# First Glance 12L (2Q17)

Financial Performance of Banks in the 12th Federal Reserve District ("12L")

## Bank Credit Quality Remained Solid, But For How Long?

**August 25, 2017**

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First Glance 12L: http://www.frbsf.org/banking/publications/first-glance-12l/

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# 12th District Overview
# "Bank Credit Quality Remained Solid, But For How Long?"

*Overall, employment growth in the District continued to outpace the nation, but the rate of growth decelerated further*. 12th District nonfarm jobs expanded 1.9% year-over-year, slower than prior quarters, but still above a national growth rate of 1.6%. Payroll gains in California, which accounted for 57% of total District jobs, slowed to below the national rate for the first time since 2012. Although strong, the pace of annual job growth also eased quarter-over-quarter in Idaho, Washington, and Arizona. In contrast, Hawaii, Oregon, and Nevada reported accelerating growth, and job losses slowed in Alaska (see table at right). Increasingly tight labor markets contributed to the deceleration in job gains in some states. Although headline wage growth has seemed muted given unemployment levels, research by FRBSF suggests that this dampened growth is a function of changes in labor force mix (e.g., as higher-paid Baby Boomers retire and lower-paid Millennials/part-time workers enter/re-enter the workforce).[1]

*The available supply of new and existing homes for sale lagged job growth, fueling further price increases*. Year-to-date, the West's 1-4 family housing starts increased 13.5% compared with the first half of 2016, nearly double the 7.6% national rate. Still, 1-4 family starts remained below historical average volumes in part because of construction labor shortages and other building impediments. Housing demand continued to outstrip a limited amount of new and existing homes for sale, especially entry-level homes, magnifying affordability strains in several states. According to CoreLogic, home price appreciation in the 12 months ended June remained especially strong in Washington, Utah, Idaho, and Oregon. These states also reported some of the strongest job growth and steepest declines in for-sale home inventories in recent years. Multifamily start rates were also up, which could lead to imbalances and adverse shifts in rent growth and vacancy rates in some markets prospectively.

*Commercial real estate (CRE) market data signals remained mixed*. Nationally, CRE prices marched higher in 2Q17, with the exception of retail properties. Quarterly CRE mortgage originations followed a similar trend, fed mainly by increased activity among Fannie/Freddie and commercial mortgage backed securities issuers. However, sales transaction volumes remained below prior-year levels. A 2Q17 Situs RERC Investor Survey indicated CRE investor optimism may have eased, with more respondents indicating it is a better time to sell than buy retail, downtown office, hotel, and apartment properties.

*Consumer credit showed signs of transition*. Nationwide, personal bankruptcy filing volumes increased year-over-year following several years of improvement. District filing volumes were still down relative to year-earlier figures; however, they may reach a similar inflection point soon. Nationally, credit card and auto loan delinquencies have been climbing higher according to Equifax.

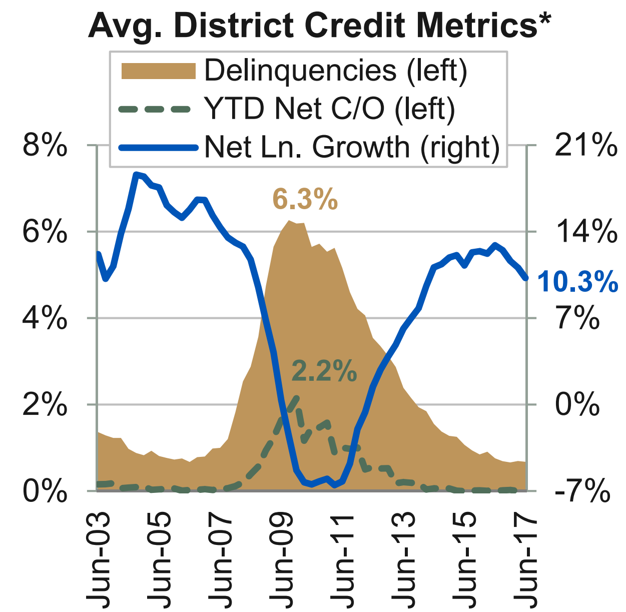
**Nonfarm Job Growth & Unemployment (%)**
*(Based on 3-Month Moving Avg., Seasonally Adj.)*

| | Year-Over-Year Nonfarm Job Growth Rate: 12-Mo. Trend | Year-Over-Year Nonfarm Job Growth Rate: 2Q17 | Unem-ployment Rate: 2Q17 |
|---|---|---|---|
| NV | | 3.38% | 4.70% |
| UT | | 3.20% | 3.23% |
| OR | | 2.47% | 3.67% |
| WA | | 2.45% | 4.53% |
| ID | | 2.43% | 3.23% |
| AZ | | 1.94% | 5.07% |
| CA | | 1.51% | 4.73% |
| HI | | 1.35% | 2.70% |
| AK | | -0.87% | 6.70% |
| US | | 1.56% | 4.37% |

Bureau of Labor Statistics / Haver Analytics

[1] *See blog post, "Good News on Wage Growth" by Mary C. Daly, Bart Hobijn, and Joseph Pedtke (http://www.frbsf.org/our-district/about/sf-fed-blog/wage-growth-good-news/).*

# 12th District Overview, Continued




*Delinquent = 30+ days past due or nonaccrual; C/O = chargeoff (year-to-date annualized); trimmed means.

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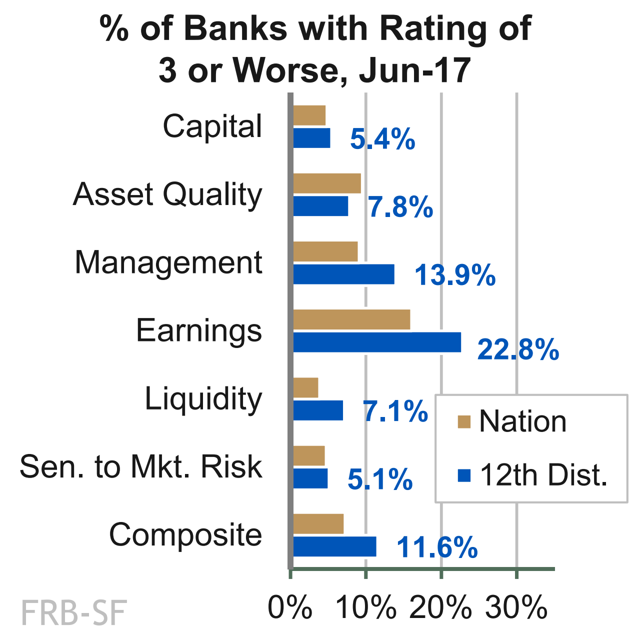


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*Loan growth slowed further in the face of easing job gains and weakening loan demand*. The District's average annual net loan growth rate decelerated to 10.3%, continuing an earlier trend (see chart at left). Nationally, the average net loan growth rate was more modest but relatively steady at 6.3%. Commercial construction and land development (C&LD) and other commercial mortgages remained an outsized source of growth, contributing to higher CRE loan concentrations. Slower growth was consistent with the Fed's Senior Loan Officer Survey, which noted continued weakening in loan demand. The District's average total past due loan ratio ebbed to 0.68%, comparable to mid-2006. However, expanding loan portfolios had a "denominator effect" on the ratio; the average growth rate in the volume of past due loans actually increased year-over-year. During the last credit cycle, the average delinquency ratio did not increase until two years after the average annual growth in delinquencies turned positive.

*Bank earnings strengthened*. The District's average first half 2017 return on average assets (ROAA) ratio (adjusted for Subchapter S tax filers) was 0.97%, up 11 bps from the same period in 2016, and surpassed a national average of 0.87%. District bank profits also improved relative to risk-weighted assets and exceeded the nationwide average for the first time since 2007. Further declines in overhead ratios and strengthening net interest margins contributed while higher effective tax rates detracted modestly. Improved technologies, stronger credit performance, and industry consolidation have fueled efficiency gains in recent years. Still, regulators have persisting concerns that cost controls may lead to shortcuts in internal controls.

*On-balance sheet liquidity weakened slightly but capital ratios stabilized*. Loan-to-asset ratios moved modestly higher year-over-year at the expense of more liquid instruments and securities. Although nonmaturity deposits (NMDs) continued to fund roughly two-thirds of bank balance sheets, the composition of those funds differed between the District and nation. Roughly half of NMDs were held in accounts with balances above $250,000, which facilitated significant loan growth since the last recession. Also, District bank NMDs were less likely to be consumer-oriented than in other regions, similar to lending patterns. In spite of balance sheet shifts, a slower rotation into higher-risk assets combined with stronger earnings contributed to the stabilization of average regulatory capital ratios, which had been trending down.

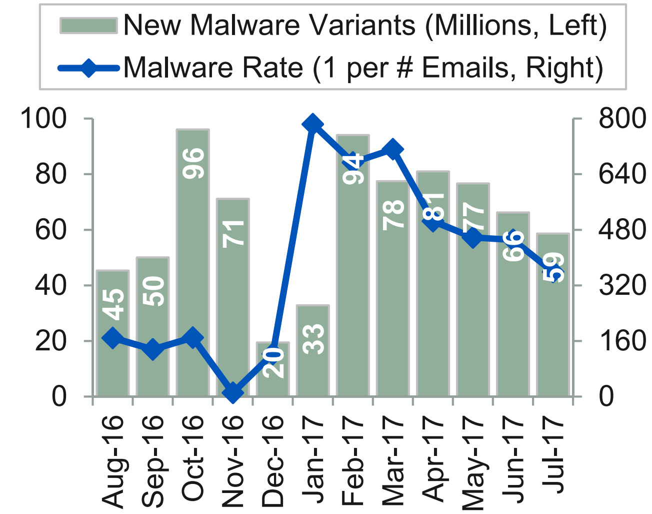
*Examination ratings improved on net*. Roughly 88% of District banks were rated satisfactory or strong for safety and soundness, with Earnings and Management ratings trailing other component areas (see chart at left). Although upgrades outpaced downgrades in the past year, increased downgrade activity was noted in several component areas, particularly Management. Favorably, more than 95% of District banks were rated satisfactory or better for consumer and/or Community Reinvestment Act compliance.

# <u>Hot Topics</u>: Areas We are Monitoring Most Closely

The following areas are drawing heightened supervisory attention within the 12th District based on risk exposures and metrics of Federal Reserve-supervised institutions:

- *Cyberthreats continued to evolve*. According to Symantec's *Monthly Threat Report*, the email malware rate worsened in July 2017 to one in every 359 emails, and there continued to be millions of new malware variants each month (see chart at right). For institutions outsourcing core operations and/or security administration, vendor management programs remain critical to managing and mitigating cyberthreats. Inherent risks can increase from a variety of factors, such as system complexity, services, and visibility. The Federal Financial Institutions Examination Council developed an optional tool to help banks assess the adequacy of their cybersecurity preparedness, which is described in SR letter 15-9, available at http://www.federalreserve.gov/bankinforeg/srletters/sr1509.htm.
- *Bank Secrecy Act (BSA)/Anti-Money Laundering (AML) compliance*. Although most banks in the District have satisfactory BSA compliance programs, BSA/AML continues to be a significant "hot topic" due to the District's role in the global economy and the array and strategic focus of supervised institutions. Year-over-year through July, BSA/AML Suspicious Activity Reports filed by depository institutions operating in the District increased and accounted for a rising share of all such filings nationwide (see chart at right). BSA/AML risks have increased now that seven District states allow recreational or medicinal cannabis use. BSA/AML-related criticisms noted at bank examinations most often relate to internal controls (e.g., institutional risk assessments, customer due diligence, and suspicious activity monitoring programs). Concerns related to weak program oversight and ineffective independent tests are also emerging as examination themes.
- *Consumer compliance issues.* In addition to redlining, overdraft practices have gained attention. Consumer overdraft fees generate a significant share of deposit service charges, but not without legal, regulatory, and reputational risk. Litigation and/or regulatory action has occurred at banks that used the "available balance method" when assessing overdraft fees, imposed "continuing negative balance" fees on extended overdrafts, or added overdraft balances to loans without customer authorization.
- *Lengthening asset maturities*. Following the financial crisis, many banks increased their holdings of longer-term assets, driven by low short-term interest rates and a relatively steep yield curve. This trend moderated somewhat in the past two years; however, the proportion of longer-dated assets remained elevated. In a rising interest rate environment, longer-term assets are slower to reprice and could mute margin expansion if not appropriately matched, hedged, or managed.

