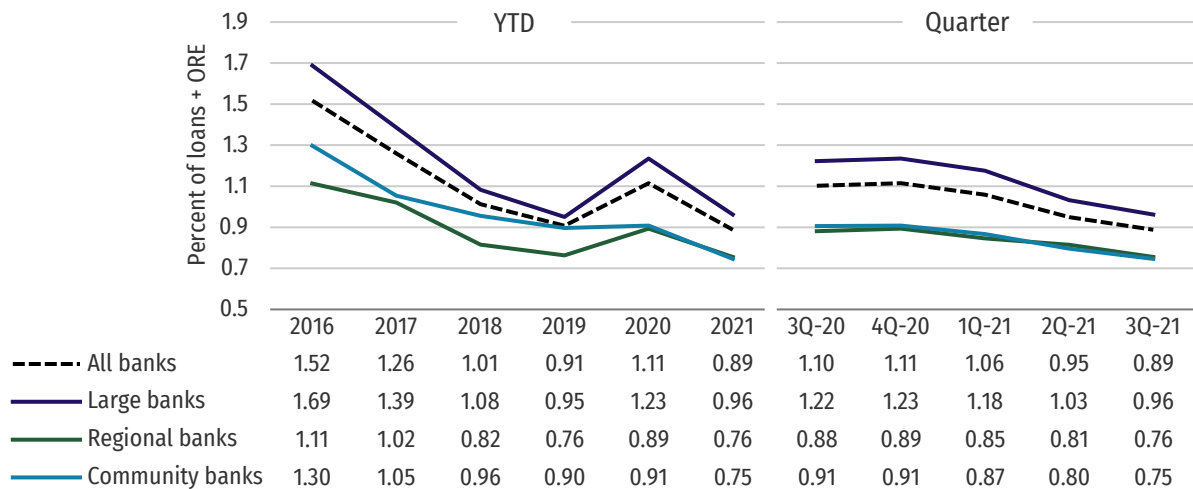


Chart B5. Problem Assets, Tenth District Commercial Banks

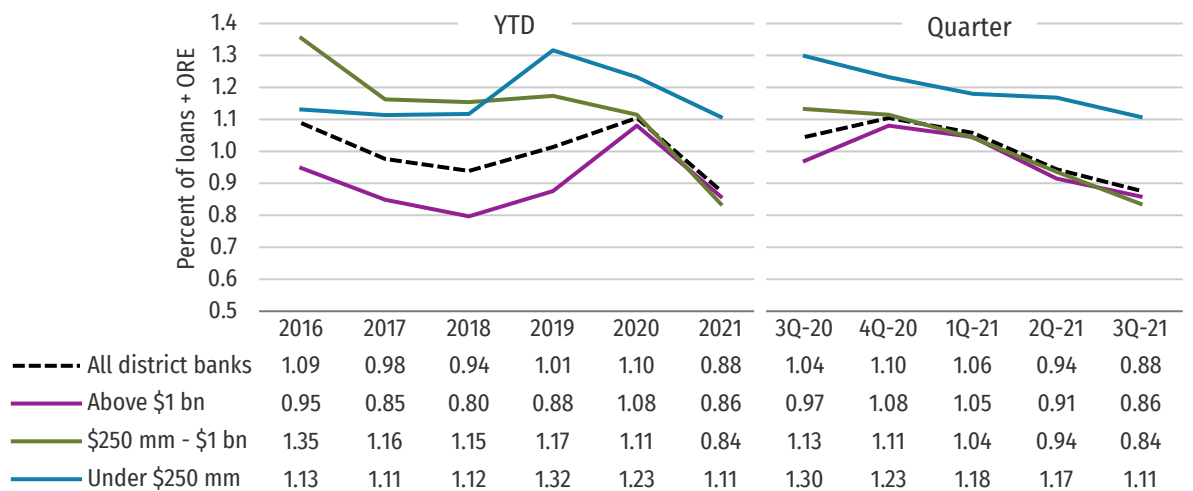


Chart B6. Noncurrent CLD and CRE Loans

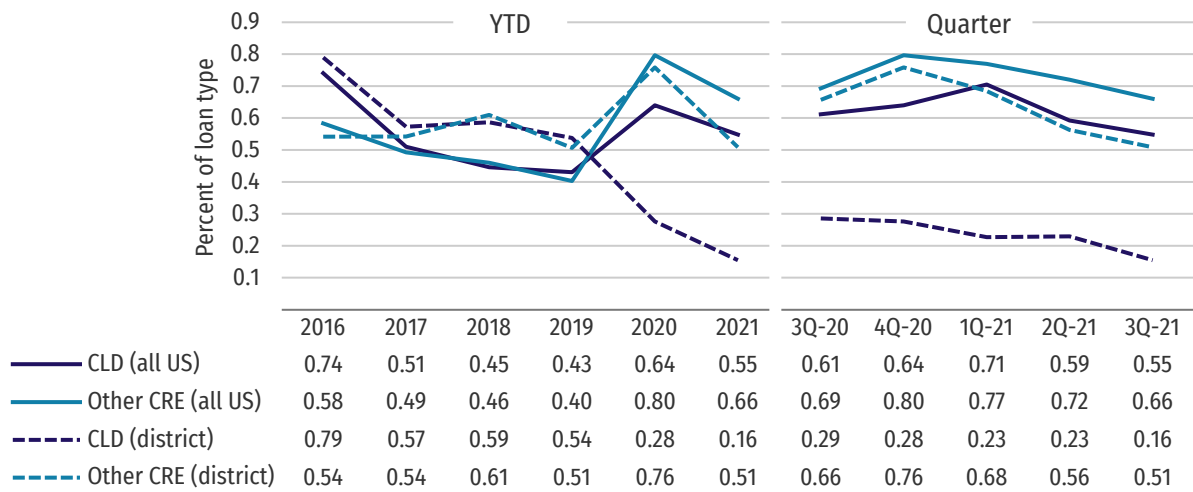


Chart B7. Noncurrent Loans by Other Loan Types, All U.S. Commercial Banks

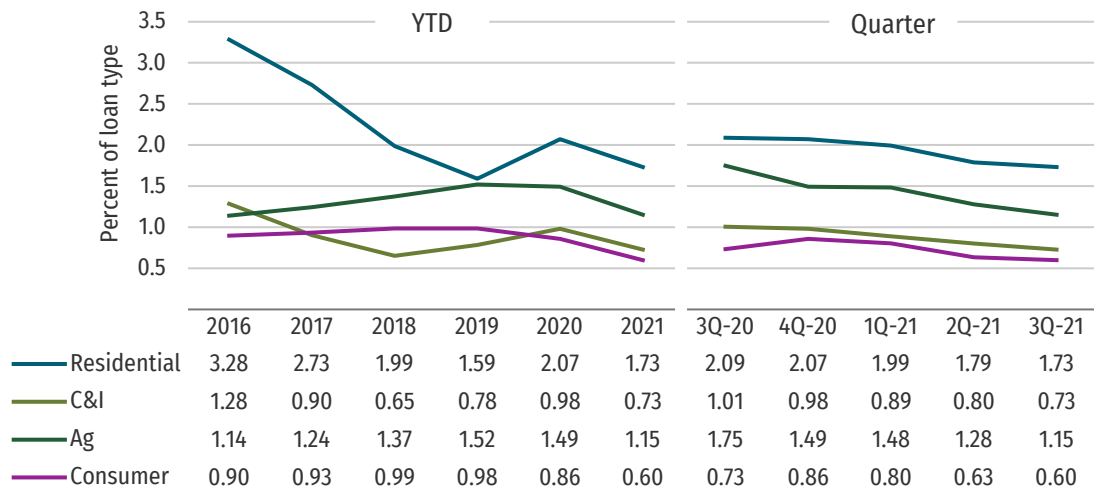


Chart B8. Noncurrent Loans by Other Loan Types, Tenth District Commercial Banks

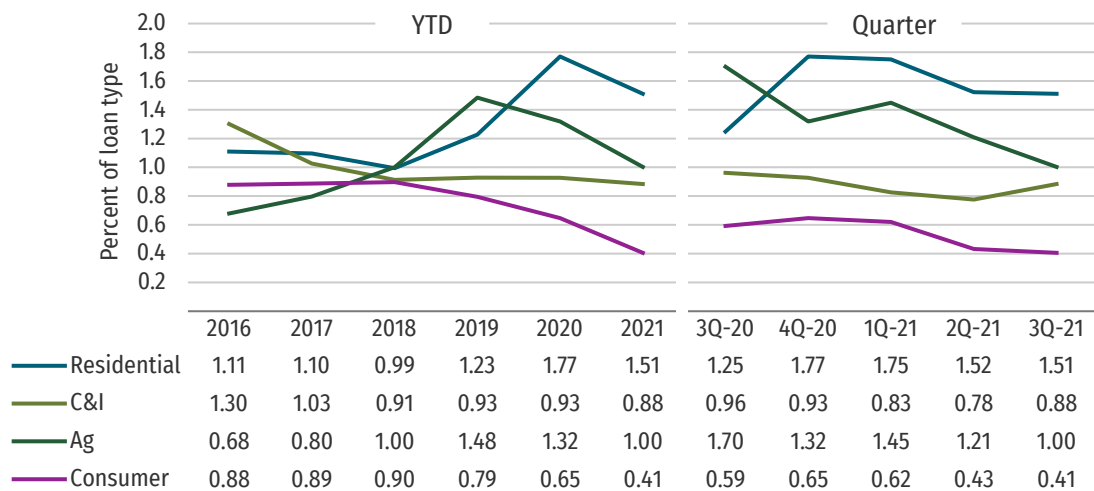


Chart B9. Noncurrent Loans by Loan Type, Tenth District States