**Malware Trends, All Industries**




Source: Symantec Monthly Threat Report, July 2017

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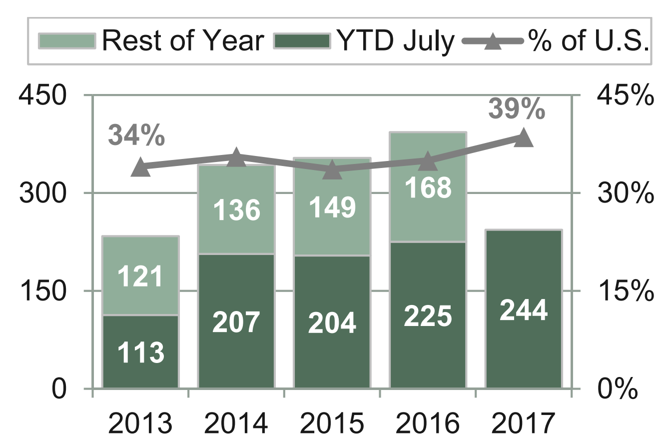
**BSA/AML-Related SAR Volumes**
***Thousands, 12th District***




SAR = suspicious activity report; includes Depository Institution SARs related to AML and structuring.
Source: FINCEN | Stats, FRBSF

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# Hot Topics: Areas We are Monitoring Most Closely

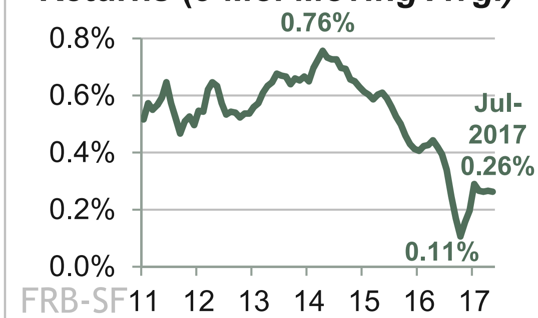
- *Quality of loan growth*. The District's average annual net loan growth continued to outpace the national average in several District states. Economic expansion played a role, as did commercial property price appreciation. However, many loans were underpinned by near-historic values and some lenders loosened standards. Recent credit performance has been good, but now is a critical time in the cycle for bankers to maintain lending discipline and enhance risk management practices.
- *Commercial real estate lending concentrations*. CRE (i.e., non-owner occupied nonfarm-nonresidential, multifamily, C&LD, and other CRE-purpose) loan concentrations to capital declined during the recession, but have edged higher since 2013, and averages remained at or above the U.S. average across all District states (see table at right). Increased loan concentration levels, combined with potential competitive easing of underwriting standards and elevated property prices heighten regulatory concern. A rising interest rate environment could negatively impact debt service coverage ratios on variable-rate commercial mortgages and pressure commercial property price appreciation. Given the increasing risks, lenders should review CRE risk management guidance, including the 2015 *Interagency Policy Statement on Prudent Risk Management for Commercial Real Estate Lending* (SR letter 15-17 available at http://www.federalreserve.gov/bankinforeg/srletters/sr1517.htm).
- *Nonmaturity Deposit (NMD) risk management*. NMDs, which are traditionally viewed as "core" deposits, have become an increasingly important source of funding for most institutions. While these products proved inexpensive in a low-rate environment, these funds may disintermediate or transition to higher-cost deposit products in a rising interest rate environment. During the last economic expansion and rate tightening cycle (2004-2006), the mix of bank funding shifted away from NMDs and toward higher-cost time deposits and borrowings as loan demand outstripped NMD availability.
- *Balancing overhead expense pressures with risk management requirements*. Asset growth has led to some economies of scale and improved efficiency ratios have helped boost profitability. There is a regulatory concern that banks may not be devoting sufficient resources to back-office operations, internal controls, and compliance programs commensurate with their increasing size and complexity.
- *Financial technology (fintech) opportunities and threats*. Depository institutions have increasingly partnered with fintech companies, and with marketplace lenders in particular. Given the different origination and underwriting methods that consumer fintech lenders may use, banks should closely evaluate transactions for credit risk, fair lending, and unfair/deceptive acts or practices, especially since credit decisions may use nontraditional data sources. Data from Orchard Platform's U.S. Consumer Online Lending Index indicated that online consumer lending returns (a function of yields, loan prices, re/prepayments, and chargeoffs) have declined since peaking in mid-2014. Returns sank in late 2016 because of loan losses and pricing, but improved with rising interest rates in 2017.

**Average Commercial Real Estate Loans / Total Capital* (%)**

| FRB-SF | 2007-17** | Jun-17 |
|---|---|---|
| NV | 385% | 262.8% |
| CA | 302% | 261.6% |
| OR | 380% | 241.2% |
| WA | 334% | 227.1% |
| AZ | 378% | 167.9% |
| ID | 251% | 159.8% |
| HI | 173% | 151.6% |
| AK | 188% | 132.7% |
| UT | 337% | 130.8% |
| Nation | 222% | 124.6% |

*Trimmed means; excludes owner-occupied ; **June of each year

**Online Consumer Loan Returns (*3-Mo. Moving Avg.*)**




*Orchard Platform U.S. Consumer Online Lending Index Returns*

# Section 1
# Economic Conditions

**Job Growth**

**Export Activity**

**Housing Market Metrics**

**Commercial Real Estate Market Conditions**

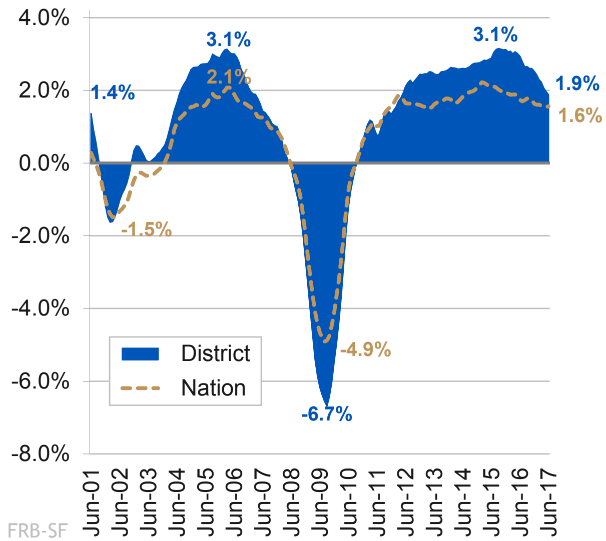
**Consumer Credit**

For more information on the District's real estate markets and economy, see:
Real Estate Lending Risks Monitor
(http://www.frbsf.org/banking/publications/real-estate-lending-risks-monitor/)
Banks at a Glance
(http://www.frbsf.org/banking/publications/banks-at-a-glance/)

For more information on the national economy, see:
FRBSF FedViews
(http://www.frbsf.org/economic-research/publications/fedviews/)
FOMC Calendar, Statements, & Minutes (https://www.federalreserve.gov/monetarypolicy/fomccalendars.htm)

# Job Growth Slowed Further; Slowing Was Relatively Broad-Based

## Year-Over-Year Nonfarm Job Growth




**Job Growth by Sector 12th District**

| Job Sector | 1-Yr % Change 2007-17* | 1-Yr % Change 2Q 2017 |
|---|---|---|
| Construction | | 5.62% |
| Educ. & Health Svcs. | | 2.81% |
| Leisure & Hospitality | | 2.80% |
| Other Private | | 2.27% |
| Transport. & Utilities | | 2.13% |
| Financial Activities | | 1.82% |
| Government | | 1.60% |
| Prof. & Business Svcs. | | 1.44% |
| Wholesale Trade | | 1.10% |
| Retail Trade | | 0.90% |
| Information | | 0.12% |
| Manufacturing | | -0.24% |
| Total | | 1.88% |

*Note: Construction sector includes mining in HI; Information sector excludes HI and NV.*

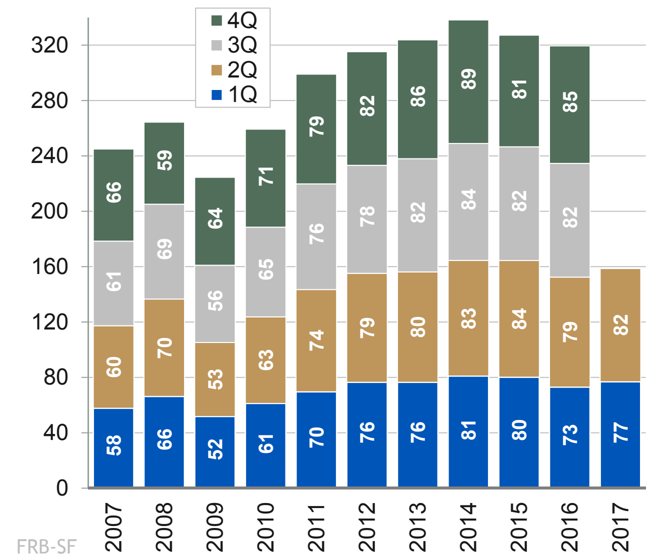
Based on average nonfarm payroll levels over trailing three months; data are preliminary estimates; *year-over-year change in sector table as of second quarter of each year. Source: Bureau of Labor Statistics via Haver Analytics.





# First Half Exports Led Higher by Machinery (CA, OR), Primary Metals (NV, CA, UT) and Ag. (WA, CA, OR)

## 12th District Exports *($Billions)*




**Export Volumes, Growth, and Importance**

| | Export Vol. ($) 2007-17 *(1H each year)* | Export 1-Year Growth Rate *(1H17)* | Exports/ GSP* *(1H17 Ann'd.)* |
|---|---|---|---|
| AK | | 2.6% | 5.2% |
| AZ | | -2.9% | 7.3% |
| CA | | 7.1% | 7.0% |
| HI | | -15.7% | 1.6% |
| ID | | -14.8% | 6.2% |
| NV | | 41.1% | 9.1% |
| OR | | 7.7% | 10.4% |
| UT | | 7.4% | 8.9% |
| WA | | -4.4% | 16.6% |
| 12L | | 4.1% | 8.3% |
| Nation | | 6.5% | 8.6% |

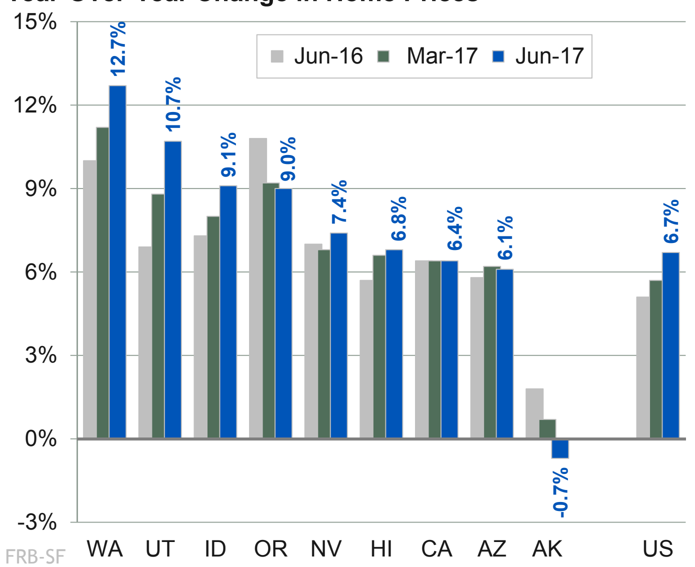
*Based upon first half 2017 exports times two divided by 2016 average Gross State Product (GSP). Sources: WISER Trade, Bureau of Economic Analysis via Haver Analytics.





# Rapid Home Price Appreciation in WA, UT, ID, and OR In Part a Function of Tight Home Inventories

## Year-Over-Year Change in Home Prices




**Cumulative Change in Inventory of Homes for Sale (%)**

| | Jun-12 to Jun-17 | Jun-16 to Jun-17 | Mar-17 to Jun-17 |
|---|---|---|---|
| WA | -48% | -23% | -6% |
| UT | -42% | -18% | -5% |
| OR | -40% | -9% | -3% |
| ID | -39% | -22% | -9% |
| CA | -36% | -19% | -5% |
| NV | -28% | -2% | -5% |
| AK | -18% | -11% | -3% |
| HI | -14% | -18% | -9% |
| AZ | -9% | -13% | -4% |

Sources: CoreLogic (includes all detached and attached homes, including distressed sales); Zillow (for sale inventory is smoothed/seasonally adjusted).

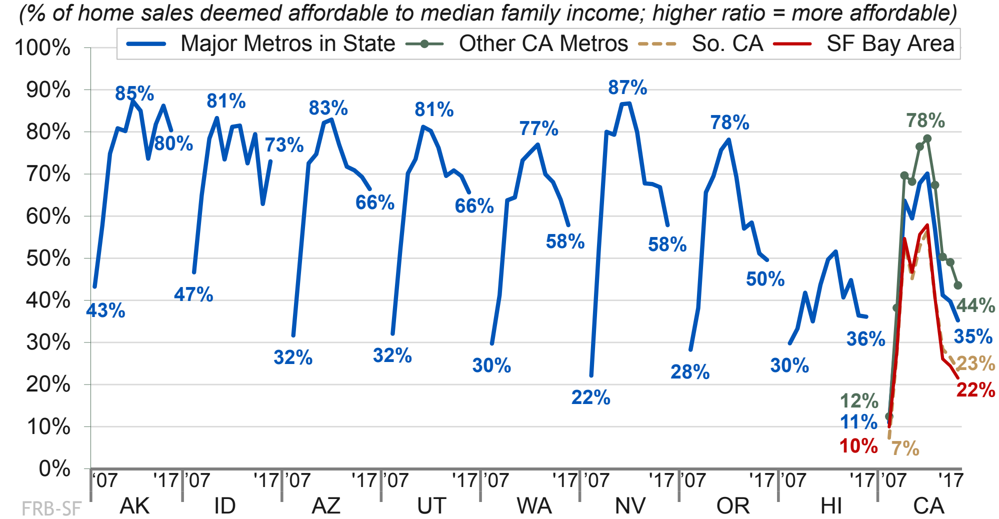




# Continued Home Price Appreciation and Higher Mortgage Rates Crimped Affordability, Especially in California

## Un-weighted Average Metro Area Housing Opportunity Index, Jun-07 to Jun-17

*(% of home sales deemed affordable to median family income; higher ratio = more affordable)*

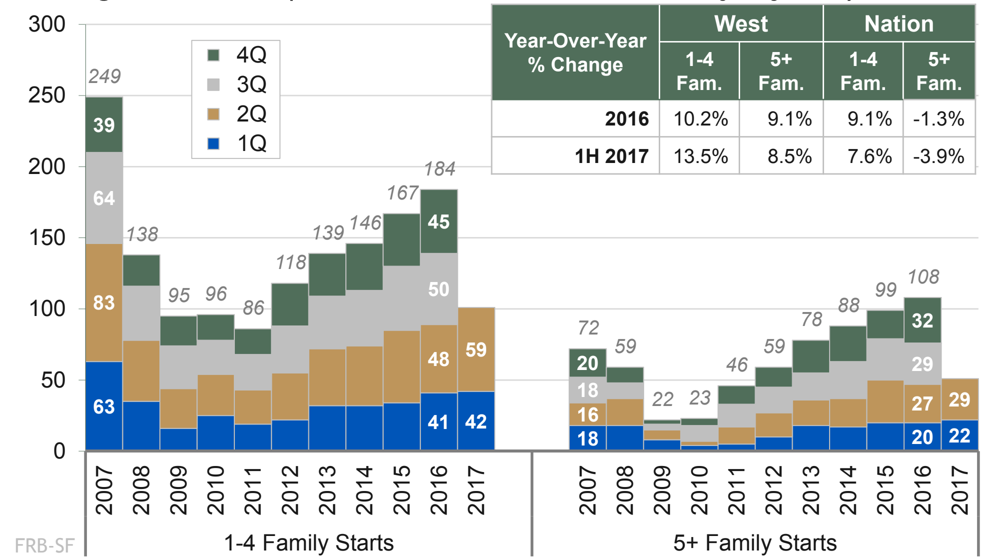



Assumes median income, 10% down payment, ratio of income-to-housing costs (principal, interest, taxes, and hazard insurance) of 28%, and a fixed-rate, 30-year mortgage; So. CA = Los Angeles, Orange, Riverside-San Bernardino, San Diego, and Ventura metros; SF Bay Area = San Francisco, Oakland, San Jose, Napa, Vallejo, and Santa Cruz metros. Sources: National Association of Homebuilders/Wells Fargo, Federal Reserve Bank of San Francisco.

Economy

## Growth in Regional 1-4 Family Starts Accelerated; Growth in Multifamily Starts Far Exceeded the Nation

**Housing Starts – West *(Thousands Of Units, Not Seasonally Adjusted)***




| Year-Over-Year % Change | West 1-4 Fam. | West 5+ Fam. | Nation 1-4 Fam. | Nation 5+ Fam. |
|---|---|---|---|---|
| 2016 | 10.2% | 9.1% | 9.1% | -1.3% |
| 1H 2017 | 13.5% | 8.5% | 7.6% | -3.9% |

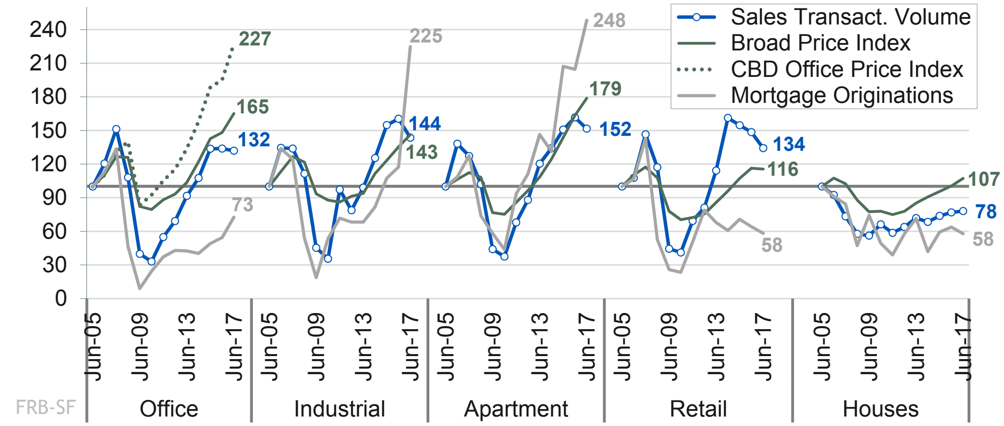
West = 12th District plus CO, MT, NM, and WY. Source: Census Bureau/Haver Analytics.



Economy

## CRE Property Prices and Mortgage Originations Surged Year-Over-Year for All but Retail; Sales Transactions Ebbed

**U.S. Real Estate Transaction and Lending Metrics *(Indexed, June 2005 = 100)***




**Memo: Year-Over-Year % Change, 2Q17**

| | Office | Industrial | Apartment | Retail | Houses |
|---|---|---|---|---|---|
| Transact. | -1% | -11% | -6% | -10% | 2% |
| Prices | 11% | 8% | 9% | -1% | 7% |
| Original. | 33% | 91% | 21% | -9% | -9% |

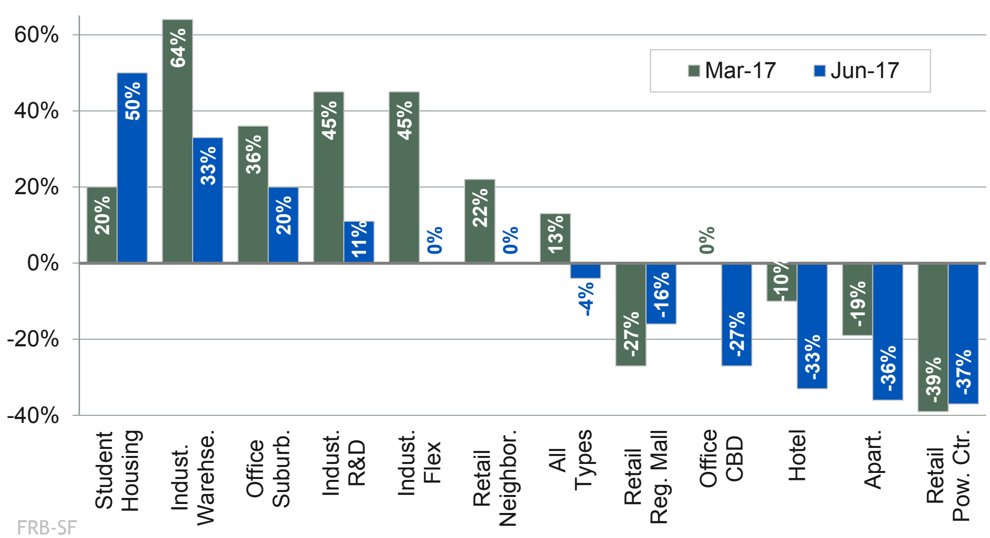
Transaction volume index based upon number of sales; CBD = central business district (downtown). Sources: Moody's/RCA (commercial property prices); Core Logic (home prices); Real Capital Analytics (commercial transaction volume), National Association of Relators (existing home sales volume); Mortgage Bankers Association/Haver (origination volumes).



Economy

## CRE Investors Less Sanguine Per Situs RERC Survey; High Prices/Weaker Outlook Left Fewer Opportunities

**Net Percent of Respondents Indicating Now a Good Time to Buy CRE in Sector**



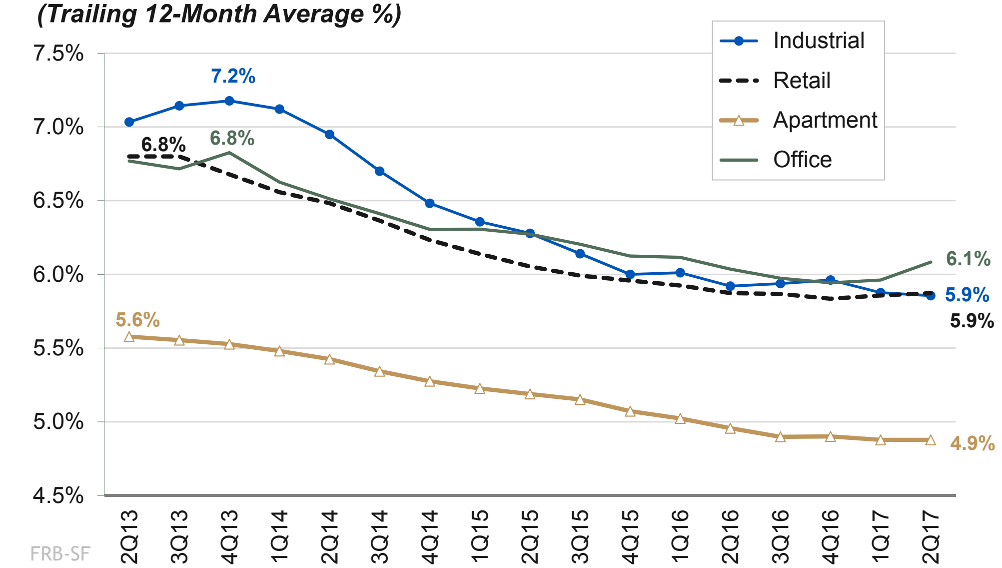

Based on a survey of CRE institutional investors; represents share stating it is a good time to buy minus those stating it is a good time to sell; R&D = research & development; CBD = central business district (downtown); Source: Situs RERC Investor Surveys (via quarterly *Flash Reports*).



Economy

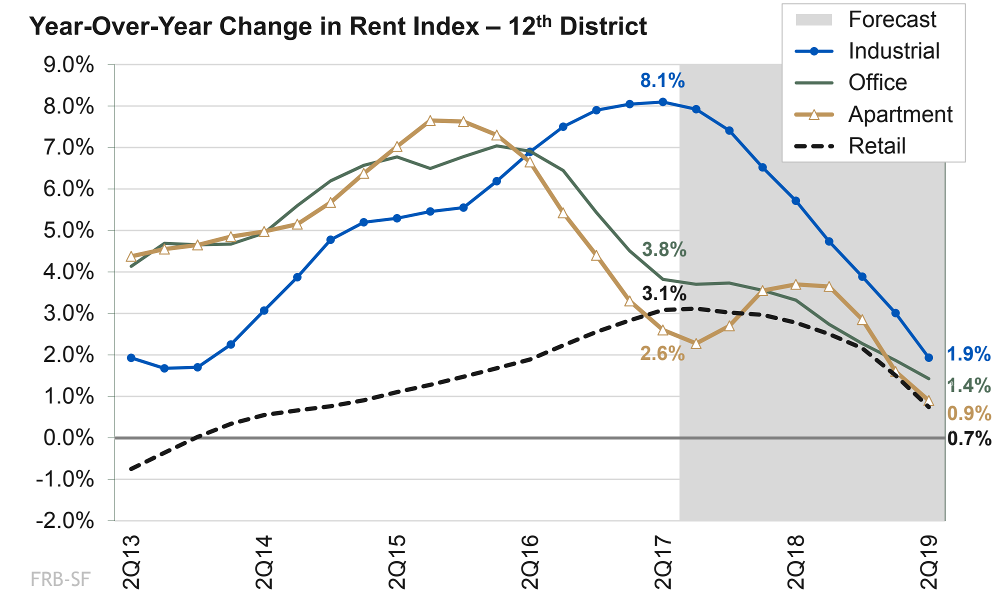
## Despite Lower Transaction Volumes, Capitalization Rates Held Steady for Most CRE Sectors in the West

**Commercial Real Estate Capitalization Rates – West *(Trailing 12-Month Average %)***




West = AK, CA, HI, ID, MT, NV, OR, UT, WA, and WY (excludes AZ); limited to property sales > $2.5 million for which capitalization rate data was available. Source: Real Capital Analytics.

## CBRE Econometric Advisors Expects Overall 12th District CRE Rent Growth to Slow Further

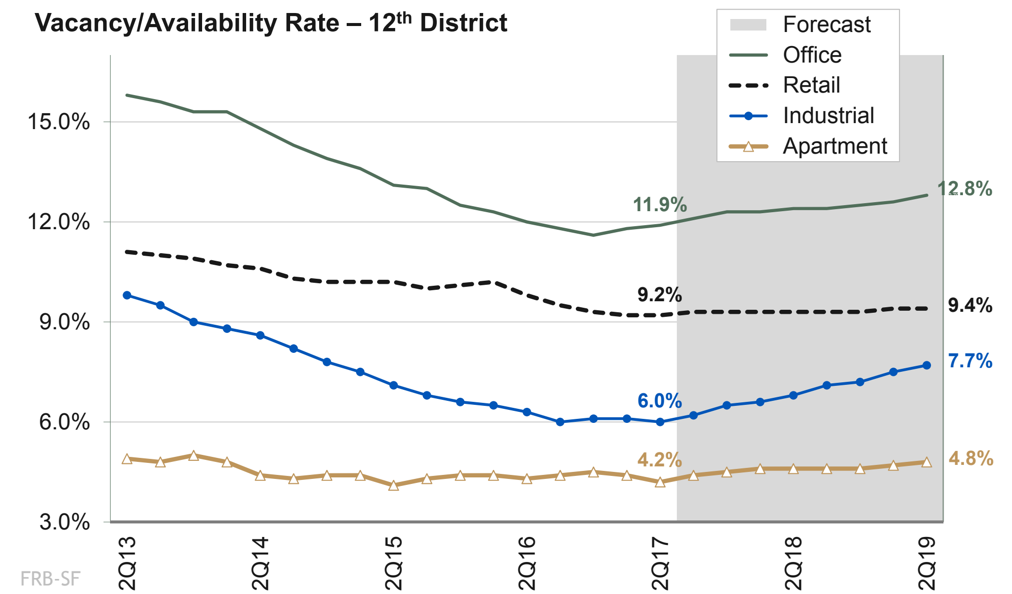



12th District based on aggregates across 15-16 large metropolitan areas; retail data relates to neighborhood and community centers only. Source: CBRE Econometric Advisors ("baseline" forecast).





## CBRE Forecasts Also Suggest Aggregate 12th District Vacancy/Availability Rates May Drift Higher

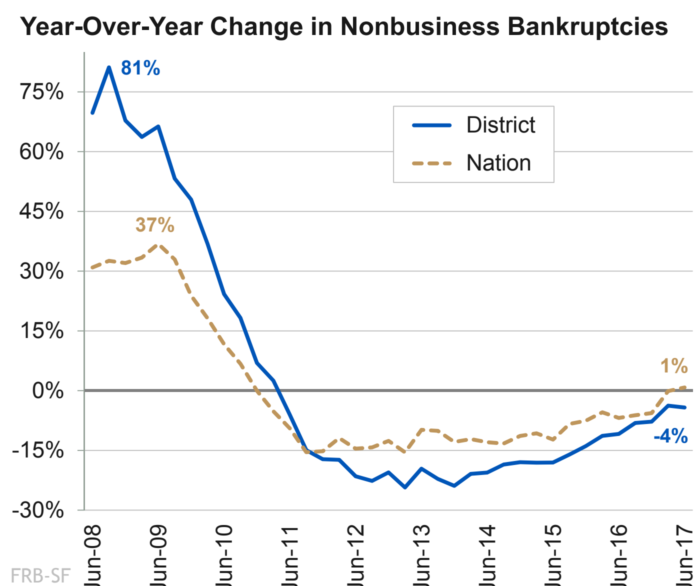



12th District based on aggregates across 15-16 large metropolitan areas; apartment vacancy based upon number of units; retail data relates to neighborhood and community centers only. Source: CBRE Econometric Advisors ("baseline" forecast).