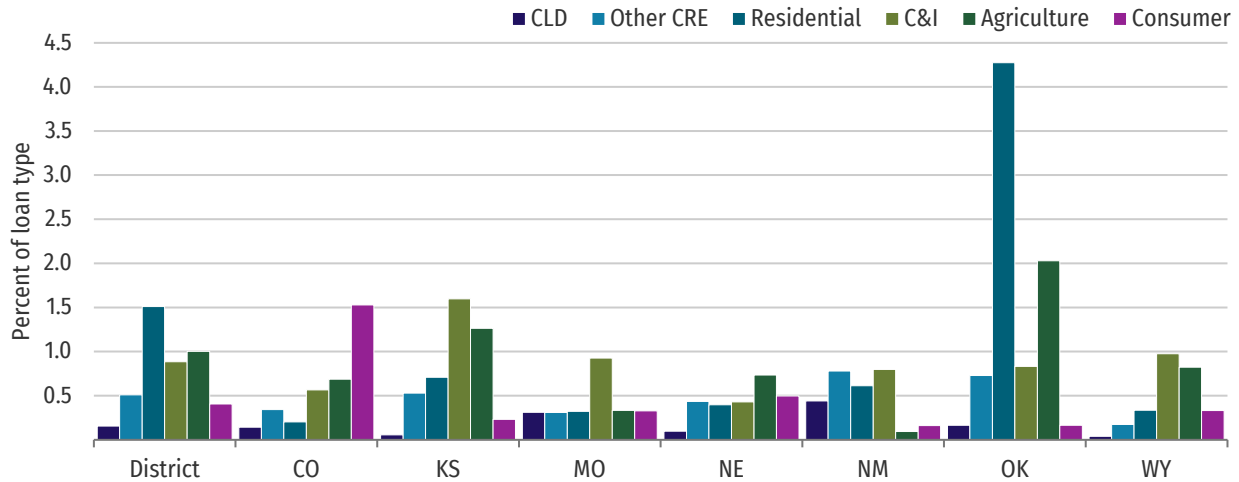


Chart B10. Texas Ratio, All U.S. Commercial Banks

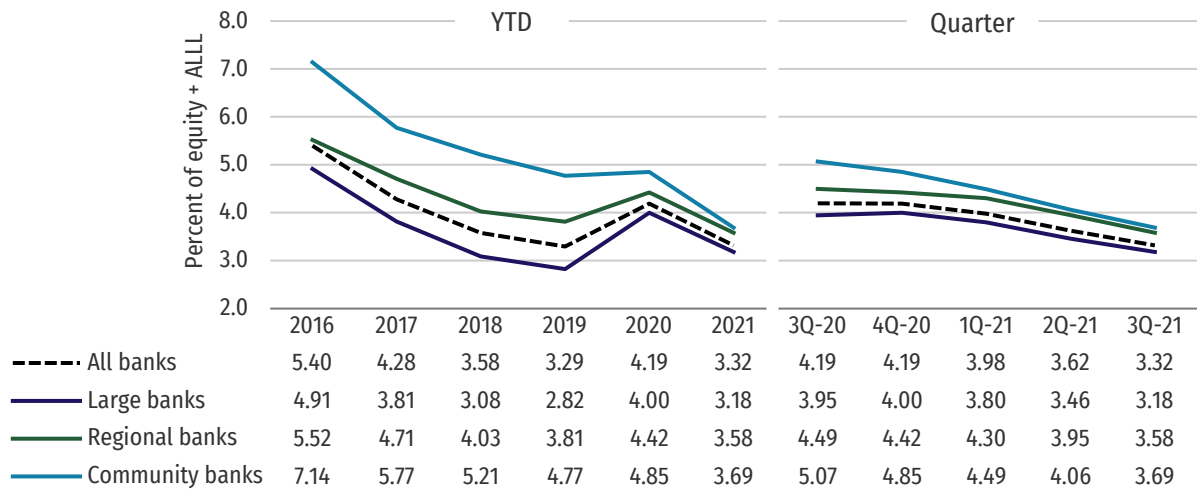


Chart B11. Texas Ratio, Tenth District Commercial Banks

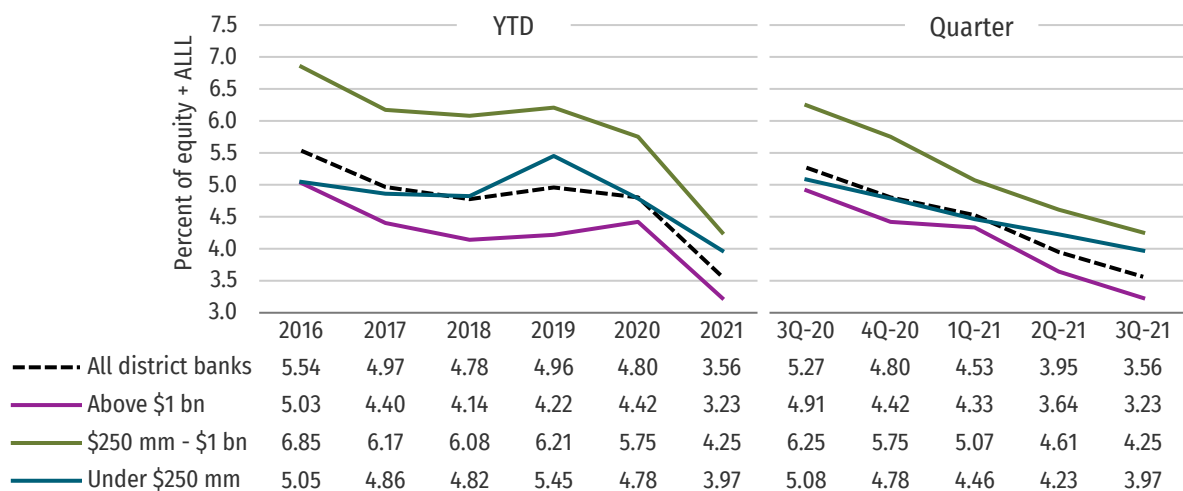


Chart B12. Coverage Ratio, All U.S. Commercial Banks

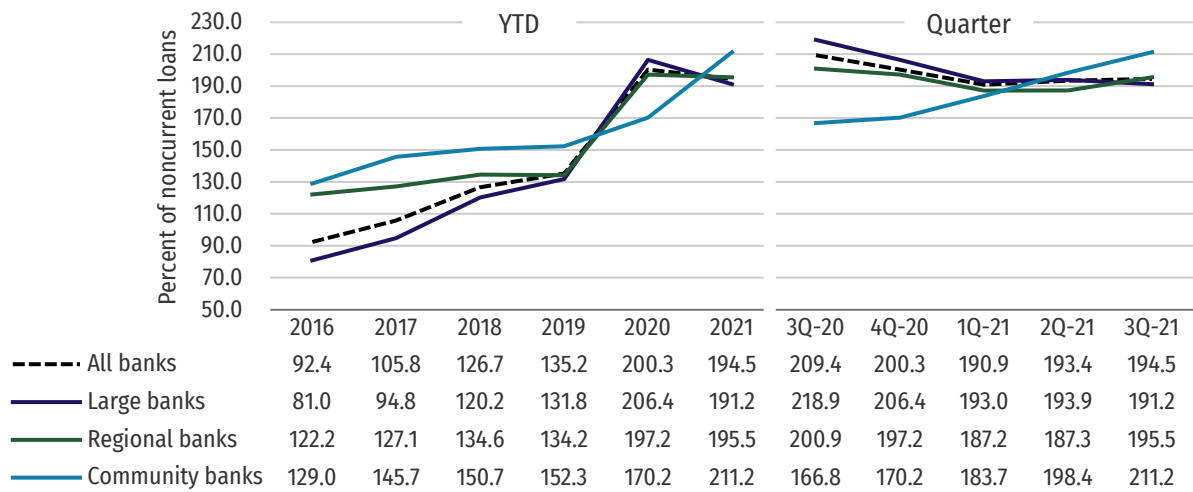
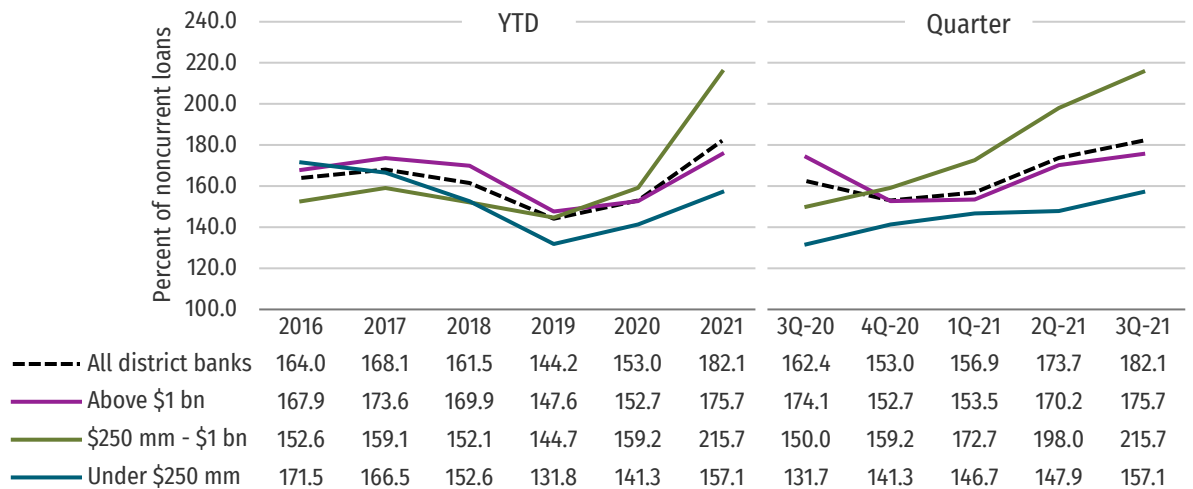


Chart B13. Coverage Ratio, Tenth District Commercial Banks



C. Balance Sheet Composition

- Deposit growth has far exceeded loan growth leading to improved liquidity metrics.

Chart C1. Loan Portfolio Breakdown, All U.S. Commercial Banks

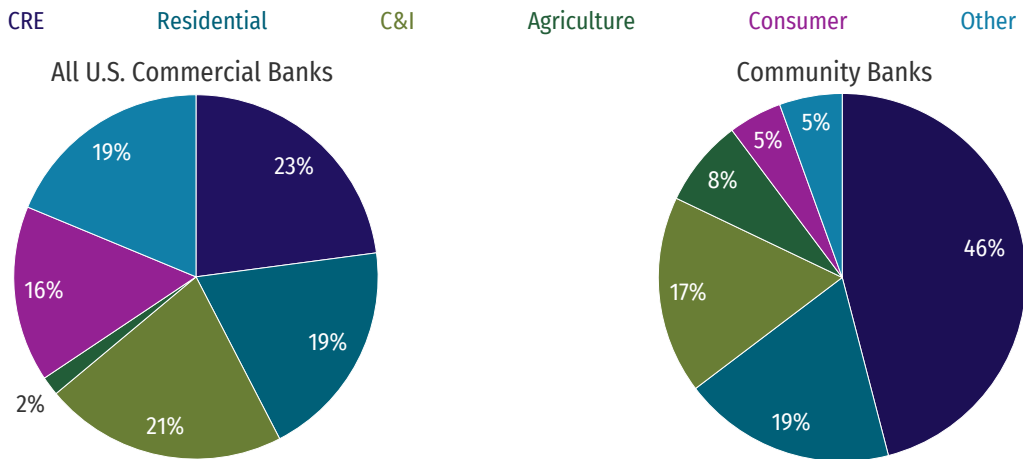


Chart C2. Loan Portfolio Breakdown, Tenth District Commercial Banks

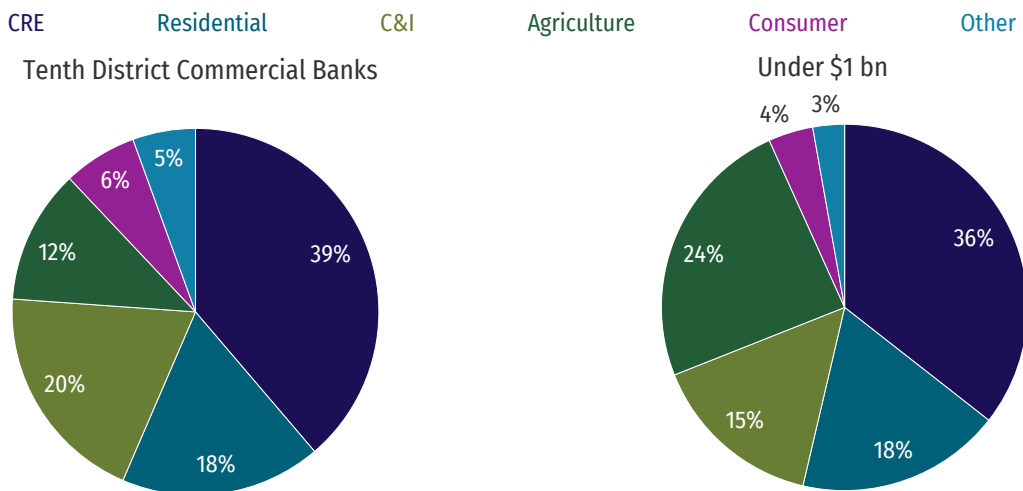


Chart C3. Balance Sheet Shifts, in Billions

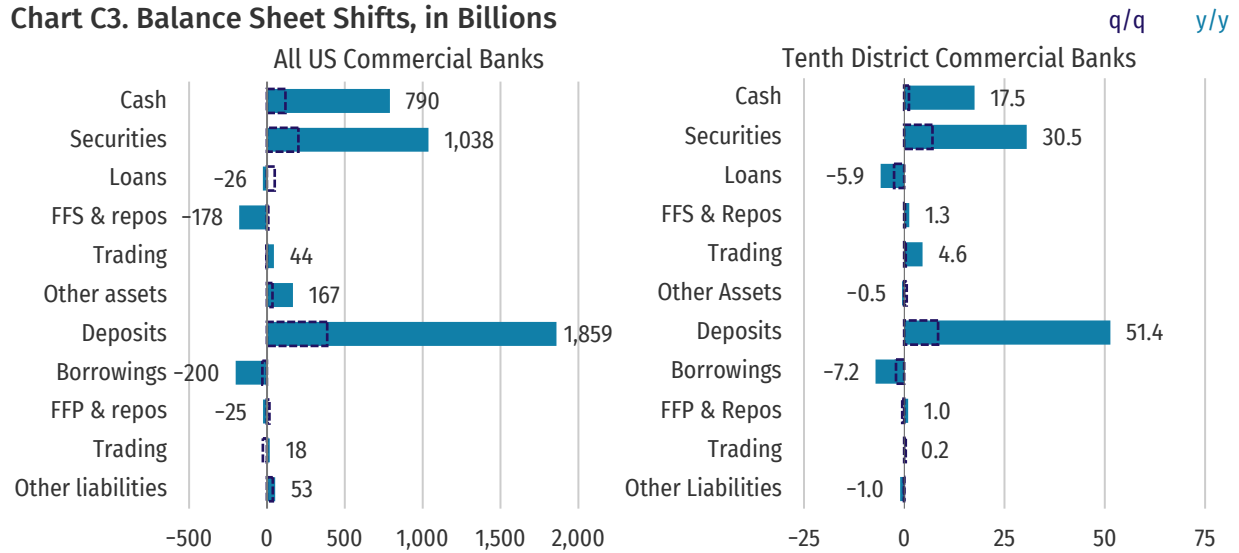


Chart C4. Change in Loan Portfolio Composition, in Billions

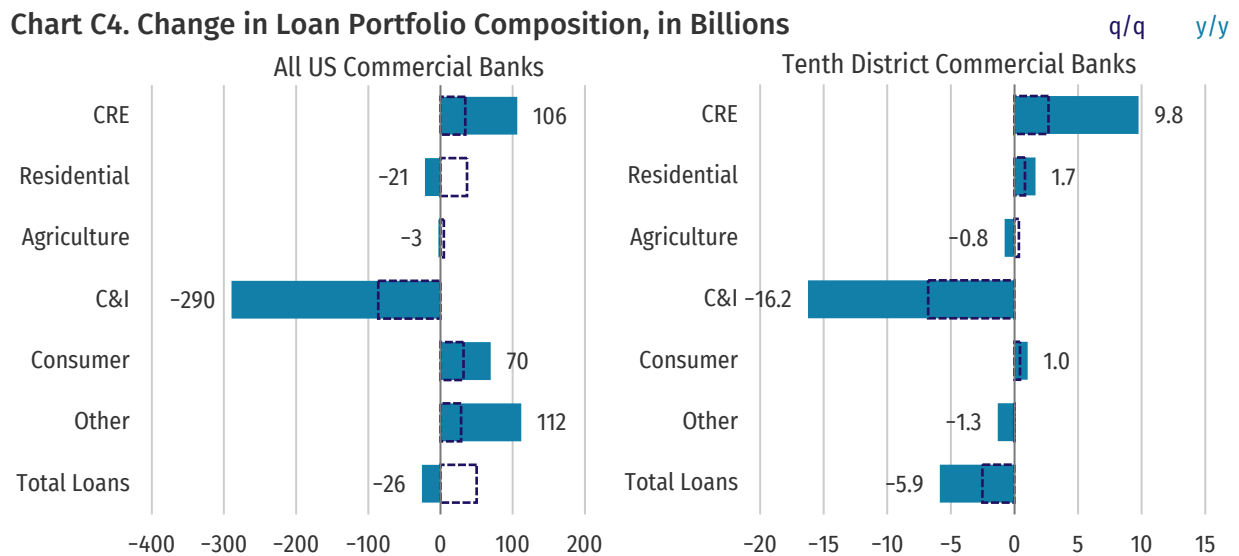


Chart C5. Loans to Assets, All U.S. Commercial Banks

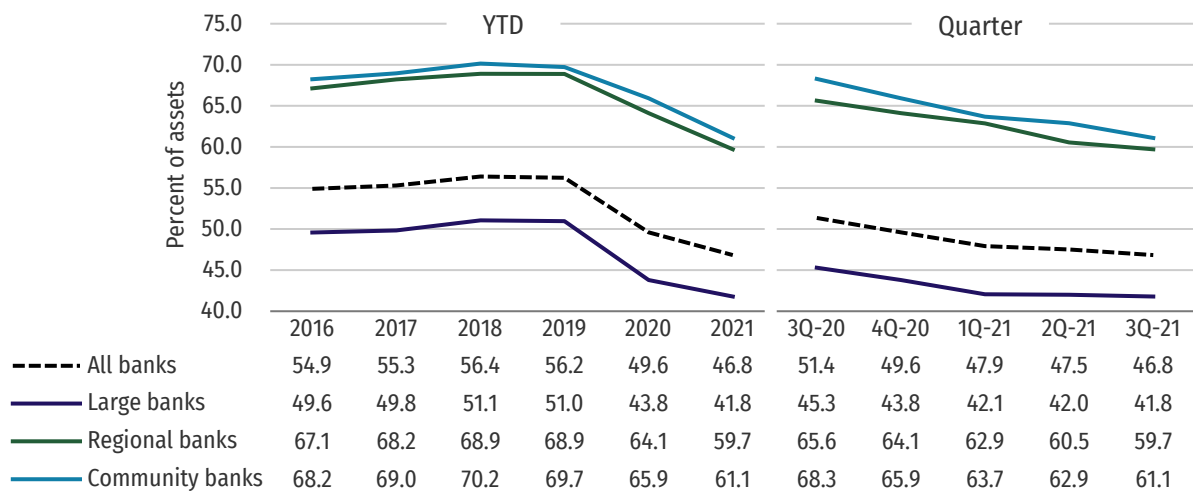


Chart C6. Loans to Assets, Tenth District Commercial Banks