## Consumer Sector Showing Signs of Transition; Are Personal Bankruptcy Filings Nearing a Trough?




**Personal Bankruptcy Filings**

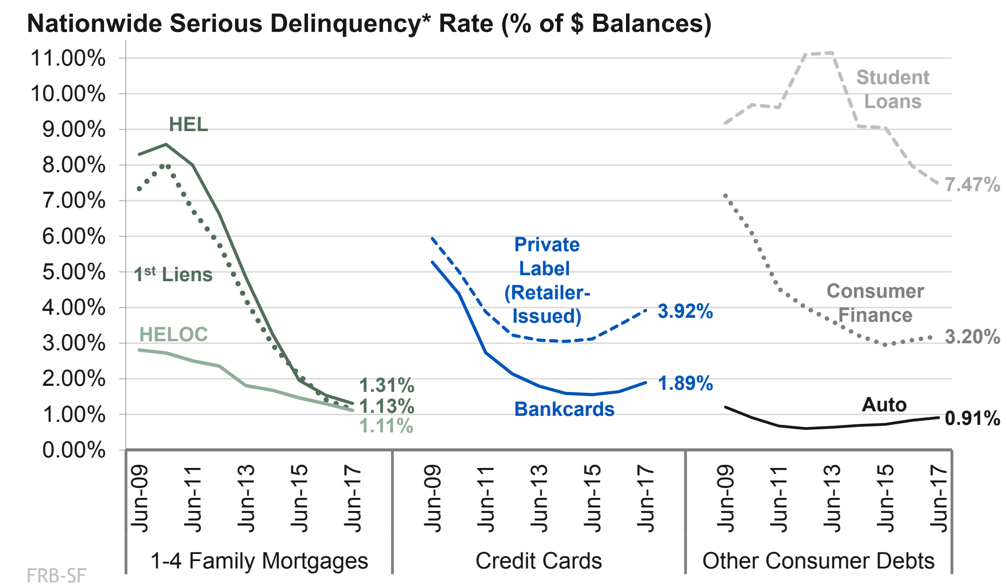
| | Year-Over-Year Change 2008-YTD 17 | Year-Over-Year Change 2Q17 | Rate Per 1,000 HH YTD Jun-17 |
|---|---|---|---|
| WA | | -10.1% | 2.83 |
| HI | | -7.6% | 1.45 |
| CA | | -6.4% | 2.76 |
| NV | | -0.3% | 4.32 |
| UT | | -0.2% | 6.25 |
| AZ | | 1.0% | 3.15 |
| OR | | 1.5% | 3.02 |
| ID | | 2.9% | 3.18 |
| AK | | 19.6% | 0.92 |
| US | | 0.8% | 3.38 |

Sources: Administrative Office of the United States Courts (bankruptcy filing volumes) and Census Bureau (2015 household (HH) counts), both via Haver Analytics.





## Year-Over-Year, Consumer Loan Delinquency Levels Ticked Up in Several Non-Mortgage Categories




Seriously Delinquent = 60+ days past due or in collection for credit cards, consumer finance, and auto loans and 90+ days past due or in foreclosure/bankruptcy for mortgages and student loans; HELOC = home equity line of credit (revolving); HEL = home equity loan (non-revolving). Source: Equifax Quarterly U.S. Consumer Credit Trends (July 2017)

# Section 2
# Commercial Bank Performance

**Earnings**

**Provisions and Loan Loss Allowances**

**Loan Growth and Concentrations**

**Credit Quality**

**Liquidity and Interest Rate Risk**

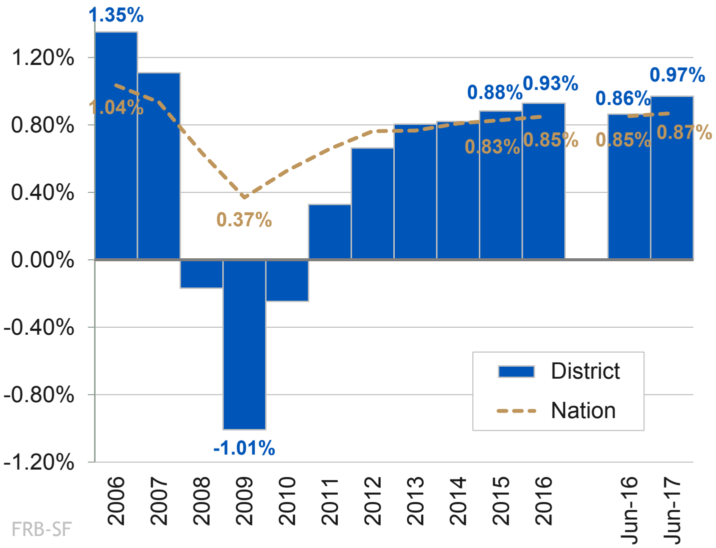
**Capital**

*Note: Bank size groups are defined as very small (<$1B), small ($1B-$10B), mid-sized ($10B-$50B), and large (>$50B) banks. The large bank group covers nationwide banks (a larger statistical population), while the other three groups cover 12th District banks.*

Earnings

## First Half Profits Up vs. 2016, Led by Lower Overhead and Stronger Net Interest Income Ratios

### Average YTD ROAA *(Adjusted for Subchapter S Filers*)*




**Average YTD Profit Components as % of Average Assets 12th District**
*(Expenses = Negative Values)*

| Profit Component | Jun-16 | Jun-17 |
|---|---|---|
| Interest Income | 3.98% | 4.03% |
| Interest Expense | -0.28% | -0.31% |
| Net Int. Income | 3.67% | 3.71% |
| Nonint. Income | 0.59% | 0.62% |
| Nonint. Expense | -3.00% | -2.86% |
| Provision Expense | -0.06% | -0.05% |

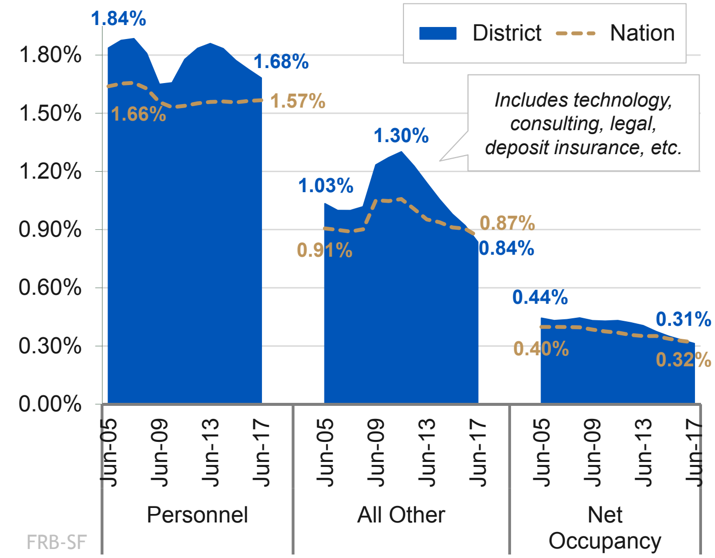
Average = trimmed mean; YTD = year-to-date (annualized); ROAA = return on average assets (net income / average assets), *adjusted for Subchapter S filers (theoretical tax expense deducted from Subchapter S filers for comparability).



Earnings

## Although Declining, Personnel Expense Ratios Continued to Reflect the High Regional Cost of Labor

### Average YTD Overhead Expense / Average Assets




**Average Overhead Metrics YTD Jun-17**

| | 12th Dist. | Nation |
|---|---|---|
| Annualized Personnel Exp./ Emp. ($Thous.) | $ 98.7 | $ 72.7 |
| Assets per Employee ($Mils.) | $ 6.3 | $ 4.8 |
| Assets per Dom. Office ($Mils.) | $118.1 | $ 63.8 |
| Total Assets ($Mils.) | $853.9 | $291.5 |

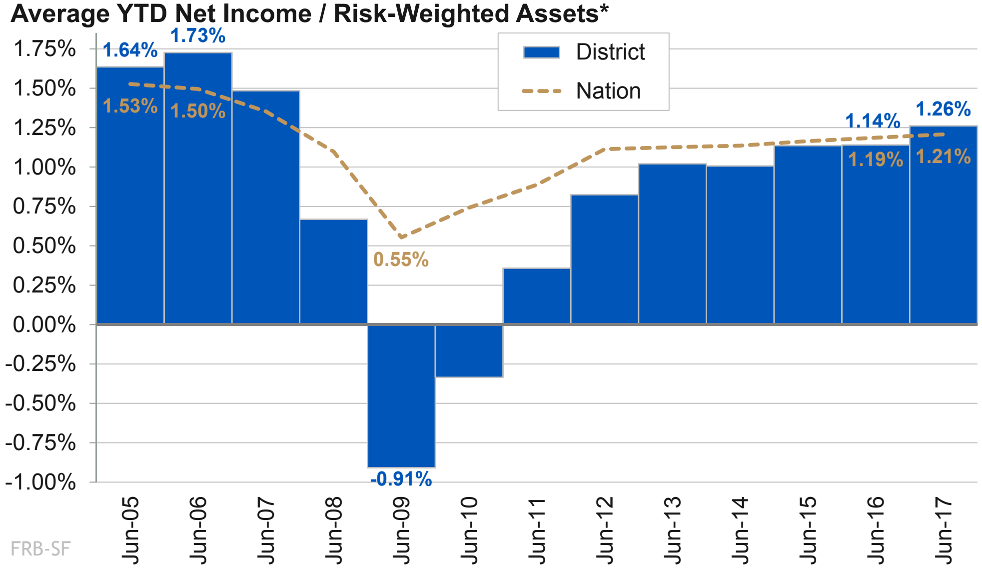
Average = trimmed mean; YTD = year-to-date (annualized); overhead = noninterest expense.



Earnings

## First Half Returns on Risk-Weighted Assets Outpaced the Nation for the First Time Since 2007

### Average YTD Net Income / Risk-Weighted Assets*



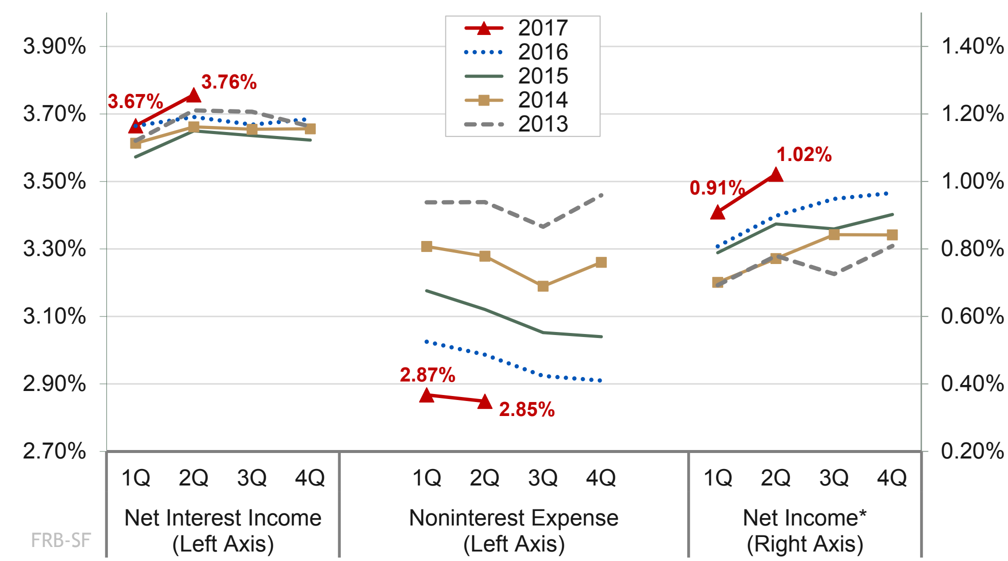

Average = trimmed mean; YTD = year-to-date (annualized); Risk-Weighted Assets are weighted according to regulatory risk-based capital rules in effect as of the report filing date (weights generally reflect perceived credit risk), including off-balance sheet values subject to credit conversion and risk weighting; *excludes Subchapter S tax filers.



Earnings

## Quarterly Annualized Earnings Increased, Lifted by Partly-Seasonal Uptick in Net Interest Income

### Quarterly Income or Expense (Annualized) / Average Assets – 12th District

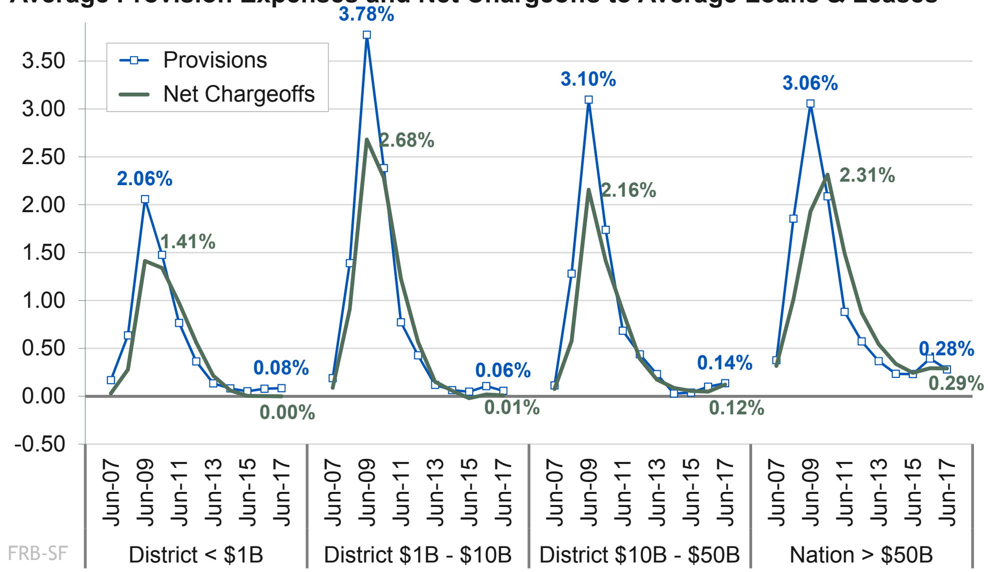



Average = trimmed mean; *adjusted for Subchapter S filers (theoretical tax expense deducted from Subchapter S filers for comparability).