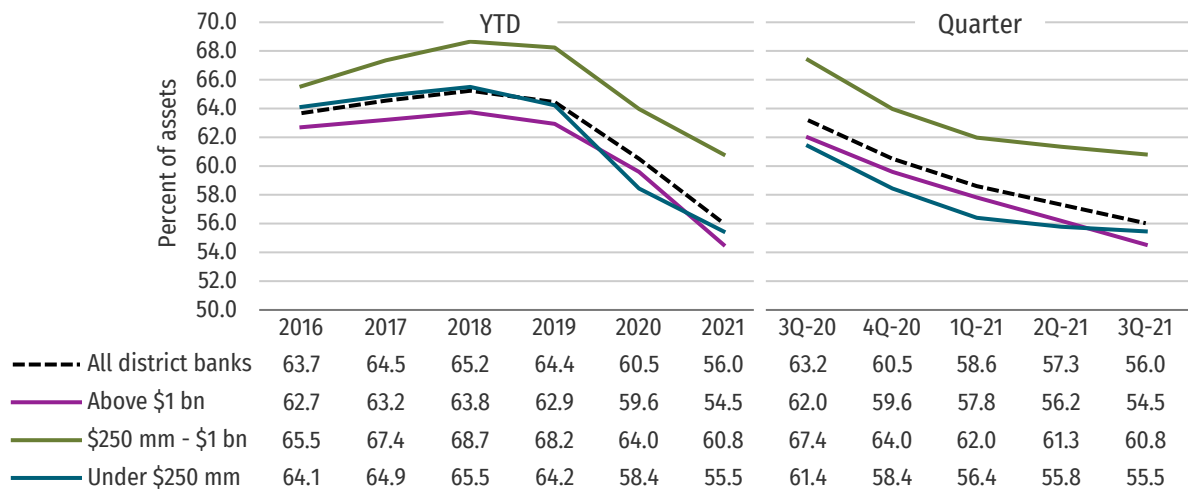


Chart C7. Loans to Assets, Tenth District States

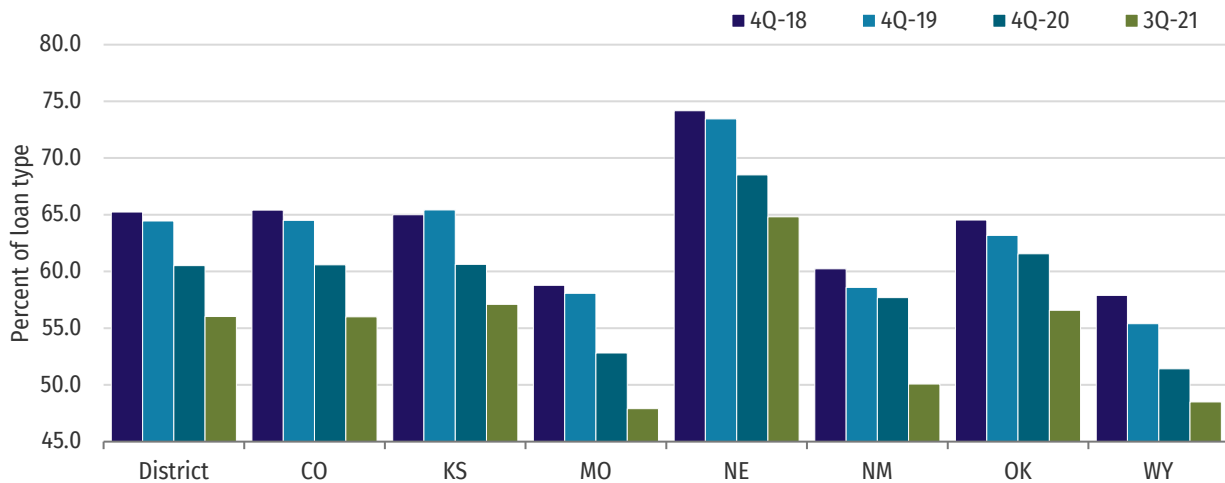


Chart C8. Year-Over-Year Loan Growth, All U.S. Commercial Banks

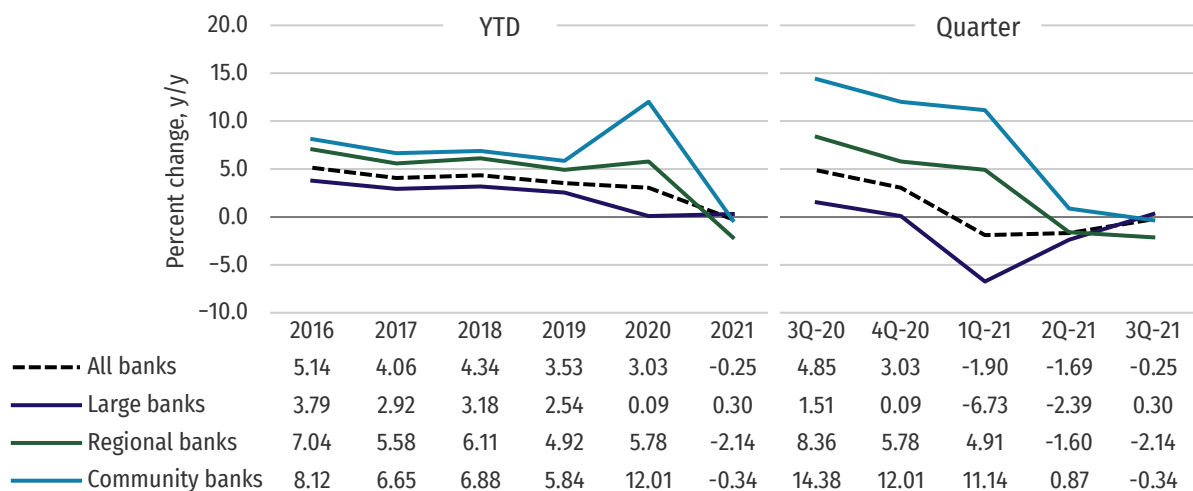


Chart C9. Year-Over-Year Loan Growth, Tenth District Commercial Banks

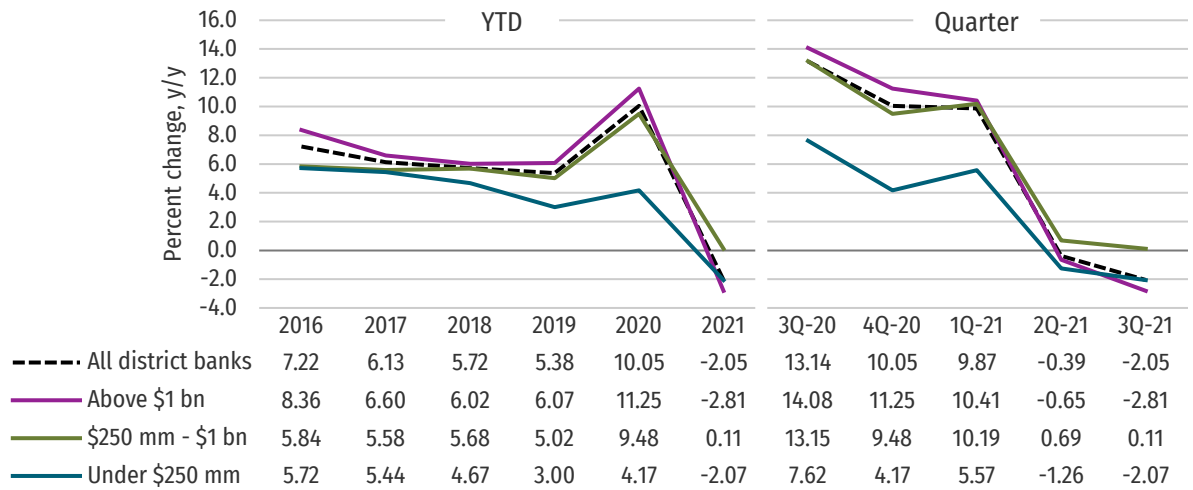


Chart C10. Year-Over-Year Loan Growth by Loan Type, All U.S. Commercial Banks

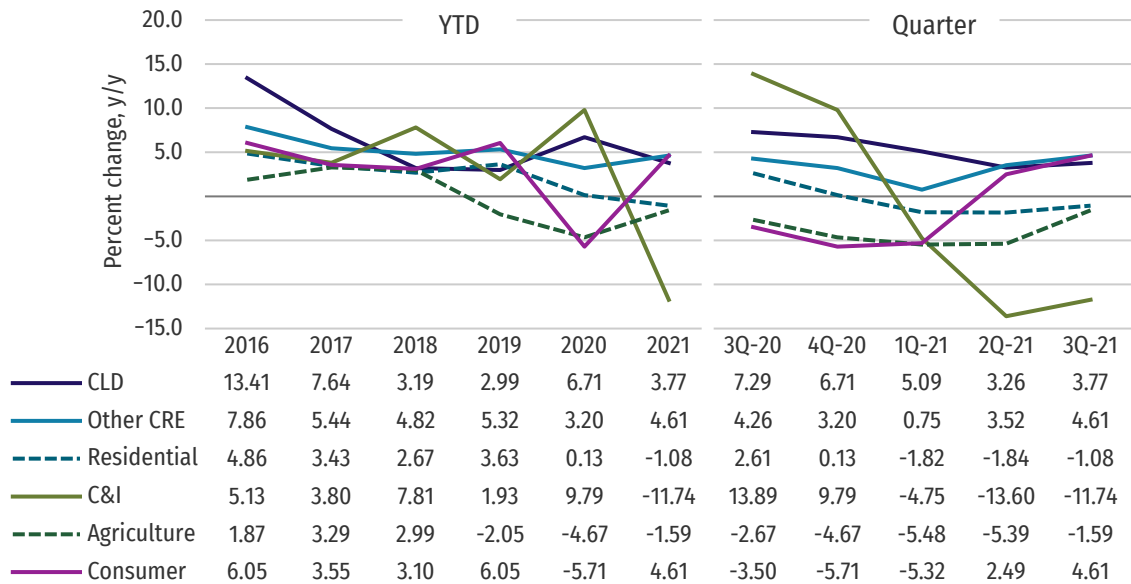


Chart C11. Year-Over-Year Loan Growth by Loan Type, Tenth District Commercial Banks

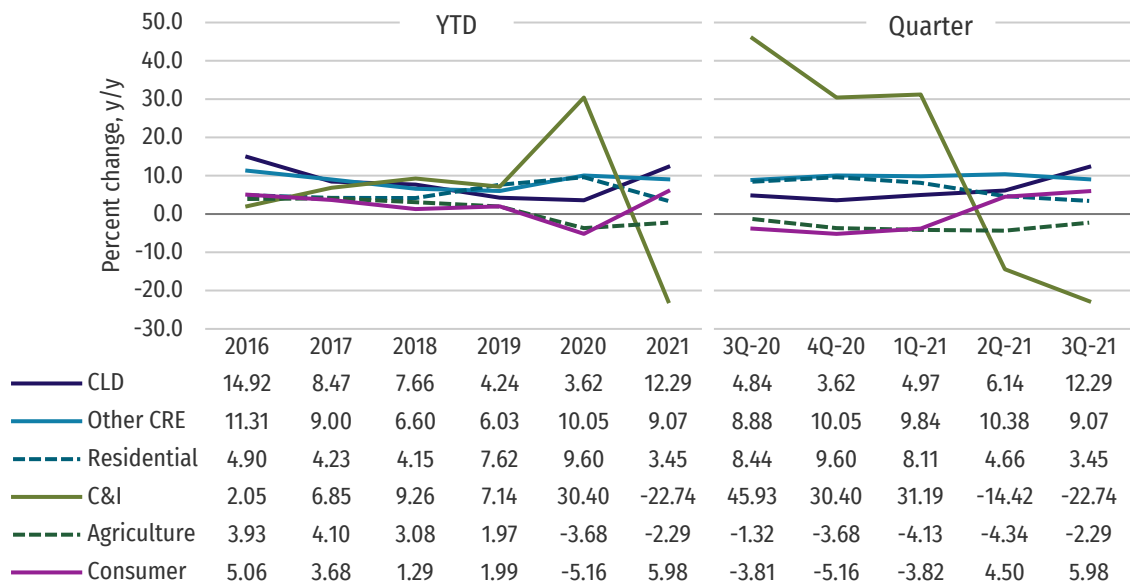


Chart C12. Quarterly Investment Securities Trends

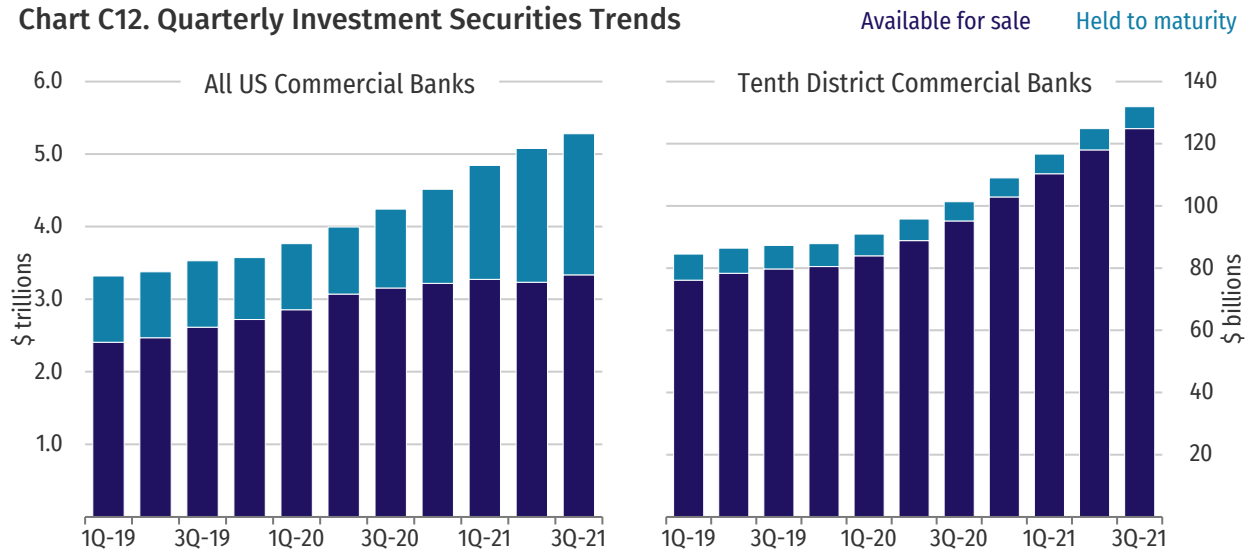


Chart C13. Investment Securities, All U.S. Commercial Banks

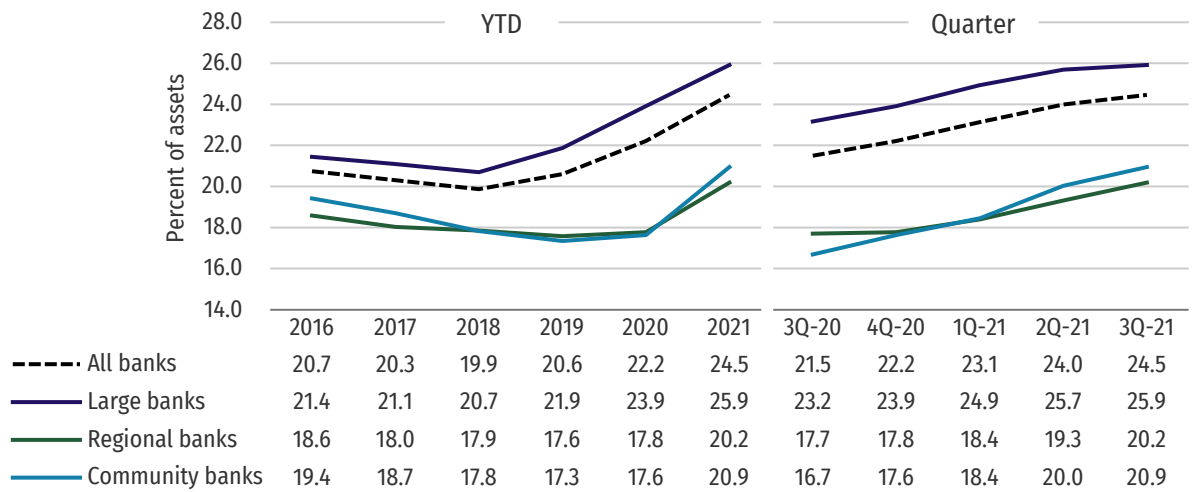


Chart C14. Investment Securities, Tenth District Commercial Banks

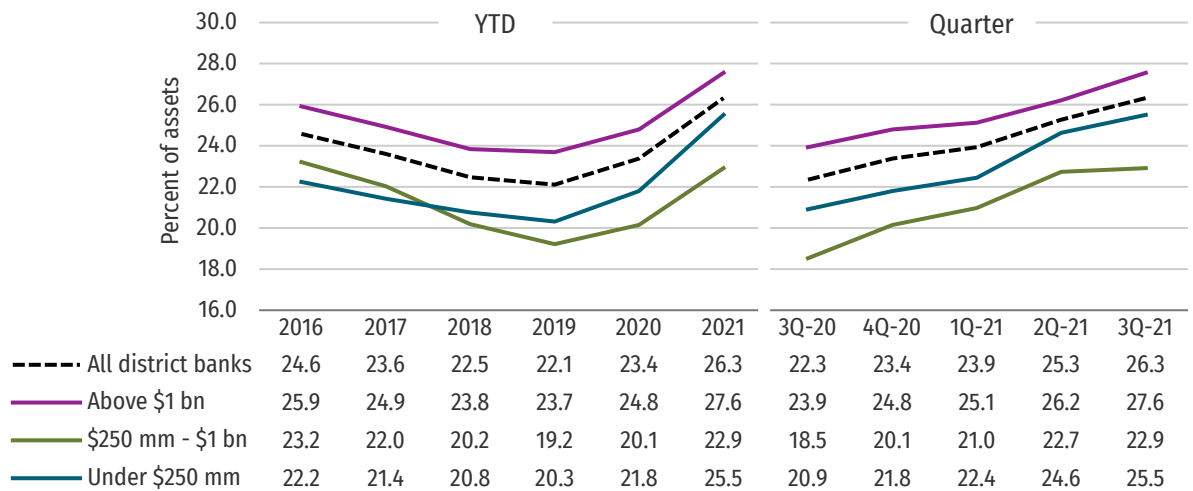


Chart C15. Cash and Reserve Holdings, All U.S. Commercial Banks

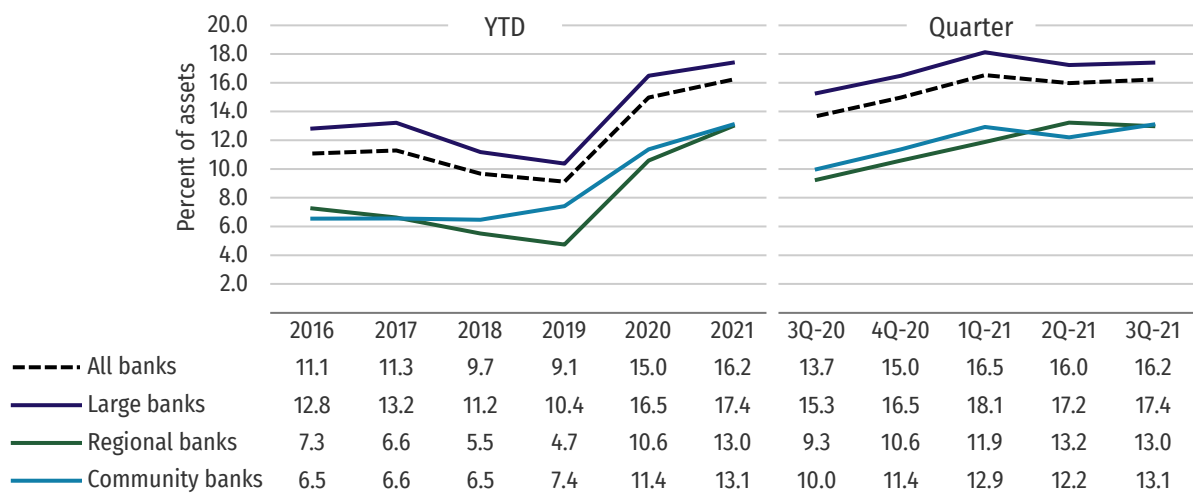
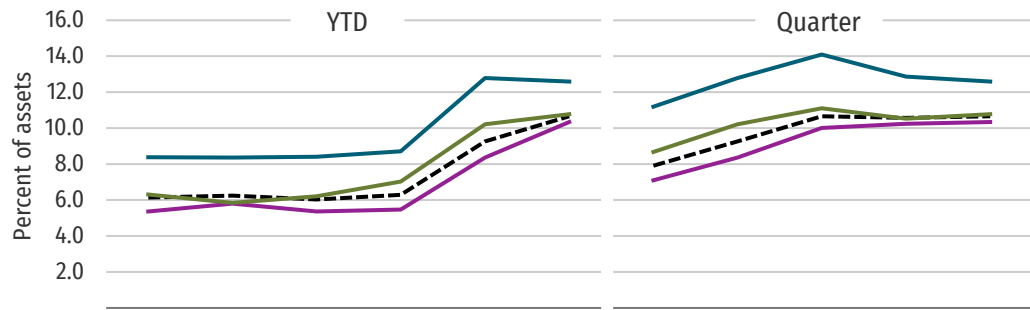


Chart C16. Cash and Reserve Holdings, Tenth District Commercial Banks



	2016	2017	2018	2019	2020	2021	3Q-20	4Q-20	1Q-21	2Q-21	3Q-21
--- All district banks	6.1	6.2	6.0	6.3	9.3	10.7	7.9	9.3	10.7	10.6	10.7
— Above \$1 bn	5.4	5.8	5.4	5.5	8.4	10.3	7.1	8.4	10.0	10.2	10.3
— \$250 mm - \$1 bn	6.3	5.8	6.2	7.0	10.2	10.8	8.7	10.2	11.1	10.5	10.8
— Under \$250 mm	8.4	8.4	8.4	8.7	12.8	12.6	11.2	12.8	14.1	12.9	12.6

D. Maturity and Funding

- The low interest rate environment incited banks to extend asset durations to protect margin.

Chart D1. Loan Portfolio Maturity & Repricing Distribution, All U.S. Commercial Banks

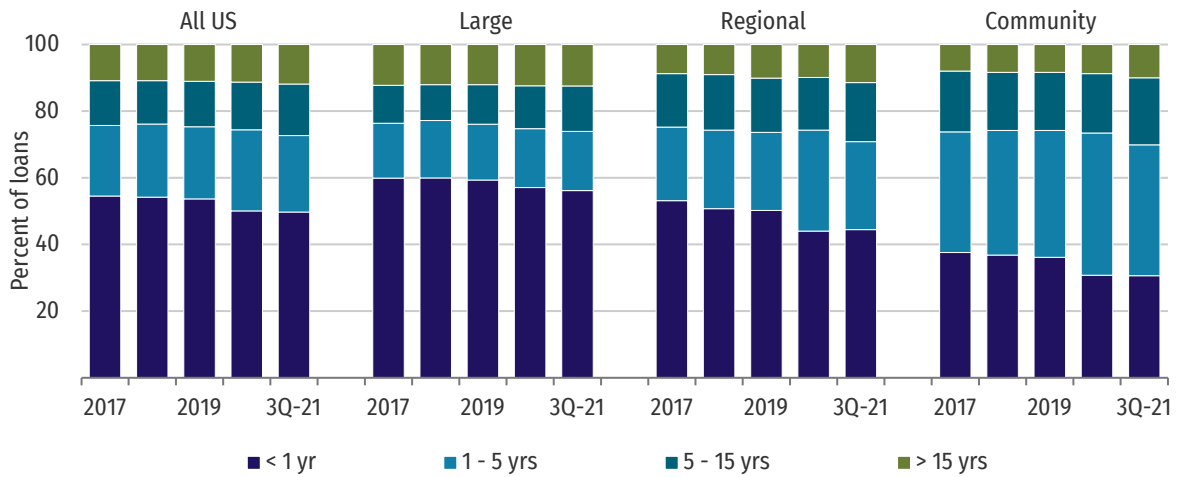


Chart D2. Loan Portfolio Maturity & Repricing Distribution, Tenth District Commercial Banks

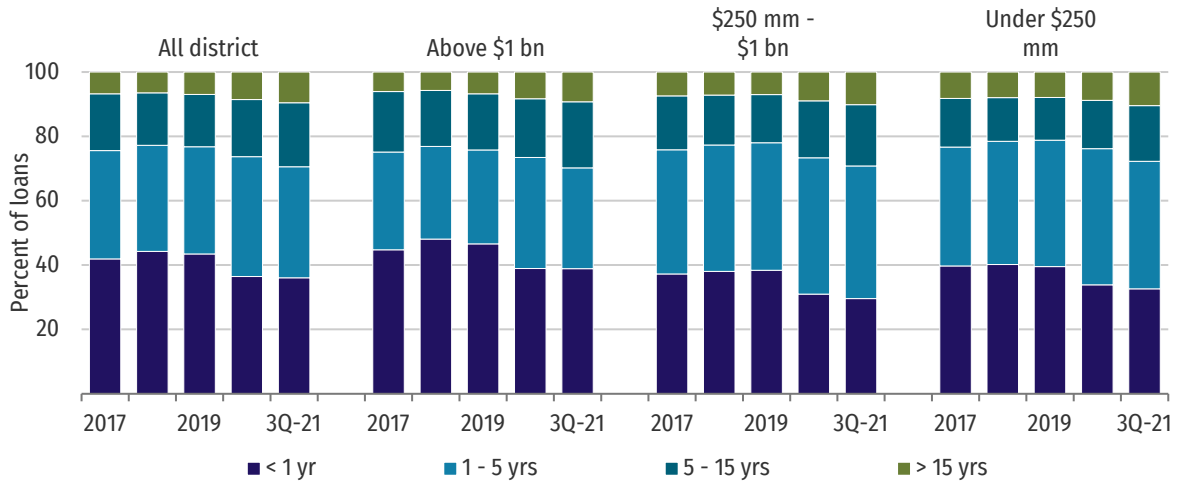


Chart D3. Securities Maturity & Repricing Distribution, All U.S. Commercial Banks