Prov. & ALLL

## Provisioning Rates Tended to be Highest at Mid-Sized and Large Banks, Mainly to Cover Higher Net Chargeoffs

**Average Provision Expenses and Net Chargeoffs to Average Loans & Leases**



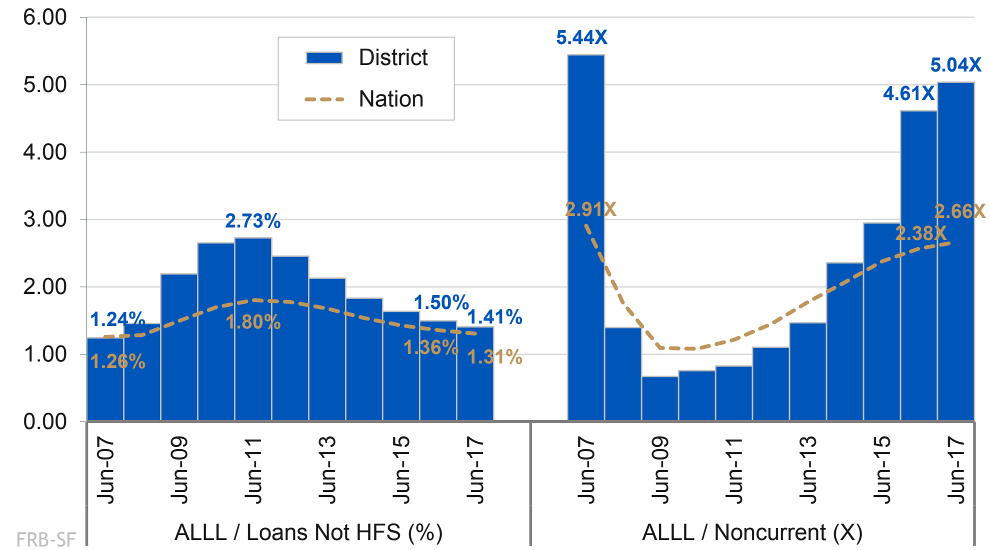

Average = trimmed mean.



Prov. & ALLL

## ALLL as a Share of Loans Slipped, But Coverage of Noncurrents Benefited From Declines in Severe Past Dues

**Average ALLL Coverage of Loans not HFS (%) and Noncurrent Loans (X)**



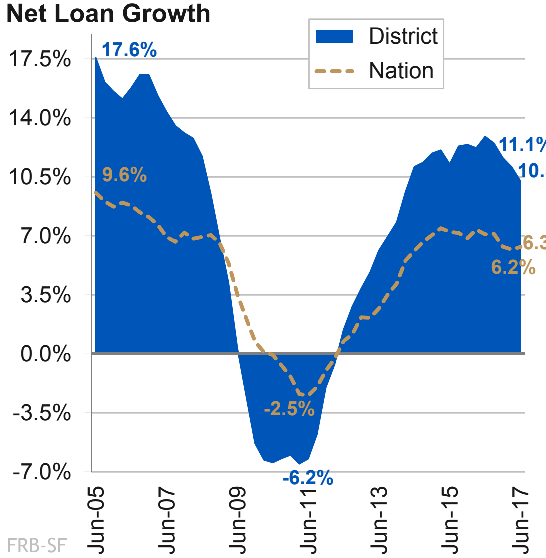

Average = trimmed mean; ALLL = allowance for loan and lease losses; HFS = held for sale; noncurrent = loans past due 90+ days or on nonaccrual status.



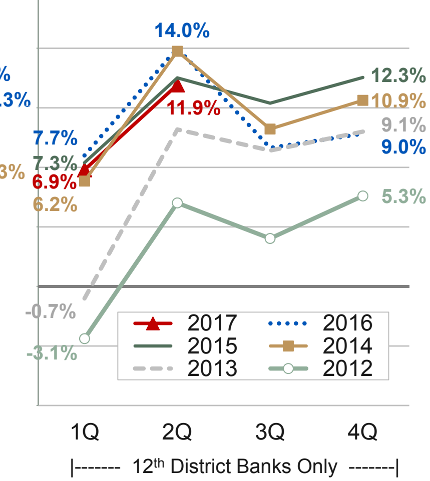
Growth

## Districtwide Average Annual Loan Growth Cooled Further; Quarterly Loan Growth Saw a Seasonal Uptick

**Average Year-Over-Year Net Loan Growth**




**Average Quarter-Over-Quarter Net Loan Growth (Annualized)**



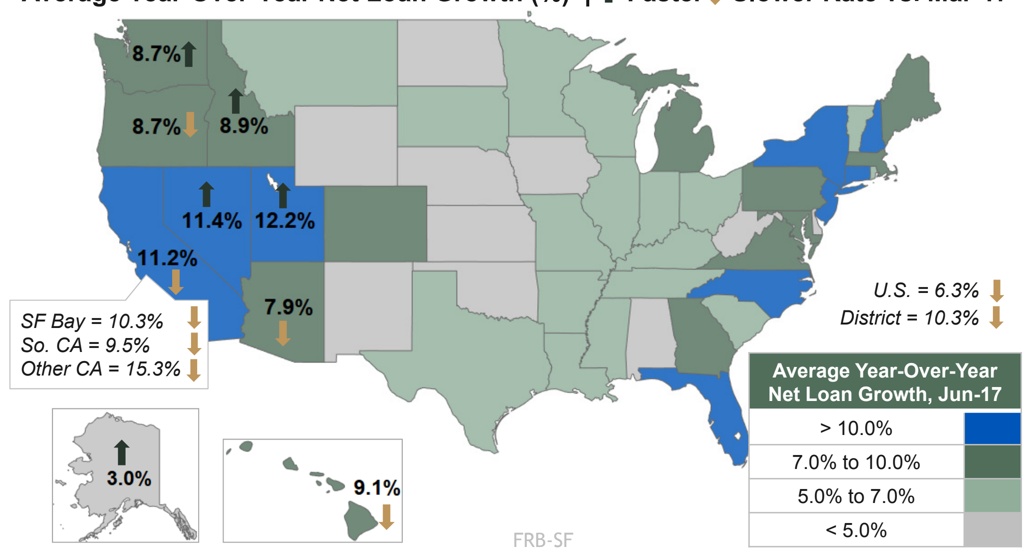

Average = trimmed mean; growth rates are not merger-adjusted.



Growth

## Not All District States Reported Decelerating Growth, But Most Had Above-Average Annual Loan Growth Rates

**Average Year-Over-Year Net Loan Growth (%) | ⬆ Faster ⬇ Slower Rate vs. Mar-17**

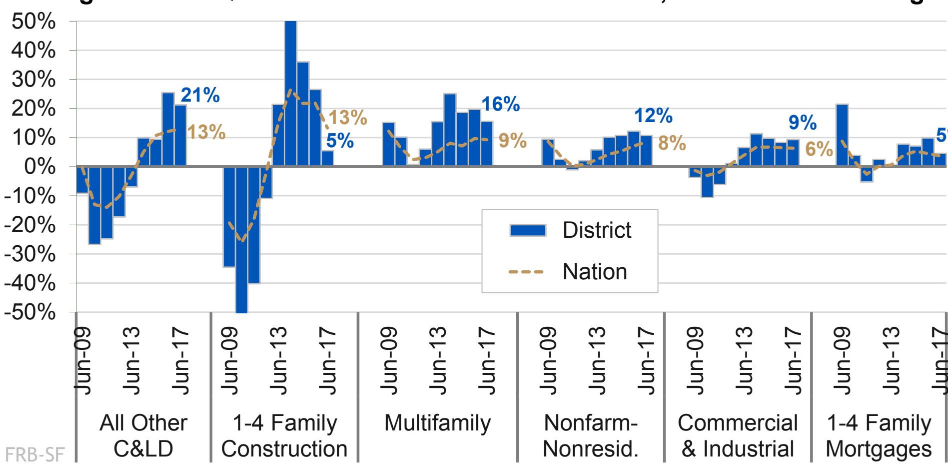



Average = trimmed mean; growth rates are not merger-adjusted; NV excludes zero loan and credit card banks. SF Bay = 42 banks based in San Francisco-San Jose Consolidated Statistical Area (CSA); So. CA = 81 banks based in Los Angeles CSA + San Diego Metropolitan Statistical Area; Other CA = 38 banks based in all other California counties.

## Growth in Other C&LD and Multifamily Remained Strongest; Growth in 1-4 Family C&LD Decelerated Sharply

Growth

### Average Second Quarter Year-Over-Year Loan Growth, Selected Loan Categories




| Memo: Average Concentration to Total Capital, Jun-17 | | | | | | |
|---|---|---|---|---|---|---|
| District | 21.76 | 9.83 | 32.16 | 260.06 | 89.50 | 80.14 |
| Nation | 18.50 | 9.53 | 13.27 | 143.31 | 71.76 | 139.33 |

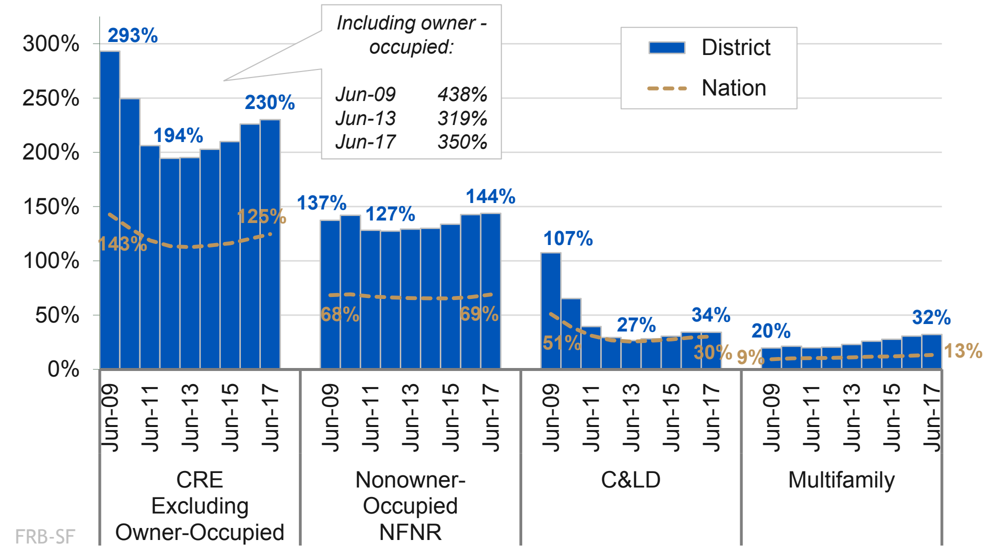
Average = trimmed mean; growth rates are not merger-adjusted; C&LD = construction and land development; nonfarm-nonresidential includes mortgages with owner-occupied collateral.



## Overall, Nonowner-Occupied CRE Loan Concentrations Remained High; C&LD Concentrations Flattened

Growth

### Average CRE Concentrations to Total Capital



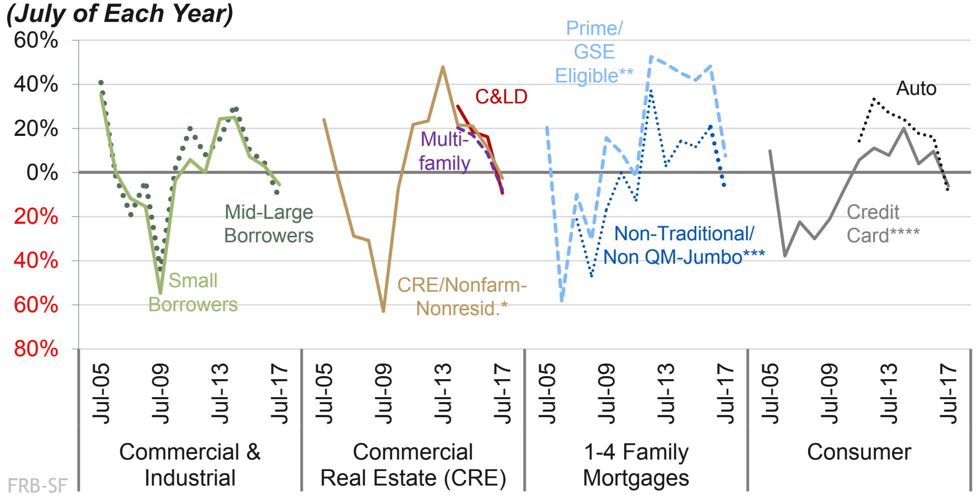

Average = trimmed mean; Commercial Real Estate (CRE) Excluding Owner-Occupied = nonowner-occupied nonfarm-nonresidential (NFNR), construction and land development (C&LD), multifamily, and other CRE-purpose loans.



## A Small but Growing Fraction of Lenders Noted Weaker Demand, Which Would Weigh on Loan Growth

Growth

### Net % of Lenders Reporting Stronger (Weaker) Loan Demand vs. 3 Months Prior *(July of Each Year)*



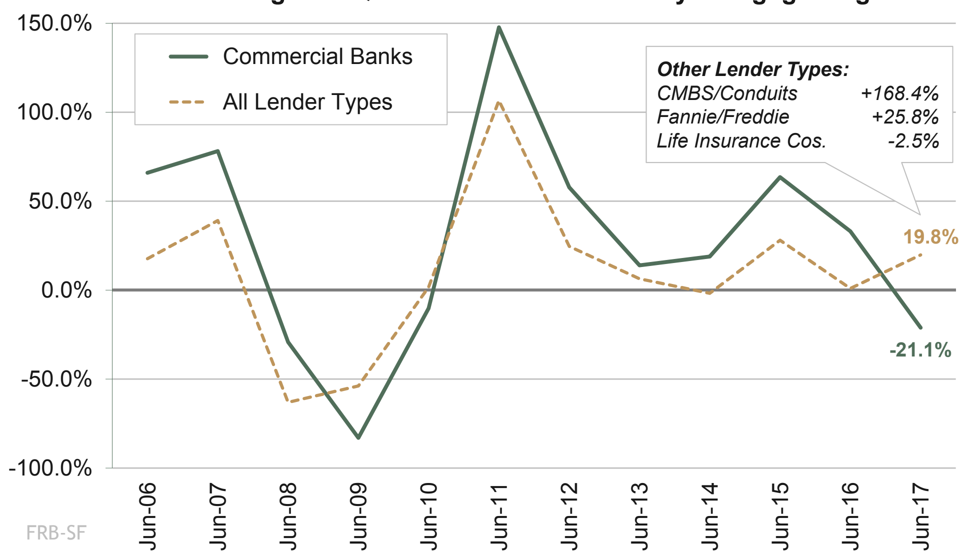

Based on a sample of loan officers at domestic banks (number varies by period and loan type); C&LD = construction and land development; *includes all CRE loans prior to 2014; **includes all residential mortgages prior to 2007, "prime" mortgages 2007-2014, and GSE-Eligible after 2014; ***includes "nontraditional" mortgages 2007-2014 and Non QM Jumbo mortgages after 2014; ****includes all consumer loans prior to 2011. Source: Federal Reserve Senior Loan Officer Opinion Survey (http://www.federalreserve.gov/BoardDocs/snloansurvey/).