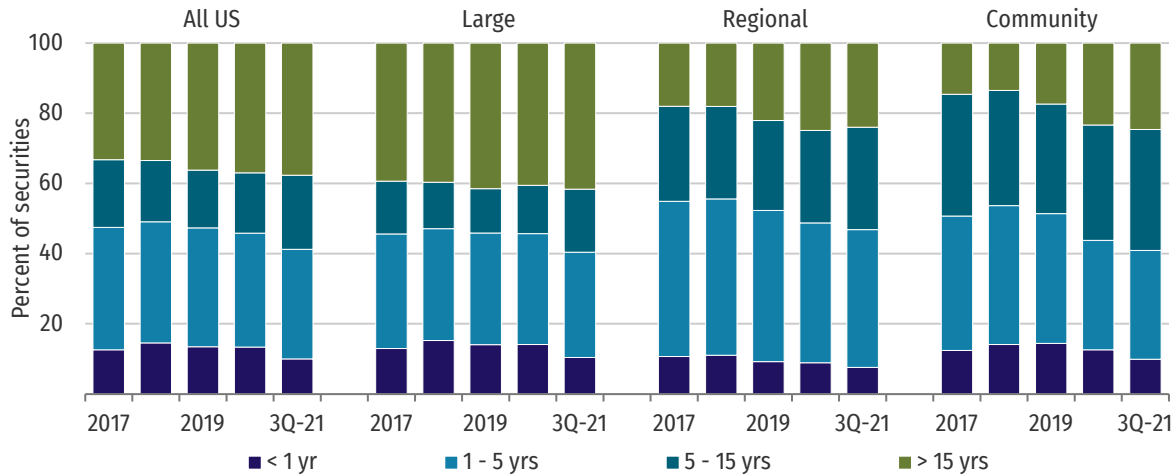


Chart D4. Securities Maturity & Repricing Distribution, Tenth District Commercial Banks

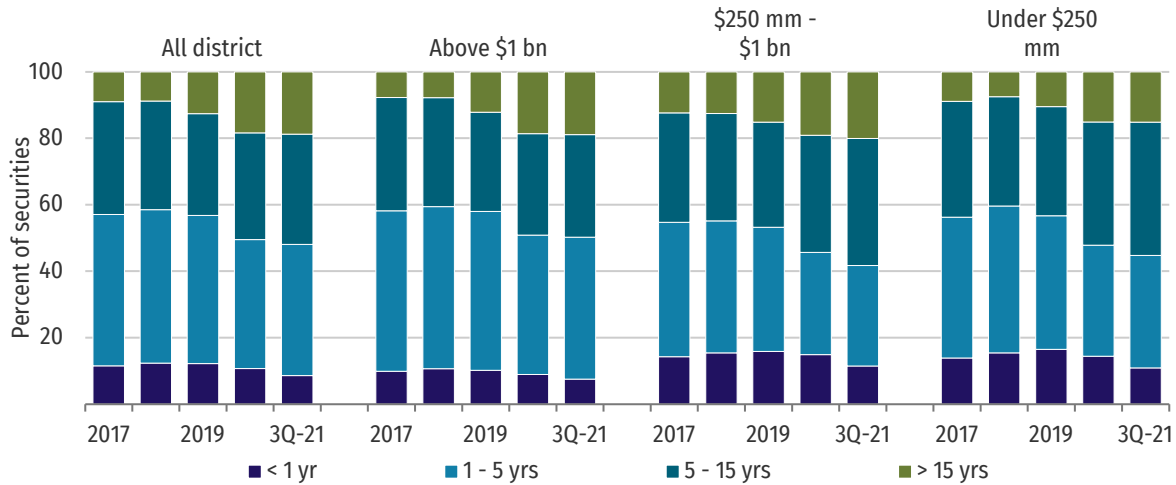


Chart D5. Loan-to-Deposit Ratios, All U.S. Commercial Banks

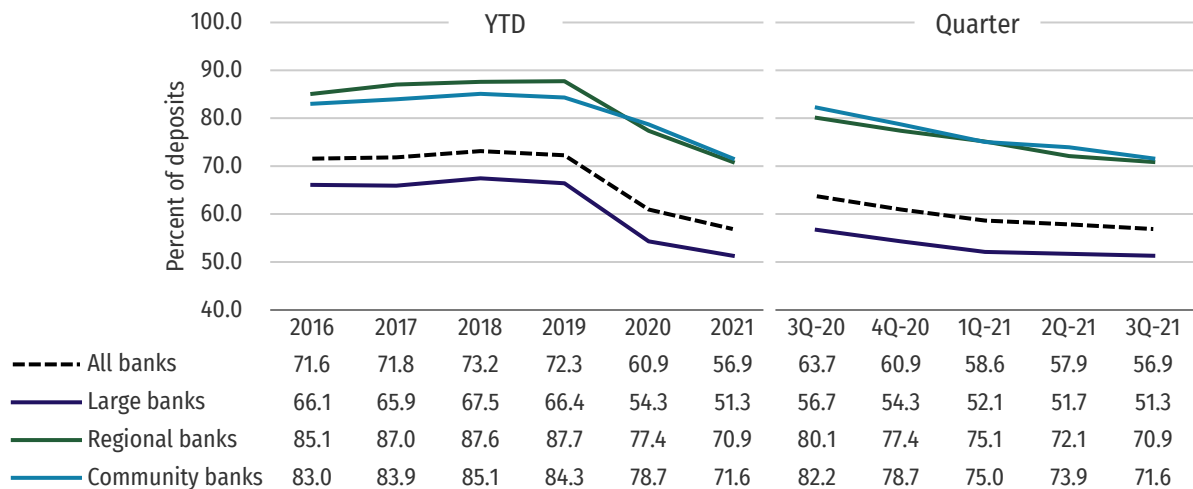


Chart D6. Loan-to-Deposit Ratios, Tenth District Commercial Banks

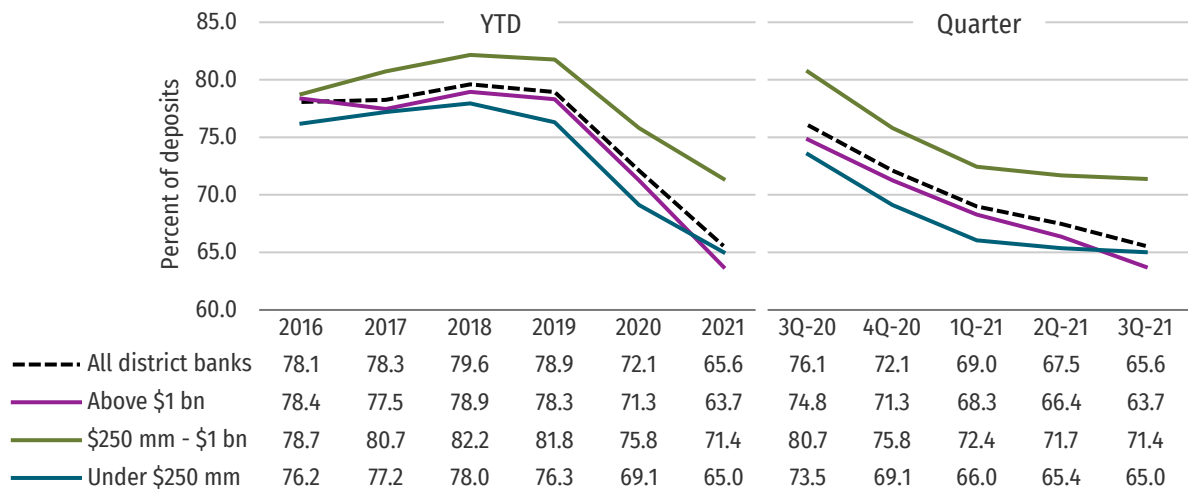


Chart D7. Quarterly Liquid Asset Trends

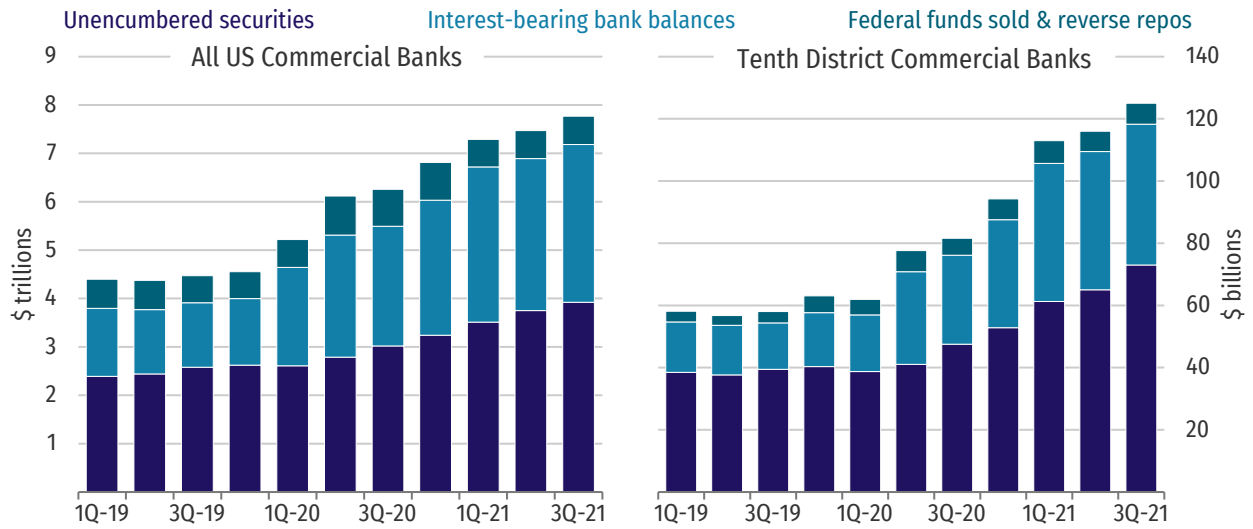


Chart D8. Liquid Asset Ratios, All U.S. Commercial Banks

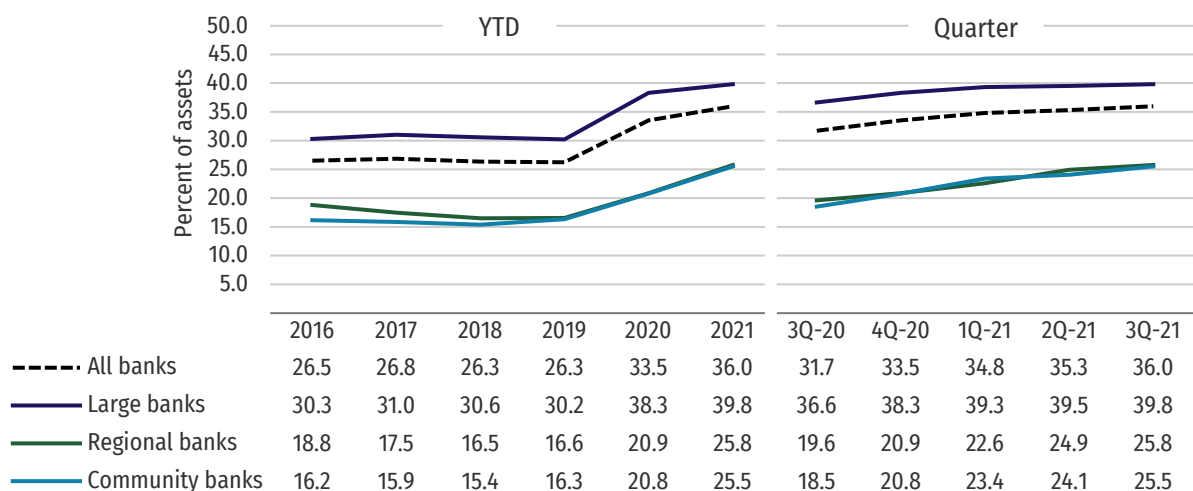


Chart D9. Liquid Asset Ratios, Tenth District Commercial Banks

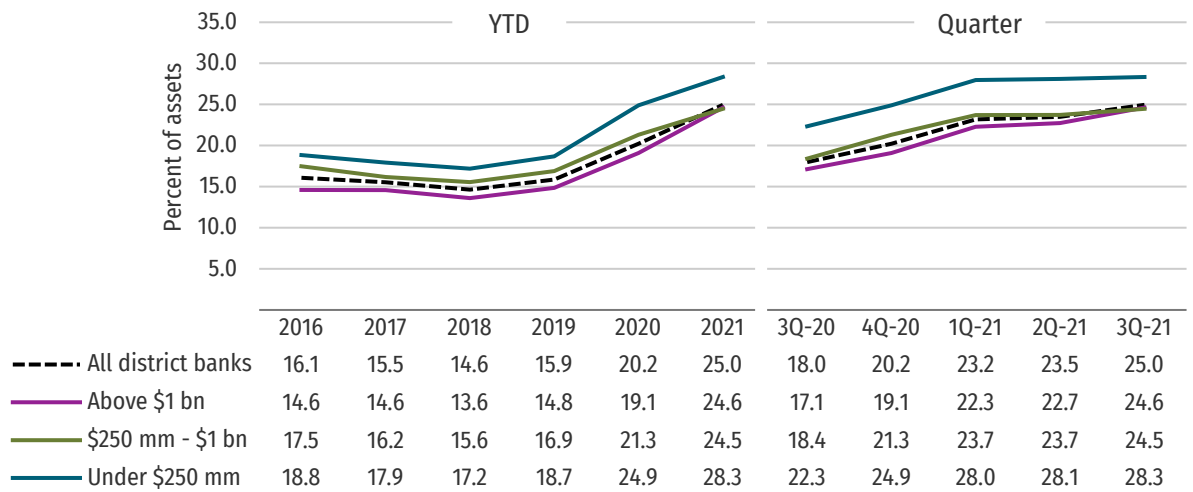


Chart D10. Quarterly Wholesale Funding Trends

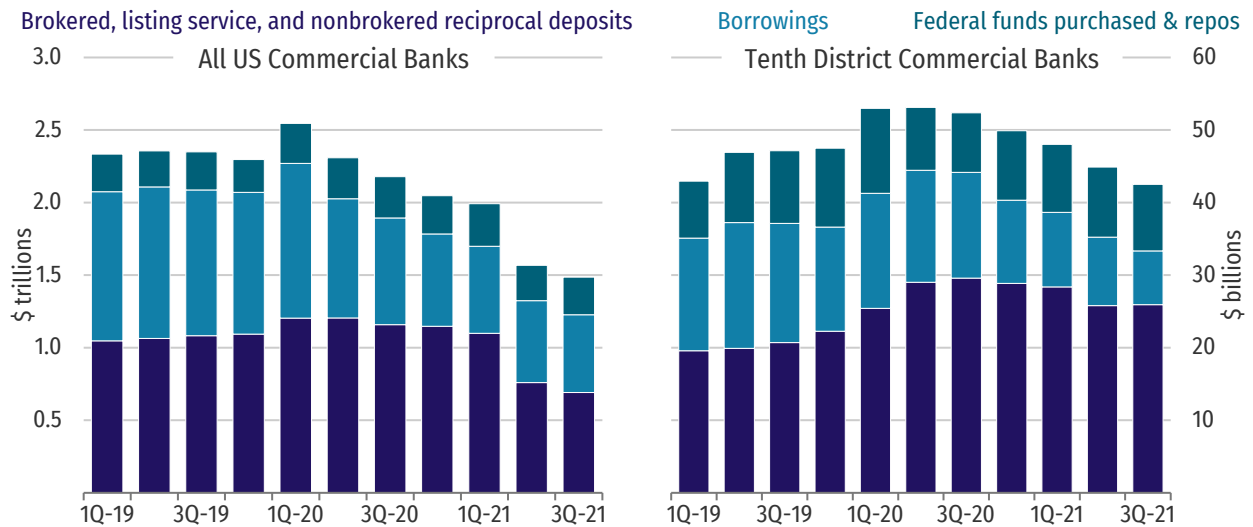


Chart D11. Wholesale Funding Ratios, All U.S. Commercial Banks

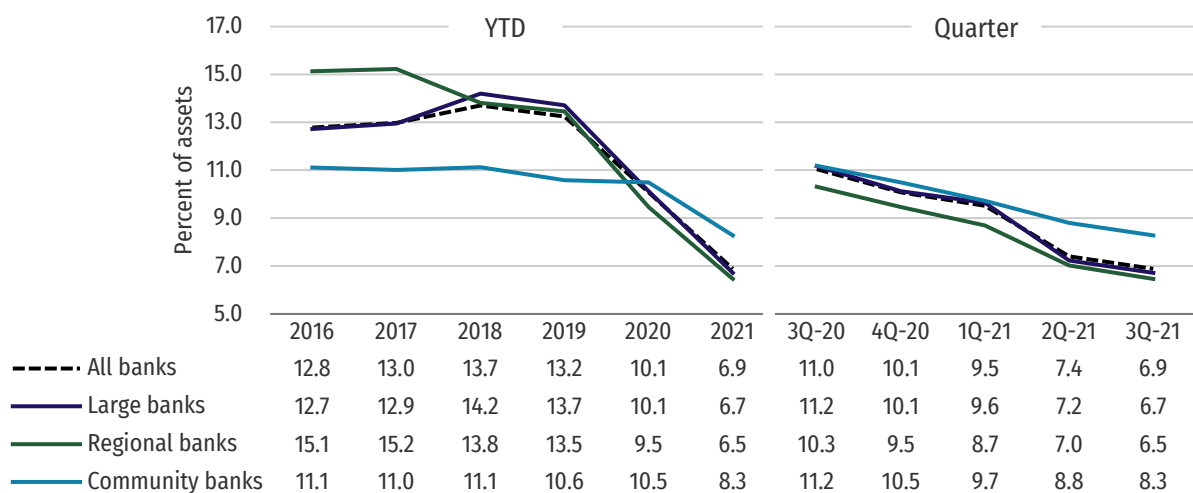
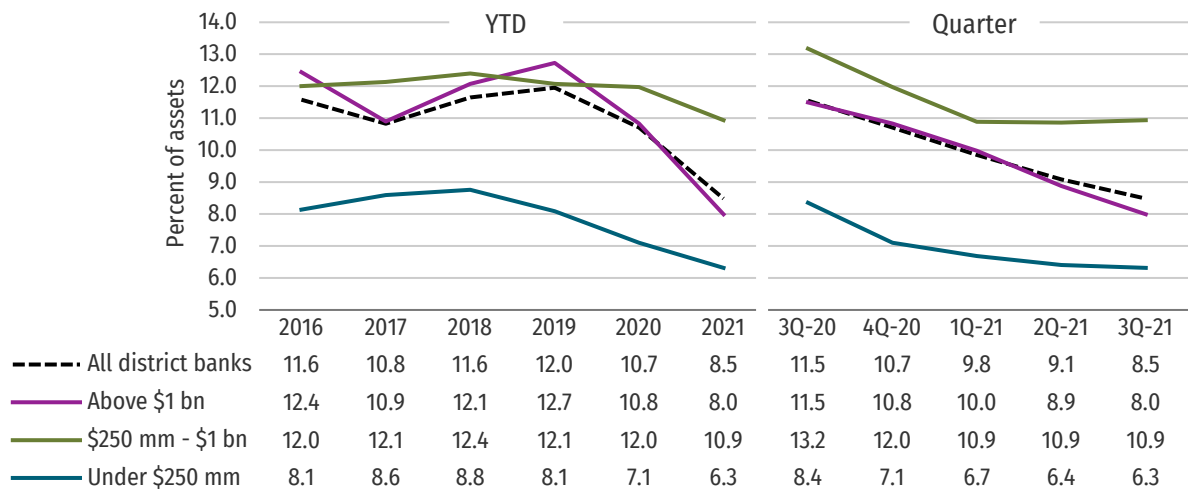