## Commercial Banks Scaled Back CRE Originations in 2Q17; CMBS and Fannie/Freddie Expanded Strongly

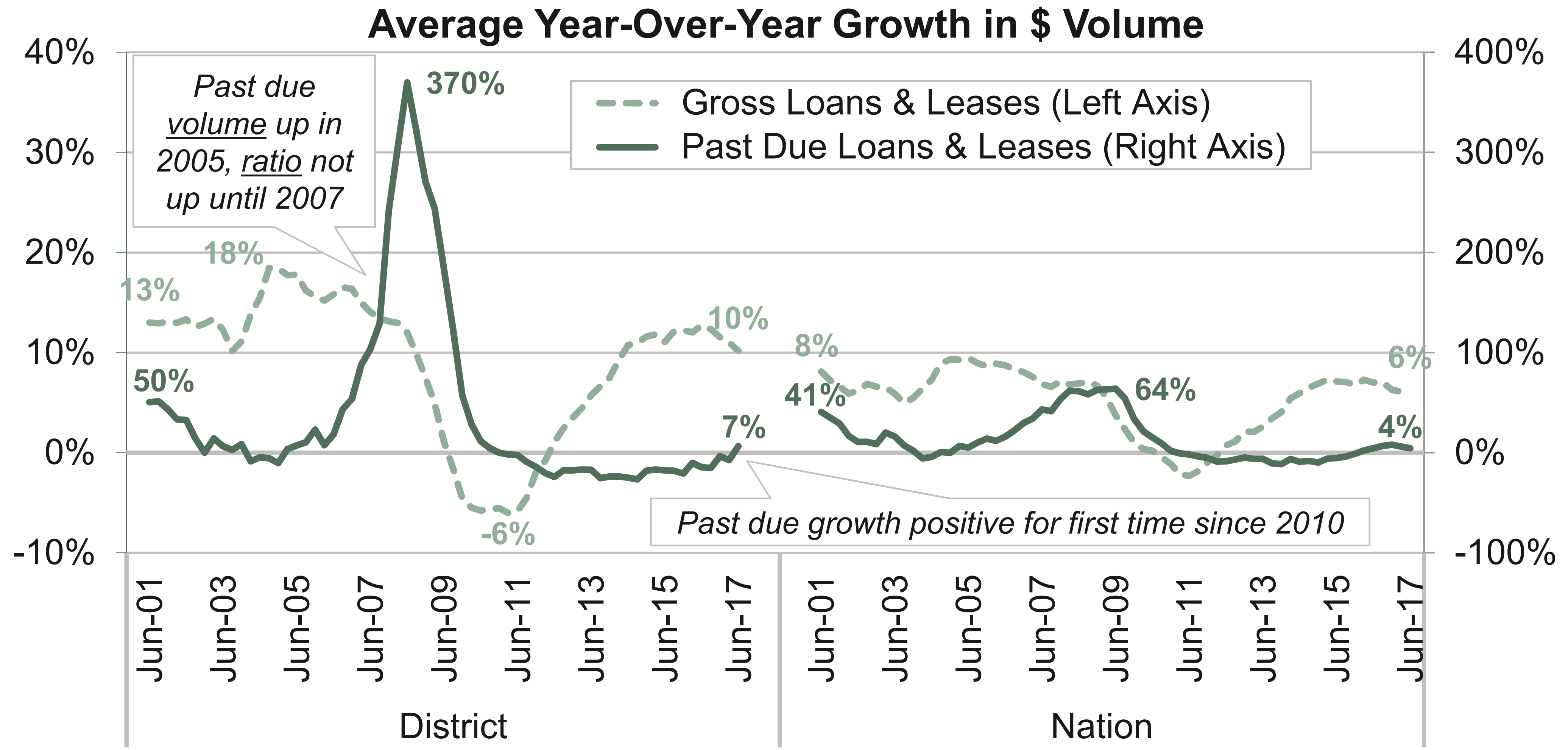
Growth

### Year-Over-Year Change in 2Q Commercial & Multifamily Mortgage Originations




All Lender Types includes commercial mortgage backed securities/conduits, commercial banks, life insurance companies, and Fannie/Freddie. Source: Mortgage Bankers Association.

# Average Past Due Loan *Volumes* Increased But Gross Loans Grew Faster, Leaving Past Due *Ratios* Lower




## Memo: Avg. Past Due 30+ Days or Nonaccrual / Gross Loans*

**District**

| 01 | 02 | 03 | 04 | 05 | 06 | 07 | 08 | 09 | 10 | 11 | 12 | 13 | 14 | 15 | 16 | 17 |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| 1.70 | 1.68 | 1.37 | 0.98 | 0.81 | 0.67 | 1.00 | 2.88 | 6.02 | 5.65 | 5.16 | 3.55 | 2.39 | 1.55 | 1.07 | 0.76 | 0.68 |

**Nation**

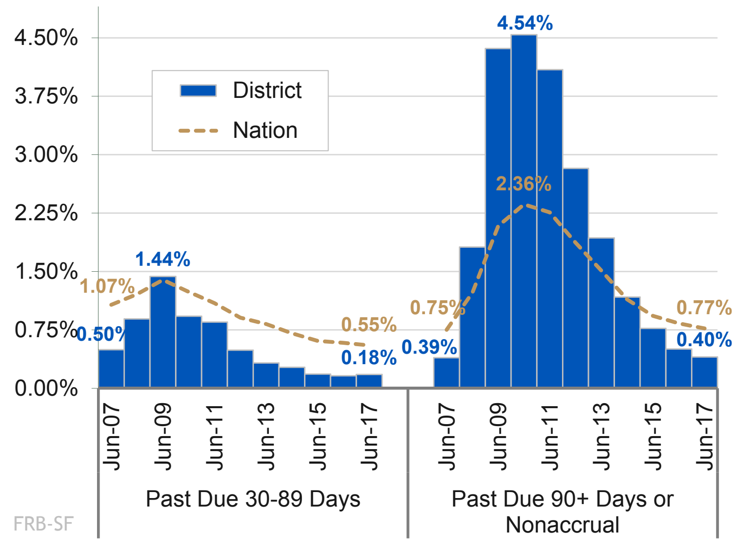
| 01 | 02 | 03 | 04 | 05 | 06 | 07 | 08 | 09 | 10 | 11 | 12 | 13 | 14 | 15 | 16 | 17 |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| 2.34 | 2.27 | 2.29 | 1.91 | 1.68 | 1.66 | 1.97 | 2.61 | 3.68 | 3.81 | 3.56 | 2.99 | 2.52 | 2.02 | 1.68 | 1.54 | 1.43 |

Average = trimmed mean; past due = loans past due 30+ days or on nonaccrual status; growth rates are not merger-adjusted; *table data as of June of each year.

Credit Quality

## Average Early-Stage Past Due Ratio Ticked Up; Noncurrent Rate Eased Further

### Average Past Due or Noncurrent / Gross Loans & Leases




**Avg. Past Due 30+ Days + Nonaccrual % 12th District**

| Loan Type | Jun-16 | Jun-17 |
|---|---|---|
| C&I | 0.76% | 0.59% |
| 1-4 Family | 0.63% | 0.60% |
| NFNR | 0.44% | 0.33% |
| *Owner-Occupied* | *0.49%* | *0.42%* |
| *Nonowner-Occupied* | *0.19%* | *0.14%* |
| Consumer | 0.29% | 0.28% |
| C&LD | 0.32% | 0.27% |
| Agriculture | 0.09% | 0.18% |
| All Loans | 0.76% | 0.68% |

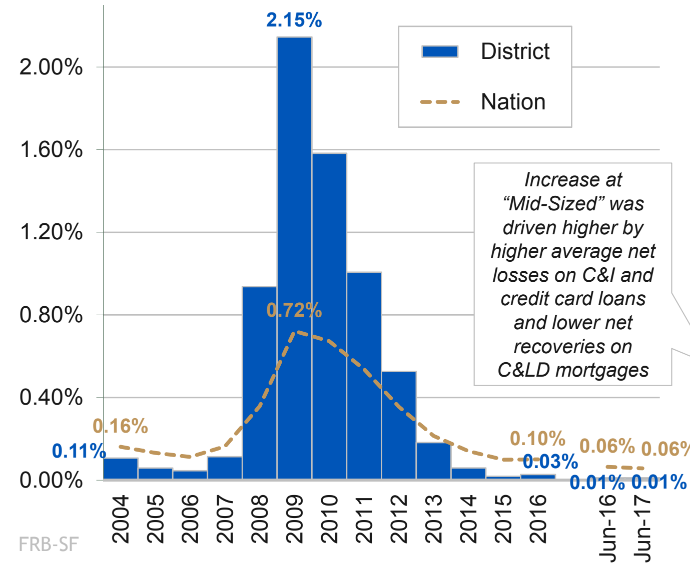
Average = trimmed mean; loans past due 30-89 days are delinquent but still accruing interest (early-stage); noncurrent = loans past due 90+ days or on nonaccrual status; C&I = commercial & industrial; NFNR = nonfarm-nonresidential mortgages; C&LD = construction & land development.



Credit Quality

## Average Net Chargeoffs Were Negligible in the First Half of 2017, Especially at Smaller Banks

### Average Net Chargeoffs / Avg. Loans and Leases




**Average Net Chargeoffs (Recoveries) / Average Loans (%)**

| Bank Size | Jun-16 | Jun-17 |
|---|---|---|
| District Very Small (<$1B) | 0.00% | 0.00% |
| District Small ($1B-$10B) | 0.02% | 0.01% |
| District Mid-Sized ($10B-$50B) | 0.05% | 0.12% |
| Nation Large (>$50B) | 0.29% | 0.29% |

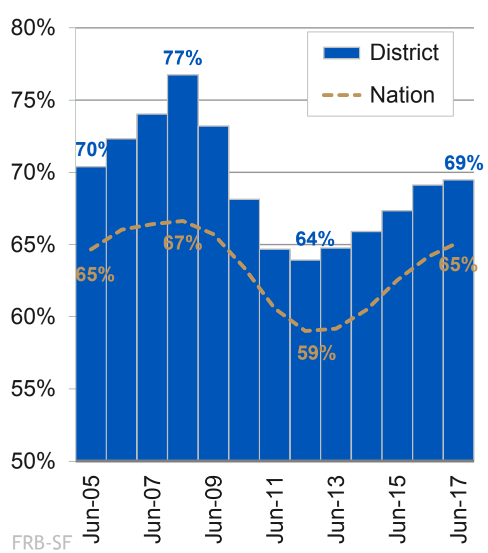
Average = trimmed mean; year-to-date annualized; C&I = commercial & industrial; C&LD = construction & land development.



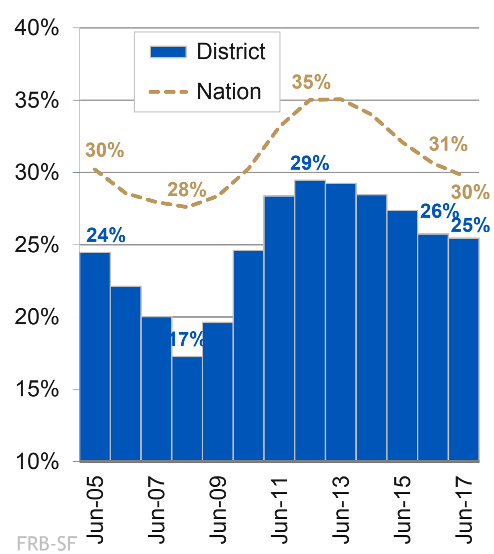
Liquidity

## Year-Over-Year, On-Balance Sheet Liquidity Dipped Slightly

### Net Loans and Leases / Assets*




### Securities & Liquid Invest. / Assets*



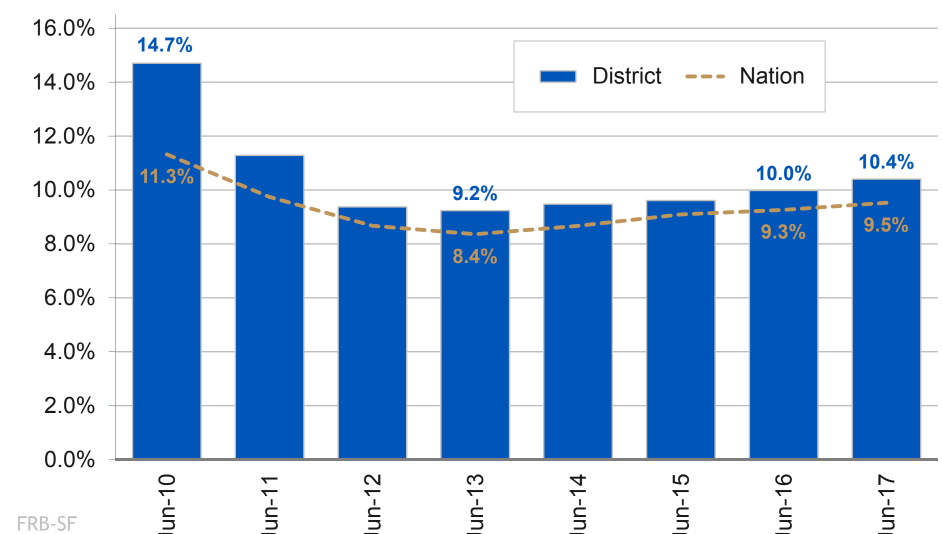

*All data are averages (trimmed means); liquid investments = cash, due from balances, interest bearing balances, and Federal funds sold & securities purchased under agreements to resell.



Liquidity

## District Noncore Funding Inched Higher

### Average Noncore Liabilities / Total Assets

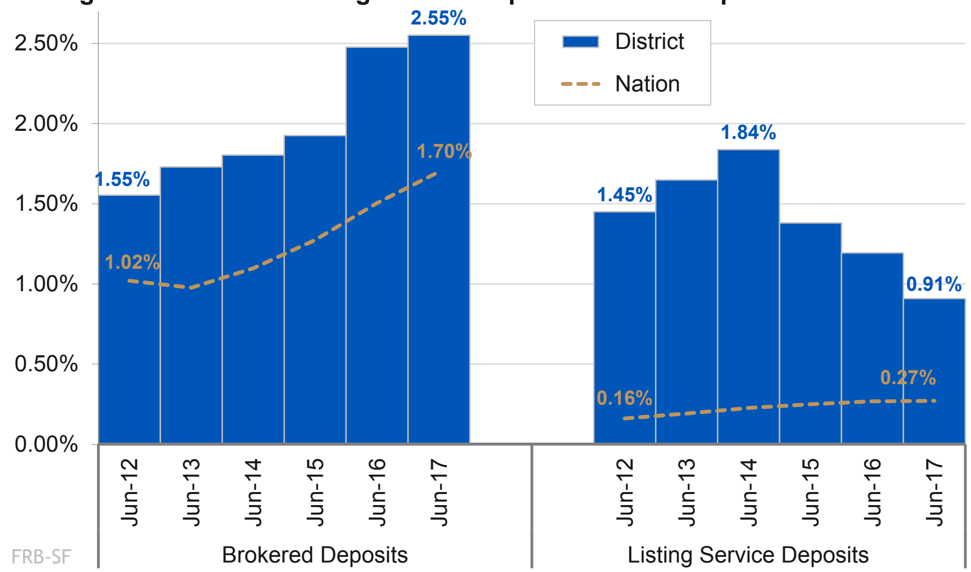



Average = trimmed mean; Noncore liabilities = sum of borrowings (Federal funds purchased, repurchase agreements, and other borrowed money), foreign deposits, certificates of deposit > $250K, and brokered deposits < $250K.

Liquidity

## Brokers Provided a Small but Increasing Share of District Deposits While Listing Services Declined in Importance

**Average Brokered and Listing Service Deposits to Total Deposits**



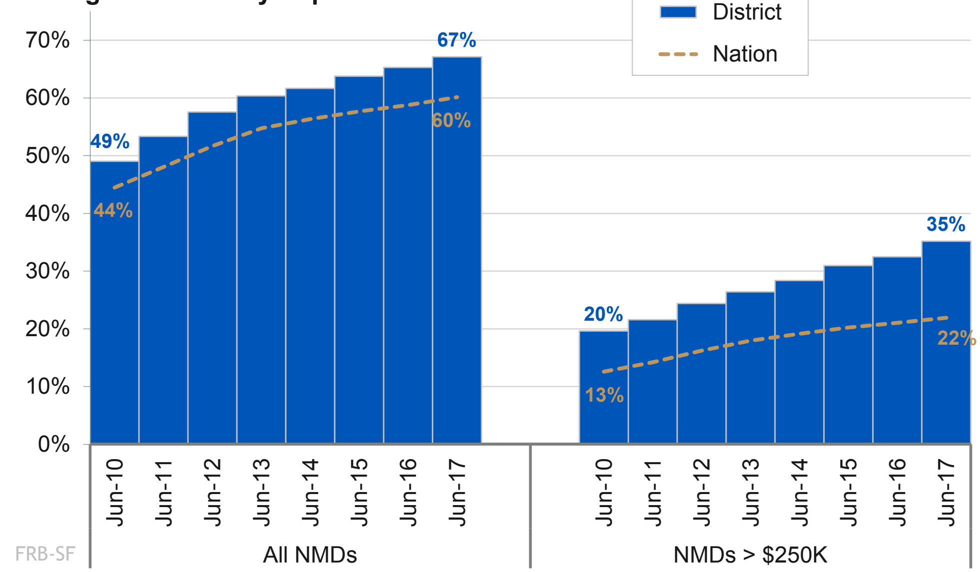

Average = trimmed mean.



Liquidity

## Nonmaturity Deposit Reliance Edged Higher, Driven Heavily in Recent Years by "Jumbo" Accounts

**Average Nonmaturity Deposits to Assets**



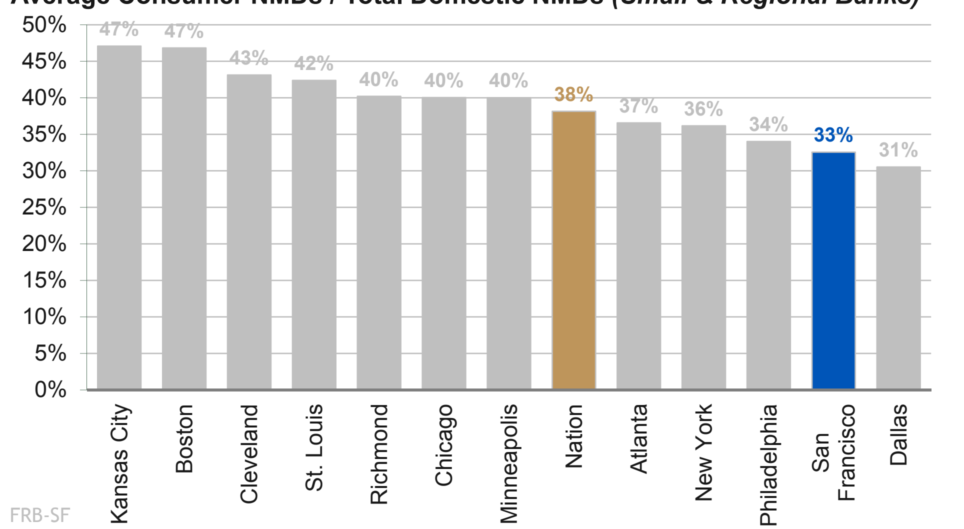

Average = trimmed mean; NMD = nonmaturity deposits (all deposits excluding time deposits).



Liquidity

## 12th District NMDs Were Less Likely to be Consumer-Oriented, More Likely to be Commercial/Institutional

**Average Consumer NMDs / Total Domestic NMDs *(Small & Regional Banks)***



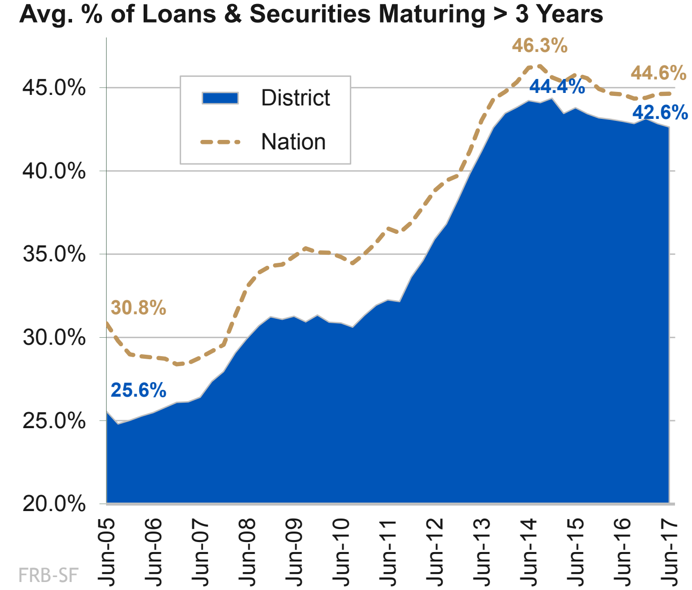

Average = trimmed mean; NMD = nonmaturity deposit (nontransaction accounts plus money market deposits and other savings accounts; excludes time deposits and foreign office deposits); Consumer = intended primarily for individuals for personal, household, or family use; includes commercial banks with total assets between $1 billion and $50 billion; all data as of 6/30/2017.



Int. Rate Risk

## Investments in Longer-Term Assets Eased Further But Remained at Relatively High Levels

**Avg. % of Loans & Securities Maturing > 3 Years**




**Average Loans & Securities > 3 Years / Assets (%)**

| | 2005-17* | Jun-17 |
|---|---|---|
| AK | | 54.3% |
| OR | | 52.5% |
| HI | | 47.4% |
| WA | | 47.1% |
| NV | | 46.0% |
| AZ | | 44.7% |
| CA | | 42.8% |
| ID | | 34.6% |
| UT | | 30.6% |
| Nation | | 44.6% |

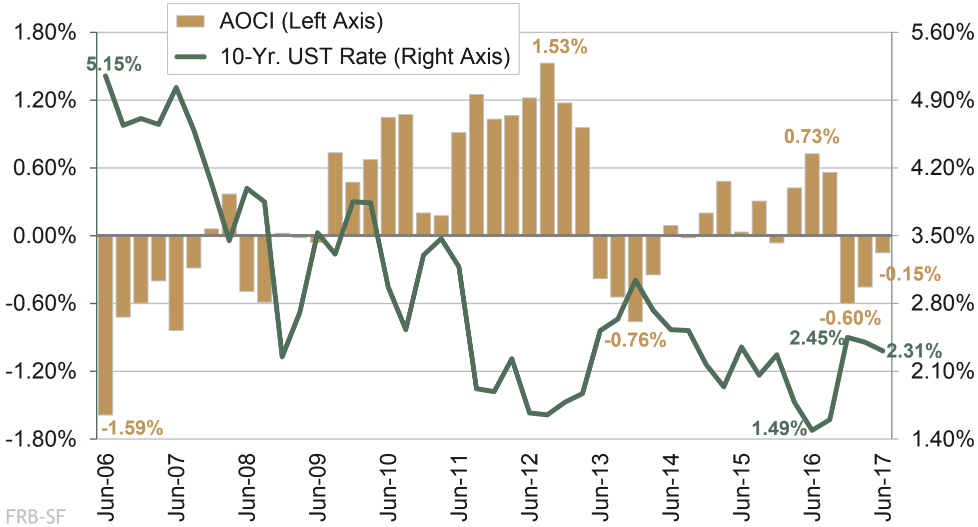
Average = trimmed mean; *June of each year; NV excludes credit card and zero-loan banks.

Int. Rate Risk

## A Second Quarter Dip in Long-Term Interest Rates Helped Reduce Net Unrealized Losses on AFS Securities

**Average Accumulated Other Comprehensive Income (AOCI) / Tier 1 Cap. – 12th District**

**End-of-Period 10-Year CM U.S. Treasury Rate**



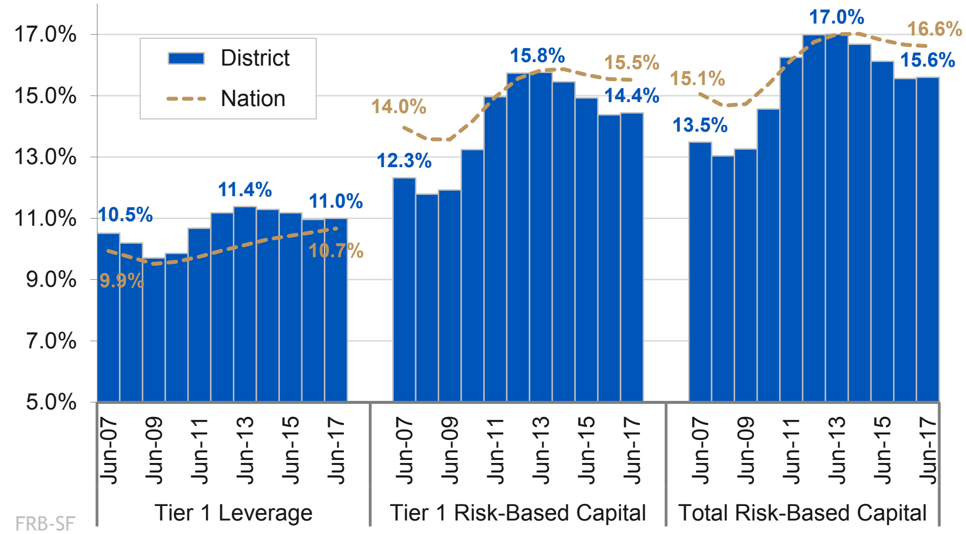

Average = trimmed mean; accumulated other comprehensive income (AOCI) includes net unrealized gains/losses on available-for-sale (AFS) securities. Source: Constant Maturity (CM) U.S. Treasury Rate from Federal Reserve via Haver Analytics.



Capital

## Average District Capital Ratios Stabilized as Earnings Improved and Asset Growth Moderated

**Average Regulatory Capital Ratios**



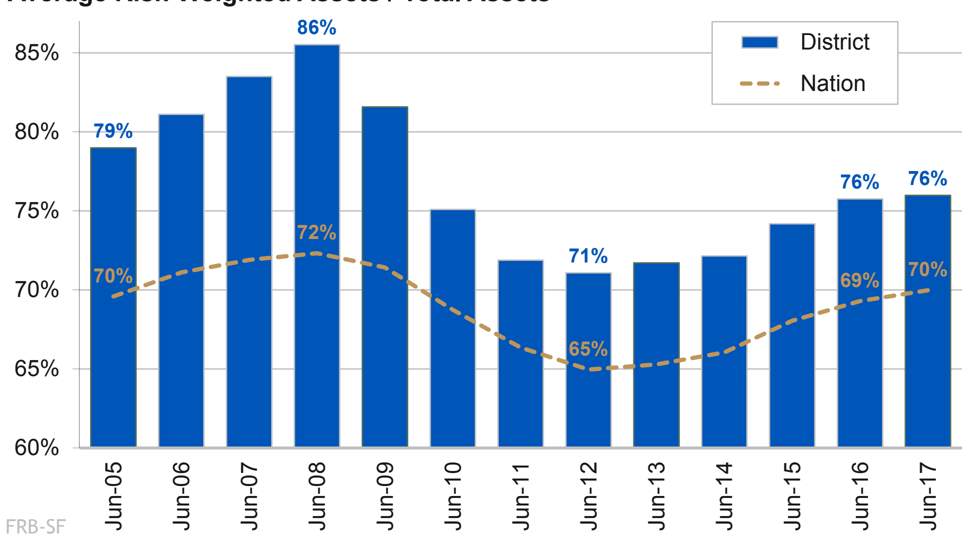

Average = trimmed mean; new risk-based capital rules that became effective March 2015 for most banks (March 2014 for some larger/more complex banks) included the phase out of some capital instruments and the introduction of higher risk weights on some asset and off-balance sheet commitment categories.