Chart D12. Wholesale Funding Ratios, Tenth District Commercial Banks



Select Ratios by Tenth District State

	Colorado		Kansas		Missouri		Nebraska		New Mexico		Oklahoma		Wyoming	
	3Q-21	3Q-20	3Q-21	3Q-20	3Q-21	3Q-20	3Q-21	3Q-20	3Q-21	3Q-20	3Q-21	3Q-20	3Q-21	3Q-20
Overview¹														
Number of Commercial Banks ²	67	67	209	214	228	233	152	156	31	31	185	188	28	28
Total Assets	\$77,966	\$68,599	\$77,809	\$73,374	\$220,199	\$191,823	\$88,587	\$81,062	\$15,212	\$13,401	\$138,663	\$128,157	\$11,455	\$10,165
Total Loans	\$43,656	\$43,071	\$44,428	\$47,108	\$126,384	\$122,737	\$57,415	\$57,401	\$7,326	\$7,626	\$78,452	\$81,215	\$5,554	\$5,527
Total Deposits	\$69,343	\$59,214	\$65,752	\$60,215	\$187,334	\$160,285	\$75,259	\$67,237	\$13,275	\$11,357	\$117,619	\$104,271	\$10,193	\$8,962
Equity Capital	\$6,863	\$6,365	\$8,570	\$8,176	\$21,010	\$19,348	\$9,439	\$8,688	\$1,459	\$1,359	\$14,647	\$13,809	\$1,111	\$1,048
Problem Assets	\$175	\$196	\$426	\$609	\$633	\$744	\$303	\$385	\$64	\$74	\$1,237	\$1,407	\$28	\$41
Earnings³														
Banks With Losses	7.46%	8.96%	2.39%	4.67%	1.32%	0.86%	1.97%	1.92%	0.00%	3.23%	1.62%	3.19%	3.57%	3.57%
Return on Average Assets	1.29%	1.23%	1.31%	1.08%	1.37%	1.21%	1.70%	1.27%	1.51%	1.51%	1.47%	1.12%	1.39%	1.34%
Net Interest Income to Average Assets	2.93%	3.22%	3.05%	3.20%	2.86%	3.08%	3.61%	3.91%	3.25%	3.61%	2.97%	3.05%	2.96%	3.29%
Provisions to Average Assets	0.03%	0.27%	0.04%	0.37%	0.02%	0.38%	0.03%	0.73%	0.06%	0.31%	-0.02%	0.51%	0.02%	0.29%
Loan Losses to Average Loans	0.01%	0.04%	0.08%	0.20%	0.09%	0.10%	0.35%	0.54%	0.08%	0.17%	0.11%	0.20%	0.04%	0.18%
Asset Quality⁴														
Problem Assets to Total Loans + OREO	0.40%	0.45%	0.96%	1.29%	0.50%	0.61%	0.53%	0.67%	0.87%	0.97%	1.57%	1.73%	0.50%	0.75%
Noncurrent CLD	0.14%	0.27%	0.06%	0.28%	0.49%	0.53%	0.10%	0.09%	0.26%	0.16%	0.16%	0.44%	0.04%	0.07%
Noncurrent Other CRE	0.34%	0.28%	0.53%	0.98%	0.32%	0.40%	0.43%	0.33%	0.59%	1.08%	0.73%	0.88%	0.17%	0.44%
Noncurrent Residential	0.20%	0.32%	0.71%	0.90%	0.32%	0.50%	0.40%	0.49%	0.68%	0.69%	4.27%	3.17%	0.33%	0.21%
Noncurrent C&I	0.57%	0.53%	1.60%	1.37%	0.63%	0.54%	0.43%	0.39%	0.95%	0.51%	0.83%	1.33%	0.97%	0.72%
Noncurrent Farm	0.26%	0.42%	0.90%	1.32%	0.27%	0.50%	0.61%	0.97%	0.00%	0.02%	1.71%	4.08%	0.78%	0.67%
Noncurrent RE Farm	0.95%	1.34%	1.54%	2.18%	0.59%	0.92%	0.88%	1.36%	0.12%	1.32%	2.25%	3.96%	0.85%	0.85%
Other Financial Ratios														
Coverage Ratio	367.80%	306.11%	188.00%	131.58%	297.86%	273.69%	333.79%	310.23%	246.97%	187.83%	96.38%	93.71%	369.97%	330.95%
Leverage Ratio	8.38%	8.68%	10.30%	10.35%	8.93%	9.18%	10.25%	10.22%	9.20%	9.56%	9.25%	9.30%	9.65%	10.01%
Tangible Equity Capital to Total Assets	8.22%	8.67%	10.48%	10.63%	8.94%	9.50%	10.10%	10.13%	9.31%	9.93%	9.55%	9.71%	9.55%	10.18%
Noncore Funding to Total Assets	3.72%	5.72%	9.37%	13.49%	7.58%	9.58%	8.01%	11.83%	5.73%	8.26%	8.87%	12.83%	7.70%	8.42%

¹ Balance sheet items shown in millions.

² Includes all commercial banks located within each state.

³ Income statement items shown as year-to-date. Average assets are calculated by using the average of YTD average assets.

⁴ Problem assets consist of loans 90+ days past due, in nonaccrual status, and other real estate owned (OREO). Noncurrent loans consist of loans 90+ days past due or in nonaccrual status.

Appendix

- The appendix provides technical notes and definitions of the financial ratios presented in this report.

Technical Notes:

The population of banks included in this report is limited to commercially chartered state member, nonmember, and national banks. The Tenth District encompasses organizations headquartered in western Missouri, Kansas, Nebraska, Oklahoma, Colorado, Wyoming, and northern New Mexico.

All financial metrics presented in this report are weighted averages. Banks are grouped into asset categories based on total assets reported as of each financial date. For purposes of this report, large banks include banks with total assets greater than \$100 billion, regional banks include banks with assets between \$10 billion and \$100 billion, and community banks include banks with assets of less than \$10 billion. Assets are measured as of each financial date. Charts that present growth rates and changes in balance sheet levels are merger-adjusted consistent with the process that FDIC analysts use to account for mergers.¹

Items from the Reports of Income are reported on a calendar year-to-date (YTD) basis by financial institutions. Ratios utilizing these items are calculated differently when presented as YTD versus quarterly. For YTD calculations, items are annualized based on values reported calendar YTD and divided by an average of the balance sheet item(s) reported for each quarter YTD. For quarterly calculations, items are annualized based on values reported for the quarter and divided by the balance sheet item(s) for that quarter.

¹ Merger-adjusted calculations add the assets and liabilities of acquired institutions to the acquiring institutions in previous periods. The analysis treats acquired and acquiring institutions as if the merger had already occurred by the beginning of the period being analyzed (Breitenstein and Thieme 2019).

References

Breitenstein, Eric C., and Derek K. Thieme. 2019. "Merger-Adjusting Bank Data: A Primer." *FDIC Quarterly*, vol. 13, no. 1, pp. 31–49.

Glossary of Terms:

Agriculture Loans

The sum of loans secured by farmland (including farm residential and other improvements) and loans to finance agricultural production and other loans to farmers.

Allowance for Loan & Lease Losses (ALLL)

The purpose of the ALLL is to reflect estimated credit losses within a bank's portfolio of loans and leases. Estimated credit losses are estimates of the current amount of loans that are probable that the bank will be unable to collect given the facts and circumstances

since the evaluation date (generally the balance sheet date).

Assets

The sum of cash and balances due from depository institutions, securities, federal funds sold and securities purchased under agreements to resell, loans and leases (net of unearned income and the allowance for loan and lease losses), trading assets, premises and fixed assets (including capitalized leases), other real estate owned, investments in unconsolidated subsidiaries and associated

companies, direct and indirect investments in real estate ventures, intangible assets, and other assets.

Cash and Reserve Holdings

The sum of interest-bearing balances (including time certificates of deposit not held for trading) and noninterest-bearing balances, currency and coin (includes cash items in process of collection and unposted debits).

Commercial and Industrial (C&I) Loans

Loans for commercial and industrial purposes to sole proprietorships, partnerships, corporations, and other business enterprises, which are secured (other than by real estate) or unsecured, single-payment or installment.

Commercial Real Estate (CRE)

The sum of CLD and other CRE.

Construction and Land Development Loans (CLD)

Construction, land development, and other land loans. Includes 1–4 family residential construction loans and other construction loans and all land development and other land loans.

Consumer Loans

Loans to individuals for household, family, and other personal expenditures. Includes credit cards, other revolving credit plans, automobile loans, and other consumer loans (includes single payment and installment loans other than automobile loans, and all student loans).

Coverage Ratio

The ALLL divided by noncurrent loans.

Earning Assets

The sum of interest-bearing balances due from depository institutions, investment securities, federal funds sold and securities purchased under agreements to resell, loans and leases (net of unearned income and the allowance for loan and lease losses), and trading assets.

Equity Capital

The sum of perpetual preferred stock (including surplus), common stock and surplus, retained earnings, accumulated other comprehensive income,

and other equity capital components, less treasury stock.

Interest Income

The sum of interest and fee income on loans, income from lease financing receivables, interest income on balances due from depository institutions (including interest income on time certificates of deposit not held for trading), interest and dividend income on securities, interest income from trading assets, federal funds sold and securities purchased under agreements to resell, and other interest income.

Investment Securities

The sum of the amortized cost of held-to-maturity securities and fair value of available-for-sale debt securities.

Leverage Ratio

Tier 1 capital divided by total assets for the leverage ratio. Total assets for the leverage ratio include quarterly average assets less deductions from common equity tier 1 capital and other deductions to total assets for leverage capital purposes.

Liquid Asset Ratio

The sum of interest-bearing balances, federal funds sold, securities purchased under agreements to resell, and unencumbered securities divided by total assets. Unencumbered securities include total securities net of pledged securities.

Loan Loss Provisions

Adjustments (charges or credits) to the ALLL level to reflect management's current estimate of expected credit losses.

Loans to Assets

Total loans and leases held for investment and held for sale (less unearned income) divided by total assets.

Loan-to-Deposit Ratio

Total loans and leases held for investment and held for sale (less unearned income) divided by total interest-bearing and noninterest-bearing deposits.

Net Interest Margin (NIM)

Interest income net of interest expense divided by average earning assets.

Nonaccrual Loans

Loans and lease financing receivables that are required to be reported on a nonaccrual basis because (a) they are maintained on a cash basis due to a deterioration in the financial position of the borrower, (b) payment in full of interest or principal is not expected, or (c) principal or interest has been in default for 90 days or longer, unless the obligation is both well secured and in the process of collection.

Noncurrent Loans

Loans past due 90 days or more and still accruing and nonaccrual loans.

Noninterest Expense

Salaries and employee benefits, expenses of premises and fixed assets (net of rental income), goodwill impairment losses, amortization expense and impairment losses for other intangible assets, and other noninterest expense.

Noninterest Income

The sum of income from fiduciary activities, service charges on deposit accounts, trading revenue, income from securities-related and insurance activities, venture capital revenue, net servicing fees, net securitization income, net gains (losses) on sales of loans and leases, other real estate owned, and sales of other assets, and other noninterest income.

Other Commercial Real Estate (CRE)

Loans secured by multifamily (5 or more) residential properties, owner-occupied nonfarm nonresidential properties, and other nonfarm nonresidential properties, and loans to finance commercial real estate, construction, and land development activities (not secured by real estate).

Other Loans

The sum of loans to foreign governments and official institutions (including foreign central banks), obligations (other than securities and leases) of states and political subdivisions in the U.S., loans to nondepository financial institutions,

loans for purchasing or carrying securities (secured and unsecured), all other loans and lease financing receivables.

Other Real Estate Owned (OREO)

Other real estate owned.

Problem Assets

Loans past due 90 days or more and still accruing, nonaccrual loans, and OREO divided by total loans plus OREO.

Residential Loans

Loans secured by 1–4 family residential properties. Includes revolving, open-end loans secured by 1–4 family residential properties and extended under lines of credit, closed-end loans secured by 1–4 family residential properties secured by first or second liens.

Restructured Loans

Loans and lease financing receivables that have been restructured or renegotiated because of a deterioration in the financial position of the obligor but remain in compliance with the modified terms of the restructuring.

Return on Average Assets (ROAA)

Net income (loss) attributable to bank divided by average assets. See technical notes for year-to-date and quarter calculations.

Revenue

Net interest income and noninterest income.

Texas Ratio

Restructured loans, nonaccrual loans, and OREO divided by equity capital plus the ALLL.

Wholesale Funding Ratio

Federal funds purchased and securities sold under agreements to repurchase, brokered deposits, deposits obtained using deposit listing services that are not brokered deposits, nonbrokered reciprocal deposits, Federal Home Loan Bank advances, and other borrowings divided by total assets.