Capital

## Risk-Weighted Assets Flattened as a Share of Assets, Suggesting a Slower Rotation into Higher-Risk Assets

**Average Risk-Weighted Assets / Total Assets**



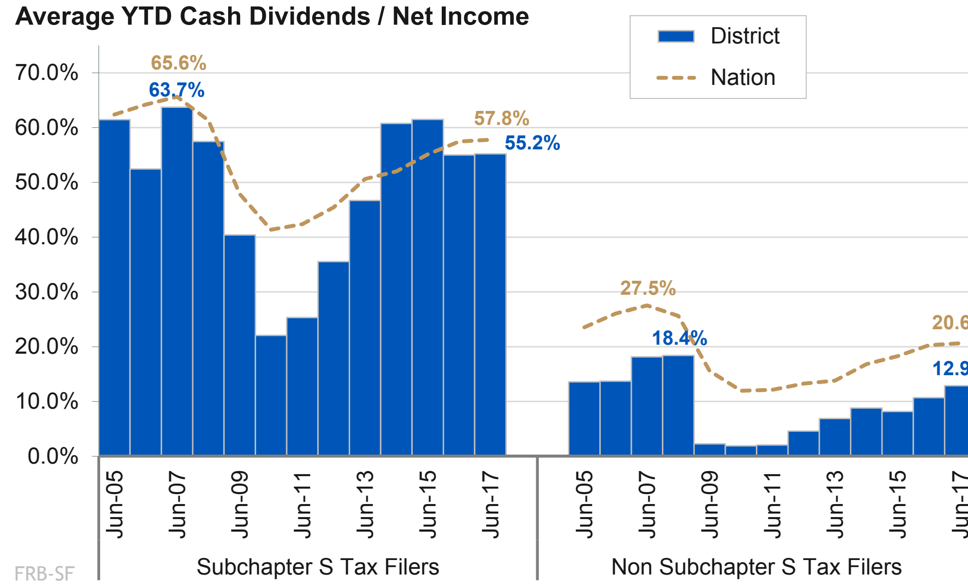

Average = trimmed mean; Risk-Weighted Assets are weighted according to regulatory risk-based capital rules in effect as of the report filing date (weights generally reflect perceived credit risk); includes off-balance sheet values subject to credit conversion and risk weighting.



Capital

## Dividend Payouts Increased Among Non Subchapter S Filing Banks, but Trailed the National Average

**Average YTD Cash Dividends / Net Income**




Average = trimmed mean; YTD = year-to-date; Subchapter S filing banks pay taxes at the shareholder rather than corporate level and typically distribute dividends so that shareholders can cover tax obligations.

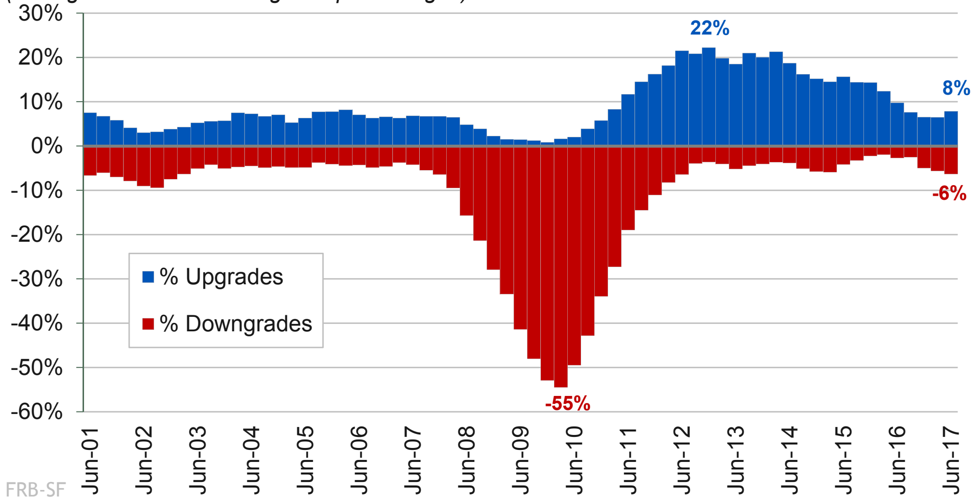
# Section 3
# Commercial Bank Regulatory Ratings & Trends

*Focusing on trends in safety and soundness, consumer compliance, and Community Reinvestment Act examination ratings assigned by regulatory agencies to commercial banks headquartered within the 12th Federal Reserve District.*

Ratings

## Upgrades Continued to Slightly Outpace Downgrades During the 12 Months Ending June

**Trailing 4-Quarter Share of 12th District S&S Examinations that Resulted in CAMELS Composite Rating Upgrade or Downgrade**
*(downgrades shown as negative percentages)*



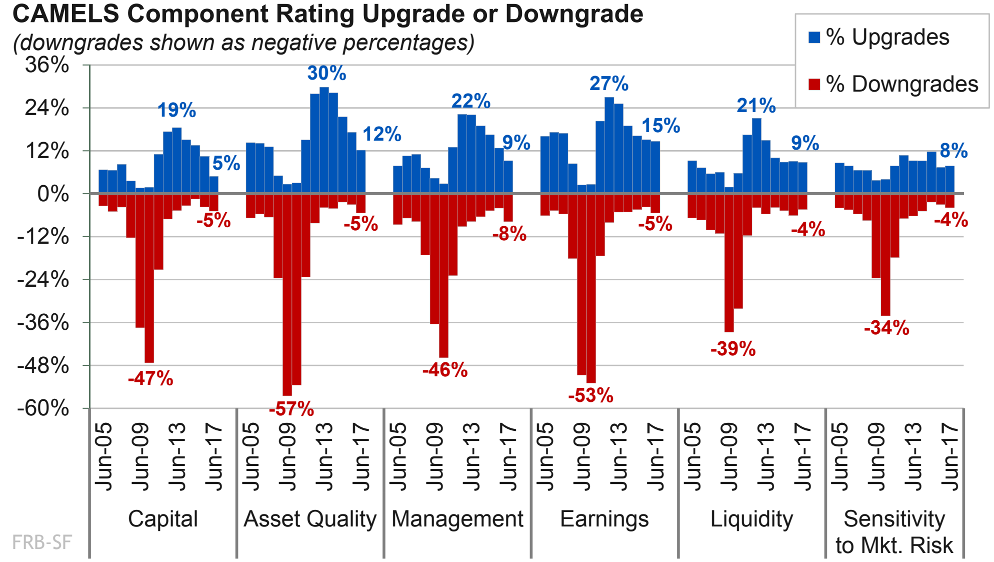

S&S = safety and soundness; includes any change in composite CAMELS rating for commercial banks; based on examination completion dates (mail dates); preliminary second quarter 2017 data updated through 8/21/17.



Ratings

## Although Upgrades Exceeded Downgrades, Downgrade Activity Ticked Up in Several Components

**Trailing 4-Quarter Share of 12th District S&S Examinations that Resulted in CAMELS Component Rating Upgrade or Downgrade**
*(downgrades shown as negative percentages)*



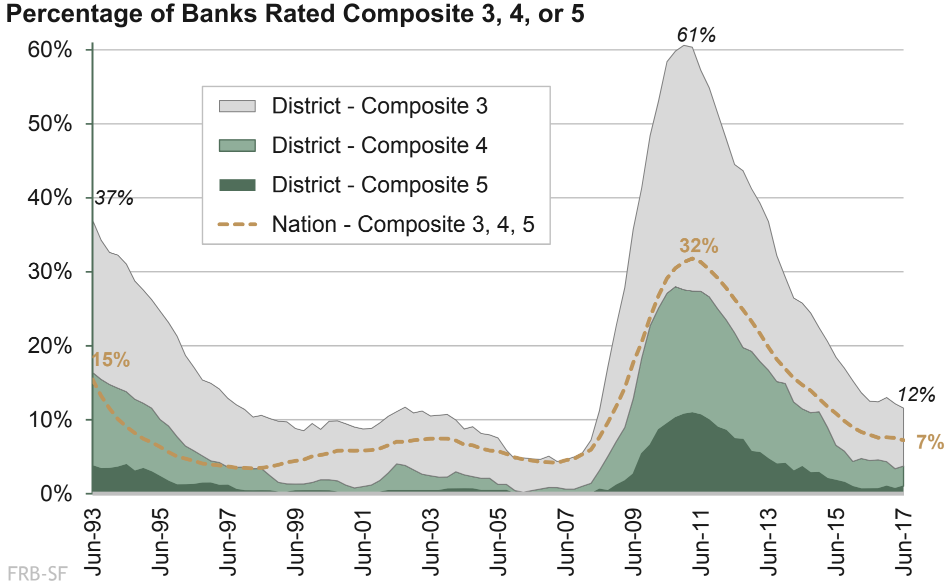

S&S = safety and soundness; includes any change in composite CAMELS rating for commercial banks; based on examination completion dates (mail dates); preliminary second quarter 2017 data updated through 8/21/17.



Ratings

## The Share of District Banks with Composite Ratings of 3, 4, or 5 Declined Further, But Still Above Pre-Crisis

**Percentage of Banks Rated Composite 3, 4, or 5**



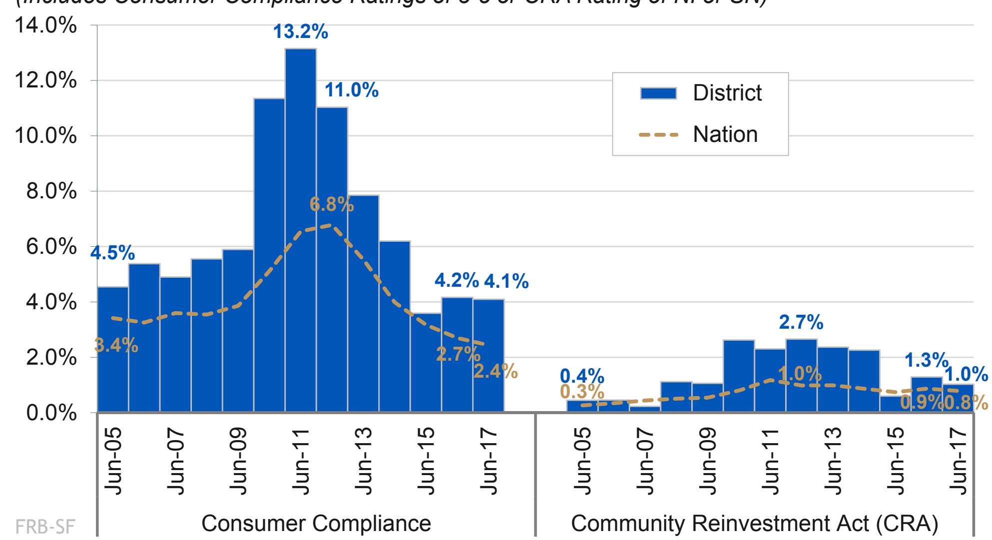

Trends for all commercial banks based on examination completion dates (mail dates); preliminary second quarter 2017 data updated through 8/21/17.



Ratings

## While District Consumer Compliance/CRA Ratings Were Weaker Than Nation, Few Were Less-Than-Satisfactory

**Percentage of 12th District Banks with Less-than-Satisfactory Ratings**
*(Includes Consumer Compliance Ratings of 3-5 or CRA Rating of NI or SN)*




Trends for all commercial banks based on examination completion dates (mail dates); NI = Needs to Improve; SN = Substantial Noncompliance; preliminary second quarter 2017 data updated through 8/21/17.

# Appendices

**Summary of Institutions**

**Technical Information**

# Appendix 1: Summary of Institutions

| Area | Commercial Banks (De Novos) | | Industrial Banks (De Novos) | | Savings Institutions (De Novos) | |
|---|---|---|---|---|---|---|
| | *Jun-16* | *Jun-17* | *Jun-16* | *Jun-17* | *Jun-16* | *Jun-17* |
| **AK** | 4 (0) | 4 (0) | - | - | 1 (0) | 1 (0) |
| **AZ** | 17 (0) | 15 (0) | - | - | 1 (0) | 1 (0) |
| **CA** | 170 (0) | 161 (1) | 3 (0) | 3 (0) | 12 (0) | 10 (0) |
| **GU** | 2 (0) | 2 (0) | - | - | 1 (0) | 1 (0) |
| **HI** | 5 (0) | 5 (0) | 1 (0) | 1 (0) | 2 (0) | 2 (0) |
| **ID** | 11 (0) | 12 (0) | - | - | 1 (0) | 1 (0) |
| **NV** | 9 (0) | 9 (0) | 4 (0) | 4 (0) | 2 (0) | 2 (0) |
| **OR** | 22 (0) | 20 (0) | - | - | 3 (0) | 3 (0) |
| **UT** | 30 (0) | 28 (0) | 15 (0) | 15 (0) | 2 (0) | 2 (0) |
| **WA** | 42 (0) | 38 (0) | - | - | 10 (0) | 10 (0) |
| **12L** | 312 (0) | 294 (1) | 23 (0) | 23 (0) | 35 (0) | 35 (0) |
| **US** | 5,210 (2) | 4,982 (4) | 25 (0) | 25 (0) | 820 (1) | 776 (1) |

Based on preliminary second quarter 2017 data.

# Appendix 2: Technical Information

**General:** This report focuses on the financial trends and performance of commercial banks headquartered within the 12th Federal Reserve District ("12L"). 12L includes nine western states: AK, AZ, CA, HI, ID, NV, OR, UT, and WA, as well as Guam.

**Banking Statistics**: Unless otherwise noted, all data are for commercial banks based upon headquarters location. Averages are calculated on a "trimmed" basis by removing the highest 10% and lowest 10% of ratio values prior to averaging to prevent distortion from outliers. Earnings figures are presented on an annualized year-to-date or quarterly basis, as noted. Growth rates are not adjusted for mergers. The latest quarter of data is considered preliminary. Other than the table to the left, graphics exclude "De Novo" banks (banks less than five years old) and industrial banks and savings institutions (which have different operating characteristics).

**Groups by Asset Size:** "Very Small," "Small," and "Mid-Sized" bank groups are based on total asset ranges of <\$1B, \$1B-\$10B, and \$10B-\$50B, respectively. The "Large" bank group uses banks with assets >\$50B nationwide because these banks typically operate beyond the District's geographic footprint and a larger statistical population is needed to construct trimmed means.